Hornby Shire Council
The Special Rate Variation

Introduction

Morrison Low Consultants has been engaged by Hornsby Shire Council ('Council') to clarify the need for and develop a special rate variation (SRV) application.

The Local Government Act requires councils to apply sound financial management principles of being responsible and sustainable in aligning income, expenses and infrastructure investment, with effective financial and asset performance management. The objectives are to:

- achieve a fully funded operating position
- maintain sufficient cash reserves
- maintain its asset base 'fit for purpose'
- have an appropriately funded capital program.

These objectives are the foundation for sound financial management and a financially sustainable council that has the financial capacity to deliver the services to its community over the long term.

Current situation

In 2016, Hornsby Shire Council lost $10 million in yearly revenue from the NSW Government's boundary adjustment which saw the area south of the M2 motorway transferred to the City of Parramatta Council. As the area transferred to Parramatta had a relatively dense population in comparison with the wider Local Government Area (LGA), there was a significant transfer of rateable properties, and annual rates revenue, with disproportionately less to transfer in terms of infrastructure, and therefore costs. As a result, Council was left in a less financially sustainable position. To manage the impacts of this, Council implemented financial management practices to contain costs over the last six years and maintain financial sustainability.

The economic impacts stemming from the COVID-19 pandemic have meant that Council can no longer sustain these practices and continue to deliver the current levels of services to the community. Effectively, Council has frozen budgets and maintained costs at 2016 levels to ensure that Council remains sustainable. In the low inflation environment that it experienced up to 2021, Council was able to continue to deliver services at the same level by finding the productivity and efficiency improvements required to keep costs down.

Implemented cost controls

Over the last 10 years, Council has implemented several cost containment strategies which has resulted in Council delivering an average of $6.2 million in annual ongoing costs savings and revenue improvements, with a further $3.2 million in one-off costs savings and revenue improvements. Since 2012, this has delivered a total of $52.5 million in benefits that were reinvested in service delivery and infrastructure. Over the course of the 10-year financial plan, this will continue to deliver $67.5 million that will be utilised to deliver services and maintain infrastructure.

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These savings are a result of:

- Savings found and implemented from a review of internal services in 2012.
- Savings found and implemented from a review of external services in 2013.
- Vigilant budgetary management through the quarterly review process, identifying and ring-fencing savings throughout the financial year.
- Utilising savings achieved to reduce the need for debt to fund the Hornsby Aquatic and Leisure Centre in redevelopment from 2013, resulting in an annual average interest savings of $513 thousand over the 20-year life of the loan.

In addition to these savings, Council implemented a general freeze on any increase to non-labour operational expenditure unless grants and/or fees and charges could support an increase in 2014-15 and again in 2017-18. In 2014-15, this resulted in costs being contained to a 1.1 per cent increase.

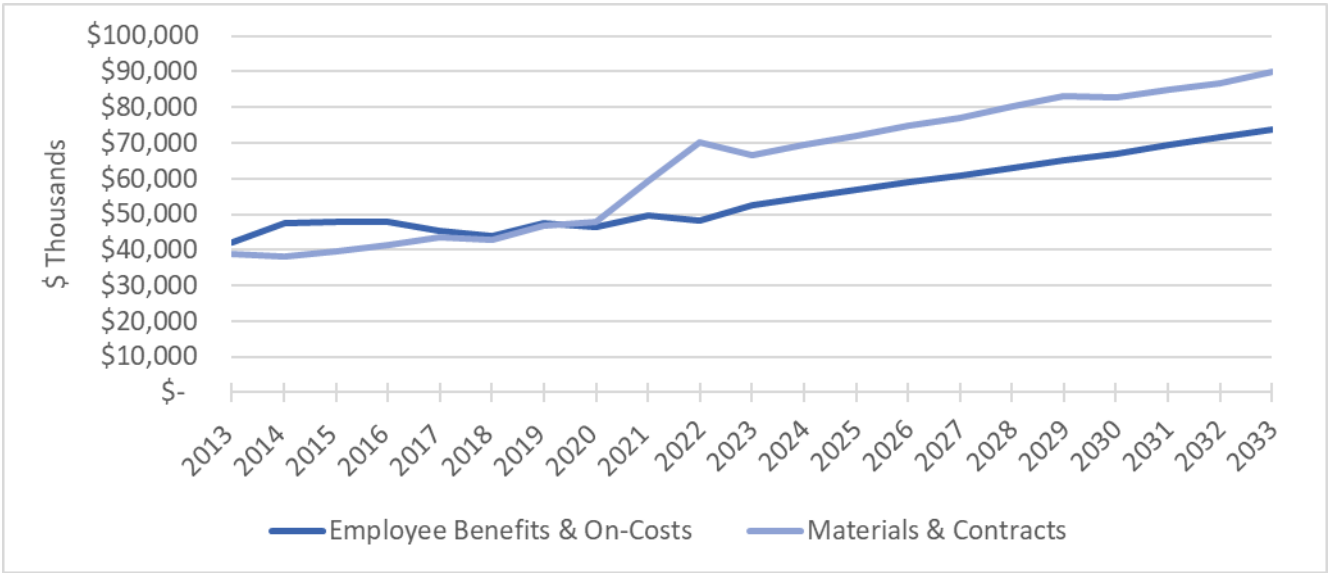
Impact of the current economic conditions

The current high levels of inflation impacting the costs of the material and contracts that Council purchases to deliver services means that it can no longer keep expenditure contained at current levels and needs to forecast increases in line with inflation in its Long-Term Financial Plan (LTFP).

Similarly, a tightening labour market because of less inbound migration since the COVID-19 pandemic means that Council needs to plan for increases to wages to be able to attract and retain the talent it needs to deliver services to the community. Additionally, Council must plan to pay the expected increases in the Compulsory Superannuation Guarantee to staff, which is increasing by 0.5% each year from 9.5% in 2020-21 to 12% in 2025-26. The Superannuation Guarantee increases from 2021-22 to 2025-26 will result in an additional $1.2 million in annual employee costs.

The graph below shows that Council's materials and contract expenditure and employee costs have been kept stable in recent years and are forecasted to grow in line with price and wage inflation estimates in the future.

Figure 1 Employee and materials costs (2013 actuals to 2033 forecasted)



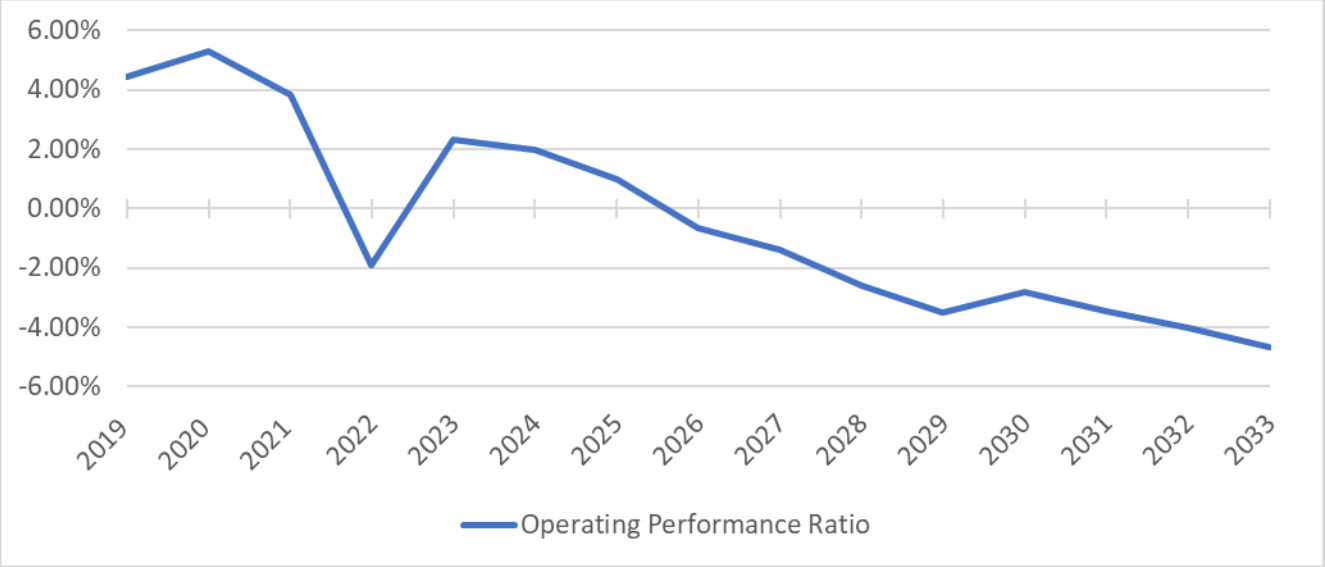
Increasing cost of asset operations and maintenance

In 2018, the NSW Government provided Council with $90 million in capital grants towards the redevelopment of Hornsby Quarry and Westleigh Park as part compensation for the impact of the boundary adjustment. These are new assets that have started to come online. While the NSW Government has funded their development, Council will need to fund their ongoing operations and maintenance and ensure that it has sufficient funds to renew the assets as they age. Over the course of the next 10 years, Hornsby Park is expected to cost $684 thousand yearly to maintain and operate. This could increase further to $1.5 million a year from 2027-28, if the proposed further redevelopment of the site is funded.

Growing core deficits in Council's General Fund are forecasted to develop over time, as a result of growing costs outpacing revenue growth and additional compliance and governance costs, including the internal audit program Audit Risk and Improvement Committee (ARIC), Emergency Service Levy, election costs and cyber security/modernisation of systems/fraud prevention.

As a result of these cost pressures, Council is projecting increasing operating deficits in its LTFP for its base case scenario.

Figure 2 Operating performance ratio (2019 actuals to 2033 forecasted)



Future population growth

The Draft Hornsby Town Centre Masterplan projects population growth with the development of 4,500 new dwellings by 2036. These dwellings will come online towards the end of the 10-year LTFP period and beyond but will see increases in rating income to Council that will support its ongoing financial sustainability.

Until this growth occurs, continued General Fund deficits restrict Council's ability to respond to community expectations for continuation of current services and maintaining asset conditions. In its 2022-26 Delivery Program and 2022-33 Long-Term Financial Plan, Council identified these issues and flagged the need to consider a SRV to address it. It committed to consulting with the community on any potential SRV before making a final decision to apply.

Currently unfunded strategic initiatives

Council has 36 strategic documents with numerous actions identified to deliver community aspirations. Many of these actions are currently unfunded. Council undertook a review of these to identify the 14 costed priority initiatives that address the top ten community issues based on the feedback received through:

- Council's Quality of Life and Asset Management Survey in March 2020.
- The Community Satisfaction Survey in April 2021.
- The Community Strategic Plan survey in September and October 2021.
- Consultation on the development of strategies throughout 2020 to 2022.

These 14 priority initiatives deliver a cross-section of outcomes from 17 strategic documents, sitting across all four themes of the Community Strategic Plan, including:

- Liveable:
    - Local Strategic Planning Statement 2020
    - Local Housing Strategy 2020
    - Social Inclusion Hornsby – Disability Inclusion Action Plan 2021-2025
    - Active Living Hornsby 2016
    - Sportsground Strategy 2018
    - Play Plan 2021
    - Unstructured Recreation Strategy 2008
- Sustainable:
    - Sustainable Hornsby 2040 (2021)
    - Biodiversity Conservation Strategy 2021
    - Climate Wise Hornsby Plan 2021
    - Hornsby Kuring-gai District Bush Fire Risk Management Plan 2016-2021
- Productive:
    - Walking and Cycling Strategy 2021
- Collaborate:
    - Community Strategic Plan – Your Vision Your Future 2032
    - Delivery Program 2022 - 2026

The 14 strategic initiatives require $67.3 million over ten years to deliver, $18.4 million of this is operating expenditure and $48.9 million is capital expenditure. A summary of the programs of initiatives and their associated costs is provided in Table 1 below, the detailed expenditure against each initiative is provided in **Appendix A**. These initiatives respond to Council's highest priority actions. There remains a number of unfunded actions across the 36 strategic and technical documents. It is Council's intention to seek other funding sources that will include grants, partnerships and where appropriate spare operational capacity identified in the organisation to deliver on these actions.

Table 1 Program of strategic initiatives

Program	Proposed total expenditure
Sustainable and resilient community	$6,035,096
Planning for our future	$1,000,000
Upgrading community infrastructure	$30,807,000
Connected walking and cycling paths	$17,982,370
Protecting bushland and Improving open space	$10,283,419
Improving our technology	$1,150,000
Total	**$67,257,886**

The proposed special rate variation

What is a special rate variation?

New South Wales has a rate capping regime in place. Each year, the Independent Pricing and Regulatory Tribunal (IPART) sets a "rate peg", which is the maximum percentage increase in total rates that all are allowed to implement. If a council needs to increase rates by more than the rate peg, it must apply to IPART for a Special Rate Variation (SRV).

Almost all NSW councils will be faced with having to apply for a special rate variation at some point. There are two types of SRVs:

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

When a temporary SRV expires, rates return to the original level at the conclusion of the approval period. Temporary SRVs are usually approved to fund specific one-off projects, such as significant infrastructure projects. As Hornsby Shire Council is looking to deliver current service levels, uplift the ongoing renewal of assets and address the core deficit in the General Fund, a permanent SRV is required. Permanent SRVs can be implemented over up to seven years.

What SRV is proposed for Hornsby Shire Council?

To achieve financial sustainability and to be able to deliver the identified strategic initiatives, Council requires a permanent cumulative rate increase of 31.05% over four years, this includes the expected rate peg increases that Council would have otherwise increased rates by.

Table 2 Proposed rate increases

	2023-24	2024-25	2025-26	2026-27	Cumulative
Permanent increase above the rate peg	4.60%	4.00%	3.50%	3.00%	
Forecasted rate peg	3.90%	3.50%	3.00%	2.50%	
Total increase	**8.50%**	**7.50%**	**6.50%**	**5.50%**	**31.05%**

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 2023-24 rate peg was based on cost increases associated with the revised rate peg for 2022-23. The rate peg increases for 2023-24 to 2026-27 have been forecasted at 3.9%, 3.5%, 3.0% and 2.5% respectively. Further details on these assumptions are outlined in Council's updated Long Term Financial Plan.

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. From 1 July 2023, changes as a result of the general revaluation undertaken by the Valuer General will also come into effect.

The following tables provides an indication of the annual rates and weekly increase likely to be experienced by the average land value for each rating category. The increases include the forecast rate peg.

Table 3 Average annual rates

Rating category	2022-23	2023-24	2024-25	2025-26	2026/27	Cumulative increase
Residential	$1,272.79	$1,380.98	$1,484.55	$1,581.05	$1,668.01	$395.21
Business	$2,437.00	$2,644.15	$2,842.46	$3,027.22	$3,193.71	$756.71
Farmland	$2,133.64	$2,315.00	$2,488.63	$2,650.39	$2,796.16	$622.52
Westfield	$268,650.80	$291,486.12	$313,347.58	$333,715.17	$352,069.50	$83,418.70
Hornsby CBD	$5,149.14	$5,586.82	$6,005.83	$6,396.21	$6,748.00	$1,598.86

The average residential rate will increase by $7.58 per week at the end of the four years, business and farmland rates increase by $14.51 and $12.71 respectively.

Table 4 Weekly increases in average rates

Rating category	2023-24	2024-25	2025-26	2026/27	Cumulative increase
Residential	$2.07	$1.99	$1.85	$1.67	$7.58
Business	$3.97	$3.80	$3.54	$3.19	$14.51
Farmland	$3.48	$3.33	$3.10	$2.80	$12.71
Westfield	$437.94	$419.26	$390.61	$352.00	$1,599.81
Hornsby CBD	$8.39	$8.04	$7.49	$6.75	$30.66

How do my rates compare to other councils?

The Office of Local Government groups councils with other similar councils for comparison. Hornsby Shire Council is in Group 7 with other metropolitan fringe councils such as Blue Mountains, Camden, Campbelltown, Central Coast, Hills and Penrith councils. In comparison to these councils, Hornsby Shire Council's rates are relatively competitive. Even after the proposed Special Rate Variation, Council's average residential rates remain within the comparator councils, and its business and farmland average rates remain significantly lower than comparator councils, as the figures below demonstrate.

Figure 3 2026-27 projected average residential rates

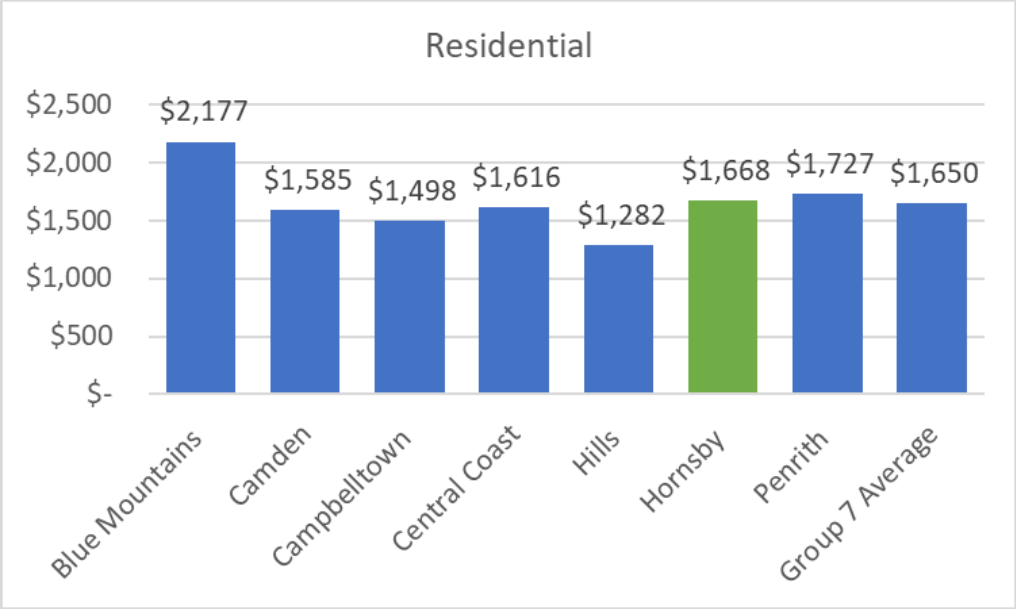


Figure 4 2026-27 projected average business rates

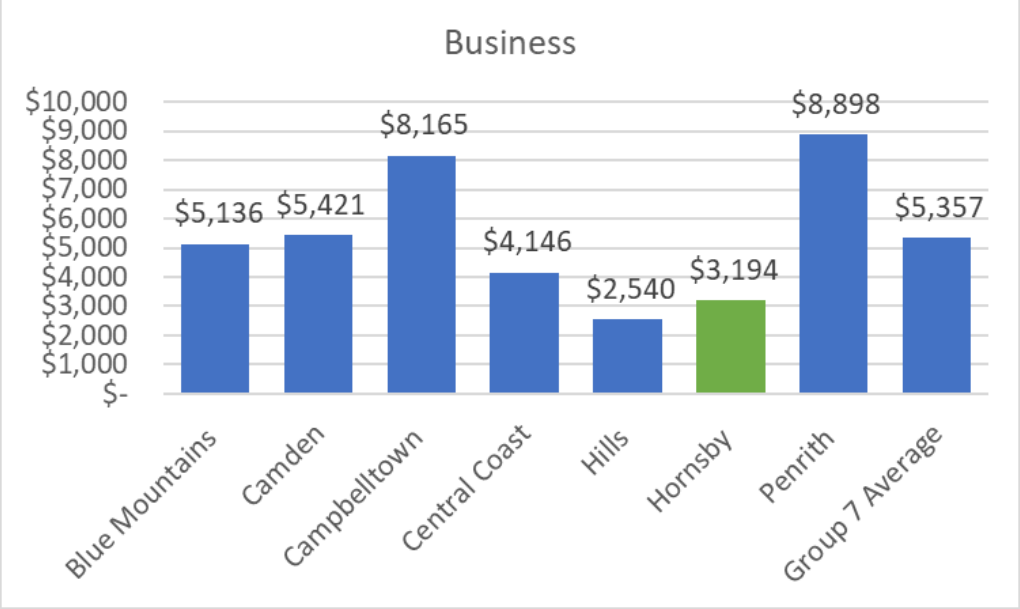
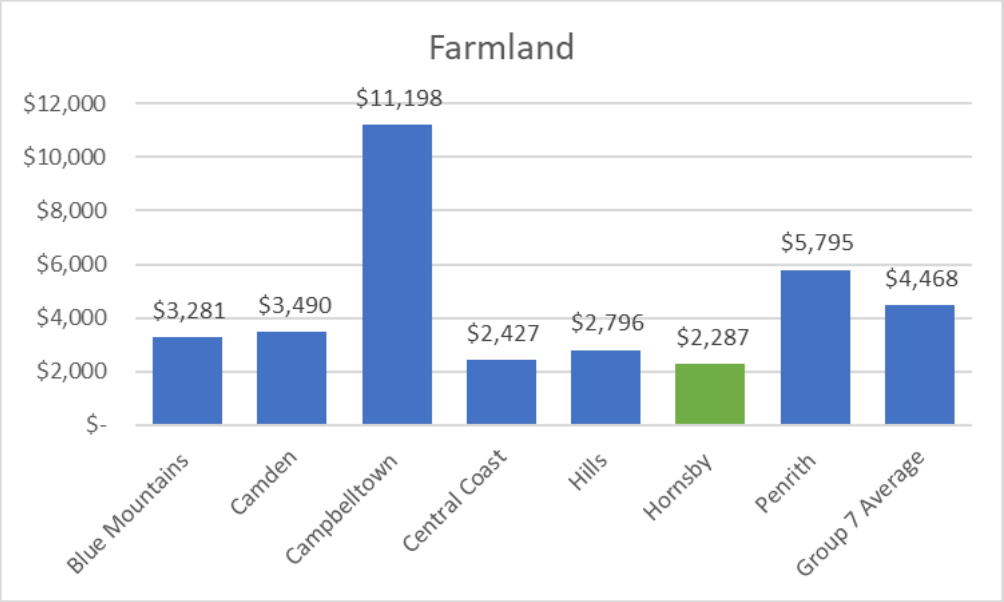


Figure 5 2026-27 projected average farmland rates



The comparison data from other councils is projected from current reported average rates using Hornsby Council's forecast rate peg. It does not include any increases that may occur in 2023-24 and subsequent years from these councils applying for their own special rate variation.

How will the increase impact Council's ongoing financial sustainability?

The proposed special rate variation will enable Council to deliver current services and maintain assets to the community, while ensuring financial sustainability in the longer-term. It will also enable Council to deliver key the strategic initiatives identified, while ensuring Council is more resilient and responsive to shocks and unexpected events in the future.

A financial sustainable council will meet the following objectives:

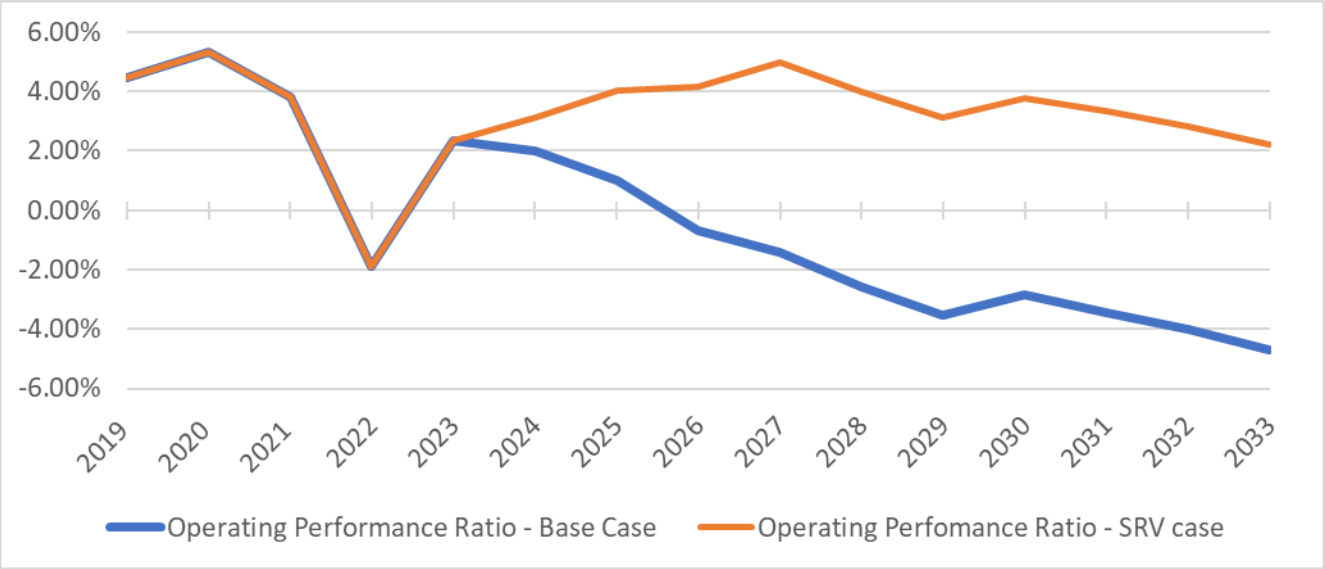
- to achieve a fully funded operating position
- to maintain sufficient cash reserves
- to have an appropriately funded capital program to maintain its asset base 'fit for purpose'.

Council has forecasted its financial performance over the next 10 years, both under the proposed Special Rate Variation and under a base case where rates are only increases by the forecast rate peg. The proposed SRV enables Council to meet all financial sustainability objectives, while the base case plans to maintain a fit for purpose asset base but does not enable a fully funded operating position, depleting Council's unrestricted cash position as a result.

Operating position

The proposed special rate variation arrests the increasing deficits seen in the base case and allows Council to maintain small surpluses, that is revenues will fully cover expected operating expenditure.

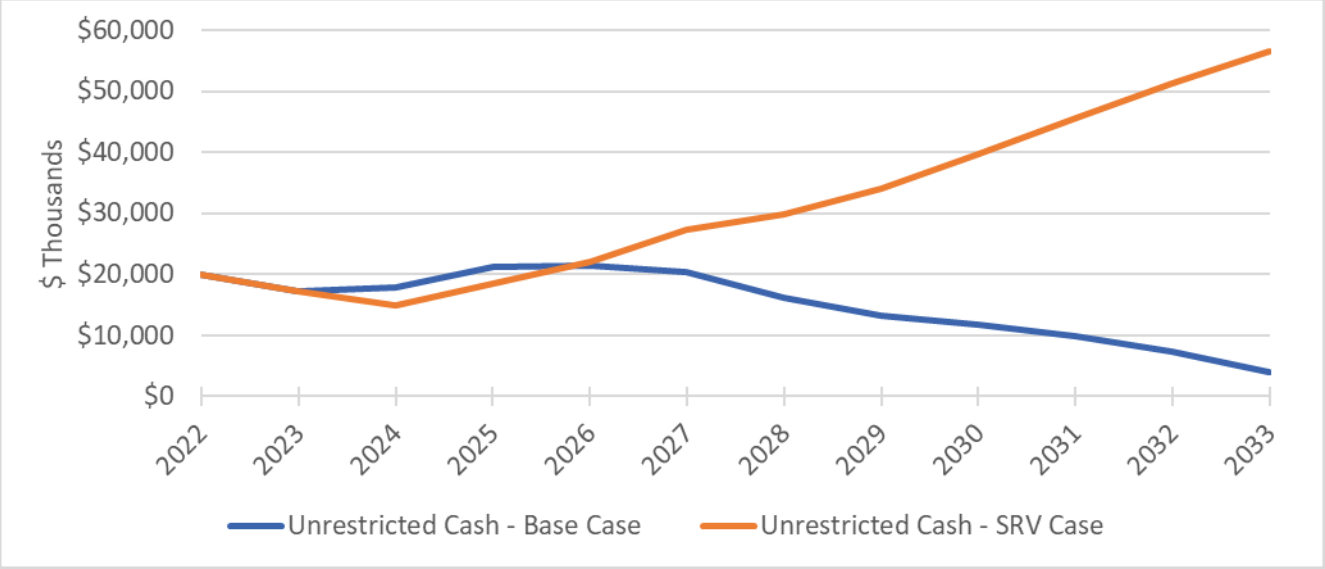
Figure 6 Forecasted operating performance ratio



Cash reserves

With increasing deficits in the base case, Council would need to deplete its cash balances to fund ongoing operations. The SRV will allow Council to continue to increase its unrestricted cash balances.

Figure 7 Forecasted unrestricted cash balances



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 can not be predicted or planned for in their Long Term Financial Plan. Hornsby 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 un-forecasted expenditure in the future. Some examples of previously unplanned expenditure at Hornsby Shire Council include:

- The 2016 boundary adjustment and abandonment of amalgamation plans for the shire that left Council with a yearly reduction of $10 million in revenue, without a commensurate reduction in costs.

- Storm events that have occurred, like that in 2018, where the full cost of clean-up operations is not fully covered by the NSW Government even when it is declared a natural disaster. Council must also manage cash flow carefully as there is often a significant time lag between when the money is spent on cleaning up and when the costs are recovered from the State government.
- The implementation of state mandated initiatives such as the Emergency Service Levy and new Audit Risk and Improvement Committee requirements which have increased ongoing costs by approximately $500 thousand per year from 2019-20.
- The urgent program to implement an asbestos remediation plan for Council's administration building from 2020.
- Remediation of the former Foxglove tip site at Mount Colah, built to the relevant standards of the day, requires significant expenditure to resolve legacy landfill issues, including property acquisition and leachate and gas remediation works.
- Absorbing reduced income and increased costs as a result of service shutdowns, physical distancing and lock downs from the COVID-19 pandemic throughout 2020 and 2021. As well as the ongoing economic consequences from the pandemic which are still being experienced.

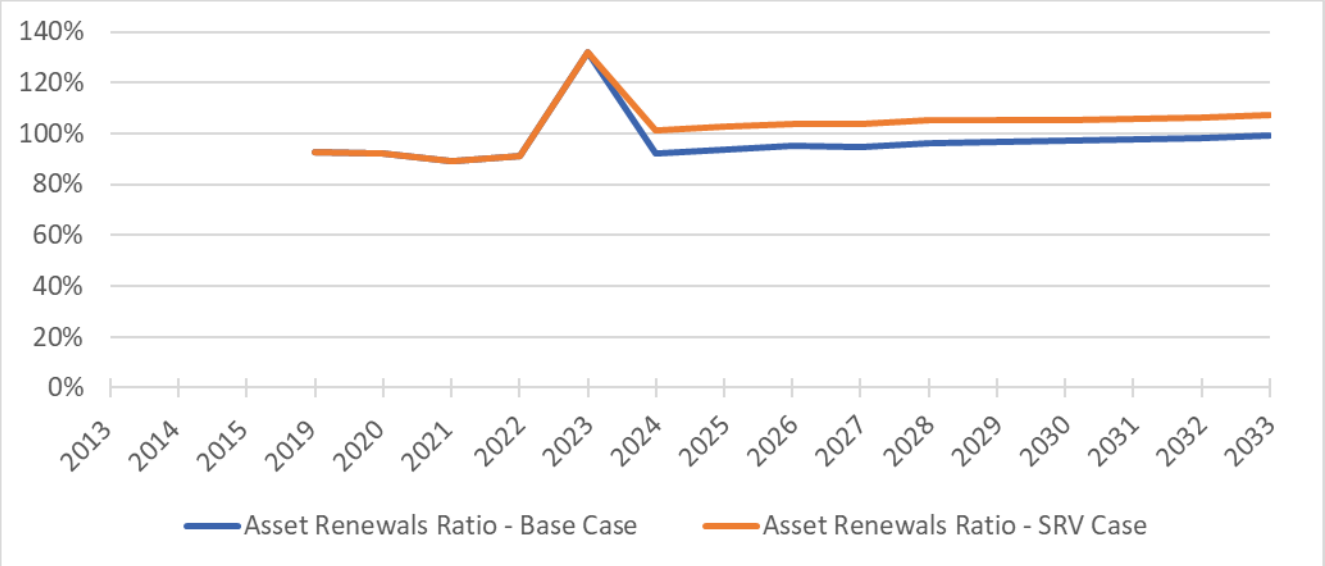
Sufficient investment in assets

Council has planned to invest sufficiently in assets to maintain a 'fit for purpose' asset base in both its base and SRV modelling. It is in part this level of investment that is driving deficits and depleting cash in the base case. While the SRV will produce sufficient revenue to fund the required investment.

The asset maintenance ratio is a measure of how much a council is spending on asset maintenance as a proportion of how much they are required to spend to adequately maintain assets. Similarly, the asset renewal ratio provides a measure of how much a council spends on renewing its assets as a proportion of how much it is required to spend to maintain assets conditions. There is some interplay between these ratios, as the maintenance ratio looks at a council's operating expenditure and the renewal looks at its capital expenditure. Whether an expenditure is operational or capital in nature is an accounting definition, so these ratios should be looked at together to really understand whether a council is sufficiently investing in ensuring assets remain fit for purpose.

Council's forecasted asset maintenance ratio is the same over the 10-year horizon under both the base case and with the SRV at an average of 95.93%. As some of the identified strategic initiatives include additional capital expenditure for asset renewal, the asset renewal ratio is slightly improved under the SRV case. However, under both cases, it is close to the target range of 100% set by the Office of Local Government, with the average asset renewal ratio over the 10-year forecast period of 96.11% in the base case and 104.71% in the SRV case.

Figure 8 Forecasted asset renewal ratio



Council has updated its Long-Term Financial Plan to show the impacts of both the base case (no SRV) and the SRV case scenario (including the SRV). This will be out for exhibition during the consultation period and is available from 4 October 20022 here: *https://yoursay.hornsby.nsw.gov.au/srv*

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

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

More information on SRVs 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?

From 4 October 2022, more information on the proposed SRV is available from Council's Have Your Say page at the following link: *https://yoursay.hornsby.nsw.gov.au/srv*

Council will also be including information on the proposed SRV in its regular newsletters and to the media. We will also be running three public forums for community and business to find out more and to ask questions as follows:

Table 5 Public forum dates

Date	Time	Location	Audience
10 October 2022	6-8pm	Hornsby RSL	Business ratepayers
17 October 2022	6-8pm	Hornsby RSL	All ratepayers and residents
25 October 2022	6-8pm	Online	All ratepayers and residents

Council will be conducting information sessions with community and business groups in addition to these open public forums.

Have your say

Council will seek feedback from the community on the SRV and its updated Long Term Financial Plan from 4 October to 8 November 2022.

From 4 October 2022, you can have your say by providing a submission or comment though Council's Have Your Say page: *https://yoursay.hornsby.nsw.gov.au/srv*

What happens after this?

Once the community consultation period concludes on 8 November 2022, 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 SRV application.

If they decide to proceed with the SRV application, the application will be submitted to IPART in February 2023. IPART will conduct its own consultation, with public submissions likely to be sought in March 2023, before they make their determination in May 2023. If successful, the SRV will be included in rates from 1 July 2023.

About Morrison Low Consultants

Morrison Low is a multidisciplinary management consultancy specialising in providing advice to local government. It has extensive experience across Australia and New Zealand and in particular assisting councils with financial modelling to understand current and future sustainability challenges. Morrison Low has supported councils to become more sustainable through improvement programs and with preparing special rates variation applications to IPART where necessary. Morrison Low undertakes community engagement on behalf of councils relating to SRVs, rates harmonisation, integrated planning and reporting and statutory engagement processes, where independence is important. More information about Morrison Low can be found on our website: *www.morrisonlow.com*.

Appendix A: Strategic initiatives identified to be funded by the proposed Special Rate Variation

Table 6 Strategic initiatives

Initiative	CSP goals	Expenditure type	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29	2029-30	2030-31	2031-32	2032-33	Total
Community climate change mitigation and adaptation program	G1.1 , G1.2, G3.1, G3.2, G3.4	Operating - employee costs	160,000	160,000	160,000								480,000
Public amenities	G1.2, G1.3, G2.3	Capital - Renewal	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	10,000,000
Enhanced cyber security maturity	G7.1, G8.1, G8.2	Operating - materials and services	250,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	100,000	1,150,000
Track and trail asset management	G1.2, G2.3, G3.1, G4.1, G5.1, G5.2.	Operating - materials and services	62,500	65,625	68,906	72,352	75,969	79,768	83,756	87,944	92,341	96,958	786,118
Track and trail upgrade including accessibility and signage	G1.2, G2.3, G3.1, G4.1, G5.1, G5.2. G4.1:	Capital New	260,000	273,000	286,650	300,983	316,032	331,833	348,425	365,846	384,138	403,345	3,270,252
Shared paths	G1.2, G2.1, G3.2, G5.1, G5.2, G6.2	Capital New	1,392,600	1,392,600	1,392,600	1,392,600	1,392,600	1,392,600	1,392,600	1,392,600	1,392,600	1,392,600	13,926,000
Inclusive community centres	G1.2, G1.3, G2.1	Capital – new	430,700	430,700	430,700	430,700	430,700	430,700	430,700	430,700	430,700	430,700	4,307,000
Drainage improvement works	G1.2, G3.1, G8.1	Capital – new	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	10,000,000

Initiative	CSP goals	Expenditure type	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29	2029-30	2030-31	2031-32	2032-33	Total
Pennant Hills town centre review	G2.2 and G26.1 and Operational Plan - 8A.K24	Operating - materials and services			250,000	250,000	250,000	250,000				1,000,000	
Bushfire risk mitigation	G3.1, G3.4, G4.1,G7.1, G7.2, G8.1,G8.2	Operating - materials and services	318,668	560,698	665,701	643,709	427,720	427,720	427,720	427,720	427,720	427,720	4,755,096
Bushland reserve asset management	G3.4, G4.1, G4.3	Operating - materials and services	750,000	787,500	826,875	868,219	911,630	957,211	1,005,072	1,055,325	1,108,092	1,163,496	9,433,419
Park amenities renewal and upgrade	G2.1, G2.3, G1.3	Capital - renewal	650,000	650,000	650,000	650,000	650,000	650,000	650,000	650,000	650,000	650,000	6,500,000
New and upgraded play spaces	G2.1, G2.3	Capital - new	85,000	85,000	85,000	85,000	85,000	85,000	85,000	85,000	85,000	85,000	850,000
Social inclusion program	G1.1, G1.3, G2.3, G7.2	Operating - materials and services	80,000	80,000	80,000	80,000	80,000	80,000	80,000	80,000	80,000	80,000	800,000
Total - operating expenditure			1,621,168	1,753,823	1,901,482	2,014,279	1,845,699	1,946,548	1,946,548	1,750,989	1,808,153	1,868,174	18,404,634
Total – capital expenditure			4,818,300	4,831,300	4,844,950	4,859,283	4,874,332	4,890,133	4,906,725	4,924,146	4,942,438	4,961,645	48,853,252
Grand total			**6,439,468**	**6,585,123**	**6,746,432**	**6,873,562**	**6,719,650**	**6,784,832**	**6,853,273**	**6,675,135**	**6,750,591**	**6,829,820**	**67,257,886**