



# ***Snowy Valleys Council – Evidence Regarding Advantages and Disadvantages of De-Amalgamation***

## **Appendix**

12/05/2023

***The University of Newcastle acknowledges the traditional custodians of the lands within our footprint areas: Awabakal, Darkinjung, Biripai, Worimi, Wonnarua, and Eora Nations.***

***We also pay respect to the wisdom of our Elders past, present and emerging.***

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## Appendix 1 – Definitions and Means of Variables, 2013-2022

Variable	Definition	All NSW	Rural Councils
<b>Regressand</b>			
Opexpercapita	Operating expenditure per capita	2.037 (1.330)	2.917 (1.487)
PCA rfp1	PCA of financial ratios	Not applicable	-0.282 (0.867)
<b>Population</b>			
Pop (ln)	Natural log of the population for each local government area	10.151 (1.378)	8.866 (0.630)
Pop2 (ln)	The square of the logged population	104.930 (28.148)	79.002 (11.027)
Density (ln)	Natural log of population density data for each local government area	2.857 (3.259)	0.074 (1.271)
<b>Controls</b>			
Median employee income	Median employee income (lagged), divided by 1,000	45.465 (8.367)	41.219 (5.606)
Median unincorporated business income	Median unincorporated business income (lagged), divided by 1,000	11.379 (5.347)	10.477 (6.686)
Aged	Proportion of people on an aged pension	12.059 (4.179)	13.621 (3.268)
Under 15	Proportion of people under the age of 15	19.041 (2.556)	19.848 (2.115)
DSP	Proportion of people on a Disability Support pension	4.020 (1.817)	4.685 (1.516)
Newstart (ln)	Proportion of people on a Newstart allowance, logged	3.642 (1.879)	4.249 (1.899)
Unsealed	Length of sealed roads	621.894 (634.639)	1048.832 (555.471)

Sealed (ln)	Length of unsealed (graded) roads, logged.	6.067 (0.714)	5.898 (0.625)
Operating Grants (ln)	Operating grants taken from audited financial statements, logged	9.305 (0.621)	9.108 (0.421)
Year	A dummy variable to control for the effect of different years	Not applicable	Not applicable
Amalgamation	A dummy variable to control for whether or not a council was amalgamated in 2016	Not applicable	Not applicable

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## Appendix 2 – Financial Sustainability Measures That Should be Implemented at SVC

We were commissioned to provide advice to Council regarding the advantages and disadvantages of a potential de-amalgamation. However, during the course of our work it became apparent that SVC faces some serious challenges and would require significant mitigation works in the event that it was not de-amalgamated. Moreover, our extensive experience working with councils in distressed conditions suggest to us that it would be prudent to start to redress some of the problems at SRV, as soon as possible – even if Council elects to pursue a de-amalgamation. Indeed, the quicker Council acts, the less pain that is likely to be felt by the community.

The following are dot points of the most important matters that need to be redressed, organised according to the topics of (i) special rate variation, (ii) capital expenditure program, (iii) financial sustainability plan, (iv) staffing, (v) financial information, and (vi) communication. Professor Drew will elaborate on these matters in his extensive workshop with Councillors on Thursday 27<sup>th</sup> April.

We stress that the following is a value-add service that we have elected to provide in view of the pressing problems confronting SVC. It is not meant to take the place of a dedicated analysis of financial sustainability and further recommendations may be warranted should additional investigations occur. We also underline the importance of exerting maximum effort to redress perceived problems as quickly as possible – irrespective of what happens on the de-amalgamation question. Some of these matters are very serious and simply cannot be allowed to continue unchecked.

### (i) *Special Rate Variation (SRV)*

- It is important to realise that the cost-base of Council has been increased permanently.
- By our estimate an SRV for an *additional* 15-30% above the cap will be required shortly (this is on top of the SRV that has already been approved by IPART). Indeed, even more rate increases may ultimately be required. Unfortunately, we were unable to obtain sufficiently robust accounting data which would be required to be more precise (especially an updated and plausible long term financial plan). {We would also need to thoroughly assess capacity to pay (especially the econometric estimation of same), assess debt capacity (through econometric estimation), and know what decisions Councillors have made with respect to de-amalgamation as well as regarding the matters that follow}.
- We believe that Council should seriously consider applying for a SRV in the next round, which commences November 2023.
- It is important to understand that the existing SRV has also probably permanently altered the location decision calculus of prospective residents. A future SRV will do likewise. Thus, spending to improve the liveability of the region – and hence attract population growth – is offset, at least in part, by the rise that it brings about to shelter costs.

### (ii) *Capital Expenditure Program*

- The capital expenditure program needs to be revisited and scaled back wherever possible. It is simply too large for a council of this size and has been distracting staff from key tasks that now stand in need of urgent redress.

- Indeed, Councillors may be well advised to take a much more critical view of potential grants for works of a discretionary nature in the future. It is sometimes appropriate to say ‘no’ to opportunities – especially when faced with pressing financial sustainability concerns or an over-stretched staff.
- Whole-of-life project costing needs to be adopted in the future. Notably maintenance, staffing and ultimate replacement costs are usually not covered by grants. These substantial costs may not have been considered carefully in the past.
- Furthermore, the willingness to pay (WTP) of the community must be assessed rigorously. This is best done through the use of sufficiently large, *randomised* surveys that cite the whole-of life cost for the asset, as well as the average cost to each individual ratepayer. Failure to robustly assess WTP can lead to entrenched fiscal illusion and hence significant financial sustainability challenges.
- More extensive and comprehensive community engagement needs to occur for large infrastructure spending with reference to whole-of-life cost and WTP. It has become clear to us that many in the community feel that some projects in the past were not consistent with the preferences of residents.
- All new programs and capex decisions should make reference to the long-term financial plan (LTFP) – specifically where surplus funds can be found in the LTFP, or alternatively, specific expenditure cuts or additional revenue streams that will be executed.
- Since amalgamation there has been greater attention given to the villages. However, it is not always clear that the level of services provided have been commensurate with the population size and needs of the said villages. Council may need to better manage the expectation of the villages or better convey the cost of providing higher-than-normal levels of services to some of these areas.
- More focus needs to be had on maintaining current infrastructure rather than new construction – especially in the Tumut area. When one travels around Tumut it is clear that there is a considerable maintenance deficit that needs to be addressed. It is possible that the large program of new capital expenditure in Tumut, in particular, has resulted in less attention being given to the state of the existing asset base.
- The robustness and detail of asset management and construction plans could be improved. Council should prioritise a better appreciation of asset conditions and also better understand the impact that this will have on the LTFP and financial sustainability.
- It appears that Council might benefit from hearing more often from the manager-level staff. It is our contention that most of the middle management are well-aware of the problems facing Council and could offer excellent advice on the way forward. However, for them to feel comfortable enough to provide sage counsel they need to feel that they are being listened too, and understand the high respect that Councillors have for their wealth of experience.
- Budgeting practice needs to improve considerably at SVC – please see the finance information section for more detail.

*(iii) Financial Sustainability*

- On the whole it would be fair to say that the extant Financial Sustainability Plan is inadequate and misguided on several matters.

- For instance, it recommends price benchmarking. This is the incorrect strategy in most cases. Council is urged to instead practice long-run marginal cost pricing<sup>1</sup> for most discretionary prices. Discretionary prices should be allocated to one of four years and each price reviewed on a revolving four-year cycle. In inter-cycle years prices should, in most cases, be increased by the relevant sub-index of the Producer Price Index (PPI) – the Consumer Price Index (CPI) should only be used for items where capacity to pay (rather than cost recovery) is the main concern.
- The financial sustainability focus needs to be far broader than the two ratios mentioned in the Financial Sustainability Plan. In particular, there needs to be a much stronger focus on the adequacy of reserves (and trends in reserves), the accuracy of budgets, and the plausibility of the LTFP. In this regard Council should expect the ARIC to closely monitor a broad suite of metrics consistent with those presented in this report.
- Care needs to be taken with respect to the assumption that shared services will definitely result in savings and efficiencies. Indeed, research by Drew et al. (2019) has shown that shared services often result in higher unit costs. However, if designed well collaborative arrangements can result in savings and in this regard, readers are referred to the guidelines in Drew (2020), pages 87-102.
- There seems to be a need for greater accountability regarding budget over-runs.
- Rigorous monthly budget reconciliations should be re-instated as soon as practical.
- It is important for Council to make subsidies both more rigorous and also more transparent. For each subsidised good or service Council ought to articulate in a publicly available document: (i) the virtue or positive externality that the subsidy addresses, (ii) the target group for the subsidy, (iii) the measurable goal for assessing the success of the subsidy, (iv) the minimum rate necessary to achieve this goal (as well as the discretionary pricing or survey evidence to support this contention), (v) how the subsidy will be clearly communicated to both donors and beneficiaries, (vi) the date that the subsidy will be reviewed (this should occur at least every four years). It is particularly important to send clear price signals in order to combat fiscal illusion. Thus, receipts for subsidised services should prominently display the quantum of the subsidy provided by the wider body of taxpayers.
- Indeed, all discretionary goods and services should be reviewed each Council term. The best approach to this is to divide the current list of discretionary projects into four equal portions and have Councillors confirm that the discretionary items are still appropriate each cycle. This decision-making should be informed by (i) the cost of the service, (ii) the measured success of the service, and (iii) Council's current financial sustainability position. Unfortunately, services of a discretionary nature are often implemented to meet a particular need but continue to be funded even when the need no longer exists, or where the service has failed to address the need (Friedman, 1993).
- Community grants should require annual applications which ask applicants to explain (i) the value, facilitated by the grant, that they will provide to the wider community, (ii) the measures the organisation is implementing to reduce grant dependency in the future, (iii) the contributions made by the members of the organisation (both financial and in-kind), (iv) what other options the organisation explored to meet their needs (such as community donations or grants from other bodies). These completed applications should be publicly available.

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<sup>1</sup> This is the cost of producing just one more item taking into account overheads, capital replacement costs, maintenance and the like.



- Council would be well advised to conduct some targeted education of staff regarding (i) financial sustainability (as a general concept), (ii) the financial sustainability position of SVC, and (iii) an improved financial sustainability plan. Staff should also be asked for their suggestions for improving efficiency and generating savings. A number of councils run appropriately incentivised schemes of this kind with great success.
- Council would be well advised to better educate the community regarding the financial sustainability challenge faced by Council. At a minimum, Council should clearly display on rates notices: (i) a chart of total debt over the last 5 years, (ii) a chart of operating results over the last five years, (iii) a pie chart showing sources of revenue, and (iv) a pie chart showing expenditure destinations. Regular information of this kind is essential to dispelling fiscal illusion.
- It may be appropriate to institute a capital advisory committee for major infrastructure projects. A committee of this kind should include people with local knowledge, decision-makers, and also staff skilled in the particular area. Committees of this kind have been implemented with great success elsewhere and have reduced budget over-runs as well as improving the utility of the infrastructure constructed.
- A service level review, heavily informed by *randomised* survey input, would seem to be in order.
- The LTFP needs to be scrutinised much more rigorously by ARIC and the Councillors. We do not believe that the current LTFP is plausible. Constructing a plausible LTFP is key to decision-making regarding assets and financial sustainability and thus should be viewed as a matter of priority.
- Consideration should be given to financial sustainability training for senior staff, Councillors, and perhaps members of ARIC.
- Consideration should be given to investigating the potential for new revenue streams associated with the green energy transition.

#### (iv) Staffing

- In general, there are limited further savings available in the area of staffing.
- However, it is clear that overtime has increased significantly in recent years and risks being permanently imputed into the personal budgets of some staff. Savings in the order of 40% may be indicated in this particular area.
- There are some minor savings that might be realised with respect to untaken leave, especially in the works area.
- There is an emerging training deficit that should be monitored carefully and redressed where appropriate.
- Staff turnover is a significant problem for SVC. High staff turnover results in a loss of institutional memory and may also damage the SVC brand with respect to future recruiting. In addition, it should be acknowledged that staff recruited from areas outside of the region will take time to understand the tastes and preferences of the community, and hence delay the necessary task of improving efficiency. Indeed, staff recruited from outside of the area often do not have the same kinds of social and family roots, and therefore may presage even more rotation in the future. For this reason, it would be wise to identify existing staff who – with appropriate training, mentoring, and opportunity – might be suitable for promotion in the future.

- There is a high likelihood that problems recruiting and retaining staff are likely to result in higher costs in the future. For this reason, it would be prudent to also establish a staff retention strategy.

(v) Finance Information

- We hold some concerns about what finance data could be accessed and the accuracy of the data. This statement should not be interpreted as a comment on the current Manager of Finance who has recently come to the organisation and is doing his best to identify and resolve problems which stretch back to the original amalgamation as well as the extensive period when the duties were apparently performed by a consultant.
- It is imperative that Councillors and the community can have absolute faith in the rigour of accounting information. Recent events – as well as our own experience – suggest that this may not be completely the case at present. Accordingly, it might be prudent for Council to appoint an experienced local government accountant with the sole task of identify and mitigating problems in the extant system. To be clear we are not talking about a consulting firm, but instead a suitably qualified and experienced person – possibly recently retired – on a six-month contract (with an option to extend for a further six months).
- It appears that there may be some gaps in the internal audit processes. This matter should be investigated and rectified as soon as possible.
- There may be some reason to believe that ARIC is not providing comprehensive advice to Council – particularly with respect to internal audit, financial sustainability, and performance improvement elements of their remit. This perception should be investigated, and measures taken to improve matters if necessary.
- Monthly budgeting reviews need to be conducted promptly, comprehensively and rigorously. Past performance with respect to budgeting suggests that redress of monthly budget reviews should be prioritised. Moreover, in view of the high turnover of staff it is important for monthly budget reviews to be documented in detail.
- As we have already noted the LTFP needs to be reviewed and revised as a matter of urgency.

(vi) Communication

- *Random* surveys need to be used to find out local priorities including the possibility that people are happy with existing infrastructure and services (and instead want downward pressure on rates).
- There is clearly a case for improving the communication between Council and the community. We have already suggested some measures relating to price signals and the like. We acknowledge that matters are difficult because of some ill-will relating to past events.
- Better communication needs to occur with staff – specifically, the impression of senior management sometimes seems to be at odds with an important portion of the staff. There also appears to be an element of fear amongst some staff (regarding the likelihood of retribution for speaking out) as well as a feeling that staff haven't always been listened to or genuinely consulted with. We make no judgement regarding whether these fears and feelings are indeed warranted. Better communication should reduce the likelihood of further losses of staff and also improve perceptions amongst potential recruits.

- If SVC were to remain amalgamated then there would be a strong case for increasing the numbers of Councillors, especially to facilitate greater voice in the villages who may feel somewhat disenfranchised. Unfortunately, as we showed earlier, the original boundary inquiry – and the Minister’s Proposal – failed to rigorously engage with s263(3)(e) the Act (1993; NSW). This has clearly caused some problems that likely warrant redress.



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