NARRANDERA SHIRE COUNCIL
Background Paper: The Special Rate Variation

Introduction

The Narrandera Shire Council ('Council') financial position is unsustainable at the current levels of expenditure and income. This has occurred for a number of reasons discussed in this background paper.

Council have made decisions on assets, services, and rating options in the best interests of their communities. However, this when combined with other external influences and legislative restrictions has gradually led to declining financial sustainability. This is a problem which Council must now address this year.

Council's 2024-2034 Long Term Financial Plan (LTFP) forecasts consolidated operating deficits to 2034. The average operating deficit for the 10-year forecast period is estimated at $2.0 million per annum. Ongoing core costs and externally imposed obligations on local governments are outpacing revenue growth and placing council budgets under increasing pressure. Unless current levels of income are increased, Council will be unable to resource renewal of assets and maintain current services. Narrandera Shire Council is not alone with some 60 NSW councils reported operating deficits in their General Fund in 2021/22

Why does Council need to be sustainable?

The Local Government Act requires councils to apply sound financial management principles and to develop Long Term Financial Plans that maintain financial sustainability into the future. The financial sustainability objectives that support service delivery are:

- Responsible and sustainable spending
- Adequate cash reserves and use of borrowings
- Responsible and sustainable infrastructure investment
- To explore options to improve financial sustainability to achieve a fully funded operating position.

These objectives are the foundation for sound financial management and are not negotiable. If a council fails to meet these principles, then the government may intervene in council operations. We only have to look at the recent government interventions of the Central Coast Council as an example, where there was a shortfall in cash for General Fund operations.

A financially sustainable council has the financial capacity to maintain assets and deliver services to its community over the long term.

Why has Council become unsustainable now?

All councils face financial sustainability challenges on a cyclic basis; this is caused by the constraints and influences on local government. Cost increases have exceeded rate increases and typically Councils reduce spending on key services like asset maintenance and renewals to keep service going and meet new costs.

There are a number of contributors to this growing financial sustainability gap, some of which are outside of Council's control and others which Council has some influence over.

Rate capping is a contributor. The Independent Pricing and Regulatory Tribunal (IPART) has set the rate peg for NSW councils by taking the increase in the Local Government Cost Index (LGCI) and applying productivity gains or allowances for one-off events. The LGCI does not recognise some cost increases councils experience, nor does it provide that some councils will experience cost increases higher than the average due to location or other events. Over time small shortfalls accumulate, and councils generally respond by spending less on asset renewals and maintenance and services until they reach a point approaching failure.

Cost shifting. Cost shifting comes in two main forms, the transfer of responsibilities and increased compliance costs and responsibilities imposed on local government by State Government.

Over the last decade, the NSW State Government, and to a lesser extent, the Australian Government have transferred costs to local government without sufficient recompense. Major types of cost shifting include the withdrawal of financial support once a program is established, the transfer of assets without appropriate funding support, the requirement to provide concessions and rebates without compensation payments, increased regulatory and compliance arrangements and failure to provide for indexation of fees and charges for services prescribed under state legislation or regulation. Key impacts on Narrandera Shire have included:

- ARIC – internal audit program using external/internal resources
- Emergency Service Levy increases
- Crown Land, Plans of Management, Compliance reporting
- Cyber security.

New assets are important for any community, especially when provided through Federal and State Government grant programs and developer contributions. Grants are often discretionary as Council is generally not compelled to apply for or accept grant funding even though it means valuable community infrastructure is funded by government. All new infrastructure generally carries hidden costs. The rate cap does not allow for the new costs associated with the operation, maintenance, renewal and depreciation of new assets, and Council has to fund these additional costs through its existing budget. Over time these costs eat into Council's sustainability as it funds more and more new asset costs from its existing budget.

Service level improvements or high service levels also contribute to the decline of financial sustainability. Over time service levels have increased, and while some service level changes have delivered net benefit, the great majority have imposed additional costs.

In the six years to 2021/22, the average operating performance ratio of NSW councils has steadily declined from 9.8% in 2016/17, to 1.5% in 2021/22. On top of this steady decline, the economic climate has changed post COVID-19. The high level of inflation is impacting the cost of materials and contracts that Council purchases to deliver services. This means that Council can no longer keep expenditure contained within the levels forecast in the LTFP without significant impact on service delivery to the community.

The cost to maintain, repair, replace or improve community assets and infrastructure has dramatically risen, increasing Council's infrastructure backlog. Infrastructure backlog is the term given by council to the total amount or value of renewal works that need to be undertaken to bring council's asset up to an acceptable standard. Council's current backlog ratio is 10.6% with the industry target of 2%. Assets will continue to deteriorate, and the backlog will increase further without additional funding.

Looking forward, the financial sustainability challenge will only increase

The tight labour market means that Council must plan for an increase in wages, particularly to attract and retain staff in rural towns across NSW. Council is reviewing its salary system with the objective to be an attractive employer with reasonable employee benefits.

A high inflation environment, low rate increases, and increased costs for materials and logistics will continue to impact financial sustainability.

Council's Community Strategic Plan and Delivery Program identify several actions to deliver community aspirations that will enhance the liveability of the Narrandera Shire LGA.

Population has steadily declined from 6,115 in 2011 to 5,731 in 2021, with future estimates decreasing to 5,551 by 2031[1]. Council does not have the revenue to provide services nor the associated demands on maintaining assets at the current levels.

Specifically, Council has some operational challenges that need to be address for long term sustainability. These include:

- construction of a stormwater line to address flooding within Narrandera urban area:
- updating the IT system to address operational and cyber security issues.
- decreasing its asset backlog ratio of 10.6%
- having a current industry aligned salary system.

What has Council done to address financial sustainability challenges?

Council undertakes regular reviews to ensure that it is containing costs and implementing efficiency gains, so that it is able to provide value for money to the community. Council has found savings to date of approximately $0.939 million per year in financial benefits plus an estimated $384,000 in additional efficiency and productivity savings. 59 initiatives were implemented, including reduction in workers' compensation claims, an optimisation of the loan cycle by taking loans at lower rates, the installation of LED street lighting and the review of village servicing.

Council also undertook a review of its Asset Management Strategy and plans with the adoption of a current set of Asset Management Plans with an overarching improvement plan – refer to Councils Strategic Asset Management Plans document.

Going forward, Council has identified further 33 improvement initiatives that it will implement in the coming years providing a further annual net benefit of $388 thousand. Council has also absorbed some key service expenditure items such as the Emergency Service Levy subsidy reduction and additional operation costs of the Barellan swimming pool totalling $169 thousand. These improvements have been included in the updated LTFP. There are an additional 6 improvement opportunities identified that need to be further assessed and costed before implementing, which are not included in the updated LTFP.

[1] NSW Department of Planning and Environment. *Planning Portal: NSW Population Projections*. https://www.planningportal.nsw.gov.au/populations

Council has also identified additional costs that it must incur to ensure its ongoing organisational sustainability, these are investing in an updated technology solution to address operational and cyber security issues and an adequate renumeration system to attract and retain staff across the whole organisation over the long term. These additional costs total $1.04 million per year including a one-off cost of $780 thousand for the IT solution, which have been included in the updated LTFP.

Further details on these improvement initiatives and organisational sustainability requirements can be found in the Council's Productivity Improvement Plan report (March 2023).

While these changes will lead to an improvement in sustainability alone, they will not be sufficient for Council to be financially sustainable.

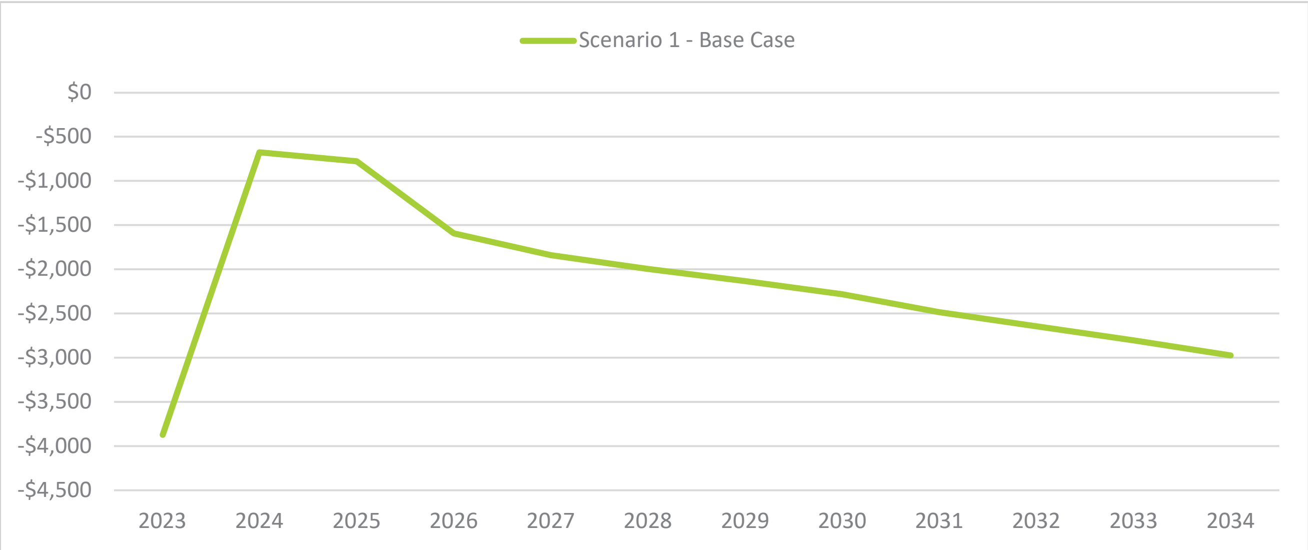
Council's Current Financial Situation

The base case or status quo outlines what would happen if Council did nothing apart from making the savings noted above. Doing nothing else would mean Council would have:

- an average operating deficit for 10-year forecast period is estimated at $2.0 million pa and shown in Figure 1 on the following page
- insufficient money to maintain current service levels and asset renewals
- inadequate funding for infrastructure renewal
- under funding for expected growth and expanded services.

The following graph illustrates ongoing estimated operating deficits culminating in 2033/34 with a $3.0 million annual operating deficit. Over the same period General Fund cash is estimated to decrease by $8 million to $15 million with an average negative unrestricted cash position of $3.6 million from 2025.

Figure 1 Ongoing estimated operating deficits (excluding capital)



It is clear that this situation is not sustainable, and Council would be negligent of its statutory obligations if it were to ignore this.

Proposed Special Rate Variation

Council believes that a special rate variation (SV) is the most viable solution to the Council's financial sustainability challenges, noting that Narrandera Shire Council has ***never*** applied for an SV.

What is a special rate variation?

With rate capping, almost all NSW councils will be faced with having to apply for a special rate variation at some point. Councils go through cycles of SVs, largely for the reasons set out earlier in this paper.

There are two types of SVs:

- a temporary SV for a fixed amount over a fixed period of time
- a permanent SV for a fixed amount over a fixed period that remains in the rate base.

When a temporary SV expires, rates return to the original level at the conclusion of the approval period and are usually approved to fund specific one-off projects like infrastructure renewal or reducing the infrastructure backlog. Narrandera Shire Council's financial challenges are more general, and a temporary SV would not solve the problem.

Permanent SVs can be for a single year or every year for an approved period. Council intends to make application for a permanent SV. Council must apply to IPART for approval to increase rates through an SV.

What SV is proposed for Narrandera Shire Council?

To achieve financial sustainability and maintain fit for purpose infrastructure, Council requires a permanent cumulative rate increase from 1 July 2024, this includes the expected rate peg increases that Council would have otherwise increased rates by.

Having considered a number of options, Council's preferred option is – Option 1 a one-year SV of 38%. Including rate peg it is a 41.5% increase. The following table details the two options that Council considered.

Table 1 Proposed SV increases

SV Options	2024-25	2025-26	Cumulative
Option 1: One-year SV including rate peg	41.5%	2.5%	45.0%
Option 1: One-year SV excluding rate peg	38.0%	0.0%	38.0%
Option2: Two-year SV including rate peg	25.5%	18.0%	48.1%
Option 2: Two-year SV excluding rate peg	22.0%	15.5%	40.9%
Forecasted rate peg	3.50%	2.5%	6.1%

Minimum rate special rate variation

Council has in place a minimum rating structure. To maintain equity Council plans to apply the proposed SV options evenly across the rating structure and will need to make an SV minimum rate application in accordance with the IPART requirements. The current and proposed minimums are detailed in the following table.

Table 2 Proposed minimum rates

Rate Category		Current Minimum Amount	Minimum for 2024/25	Minimum for 2025/26
Residential Ordinary	1 year SV	$510	$720	$740
Residential Ordinary	2 year SV	$510	$640	$755
Business Ordinary	1 year SV	$510	$720	$740
Business Ordinary	2 year SV	$510	$640	$755
Business Narrandera	1 year SV	$570	$810	$825
Business Narrandera	2 year SV	$570	$715	$845
Farmland Ordinary	1 year SV	$510	$720	$740
Farmland Ordinary	2 year SV	$510	$640	$755

IPART determines the annual rate peg that councils receive each year, based on the increase in cost of a selection of goods and services that NSW councils purchase. This calculation looks back over the past year of cost increases and applies the rate peg to the next financial year. The 2024-25 rate peg will be based on cost increases experienced in 2022-23. The rate peg increases for 2024-25 and 2025-26 have been forecasted at 3.5%, and 2.5% respectively. Further details on these assumptions are outlined in Council's updated Long Term Financial Plan. It is noted that IPART is currently reviewing the rate peg methodology.

What do these proposed changes mean for ratepayers?

The impact on an individual's rates will be different depending on the unimproved land value of their property. The following table provides an indication of the annual rates increase likely to be experienced by the average land value for each rating category. The increases include the forecast rate peg.

Table 3 Estimated average rates to 2025/26

Rate Category	Average Rate 2023/24	Average Rate Cumulative 2024/25	Average Rate Cumulative 2025/26
Residential			
No SRV – rate peg only	$743	$769	$788
1 Year SV	$743	$1,051	$1,078
2 Year SV	$743	$932	$1,100
Business			
No SRV – rate peg only	$1,265	$1,309	$1,342
1 Year SV	$1,265	$1,790	$1,835
2 Year SV	$1,265	$1,588	$1,873
Farmland			
No SRV – Rate peg only	$3,957	$4,095	$4,198
1 Year SV	$3,957	$5,599	$5,739
2 Year SV	$3,957	$4,966	$5,860

How do my rates compare to other councils?

The Office of Local Government groups councils with other similar councils for comparison. Narrandera Shire Council is in Group 10 with 22 other councils. This group of councils represents a diverse cross section of geographies and communities across New South Wales. The neighbouring Councils of Leeton and Griffith have also been included for comparative purposes.

Firstly, the below table reflects the average rates by category, paid by residents of similar councils in 2021/22. When you compare rates paid by other like-size councils, Narrandera Shire Council average rates are currently clearly lower than most other councils with the exception of farmland rates.

Table 4 2021/22 Average residential, business and farmland rates compared to other councils.

2021/22 Average Rates: Group 10 councils	Average Residential Rate ($)	Average Business Rate ($)	Average Farmland Rate ($)
Berrigan	771	1,427	2,351
Blayney	1,280	1,134	3,110
Cobar	1,552	1,165	1,683
Dungog	1,272	1,319	3,254
Edward River	1,051	2,089	3,319
Forbes	890	2,823	2,628
Glen Innes Severn	881	1,596	3,189

2021/22 Average Rates: Group 10 councils	Average Residential Rate ($)	Average Business Rate ($)	Average Farmland Rate ($)
Gwydir	769	1,702	5,771
Junee	829	2,106	3,303
Kyogle	1,134	1,422	1,974
Lachlan	570	735	3,449
Liverpool Plains	819	1,433	4,774
Narrandera	**688**	**1,233**	**3,669**
Narromine	778	1,948	4,235
Oberon	959	1,094	2,019
Temora	660	1,481	2,228
Tenterfield	637	1,388	1,629
Upper Lachlan	575	1,450	1,910
Uralla	715	680	4,027
Walgett	398	766	4,840
Warrumbungle	625	1,717	3,186
Wentworth	793	6,237	1,777
Leeton	**1,112**	**976**	**3,714**
Griffith	**1,078**	**2,865**	**3,815**
Average Group 10	**848**	**1,679**	**3,106**
Median Group 10	**785**	**1,430**	**3,187**

The following tables detail the estimated average for the rates to 2024/25 and 2025/26 with the application of Council's preferred one year option. Where known any approved SV or proposed SV have been included for other councils. Narrandera Shire Council's average residential rates has increased slightly higher than the group average, for business rates they remain well below the group average. The average farmland rate remains relative to other councils in terms of its ranking; however, the amount has increased well above the group average.

Table 5 2024/25 Estimated average residential, business and farmland rates compared to other councils

Estimated average rates for 2024/25			
2024/25 Average rates: Group 10 LGA	**Estimated Average Residential ($)**	**Estimated Average Farmland ($)**	**Estimated Average Business ($)**
Berrigan	848	2,587	1,570
Blayney	1,408	3,421	1,247
Cobar	1,708	1,852	1,282
Dungog	1,409	3,604	1,461
Edward River	1,164	3,676	2,314
Forbes	980	2,893	3,108

Estimated average rates for 2024/25			
2024/25 Average rates: Group 10 LGA	**Estimated Average Residential ($)**	**Estimated Average Farmland ($)**	**Estimated Average Business ($)**
Glen Innes Severn	970	3,508	1,756
Gwydir	849	6,374	1,880
Junee	1,040	4,141	2,640
Kyogle	1,248	2,172	1,565
Lachlan	627	3,794	809
Liverpool Plains	1,028	5,993	1,799
Narrandera	**1,051**	**5,599**	**1,790**
Narromine	855	4,659	2,143
Oberon	1,055	2,221	1,204
Temora	727	2,451	1,629
Tenterfield	973	2,487	2,120
Upper Lachlan	633	2,101	1,595
Uralla	786	4,431	748
Walgett	438	5,325	843
Warrumbungle	687	3,505	1,889
Wentworth	873	1,955	6,862
Leeton	**1,223**	**4,086**	**1,074**
Griffith	**1,260**	**4,461**	**3,350**
Average Group 10	**971**	**3,580**	**1,921**
Median Group 10	**971**	**3,506**	**1,693**

Table 6 2025/26 Estimated average residential, business and farmland rates compared to other councils.

2025/26 average rates: Group 10 Councils	Estimated Average Residential Rate ($)	Estimated Average Farmland Rate ($)	Estimated Average Business Rate ($)
Berrigan	869	2,652	1,609
Blayney	1,443	3,507	1,278
Cobar	1,750	1,898	1,314
Dungog	1,445	3,694	1,497
Edward River	1,193	3,768	2,372
Forbes	1,004	2,966	3,186
Glen Innes Severn	994	3,596	1,800
Gwydir	870	6,533	1,927
Junee	1,170	4,659	2,970

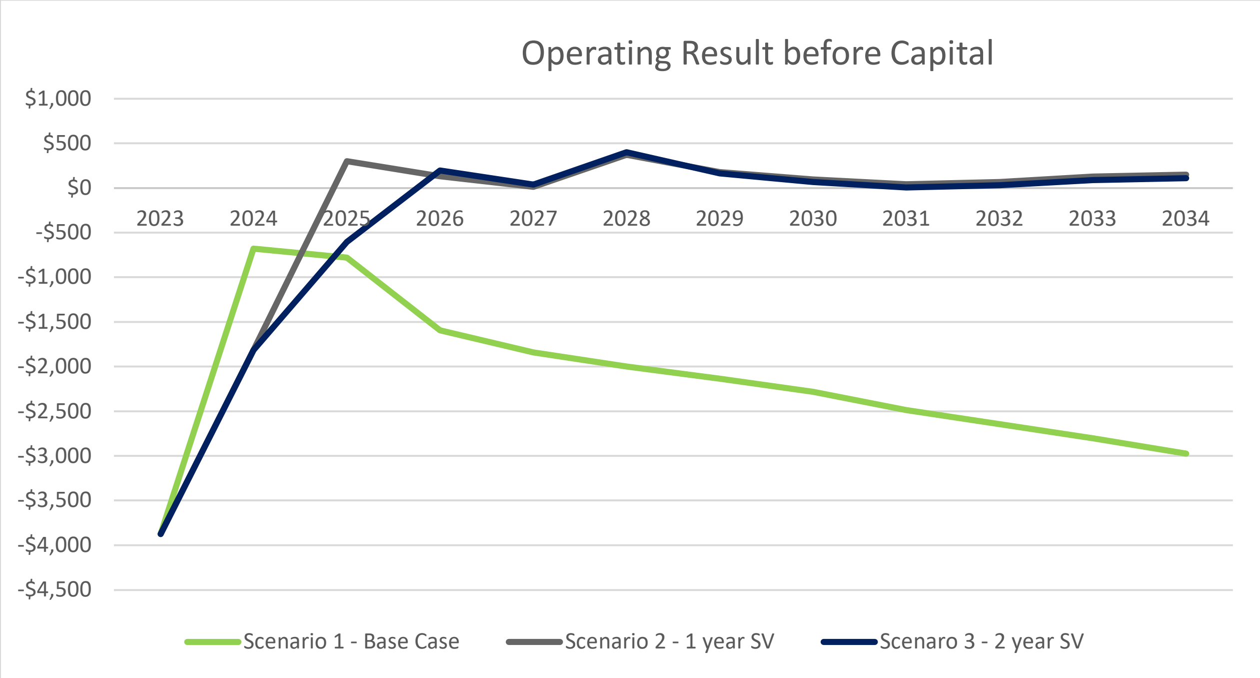
2025/26 average rates: Group 10 Councils	Estimated Average Residential Rate ($)	Estimated Average Farmland Rate ($)	Estimated Average Business Rate ($)
Kyogle	1,279	2,226	1,604
Lachlan	642	3,889	829
Liverpool Plains	1,054	6,142	1,844
Narrandera	**1,078**	**5,739**	**1,835**
Narromine	877	4,776	2,196
Oberon	1,081	2,276	1,234
Temora	745	2,512	1,670
Tenterfield	997	2,550	2,173
Upper Lachlan	648	2,154	1,635
Uralla	806	4,541	766
Walgett	449	5,458	864
Warrumbungle	705	3,593	1,936
Wentworth	895	2,004	7,033
Leeton	**1,254**	**4,188**	**1,101**
Griffith	**1,386**	**4,907**	**3,685**
Average Group 10	**1,000**	**3,688**	**1,981**
Median Group 10	**995**	**3,594**	**1,735**

For more information on ratepayer impact and capacity to pay, refer to Capacity to Pay report. The report finds there is a level of capacity to pay across the Narrandera Shire Council area.

How does this improve Council's financial sustainability?

A combination of the improvement savings and proposed special rate variation will enable Council to deliver current services and improve assets to the community, while becoming financially sustainable over the longer term. The proposed special rate variation arrests the ongoing deficits seen in the base case and allows Council to maintain surpluses, that is revenues will fully cover expected operating expenditure.

Figure 2 General Fund forecast operating result



With a forecast modest surplus, council is able to borrow to invest in its asset upgrade and renewal and start to address the backlog of infrastructure that is below a satisfactory condition. Over the ten-year forecast, Council would be able to sustain an asset renewal rate averaging 100%, equivalent to the benchmark. As a result, Council would be able to reduce its backlog (cost to bring asset to a satisfactory level) from approximately 10.6% of its total asset value to 9.1% over the ten-year forecast period.

Figure 3 Forecast asset renewal ratio

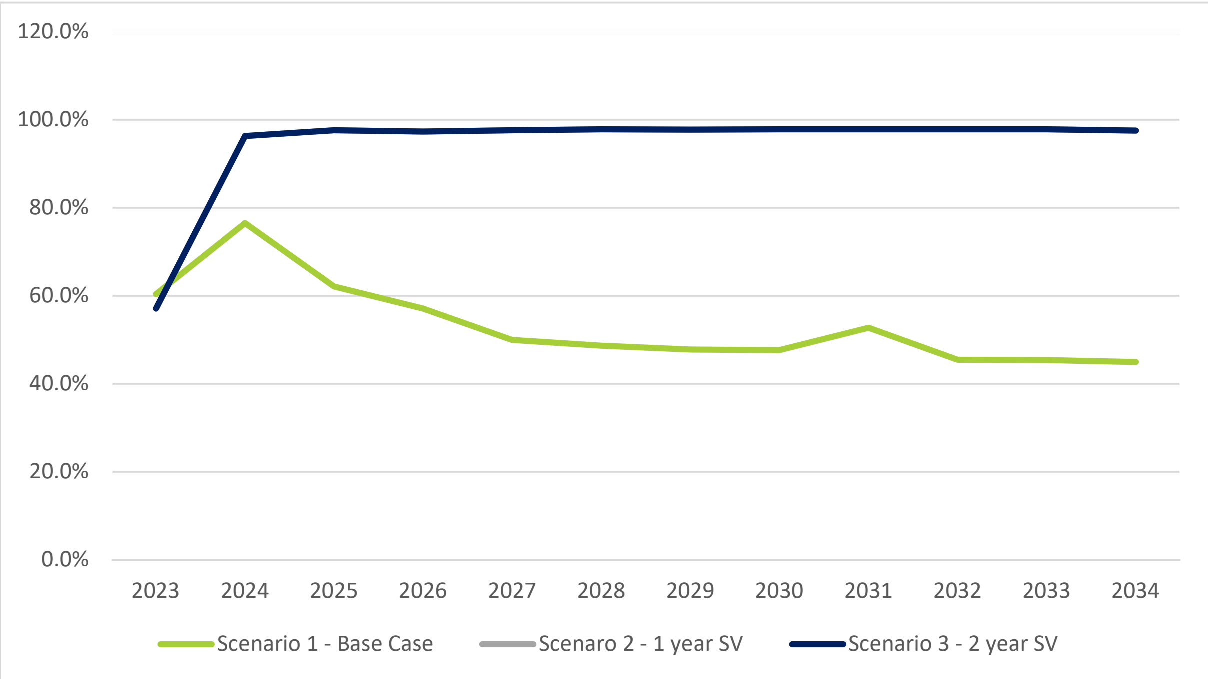
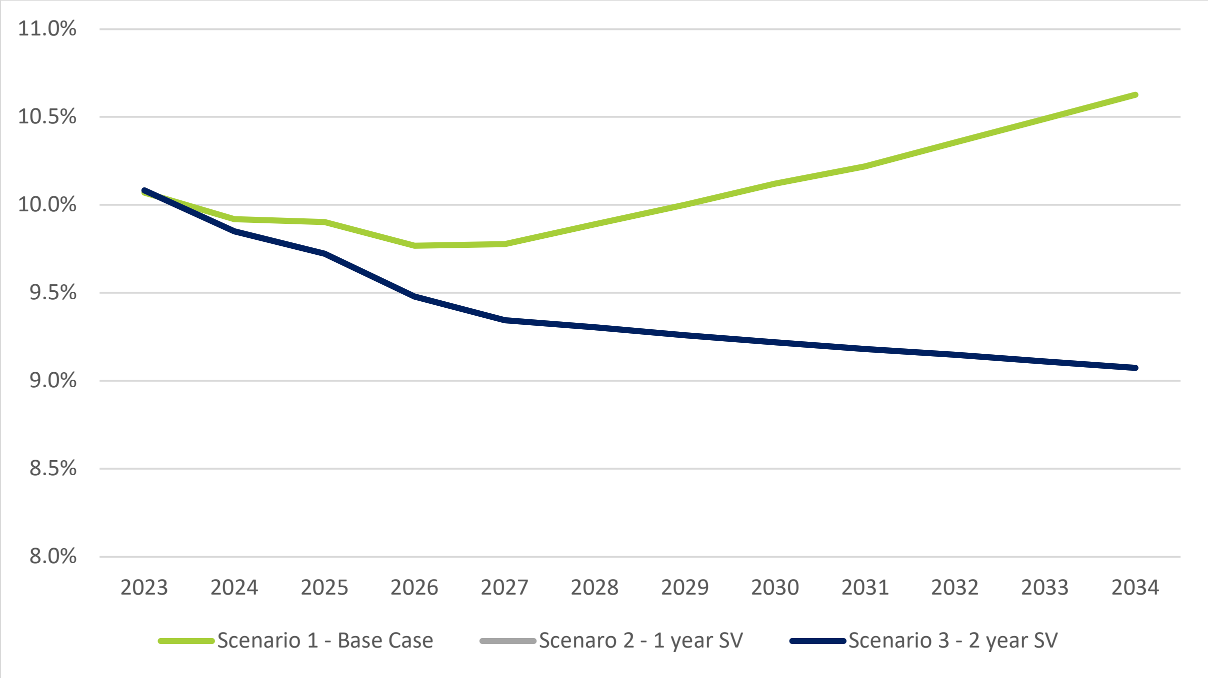
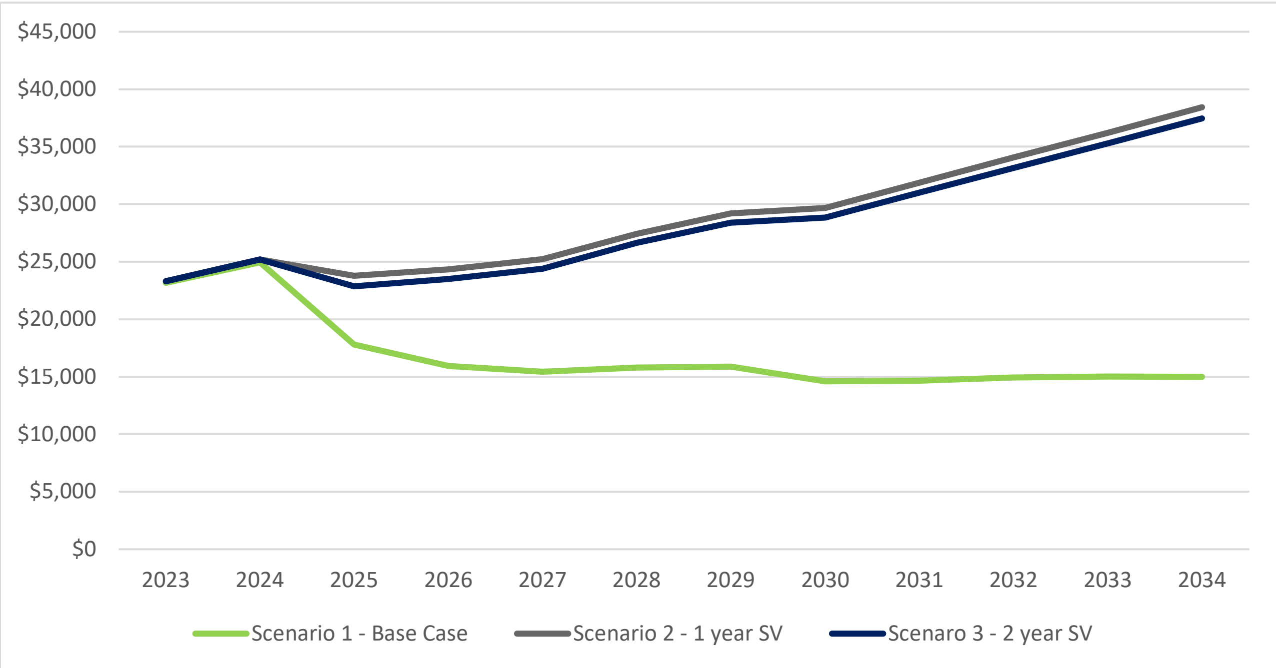


Figure 4 Forecast backlog ratio



In addition to addressing the operating deficits the additional income will resolve the cash position and based on the receipt of a modest flow of grant funds ($2.0m) for community asset renewal the unrestricted cash position should increase from a negative $2.6 million annual average to $6.0 million annual average. General funds overall estimated cash position is detailed in the following chart.

Figure 5 General Fund forecast total cash position



All Councils need to hold sufficient unrestricted cash balance to at least cover the next four months of day-to-day operating expenditure, at which point Council starts to collect the majority of its rates revenue for that quarter.

Sound financial management encourages planning for modest operating surpluses and building of unrestricted cash reserves over time. This enables councils to respond to events that cannot be predicted or planned for in their Long-Term Financial Plan. Narrandera Shire Council has experienced these events and, while what exactly will occur in the future is unpredictable, it is prudent that it plans for similar unplanned expenditure in the future. This exact situation occurred in Narrandera with the 2022 emergencies where significant expenditure was required by Council to fund emergency response – expenditure yet to be reimbursed. The above forecast unrestricted cash position does not take into account any movements in internal restrictions. As Council builds its cash balances over time, it will be able to transfer unrestricted cash for specific purposes to internal restrictions, including Employee Leave Provisions, which will reduce its reported unrestricted cash.

Council has updated its Long-Term Financial Plan to show the impacts of both the base case (no SV) and the proposed SV case scenario. This will be out for exhibition during the SV consultation period.

What would happen if Council does not increase its rates by the proposed amounts?

Council's current base case is not financially sustainable, as it involves significant General Fund deficits of an average of approximately $2.0 million over the ten-year forecast. On its current path, Council would likely run out of unrestricted cash to fund its day-to-day operations in 2024-25.

If Council could not increase its rates revenue through an SV, it would need to cut its operating costs by around $2.0 million per year and continue not to adequately fund its asset renewal. Council would be faced with the decision to stop or significantly reduce discretionary services such as cultural or recreational services and facilities. Council's infrastructure would also continue to deteriorate without sufficient funds to maintain them fit for purpose.

What is the process for Council to apply for an SV?

Council must apply to IPART for approval to increase rates through an SV. Before doing so, Council must demonstrate that it has engaged the community about the possibility of an SV and has considered its views. IPART will also seek community feedback.

More information on SVs can be found on IPART's website:
https://www.ipart.nsw.gov.au/Home/Industries/Local-Government/Special-Variations

Where can I get more information?

More information on the proposed SV is available from Council's Have Your Say page at
https://www.narrandera.nsw.gov.au/council/contact-us/have-your-say

Council will also be including information on the proposed SV in its regular newsletters and to the media. We will also be running public forums for community to find out more and to ask questions. Dates and locations will be advised shortly.

Council will seek feedback from the community on the SV and its updated Long Term Financial Plan. The community is encouraged to provide feedback to Council.

What happens after this?

Once the community consultation period concludes, Council will review the feedback received.

A report will then go to Council for their consideration of the feedback and any updates required to the LTFP. Council will decide whether to proceed with the SV application.

If they decide to proceed with the SV application, the application will be submitted to IPART in February 2024. IPART will conduct its own consultation, with public submissions likely to be sought in March 2024, before they make their determination in May 2024. If successful, the SV will be included in rates from 1 July 2024.