Colac Otway
SHIRE

Our Ref: F15/5923

27 August 2015

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- 1 SEP 2015
ESSENTIAL SERVICES COMMISSION

Dr Ron Ben-David
Chairperson
Essential Services Commission
Level 37/2 Lonsdale Street
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localgovernment@esc.vic.gov.au

Dear Dr. Ben-David

**Response to the Draft Blueprint for Change, Local Government Rates Capping & Variation Framework Review**

I refer to the report "A Blueprint for Change, Local Government Rates Capping and Variation Framework Review". Thank you for the opportunity to make a submission on the draft report.

At Colac Otway's Council meeting held on Wednesday 26 August 2015, Council resolved:

"1. *Endorses the submission incorporating responses to the recommendations from the Local Government Rates Capping and Variation Framework Review being forwarded to the Essential Services Commission.*

2. *Recommends the ESC delivers a differential model of rate capping, acknowledging the inequity of the proposed draft and the adverse impact it will have on delivery of services and infrastructure maintenance and renewal, especially roads and bridges."*

Please find attached Council's submission which addresses the draft recommendations from the report as well as providing additional information.

The additional information provides details of impacts that Rate Capping will have on Council's finances, services and the Asset Renewal Gap.

If you require further information or would like to discuss aspects of Council's submission, please don't hesitate to contact me on ph: 5232 9454 or email at sue.wilkinson@colacotway.vic.gov.au.

Yours sincerely

Sue Wilkinson
**Chief Executive Officer**

Colac Otway
SHIRE

# RESPONSE TO "A Blueprint for Change – Local Government Rates Capping & Variation Framework Review"

## ESSENTIAL SERVICES COMMISSION VICTORIA (ESC)

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## EXECUTIVE SUMMARY

This is Colac Otway's response to the draft recommendations in the Draft Report from the Essential Services Commission Victoria (ESC) "A Blueprint for Change – Local Government Rates Capping & Variation Framework Review" and information which is relevant from Council's initial submission on Rate Capping.

Colac Otway appreciates the opportunity to respond to the questions in the Draft Report and further provide information which is relevant to the significant issue of Rate Capping which will impact Local Government.

It should be noted from the outset that only providing a 4 week period to respond to what will be one of the most important issues that confronts Local Government in Rate Capping is fundamentally unfair.

Colac Otway like many other Victorian councils has significant concerns regarding the impacts of rate capping on the municipality and does not believe that rate capping represents strong public policy outcomes.

As noted in our previous submission it is important that the ESC investigated all possible options. The ESC is encouraged to explore other alternatives to Rate Capping taking into account the significant pressures that Rate Capping will place on Councils.

It is important that Local Government in Victoria continues to have the capacity to raise the appropriate level of rates to levy. The level of rates that Colac Otway charges is based on the services that Council delivers and the funding required to maintain the community's assets to the level required.

It is also important that not only financial considerations are taken into account when Rate Capping is being proposed. Councils play a critical role in community development and delivery of social policy outcomes for the community which cannot be ignored.

Colac Otway Shire currently delivers approximately 90 services, many of which impact various sectors in the community. Rate capping will mean that smaller Councils like Colac Otway will need to further review services that are delivered, placing further burdens on the community.

The impacts of rate capping will have a significant impact on Colac Otway Shires sustainability and directly affect our community. The implementation of rate capping for Victorian Councils has the potential to threaten the delivery of vital services and works to local communities.

It is unclear as to what is the purpose of rate capping:

- What is to be achieved?
- What are the issues that exist in the Local Government sector that need to be addressed?
- Were other methods to address these issues explored/considered?

It should also be noted that there is an inherent contradiction that the current process highlights that the ESC have been requested by the State Government to design a system to introduce rate capping as well as a system to work around rate capping.

**Draft recommendations in the Draft Report from the Essential Services Commission Victoria (ESC) "A Blueprint for Change – Local Government Rates Capping & Variation Framework Review".**

The following is a response to each of the 11 recommendations and matters for further consideration.

## THE CAP

### Draft recommendation 1

The Commission recommends that there should be one rate cap that applies equally to all councils in Victoria.

***Colac Otway Response:***

*It is recognised that by having one cap creates an illusion of equality across all councils, but it also needs to be recognised that each grouping of Councils and each Council has different needs and pressures.*

*It is important to note that a number of councils in rural areas have limited other income streams. It has been well documented the financial pressures that smaller sized councils (in terms of population) are under in maintaining financial sustainability in the current environment. Further pressures on rating which is Council's main revenue stream will place added pressure on Council's already tight budgets and financial situation.*

*The impact for Councils in regional and rural areas will be significantly bigger as the opportunity to raise revenue from other income sources like fees and charges is harder than in Metropolitan areas.*

*It is also important to note that rural municipalities have significant infrastructure to maintain. For example Colac Otway maintains 1,632 kms of local roads and 134 bridges and culverts.*

*It is suggested that there is further consideration given to having a different level of rate cap for the various Council groupings.*

### Draft recommendation 2

The Commission recommends that:

- revenue from general rates and municipal charges should be subject to the rate cap
- revenue from special rates and charges, 'revenue in lieu of rates' and the fire services levy should not be included in the rate cap and
- service rates and charges should not be included in the rate cap, but be monitored and benchmarked.

***Colac Otway Response:***

*Colac Otway agrees with the recommendation.*

*With respect to service rates and charges, Colac Otway reviews its Waste Management Charge on an annual basis to ensure that the charge covers the cost of providing the service to those receiving it.*

*It needs to be noted that with respect to Waste Management charges they have been impacted by the higher standards required by State Government. The trend indicates that the waste disposal gate fee has been increasing at a rate of approximately 15% per year. This not only affects the kerbside budget but also Council waste and litter disposal costs. These costs are unavoidable and will still need to be paid when rate capping is implemented.*

*The Landfill Levy implemented by the State Government has increased from $7 per tonne in 2009 to $29.30 per tonne for the rural landfill sites. This has had a significant impact on Council rates and the annual waste charge. This will not only affect the kerbside budget but also Council waste and litter disposal costs. These costs are unavoidable and will still need to be paid when rate capping is implemented.*

*Many of the contracts including the waste contract involve transportation which is affected by fuel costs. These costs are highly variable and impacted by international factors as well as the rise and fall of the Australian Dollar which are outside Council's control. Council's rate has to be responsive to the variable fuel price on a year to year forecast basis.*

*Fire Services Levy:*
*It is also important to note that while Local Government is being asked to keep rates and charges increases to a minimum the State Government has significantly increased the Fire Services Property Levy (FSPL) for 2015-16.*

*Whilst this is not a Council charge, Council is forced to collect the FSPL on behalf of the Victorian Government through the rate collection process. The fixed portion of the FSPL will increase in 2015-16 by $2 per property (from $102 to $104) for residential properties, and by $5 (from $205 to $210) for other properties.*

*The large increase however, will be in the variable rate, which sees a 32% increase for residential properties, with a 13% increase for commercial and primary production and a 12% increase for industrial properties. Whilst the proportion of the variable charge is significantly less than the fixed charge as a whole of the charge, the overall rise in the FSPL payable by ratepayers per category is as follows:*

| | |
|---|---|
| *Residential* | *9%* |
| *Commercial* | *8%* |
| *Industrial* | *9%* |
| *Primary Production* | *5%* |
| *Public Benefit* | *7%* |
| *Vacant Land (other than residential)* | *7%* |

*The FSPL is collected by Council on behalf of the Victorian Government via the rate collection process – i.e the FSPL actually appears on each ratepayer's rate notice. Council needs to be very vigilant in identifying the different charges to ratepayers so as to make it clear that the increase in the FSPL is not a result of a Council decision.*

## Draft recommendation 3

The Commission recommends that the cap should be applied to the rates and charges paid by the average ratepayer. This is calculated by dividing a council's total revenue required from rates in a given year by the number of rateable properties in that council area at the start of the rate year.

***Colac Otway Response:***
*Colac Otway agrees with the recommendation providing the guidelines are very clear on the way supplementary rates are accounted for. Councils cannot be disadvantaged by the method of calculating the average rates and charges. Supplementary rates should be excluded from the cap. Supplementary rates would become part of the base for the following year.*

### Draft recommendation 4

The Commission recommends that the annual rate cap should be calculated as:

Annual Rate Cap = (0.6 x increase in CPI)
+ (0.4 x increase in WPI)
- (efficiency factor)

With: CPI = DTF's forecast published in December each year

WPI = DTF's forecast published in December each year

The efficiency factor will initially be set at zero in 2016-17 but increasing by 0.05 percentage points each year from 2017-18. The Commission will undertake a detailed productivity analysis of the sector to assess the appropriate long-term rate for the efficiency factor.

***Colac Otway Response:***

*Colac Otway disagrees with the methodology in setting the rate cap. It is recommended that the CPI represents 60% of the proposed Annual Rate Cap. As highlighted by most councils during the previous submission process the CPI does not reflect movements in costs of the delivery of council services and that the wages, construction costs and utility costs have all been typically rising above the CPI.*

*It has been well documented that CPI is not a true measure of the annual increase on Council's operations and it is critical that all other options are explored.*

*One option available is a "Local Government Cost Index" which takes into account the impacts such as Local Enterprise Agreements and Cost Shifting from other levels of Government have on the ability of Councils to keep rate increases at CPI.*

*The ESC is strongly encouraged to consider other options. These could include:*

*(a) In the 2014 Federal Budget, the Commonwealth Government announced that indexation of the national pool of financial assistance grants would be paused for a period of three years.*

*It is recommended that the ESC consider the addition of an additional factor to account for the lost revenue to Local Government as a result of the pause.*
*The information on the amounts lost for each municipality would be readily available through the Victoria Grants Commission and would assist Local Government while the grants are paused.*

*(b) The ESC should consider having a transitional year in 2016-2017. As pointed out in a number of submissions the 2016-2017 financial year will be the first year of a revaluation across Local Government. This will mean that there will be no consistency across properties as to the increase in rates and charges and may result in confusion for ratepayers.*

*It should also be noted that in 2016-2017 Local Government will incur significant costs in undertaking the next Local Government Elections. For Colac Otway the costs could be in the vicinity of $150,000. This equates to an approximate 0.6% increase required in rates and charges.*

*Having a transitional year will also provide further time to refine the most appropriate model and review and amend existing legislation and regulations.*

*Colac Otway also does not agree with the additional burden of an efficiency factor. Rate Capping is itself an efficiency measure. By adding a further factor has the effect of a "double efficiency" factor.*

*Council has limited capacity to raise funds through traditional means i.e. rates. This results in a tension in finding a balance between the financial burden faced by the community and the ability to meet future needs and aspirations. The introduction of rate capping will increase the pressure on our capacity to provide services.*

*An estimate of the effects of rate capping shows that Council will be placed in an unsustainable financial position if it continues to rely on rate revenue to fund its operations to the extent that it currently does. The only options to ameliorate this situation are to:*

- *cut expenditure, and as an inevitable result, reduce service levels; or*
- *increase funding from alternative sources.*

*In Colac Otway rate capping will very likely limit the ability for Council to continue to provide any services other than those required by legislation thus impacting on some of the most disadvantaged members of our community.*

*It is therefore recommended that there be no efficiency factor added on an annual basis commencing from 2017-18.*

### Draft recommendation 5

The Commission recommends that the 2015-16 rates (general rates and municipal charges) levied on an average property should be adopted as the starting base for 2016-17.

***Colac Otway Response:***

*Colac Otway agrees with the recommendation providing the guidelines are clear on the way supplementary rates are accounted for. Supplementary rates should be excluded from the cap. Supplementary rates would become part of the base for the following year.*

## VARIATION

### Draft recommendation 6

The Commission recommends that the framework should not specify individual events that would qualify for a variation. The discretion to apply for a variation should remain with councils.

***Colac Otway Response:***

*Colac Otway agrees with the recommendation.*

### Draft recommendation 7

The Commission recommends that the following five matters be addressed in each application for a variation:

- The reason a variation from the cap is required
- The application takes account of ratepayers' and communities' views
- The variation represents good value-for-money and is an efficient response to the budgeting need
- Service priorities and funding options have been considered
- The proposal is integrated into the council's long-term strategy.

***Colac Otway Response:***
*It is noted that whatever information is required for a variation it will require additional resources which will place additional administrative burdens on Council. It is important that the variation process does not create unnecessary levels of bureaucracy as Council is already financially constrained.*

*Level of Debt:*
*The variation process should not be impacted by the level of debt each council maintains.*

*Each council is different and the level of debt that is appropriate for Colac Otway Shire Council may not be acceptable for another council.*

*The following factors are seen as important issues for consideration by Colac Otway Shire Council:*

- *level of debt servicing as a proportion of rate revenue;*
- *ability to raise revenue in addition to rates;*
- *level of realisable assets to support the indebtedness;*
- *achieving the right mix of capital works and debt commitments;*
- *growth rate of municipality;*
- *community needs; and*
- *demographics*

*Council is responsible and accountable for indebtedness and the cost of debt servicing needs to be controlled to manageable levels.*

*Proposed Timelines:*
*The major issue with variations is the proposed timelines. Council usually commences its budget process in the prior calendar year and then it is an extensive process right through until the budget is adopted by 30 June.*

*The proposed timelines for variations indicate that Councils notify ESC of intention to seek a variation in January 2016. Part of the matters to be addressed is to take account of ratepayer's and communities' views. What will be required to satisfy this point?*

*The proposed timelines also indicate that the ESC will notify councils of decisions on variations in May 2016. This is clearly unsatisfactory as Council will not meet its statutory obligations with respect to a consultation process under the Local Government Act.*

*Councils are required under the Act to give 28 days' public notice of their proposed budgets. Colac Otway requires up to 6 weeks. Therefore Councils commence the preparation of budgets well in advance to enable a draft budget to be advertised in April of each year.*

*A process to consider applications for increases above the recommended rate cap will need to be completed well before Councils complete their Draft budgets. For the 2015/16 Budget Colac Otway considered its draft budget at the 22 April 2015 Council meeting.*

*Any decision to apply for application of rate increases above the rate cap will need to be considered well before this time as the Draft Budget will need to reflect any outcomes of applications.*

*It is recommended that the proposed timelines for variations need to be reviewed in light of the requirements of the Local Government Act and Council policies. It is recommended that the 30 June date for adoption of budgets should remain in the Local Government Act.*

*As previously noted having a transitional year in 2016-2017 will also provide further time to refine the most appropriate model and review and amend existing legislation and regulations.*

Draft recommendation 8

The Commission recommends that in 2016-17, variations for only one year be permitted. Thereafter, councils should be permitted to submit and the Commission approve, variations of the length set out below.

| First year of variation | Length of permissible variation |
|---|---|
| 2016-17 | One year (i.e. 2016-17 only) |
| 2017-18 | Up to two years (i.e. 2017-18 only or 2017-18 and 2018-19) |
| 2018-19 | Up to three years (i.e. up to 30 June 2021) |
| 2019-20 and beyond | Up to four years (i.e. up to 30 June 2023) |

***Colac Otway Response:***

*Colac Otway agrees with the recommendation that variations for only one year be permitted in 2016-2017. It is important that the process with respect to variations is established before multi-year caps are introduced.*

*Colac Otway recommends that once the process is established after the first year, that the length of permissible variation should be 4 years. This will then be consistent with Council's planning processes.*

*Colac Otway agrees that Councils should have the flexibility to be able to apply for temporary and permanent variations from the cap. As noted in the report a temporary variation would enable councils to address costs that arise once and were not expected to recur.*

Draft recommendation 9

The Commission recommends that it should be the decision-maker under the framework, but only be empowered to accept or reject (and not to vary) an application for variation.

***Colac Otway Response:***

*Colac Otway agrees with the recommendation providing it is clear how the ESC will assess applications for any variations.*

*It should be noted that Colac Otway strongly believes that the State Government should fund the operations of the Essential Services Commission with respect to the Rate Capping and variation processes.*

*It is also important that the variation process does not create unnecessary levels of bureaucracy as Council is already financially constrained.*

## MONITORING

Draft recommendation 10

The Commission recommends that it monitor and publish an annual rates report on councils' adherence to the cap and any approved variation conditions.

***Colac Otway Response:***

*Colac Otway agrees with the recommendation.*

*As noted in the Draft Report it is important that only minimal additional reporting obligations are imposed. The information that is required should already be collected by Local Government.*

Draft recommendation 11

The Commission recommends that it monitor and publish an annual monitoring report on the overall outcomes for ratepayers and communities.

***Colac Otway Response:***

*Colac Otway agrees with the recommendation.*

*It is important that there is transparency and accountability through the process.*
*As per recommendation 10 it is important that only minimal additional reporting obligations are imposed. The information that is required should already be collected by Local Government.*

**MATTERS FOR FURTHER CONSIDERATION**

The Commission recommends that the Government consider making a formal review of the rates capping and variation framework a statutory obligation. The review should draw on any data and trends identified through the ongoing monitoring regime and all interested parties should have an opportunity for the sector to provide input to that review. The Commission considers a review period of 4 years to be appropriate.

***Colac Otway Response:***

*Colac Otway agrees that the Government should consider making a formal review of the rates capping and variation framework a statutory obligation, but the review should be undertaken after a 2 year period not 4 years in the first instance.*

*Colac Otway also supports the current inquiry into Rate Capping being undertaken by the Environment and Planning Committee:*

> *"That pursuant to Sessional Order 6 this House requires: the Environment and Planning Committee as part of its oversight of Local Government Victoria, to inquire into and report every six months on the outcome of the State Government policy of local government rate capping on councils' viability, service impacts on local communities and impacts on the provision of local infrastructure."*

The Commission recommends that the Government consider amending the *Local Government Act 1989* to require that service rates and charges must reflect the efficient costs of providing the underlying service.

***Colac Otway Response:***

*Colac Otway agrees that the Government should consider amending the Local Government Act 1989 to require that service rates and charges must reflect the efficient costs of providing the underlying service, but noting the points in recommendation 2 with respect to the increases in the Landfill Levy and contractual obligations.*

The Commission recommends that the Government consider initiating a periodic review to ensure that statutory fees continue to reflect councils' efficient cost of providing statutory services.

***Colac Otway Response:***
*Colac Otway agrees that the Government should consider initiating a periodic review to ensure that statutory fees continue to reflect councils' efficient cost of providing statutory services. The first review should be undertaken as soon as possible as a review of some fees e.g. Statutory Planning Fees is well overdue and needs to be urgently addressed.*

*Many fees that Council collects which contribute to services are set by State agencies. It is critical that the level of fees reflect the real costs of delivering the service and are paid for by the applicant or recipient of the service. At the present time this gap must be recovered from rates and charges.*

*It is also important that once the fee has been set at the correct level that there is a regular escalation to the fees similar to many State Government fees and charges.*

## COLAC OTWAY SHIRE ADDITIONAL INFORMATION

The following information is taken from Colac Otway's initial submission to highlight the key issues that Colac Otway faces if Rate Capping is implemented.

**The Shire at a Glance**

- Area: 3,427 sq kilometres.
- Length of Local Roads: 1,632 kilometres.
- 134 Bridges and Culverts
- Coastline: 95 kilometres.
- Forest and National Park: 110,000 hectares.
- Estimated population: 20,973
- Population born overseas: 7.5%
- Population growth rate: 1.2%
- Employment rate: 97% (full time, 57%)
- Rateable properties: 14,768

**Challenges Facing Council**

The challenges we face can be clustered into two broad areas, these are:

1. **Council specific challenges.**

   These challenges are directly under the control or responsibility of Council and Council will need to decide if the challenge requires a strategic response and resource allocation.

2. **Broad Shire community challenges.**

   These liveability issues are faced by the whole Shire, not just the Council as a Local Government Authority, and therefore require multi-agency collaboration if they are to be addressed.

**Financial Constraints**

Council has limited capacity to raise funds through traditional means i.e. rates. This results in a tension in finding a balance between the financial burden faced by the community and the ability to meet future needs and aspirations. The introduction of rate capping by the State Government, to take effect from July 2016, will increase the pressure on our capacity to provide services.

**Complex Regulatory Environment**

Colac Otway Shire operates in a highly regulated environment, with complex planning and building control systems administered by the State Government.

Given the topography and location of the Shire, properties along the southern extent of the Shire are burdened by an array of zones and overlay controls that apply to ensure that important land use and development issues are addressed.

**Ageing Population**

Colac Otway Shire has a growing ageing population, which presents challenges to future planning for:

- community care services
- arts, culture and open space facilities and events
- infrastructure to ensure accessibility.

An ageing population also has workforce implications, with a potential mass exodus of 'baby boomers' related to retirement and consequent loss of talent and experience.

**Significant Levels of Disadvantage.**

Colac Otway Shire has pockets of high socio-economic disadvantage characterised by lower incomes, education and skill levels, alongside higher levels of unskilled occupations, family and health issues.

The median net income of couple families is comparatively low, the proportion of sole parent families is higher than that for the rest of Victoria and education attainment for parents is lower.

**Transport Network**

There is increasing pressure and growing need to increase public transport services (bus, rail etc), including:

- Connection with Geelong
- Connection within the Shire e.g. Apollo Bay – Colac
- Within the city of Colac

The potential for significant increases in road freight volumes will impact on liveability and tourism values across the shire. Responses to this may need to include:

- Supporting VicRoads to develop an alternate truck route for Colac
- Improved pedestrian and cycling infrastructure.

**Assets – Renewal, Maintenance and New**

The challenge of addressing infrastructure assets is multi-faceted dealing with assets that are at the end of their useful life and the need to construct new infrastructure that meets modern service requirements and future demand as population grows. Other issues include:

- Major drainage issues across the Shire.
- Asset renewal, maintenance and provision of new infrastructure. Assets include roads, footpaths, drainage, bridges, public spaces, buildings and recreation facilities.
- The current standards do not meet community expectations.
- There is an unfunded community infrastructure renewal gap.

**Impacts**

Rate capping will have a significant impact on Council policies and procedures. The implementation of rate capping for Victorian Councils has the potential to fundamentally change the way in which local government approaches service delivery for our communities. Through a significantly reduced revenue stream Council will need to reassess all service level policies and priorities, with an aim to reduce expenditure where possible.

The challenges facing Colac Otway which are noted above are more than likely to increase as a result of the significant pressures on Council's finances and resources.

## CONTEXT/PURPOSE OF RATE CAPPING

An estimate of the effects of rate capping shows that Council will be placed in an unsustainable financial position if it continues to rely on rate revenue to fund its operations to the extent that it currently does. The only options to ameliorate this situation are to:

- cut expenditure, and as an inevitable result, reduce service levels; or
- increase funding from alternative sources.

The impacts would be scalable depending on the rationale applied to rate capping. There is the obvious impact which will be the ability for Council to continue business as usual in line with the currently adopted SRP (being an approximate 6% rate rise per annum). The budget for 2015/16 indicates an increase in rates and charges of 4.9%.

In Colac Otway rate capping will very likely limit the ability for Council to continue to provide any services other than those required by legislation thus impacting on some of the most disadvantaged members of our community.

It should be noted that each of the 79 councils in Victoria are different.

The differences include:
- size
- population
- isolation
- road lengths
- services provided

As well as these obvious differences each council also has established a level of rates and charges over time to provide services to their communities.

Applying a standard percentage rate cap to all councils may not be equitable or sustainable for the assessment of future rates and charges.

**Potential Impacts for Colac Otway**

### Colac Otway's Reliance on Rates and Charges

The following table provides details of the breakdown of Council's Income over the period 2004-05 to 2015-16.

As can be seen by the income figures for the 12 year period Council's reliance on rates and charges (waste) has continued to increase over the period: from 39.4% in 2004-05 to 57% in 2015-16 (budget).

With a reduction in other forms of revenue Council has relied more and more on rate revenue.

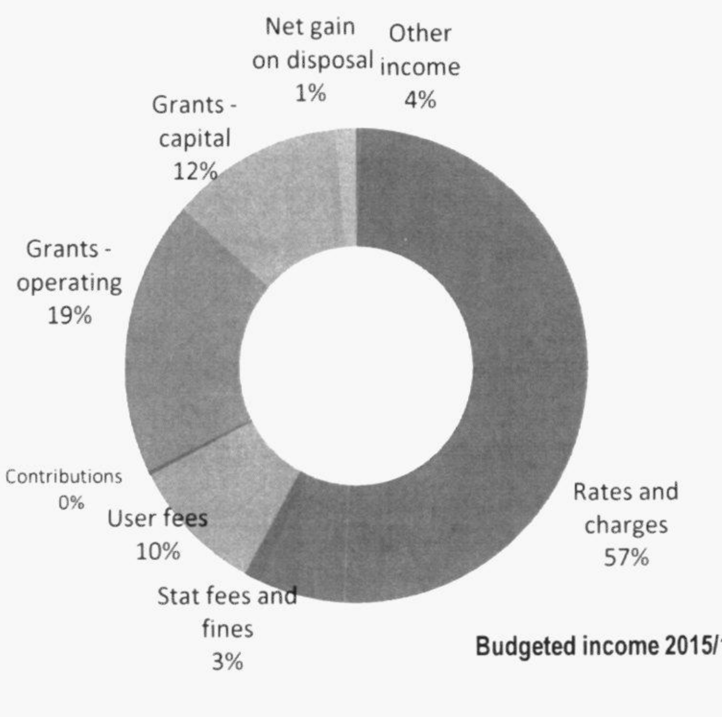
Rate capping will place significant pressures on Council's main source of revenue.

| BREAKDOWN OF INCOME % 2004-05 to 2015-16 | | | | | | |
|---|---|---|---|---|---|---|
| | **Rates & Charges %** | **Grants %** | **Fees & Charges %** | **Reimb. & Contrib. (cash) %** | **Interest %** | **Other %** |
| 2004-2005 | 39.4 | 30.1 | 13.1 | 5.3 | 1.2 | 10.9 |
| 2005-2006 | 42.5 | 37.2 | 11.9 | 3.5 | 1.5 | 3.4 |
| 2006-2007 | 46.4 | 30.3 | 11.5 | 2.4 | 1.5 | 7.9 |
| 2007-2008 | 49.7 | 32.8 | 10.9 | 3.5 | 1.8 | 1.3 |
| 2008-2009 | 46.6 | 34.6 | 10.2 | 1.6 | 1.1 | 5.9 |
| 2009-2010 | 46.8 | 30.9 | 10.8 | 6.3 | 1.2 | 4.0 |
| 2010-2011 | 50.0 | 35.0 | 9.1 | 1.6 | 1.4 | 2.9 |
| 2011-2012 | 50.0 | 36.3 | 9.3 | 1.6 | 1.4 | 1.4 |
| 2012-2013 | 52.4 | 34.2 | 9.8 | 1.4 | 1.1 | 1.1 |
| 2013-2014 | 57.0 | 31.1 | 9.1 | 1.0 | 1.3 | 0.5 |
| 2014-2015* | 49.0 | 39.6 | 7.6 | 1.7 | 0.9 | 1.2 |
| 2015-2016 (budget) | 57.0 | 30.7 | 10.5 | 0.3 | 0.9 | 0.6 |

** The figures for 2014-15 reflect Federal Government Grants in advance and grants for Bluewater.*

The following pie diagram is taken from Council Draft Budget for 2015-16 which highlights in a diagrammatic form council's reliance on rates and charges.

For 2015-16 the estimated percentage of total income from rates and charges is 57%.




**Budgeted income 2015/16**

## STRATEGIC RESOURCE PLAN (SRP) 2014-2015 to 2017-18

A Strategic Resource Plan is a requirement under the Local Government Act 1989 for Council's to prepare and include in their Council Plan.

The Strategic Resource Plan is prepared in conjunction with the Council Plan to reflect the financial and non-financial resources required to achieve the strategic objectives included in the Council Plan.

The purpose of the Strategic Resource Plan is to:

- Establish a framework to manage the resources required to achieve the strategic objectives as expressed in the Council Plan;
- Provide an assessment of the resources required to achieve the strategic objectives of the Council Plan;
- Plan for the long-term financial sustainability of the Council;
- Establish a basis to measure Council's adherence to the principles of the Strategic Resource Plan; and
- Assist the Council to comply with sound financial management principles in accordance with the Act.

In preparing the SRP key questions are considered.

- Is sufficient revenue being generated to provide the services and level of service required by its community?
- Is the condition of existing assets providing an acceptable level of service to the community?
- What level of funding is required to upgrade existing assets or construct new assets?
- When should debt be used to fund capital projects?
- What is an acceptable rate and charge increase?

### Colac Otway's Strategic Resource Plan 2014-15 to 2017-18

The Strategic Resource Plan (SRP) 2014-15 to 2017-18 included rate rises of 5.1% for the four year period. This was to achieve the following objectives:

- Maintain the existing range and level of service provision and develop the capacity to grow and add new services;
- Maintain a strong cash position, ensuring Council remains financially sustainable in the long-term;
- Achieve underlying surpluses from operations;
- Maintain debt levels below prudential guidelines;
- Continue to pursue ongoing grant funding for strategic capital funds from the state and federal government;
- Provide for rate increases that establish a funding level for a sustainability index of 100 percent, including increasing funding for capital works (asset renewal, expansion, upgrade) and asset maintenance; and
- Ensure critical renewal is funded annually over the timeframe of the SRP.

With rate capping the forecast revenue over the 4 year period will decrease significantly.

Some basic modelling with has been prepared showing the current Strategic Resource Plan (SRP) and Long Term Financial Plan (LTFP) model results for rate rises at 5.1% for the first four years (to 30 June 2019) and 6.1% for the remaining six years (to 30 June 2025), and comparing this to an estimate of rate rises at the announced model cap of 3.05% for 2016-17, 2.85% for 2017-18 and 2.80% for 2018-19 and then decreasing with the 0.05% 'efficiency gain' reduction each year thereafter.

The parameters for this were:

- Capping only applies to rates (including municipal charge)
- Capping is applied using the total rate revenue methodology
- Waste Management and Recycling charges indexed at 5.0% per annum
- Financial Assistance Grants frozen
- Other grants indexed at 3.0% per annum
- Only guaranteed secure capital grants included (Roads to Recovery)
- Assumption that all other capital expenditure will be funded internally
- No additional borrowings
- The $1 million bond taken out through the Local Government Funding Vehicle will be rolled over and continued.
- Assumes underlying CPI and WPI stay constant over the period.
- Assumes 'efficiency gain' of 0.05% reduction in rate cap per annum from 2017-18

The analysis shows that Council will lose a significant amount of cash over the 10 year period, moving from a cash balance of approximately $9.6 million at the end of 2015/16 to a negative cash balance by the end of 2024/25.

This clearly puts Council in an unsustainable position. Council estimates that a cash 'floor' level of approximately $4.5 million must be maintained to cover employee entitlement requirements.

The estimated cash and operating position of Council will under each model be as follows:

| | **Current Forecast** | **Projected** |
|---|---|---|
| **Cash position at 30 June 2025** | $5.56 million | - $0.06 million |
| **Operating Result at 30 June 2025** | -$0.002 million | -$0.195 million |

As can be seen by the current forecast column, Council was anticipating that even with 5.1% to 6.1% rate rises; we would incur a significant decline in cash over the next ten years (barring any grant increases). With the move to rate capping this will be greatly exacerbated. This highlights Council's dependency upon rate revenue as a funding source.

Council could experience a $9 million impact to its cash reserves in 2025-26 as a direct result of rate capping. It is important to realise what this means: in 2025-26 Council will be at least $9 million worse off **in that year.** In the previous year Council would be approximately $7.9 million worse off **in that year,** and so on back to the first year of rate capping where Council would be approximately $0.5 million worse off.

In fact the cumulative effect of rate capping over the ten years is that Council could lose up to $35 million in revenue (i.e the additions of each year's losses).

## EXTERNAL IMPACTS ON COUNCIL FUNCTIONS

Council's original submission provided details on a number of Council's functions. The following provides details on key points:

- Federal Government Grants
- State Government Grants
    - Library Services
    - Roads and Bridges
    - Other Services
- Fees and Charges

### Federal Government Grants

Grants from Federal and State Governments have varied over the period 2004-2005 to 2014-2015. This is impacted by projects that have received grants in a particular year.

The federal budget for 2014-15 announced that Financial Assistance Grants to Local Government will be frozen for the next three years.

Colac Otway's loss of revenue amounted to $112,000 in 2014-15. (this equates to approximately 0.5% of rate value).

The reduction in this first year meant a number of planned projects were either reduced or deferred. The flow on effects into future years will be greater as cost increases place greater pressure upon Council's financial resources. This reduction must be considered in light of Council's balancing of service provision with its capacity to raise funds from other sources.

In February 2015, the Victorian Auditor General tabled a Report to Parliament on Local Government: Results of the 2013-14 Audits.

The report notes on page 17:

*"While the re-phasing of financial assistance grants has impacted the current year's results for some local councils, the Commonwealth's decision to pause indexation of financial assistance grants will have a greater impact on small and large shire councils that rely on Commonwealth grant funding to support their operations. These shires will need to monitor, control and constrain expenditure growth if grant revenue is unlikely to increase in the foreseeable future."*

It should be noted that core financial assistance has declined from 1.2 per cent of Commonwealth revenue in 1993-94 to 0.59 per cent in 2013-14. Government grants are usually indexed to CPI or less, meaning that grants are lower than actual cost movements to deliver the service, leaving councils to fund the gap from rates revenue. In a number of services that Council delivers, Government grants are increased by CPI or less each year.

### State Government Grants

The following provides examples of where there is pressure on Council's budget both from the community's expectation as well as less funds from State Government.

**Library Services**
The level of state funding as a proportion of total revenue for 2015/16 is forecast to be at approximately 26%. This is an example of where State Funding has not kept pace with what is required to deliver improved services.

Over a number of years the % has continued to reduce. In 2000/01 the % was 40.7%. In 2005/06 the % was 34.4%.

As indicated above this is now forecast to be 26% in 2015/16. This is a significant reduction and has placed significant pressures on Local Government to continue to fund what is seen as a vital service not only for Local Government but for all Victorians.

This is an example of where State Funding has not kept pace with what is required to deliver improved services.

Any reductions impact on the level of service currently provided even though Library services are seen as a vital service.

"*Today's public library brings people together; it removes isolation; it fosters social inclusion; and it creates strong and connected communities.*
*It plays a pivotal role in lifelong learning, literacy and knowledge creation and, through this, will contribute to the development of self-reliant communities.*"
*Review of Victorian Public Libraries Stage 1 Report – December 2012*

**Roads and Bridges**

Over a four year period 2011/12 to 2014/15 Council's in rural Victoria received a $1m a year for roads and bridges. This enabled Colac Otway to put significant funding into its bridges. It had been identified that many of Council's bridges needed to be replaced or have significant maintenance undertaken.

This funding is now no longer available under the Labour State Government. This will place additional pressure on Council's resources.

**Other Services**

Other significant services where Council subsidises service delivery for the State Government include:

- Maternal and child health
- Home and Community Care including Meals on Wheels
- School Crossings
- Surf Lifesaving Clubs
- State Emergency Services

In each of the services the level of funding has not kept pace with the increasing demands on the service. In some cases the services provided by Council are not a responsibility of Local Government.

It is important to note that these services are delivered in partnership with the State Government with the main beneficiary being the community. With the pressure of rate capping it is inevitable that Councils will need to look at the way it delivers the services. This may mean a reduction in service and/or increased fees and charges.

This may then have a flow on effect on the community and possible negative social outcomes.

**Fees and Charges**

While Rates & Charges has continued to increase steadily over the period, the fees and charges % has gradually decreased from 13.1% in 2004-05 to a forecast % of 8.6% in 2014-15.

These figures highlight further the significant effects that Rate Capping on Council's main income stream.

Council is limited on the options to increase fees and charge, but will need to further review the level of them in light of rate capping and service reviews that will need to be undertaken.

It is also noted that many of the fees applied for planning permit applications and subdivisions are set by State regulations and have not increased for many years.

**Summary**

The impacts of additional costs and reporting being imposed on councils puts upward pressure on local rates.

Council will need to review the current arrangements and in some cases consider either reducing the current level of service or hand the responsibilities back to the State Government.

## ASSET RENEWAL GAP

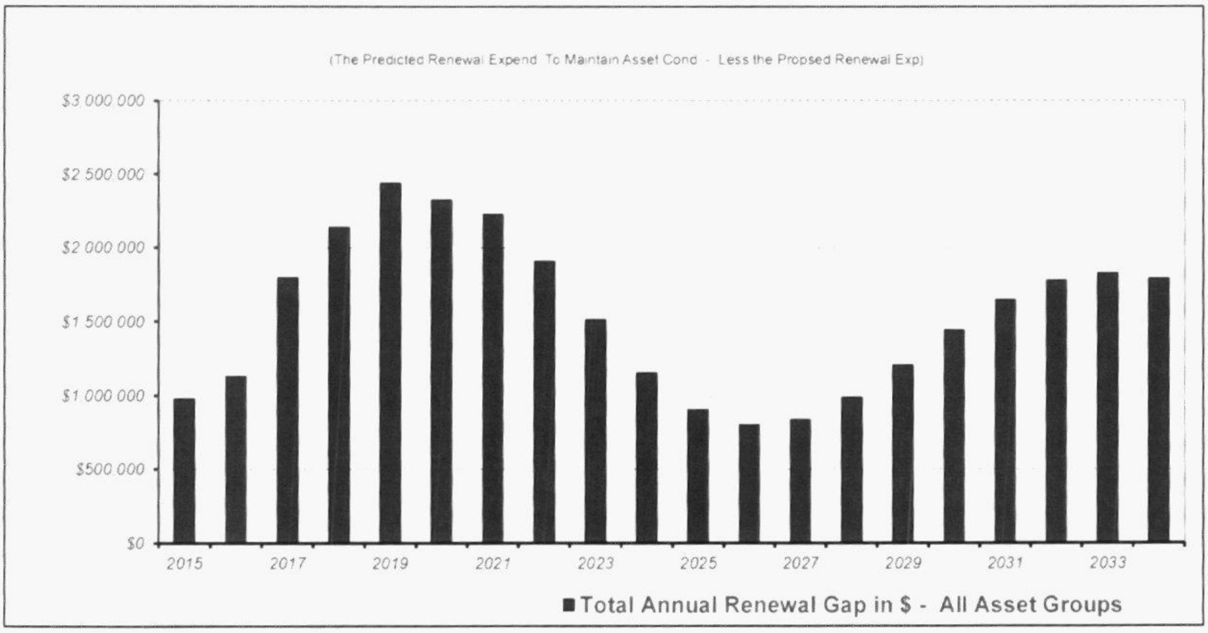
In a report on Asset Management on 19 February 2014 the Auditor General reported to the Parliament:

"*Victorian councils manage around $73 billion of infrastructure assets. Council spending on renewing or replacing existing assets is not keeping pace with their rate of deterioration, resulting in cumulative renewal gaps that grow each year*".

Colac Otway Shire Council recognises the challenge known as the Asset Renewal Gap. The gap exists due to the inability to fund infrastructure asset replacement when asset condition degrades and the associated services are unable to be delivered. In order to address this, Council has had an ongoing commitment to recognising asset renewal expenditure as 'non-discretionary' and providing responsible levels of funding for the renewal of community assets over a number of years.

### *Total Annual Renewal Gap*

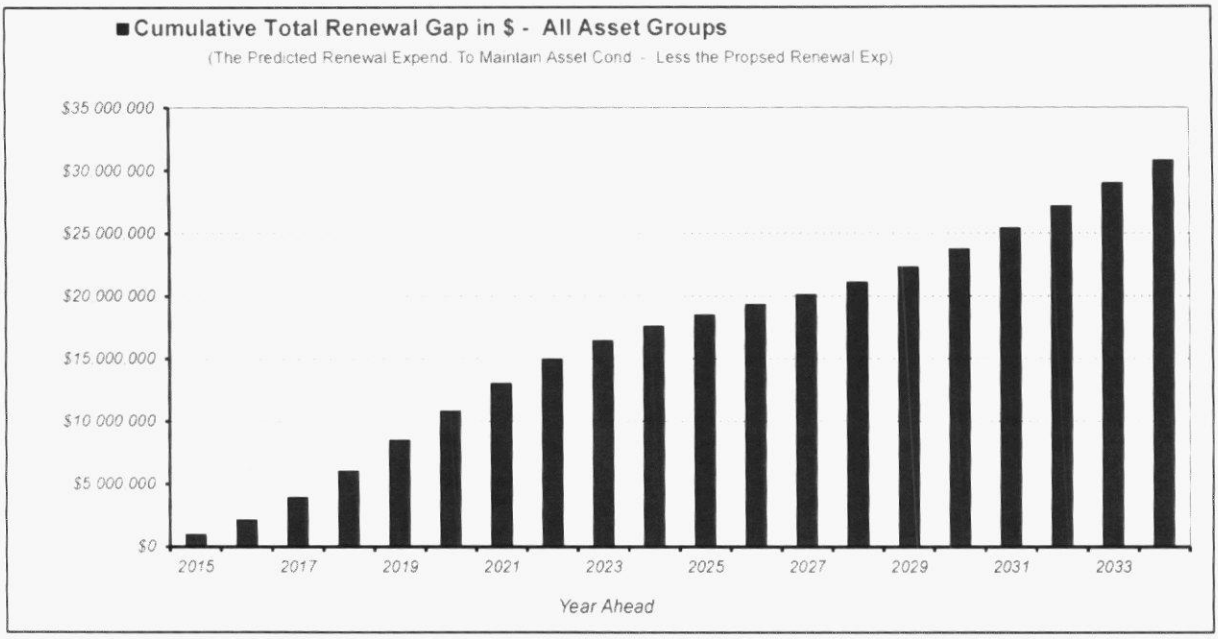
The following graph presents the projections of Council's annual renewal gap over the next twenty (20) years. This is based on the projections of funding dedicated to asset renewal included in Council's Long Term Financial Plan. The majority of Council's renewal funding is drawn from Council's own source funds which are predominantly raised through rates.




The graph indicates that, based on the assumed renewal expenditure profile, Council faces a renewal gap of approximately $980K in 2015/16. The gap then trends upwards to a maximum of approximately $2.44M in 2019/20.

### *Cumulative Total Renewal Gap*

The following graph shows the cumulative impact of Council's annual asset renewal gap. At the end of the twenty (20) year forecast period, the cumulative renewal gap is $30.8M (or approximate average of $1.5M per annum).




The implementation of rate capping will erode Council's ability to adequately fund the maintenance, replacement, and rehabilitation of assets which the community relies on for basic services. This will lead to significant disrepair in assets increasing the risk of catastrophic failure and declining customer satisfaction.

With limitations on Council's ability to raise capital funds from rates revenue and the declining financial support from other levels of government as evidenced by the cessation of the Country Roads & Bridges Program and freezing of Federal Assistance Grants, the community will notice a progressive deterioration in the quality and condition of assets such as roads, bridges, footpaths, and buildings. The only means that Council will have to manage this will be to reduce levels of service and to decommission assets which are deemed to be aligned with discretionary services.

As councils have a limited capacity to raise additional revenue, they often use a range of funding options such as rate rises, lower service levels, asset rationalisation and borrowings.

## VICTORIAN AUDITOR GENERAL

In February 2015 the Victorian Auditor-General provided a report to the State Government "*Local Government: Results of the 2013/2014 Audits*".

On page 27 of the report:

***Background***

*"To be financially sustainable, entities need to be able to meet current and future expenditure as it falls due and to absorb foreseeable changes and risks without significantly changing their revenue and expenditure policies."*

**Financial Sustainability Risk Assessment Results 2013/2014**

The figures in the report indicate that Colac Otway is categorized as low risk in each of the indicators.

It should be noted that in 2006-07 which is less than 10 years ago the Victorian Auditor-General report to the State Government "*Local Government: Results of the 2006-07 Audits*" indicated the following:

> *Within the large shire group, only **Colac Otway** exhibited immediate liquidity concerns.*
>
> ***Colac Otway** has reported mixed results over the past 5 financial years making it difficult to identify a pattern of performance. **Colac Otway** has, on average over 5 years, underspent on asset renewal, as well as reporting an average negative underlying result for the same period.*
>
> ***Colac Otway** has been rated as high risk both because of the combination of its relatively high operating deficits and its underspending on infrastructure renewals over the past 5 years, and because its forecasts for the next 3 years for these items remain negative.*
>
> **RESPONSE provided by the Chief Executive Officer of the Colac Otway Shire Council**
> *Colac Otway Shire has been rated as high risk based on trend data over the past 5 years. However, trend data over the past 2 years and forecasts for the next 3 years clearly indicates that Colac Otway has met and will meet all targets related to the 5 viability measures as a result of strong financial decisions Council has made over the past 3 years.*
>
> *Council's underlying result over the past 5 years has been significantly influenced by one off extraordinary factors such as recognition of landfill rehabilitation costs.*
>
> *Our Strategic Resource Plan indicates that Council will achieve ongoing operational surpluses, achieve asset renewal expenditure targets and continuing reduction in loan liability which ensures the Shire's long term financial viability.*
>
> *Council acknowledges that over the past five years it has operated with a constrained ability to meet the required level of infrastructure spending. With significant growth occurring within urban areas of the Shire, there has been a need to develop new and upgraded community infrastructure whilst trying to maintain existing infrastructure.*

Council has continued to make strong financial decisions. As a result Colac Otway is now categorised as low risk in each of the indicators.

**Large Shire Councils – Financial sustainability risk assessment results 2013-14.**

The following information is taken from Appendix E of the report.

| | |
|---|---|
| *Underlying Result (%)* | |
| ***Colac Otway*** | ***4.41%*** |
| *Category Average* | *3.51%* |
| *Category Risk Assessment* | *Low* |
| *Liquidity* | |
| ***Colac Otway*** | ***1.93*** |
| *Category Average* | *1.76* |
| *Category Risk Assessment* | *Low* |
| *Indebtedness (%)* | |
| ***Colac Otway*** | ***26.49%*** |
| *Category Average* | *27.92%* |
| *Category Risk Assessment* | *Low* |
| *Self-Financing (%)* | |
| ***Colac Otway*** | ***34.25%*** |
| *Category Average* | *20.19%* |
| *Category Risk Assessment* | *Low* |
| *Capital Replacement* | |
| ***Colac Otway*** | ***1.54*** |
| *Category Average* | *1.46* |
| *Category Risk Assessment* | *Medium* |
| *Renewal Gap* | |
| ***Colac Otway*** | ***1.16*** |
| *Category Average* | *1.04* |
| *Category Risk Assessment* | *Low* |

It is important to note again the statement from the Victorian Auditor General.

*"To be financially sustainable, entities need to be able to meet current and future expenditure as it falls due and to absorb foreseeable changes and risks without significantly changing their revenue and expenditure policies."*

The impacts of rate capping particularly on small and large shire councils will have significant impacts on Council's ability to maintain the services and infrastructure that they currently provide.

The improvement in Colac Otway Shire's financial position has come about as a strong commitment by Council over a number of years. It will be critical that the improvements are not diminished as a result of the impacts of rate capping.