Advice

Local Government Advice - Attachment

City of Salisbury

February 2023

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A The Commission's approach

In providing the Advice for the City of Salisbury (**Council**), the Essential Services Commission (**Commission**) has followed the approach it previously explained in the Framework and Approach – Final Report (**F&A**).[1]

The Commission has considered the Council's strategic management plan (**SMP**) documents (as in the box below), with a particular focus on its performance and outlook against three financial indicators: the operating surplus ratio, the net financial liabilities ratio and the asset renewal funding ratio.[2] Analysis of these three indicators captures financial and service sustainability, in addition to cost control and affordability risk.[3]

- 2022/23 Long Term Financial Plan and Annual Business Plan (adopted June 2022)
- Interim Strategic Asset Management Plan 2022 (published May 2022)
- Annual Plan 2021-22, includes the Long Term Financial Plan (adopted June 2021)
- Buildings Asset Management Plan (approved November 2015)
- Drainage and Waterways Asset Management Plan (approved November 2015)
- Plant and Fleet Asset Management Plan (approved November 2015)
- Parks and Streetscapes Asset Management Plan (approved November 2015)
- Salisbury Water Asset Management Plan (approved November 2015)
- Street Trees Asset Management Plan (approved November 2015)
- Transport Asset Management Plan (approved November 2015)

Given that the Commission must, in providing advice, have regard to the objective of councils maintaining and implementing their infrastructure and asset management plans (**IAMPs**) (usually termed AMPs) and long-term management plans (**LTFPs**),[4] it has also considered the Council's performance in that context. Findings regarding the content of the City of Salisbury's AMPs, and the alignment between its LTFP and AMPs,[5] are discussed in section C.3.

The Commission has also reviewed the Council's template data which contains its 2022-23 LTFP forecasts for 2022-23 to 2031-32, as well as its 2021-22 LTFP forecasts, and historical financial data and number of rateable properties and council staff (Full Time Equivalent (**FTE**)) numbers from 2011-12

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1 Commission, *Framework and Approach – Final Report*, August 2022, available at www.escosa.sa.gov.au/advice/advice-to-local-government.

2 The indicators are specified in the *Local Government (Financial Management) Regulations 2011 (***Regulations***).* Since 2011, each council has been required to refer to these three indicators in its plans, annual budget, mid-year budget review and annual financial statements. The councils can adopt their own target range for each ratio, but the Commission has adopted the previously suggested Local Government Association (**LGA**) target ranges as a basis for its analysis, which were established and agreed during the development of the LGA Financial Sustainability Papers (2006-2011).

3 The F&A listed 29 analytical questions that the Commission has answered in assessing the Council's performance against these indicators to determine affordability, cost control and other sustainability risks.

4 *Local Government Act 1999* (**LG Act**) s122(1g)(a)(i).

5 As required under s122(1b) of the LG Act.

onwards.[6][7] All charts and tables in the Advice are primarily sourced from these datasets. In addition, the Commission has reviewed the Council audit committee reports, and other public information, as appropriate.

The Commission has reported estimates in nominal terms, for consistency with the Council's plans and actual rate levels, but it has compared estimated inflation impacts to these trends as a guide to identify 'real' rather than 'inflationary' effects. In the charts, the Consumer Price Index (CPI) line shows the cumulative growth in the CPI (Adelaide) series from 2011-12, and then projections of this series from 2022-23 based on the Reserve Bank of Australia (RBA) (Australia-wide) inflation forecasts (to the June quarter 2025), and the midpoint of the RBA target range (2.5 percent) thereafter.

Finally, in formulating this Advice, the Commission has had regard to the circumstances of the City of Salisbury, including its location as an urban council, its income level ($135.9 million) and the size of its rates base (more than 61,400 ratepayers[8]).

[6] Sourced from the Local Government Grants Commission (including data reported by the Office of the Valuer-General) and Council's data.

[7] The Council's estimates for the 2021-22 financial year, relied on at the time of preparing this advice, were unaudited.

[8] Based on the estimated number of property assessments in 2022-23.

B Material plan amendments in 2022-23

The City of Salisbury has made various amendments to its 2022-23 budget and forward projections, partly for inflation and partly for other revenue and spending initiatives. The material amendments to some of its main financial forecasts are listed in the table below (in nominal terms).[9] To ensure a comparable analysis of estimates between the 2021-22 and 2022-23 LTFPs, the Commission has reviewed the nine overlapping years' statistics: 2022-23 to 2030-31 and identified material amendments accordingly.

Selected Financial Item	Sum of 2022-23 to 2030-31 estimates in 2021-22 LTFP ($ million)	Sum of 2022-23 to 2030-31 estimates in 2022-23 LTFP ($ million)	Change in 2022-23 estimates ($ million)	Change in 2022-23 estimates (percent)
Total operating income	1,382.6	1,464.6	+82.1	+6
Total income from user charges	53.4	79.9	+26.5	+50
Total operating expenses	1,363.8	1,451.9	+88.1	+6
Employee costs	407.6	445.6	+38.0	+9
Materials, contracts and other expenses	611.7	653.2	+41.6	+7
Total capital expenditure	344.9	397.6	+52.7	+15
Capital expenditure on new and upgraded assets	151.9	204.9	+52.9	+35

B.1 Indexation adjustments

Based on the Council's assumptions in its 2022-23 LTFP, an increase in its costs and revenue estimates by up to around 6 percent over the 2022-23 to 2030-31 forecast period[10] would account for higher inflation, compared with same estimates in its 2021-22 LTFP.

The Council has assumed CPI inflation growth of 3.3 percent in 2022-23, then 2.8 percent in 2023-24 and 2.5 percent per annum from 2024-25. The Commission notes that, compared with RBA estimates, the Council's stated assumptions for indexation in the short term could be low in the current inflationary environment. The RBA forecasts for CPI to increase by 6.7 percent in the year to the June 2023 quarter and by 3.0 percent in the year to the June 2025 quarter.[11] Beyond June 2025, the RBA has not published inflation forecasts, but a return to the long-term average (of 2.5 percent based on the midpoint of the RBA's target range of 2 and 3 percent) is a reasonable assumption.

Notwithstanding the need for the Council to endeavour to find savings and reduce any inflationary impact on its community, the Commission has found that it would be appropriate for it to:

[9] This table shows only selected financial items to demonstrate the material amendments made by the Council in its 2022-23 estimates. It excludes various financial items and individual items do not sum to totals.

[10] The set of nine years forecast in both the 2021-22 and 2022-23 LTFP projections.

[11] RBA, Forecast Table - February 2023, available at https://www.rba.gov.au/publications/smp/2023/feb/forecasts.html.

1. **Continue** to review its inflation forecasts in its budget and forward projections, given the potential for higher short-term outcomes before a return to long-run averages.

B.2 Increase to operating income estimates

The City of Salisbury's estimated operating income to 2030-31 has increased by $82.1 million or 6 percent in its 2022-23 LTFP estimates.[12] Most of this increase is due to higher rates and user charges,[13] with the estimates for rates revenue increasing by $47.4 million or 4 percent, and the estimates for user charges increasing by $26.5 million or 50 percent, compared to the 2021-22 estimates (for the period 2022-23 to 2030-31). These increases were offset by a small reduction in investment income.

The increase in user charges estimates is predominantly related to the Council's approved Salisbury Aquatic Centre,[14] a significant project involving the redevelopment of the existing Salisbury Recreation Precinct, and which is currently expected to be operational by mid-2024.[15] Various new facilities will be established as part of the redevelopment,[16] and the Council has included revenue estimates for several activities, the majority from centre memberships, aquatic programs/lessons, and casual entries.[17] A key assumption in the Council's estimates is that the facility will not operate at 100 percent of expected operations until year four (or approximately 2026-27), and by then it is estimated to generate over $3.5 million per annum.[18]

The Council has stated in its LTFP 2022-23 that it increased rates by an average of 0.6 percentage points per annum above inflation.[19] The need to 'lock in' annual rate increases above inflation in the LTFP projections is discussed further in section C.4 below. The revised rates revenue estimates also incorporate a reduction in the assumed average growth of rateable properties from 1.0 percent per annum (in the 2021-22 LTFP) to approximately 0.6 percent per annum (in the 2022-23 LTFP).[20]

B.3 Increase to operating expense estimates

The City of Salisbury's estimated operating expenses have increased by a total of $88.1 million or 6 percent from 2022-23 to 2030-31, compared with its 2021-22 LTFP estimates. Approximately half of

[12] This compares the LTFP estimates aggregated over the nine years from 2022-23 to 2030-31. The 2022-23 LTFP estimates for 2031-32 are not included in the comparison.

[13] User charges represent the recovery of service delivery costs through the charging of fees to the users of the Council's services (City of Salisbury, *2022/23 Long Term Financial Plan and Annual Business Plan*, June 2022, p. 48, available at https://www.salisbury.sa.gov.au/assets/downloads/Council/22-23-Long-Term-Financial-Plan-and-Annual-Business-Plan.pdf).

[14] City of Salisbury, *Written Statement of Material Amendments*, 30 September 2022.

[15] City of Salisbury, *Media Release: 'Exciting plans released for new Salisbury Aquatic Centre',* 23 December 2022, available at: https://www.salisbury.sa.gov.au/.

[16] Such as an indoor multi-use lap/leisure pool and specialty program pool, fitness gym and café, outdoor swimming pool, and new outdoor water slides and waterplay area (City of Salisbury, *2022/23 Long Term Financial Plan and Annual Business Plan*, June 2022, p. 23).

[17] Other user charges include café and merchandise sales (Dean Newbery, *Prudential Report, Salisbury Recreation Precinct Project,* November 2021, p. 18).

[18] The City of Salisbury estimates that the new centre will attract over 285,000 attendances annually (compared to approximately 55,000 attendances at the current facilities). This will include 1,550 centre members, 45,000 swimming lesson attendances, and 65,000 single attendances (Department of Treasury and Finance and City of Salisbury, *Submission to Public Works Committee*, *Salisbury Recreation Precinct Redevelopment Project*, 2 December 2021, p. 4, available at: https://www.parliament.sa.gov.au/api/sitecore/search/GetCommitteeFileDownload?id=177&fileId=a31b9a17-ee9b-4a3b-9663-eac4dcf4dd14.

[19] City of Salisbury, *2022/23 Long Term Financial Plan and Annual Business Plan*, June 2022, p. 17.

[20] City of Salisbury, *2022/23 Long Term Financial Plan and Annual Business Plan*, June 2022, p.17 and City of Salisbury, *Annual Plan 2021-22*, June 2021, p. 14.

the higher operating cost estimates are due to higher estimates for 'materials, contracts and other' expenses, with an increase of $41.6 million or 7 percent on the 2021-22 LTFP estimates (from 2022-23 to 2030-31). Additionally, 'employee' expenses, which account for 43 percent of the higher operating costs, increased by $38 million or 9 percent over the previous years' LTFP estimates. These increases were offset by lower estimates for interest expenses due to lower forecast borrowing levels.

The Council has advised that the changes are due to several factors, mainly higher anticipated wage inflation, and increases in 'materials, contracts and other' expense due to the expanded scope of the Salisbury Aquatic Centre, as well as for other inflationary effects.[21] The Council's 'employee' expenses are budgeted to increase by 11 percent in 2022-23 when compared to the unaudited 2021-22 estimates, and the change in its inflation assumptions is approximately 0.6 percent per annum.[22] The Council's historical and projected operating performance is discussed in section C.1.

B.4 Increase to capital expenditure estimates

In terms of capital expenditure, the Council's 2022-23 LTFP indicates an increase in expenditure for new and upgraded assets by $52.9 million or 35 percent, compared to the previous year's LTFP (for the period 2022-23 to 2030-31). This increase in new and upgraded asset expenditure is a key driver of the Council's increased total capital expenditure budget (by 15 percent), as there are no material changes in planned asset renewal expenditure (except for some timing differences). The Council advises that the material capital expenditure amendments relate to:[23]

- The expanded scope of the Salisbury Aquatic Centre, from an initial nominal construction cost of $15.5 million (included in the 2021-22 LTFP), to $28.4 million (included in the 2022-23 LTFP). This increase reflects the construction of additional facilities (rather than a replacement or modern equivalent of the existing facility), and reflects the facility being operated directly by the Council rather than a recreation service provider.
- The carryover of part of the Council's COVID-19 Infrastructure Recovery Program into 2022-23.[24] In November 2021, the Council rescheduled and amended its recovery program, due to several economic and capacity constraints impacting on the delivery of projects arising from the COVID-19 pandemic (such as the shortage in materials and supplies, price escalation and delays associated with the supply chain). Due to these issues and in addition to the Council's concerns on financial sustainability, the recovery program was reduced from approximately $170 million (across 2020-21 to 2021-22) to approximately $85 million.
- The increase in new and upgraded asset expenditure by $19.0 million (over the period 2025-26 to 2030-31). This is due to the Council's inclusion of 'uncommitted new capital funding' in its 2022-23 LTFP which relates to projects yet to be adequately defined and costed.[25]

The Commission notes that the Council generally demonstrates good governance related to its capital enhancement projects and the regular consultation of its community on service priorities and funding requirements.

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[21] City of Salisbury, *Written Statement of Material Amendments*, 30 September 2022; and Council's Excel template provided to the Commission.

[22] Based on the Commission's review of assumptions disclosed in the 2021-22 LTFP and 2022-23 LTFP. The Council has not disclosed projected FTEs in its information provision to the Commission.

[23] See footnote 14.

[24] City of Salisbury, *Urban Services Committee 15 November 2021, Agenda Item 4.1.6 Revised Capital Infrastructure Program*, p. 51, available at https://www.salisbury.sa.gov.au/assets/meetings/2021/11-November/community-wellbeing-and-sport-16-nov-2021/agendas/16112021-Agenda-and-Reports-Community-Wellbeing-and-Sport-Committee-AMENDED.pdf.

[25] City of Salisbury, *2022/23 Long Term Financial Plan and Annual Business Plan*, June 2022, p. 18.

However, an implication of the Council 'locking in' significant funding allocations in its 2022-23 LTFP for undefined future projects is that it must also plan for further rate increases above inflation to fund them.

While the decision to proceed with the Salisbury Aquatic Centre was a matter of priority for the Council, it is noted that the facility was not contemplated in the Council's City Plan 2035 nor was it a high priority in recent overarching community survey results. The Commission also notes that the Council is yet to publish the community consultation results that relate specifically to the project.[26]

The Commission finally notes that, as for all major capital projects of this nature, it will be important for the Council to focus on post-construction ownership and operating risks and to have regard to competitive neutrality obligations.[27] For these reasons, the Commission has found that it would be appropriate to the City of Salisbury to:

2. Focus on controlling cost growth in its budgeting, including by reviewing its projected capital expenditure allocations (in consultation with the community, as required) to remove those which are not yet tied to defined and costed projects, and reduce the need for further rate increases.

3. Ensure that it publishes relevant reports regarding community consultation outcomes about large infrastructure projects which are to be significantly rate-funded.

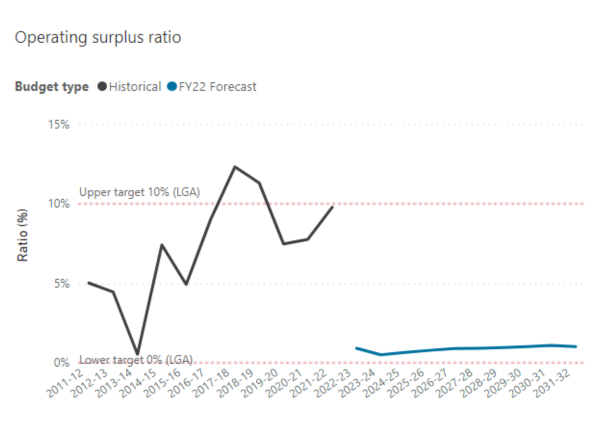
[26] This refers to consultation undertaken by UPRS in 2021, as referenced in Dean Newbery, *Prudential Report, Salisbury Recreation Precinct Project,* November 2021, p. 6. The Council's website otherwise provides consultation outcomes for its key infrastructure projects.

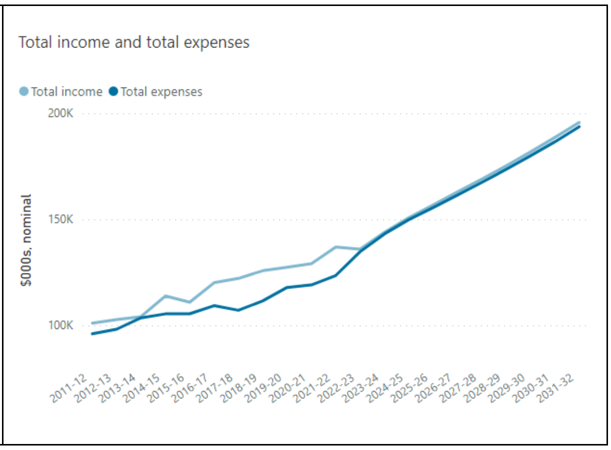
[27] Dean Newbery, *Prudential Report, Salisbury Recreation Precinct Project,* November 2021, pp. 15 and 26.

C Financial sustainability

C.1 Operating performance

The City of Salisbury has run operating surpluses from the period 2011-12 to 2020-21, and in the last five years (to 2020-21) it had achieved an operating surplus ratio averaging 9.5 percent (or $11.9 million) per annum.[28] Its operating surplus ratio is forecast to significantly decrease in 2022-23 to 0.9 percent (or $1.2 million) and largely stay at this level over the forecast period (see the left chart below). The decline in its projected operating performance is attributed to budgeting for additional expense growth, which is supported by continued increases in rates and user charges (see the right chart below).





Rates revenue has increased on average by 4.0 percent per annum from 2011-12 to 2020-21[29] (when rateable property growth averaged 0.6 percent and CPI growth averaged 1.7 percent[30]). Over the same period, 'statutory charges' (accounting for 3 percent of total operating income) increased by an average of 4.7 percent per annum. These increases were offset by declines in 'user charges' income (accounting for 4 percent of total operating income) which fell by an average of 3 percent per annum and 'grants, subsidies, and contributions' (accounting for 12 percent of total operating income) which fell by an average of 1.7 percent per annum. Grants income has been 'lumpy' from year to year[31], and the three-year average of $267 per ratepayer in 2021-22 compares with the three-year average of $242 in 2013-14, which reflects a marginal decrease in value in real terms.

The Council's operating expense growth (from 2011-12 to 2020-21) averaged 2.4 percent per annum and was primarily due to an average annual increase of 4.4 percent in depreciation charges and 2.7 percent in 'materials, contract and other' expenses.[32] 'Employee' expenses increased by an average of 1.4 percent per annum, lower than average CPI inflation growth (1.7 percent per annum) over this

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28 The operating surplus ratio is defined as: Operating Surplus (Deficit) ÷ Total Operating Income. The general target is to achieve, on average over time, an operating surplus ratio of between zero and 10 percent (Local Government Association of South Australia, *Financial Sustainability Information Paper 9 - Financial Indicators Revised,* May 2019 (LGA SA Financial Indicators Paper), p. 6).

29 Based on the compound average annual growth rate formula (which is the adopted approach to calculating average annual growth rates throughout the Commission's advice).

30 CPI Adelaide (All groups). Average annual growth in the LGPI published by the South Australian Centre for Economic Studies was similar (at 1.9 percent). Available at https://www.adelaide.edu.au/saces/economic-and-social-indicators/local-government-price-index.

31 Due to the timing of different grants and sometimes advance grant payments (as for the 2022-23 grant allocation).

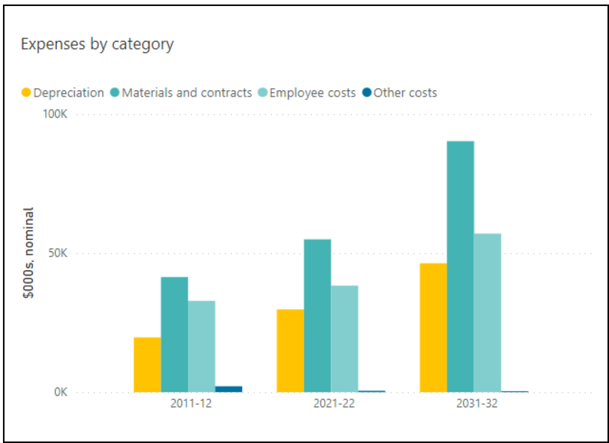
32 This includes the increase in the solid waste levy over the past 10 years which has impacted councils' waste management costs.

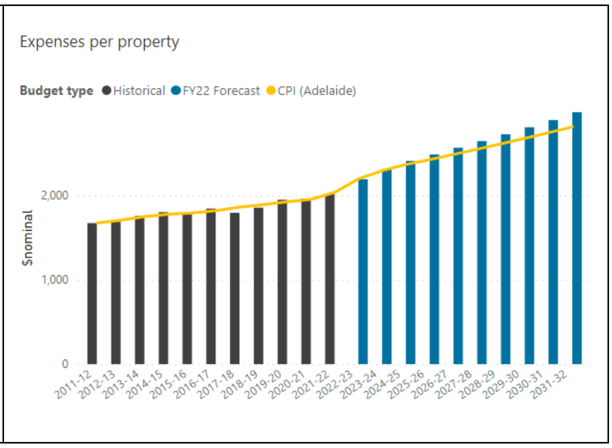
period (see the changes by expense type in specific time periods in the left chart below). Lower 'employee' expenses reflect the Council's reduction in its staffing levels from 454 FTEs (in 2011-12) to 399 FTEs (in 2020-21), a reduction of approximately six FTEs each year. This trend is consistent with other indicators[33] suggesting a period of service consolidation by the Council.

Looking forward, the Council is projecting average annual rates revenue growth of 4.2 percent to 2031-32, which is noticeably above RBA-based forecast inflation of 2.8 percent per annum,[34] and expected average expense growth (projected rates are discussed in more detail in section D).

Operating expenses are forecast to increase by an average of 4.1 percent per annum from 2022-23 to 2031-32, which is still above forecast inflation growth[35] and would represent a shift from the Council's past performance (with average annual growth of 2.4 percent in the 10 years to 2020-21).

Expenses per property (a metric which also accounts for growth) are expected to increase by an average of 3.5 percent per annum over this period, which would still represent a cost increase in real terms (based on current inflation projections) (see the right chart below).





'Materials, contracts and other' expenses and costs for depreciation are forecast to increase by an average of 4.9 percent and 4.3 percent per annum respectively, from 2022-23 to 2031-32. Overall, this would reflect an expansion of the Council's service provision over this period, as a result of its capital enhancement projects.

As stated previously, the Council is budgeting in 2022-23 significant operating cost increases across most of its cost categories, notably 'finance charges' (from $0.5 million to $1.4 million reflecting an increase in budget borrowings by $52 million), 'employee' expenses (by $4.2 million or 11.0 percent), and 'materials, contracts and other' expenses (by $3.9 million or 7.1 percent, reflecting increases in information technology, COVID-19 cleaning measures and service level increases).[36]

To avoid further cost pressure, it is important that the Council finds opportunities for tangible savings in its budget, where possible. The Council noted that it had implemented an energy efficiency program in its 2022-23 budget.[37] However, it does not appear to have identified the quantum of the savings generated nor identified any other tangible savings. Given the extent of the Council's increase in

33 Such as the average value of assets per property.
34 The forecast average annual growth in the CPI from 2022-23 to 2031-32 is estimated to be 2.8 percent based on the RBA forecasts for the CPI (Australia-wide) to June 2025 (and the Commission's calculations of average annual percentage growth) and the midpoint of the RBA's target range (2.5 percent) from 2025-26.
35 See footnote 34.
36 City of Salisbury, *2022/23 Long Term Financial Plan and Annual Business Plan*, June 2022, p. 50.
37 City of Salisbury, *2022/23 Long Term Financial Plan and Annual Business Plan,* June 2022, pp. 88 and 90.

operating expenses forecast over the next 10 years, the Commission considers that it would be important for the City of Salisbury to:

4. **Report** its actual and projected cost savings in its annual budget, to provide evidence of constraining cost growth and achieving efficiency across its future operations and service delivery.

The Salisbury Aquatic Centre will contribute to the Council's higher operating expenses with net operating losses forecast for the facility, over the first five years of operation, totalling $5.4 million (including depreciation and excluding debt servicing costs). This contrasts with the cost of the existing swimming pool facility of $0.6 million per annum. The average forecast operating loss in the fourth and fifth year is estimated to be $1 million annually (or around $16 per ratepayer),[38] with continued losses thereafter.

Although the additional cost per ratepayer is not high at this stage, there are additional cost risks attached to these estimates, as was noted in section C.4.

To manage the risks related specifically to the new aquatic facility, the Commission has found that it would be appropriate for the Council to:

5. **Develop** and **publish** a risk management plan for the Salisbury Aquatic Centre, which incorporates an annual review of the requirements for recurrent spending (given demand estimates and outcomes), and the associated impact on the Council's operating capacity and quantum of rate contributions.

C.2 Net financial liabilities

With the Council's operating surpluses from 2011-12, its net cash flows after operating and investing (that is, capital-related) activities has averaged $2.5 million annually between 2011-12 and 2020-21. (This is different to the top left chart over the page which shows cash held by the Council at the end of each year, including financing activities such as loan drawdowns and repayments).

The City of Salisbury has used loan borrowings with the Local Government Finance Authority of South Australia (**LGFA**) to fund its assets as required. It has also used other financing sources, such as leases, for its information technology assets and land utilised as part of its recycled water operations.[39] The Council has an undrawn 'Cash Advance Debenture' facility of $50.3 million, which it intends to utilise over time to fund its capital program.[40]

The Council's net financial liabilities ratio has trended between 23.6 and negative 4.8 percent between 2011-12 and 2021-22 (see the bottom left chart over the page). This is within (or below) the suggested LGA target range for the indicator of between zero and 100 percent and at a level which demonstrates that the Council is only accumulating liabilities that its operating income can reasonably service (see the top right chart over the page).[41] However, the negative ratio and associated accumulation of cash

38 Dean Newbery, *Prudential Report, Salisbury Recreation Precinct Project,* November 2021, pp. 8-9.

39 City of Salisbury, *General Purpose Financial Statements for the year ended 30 June 2022,* Note 17, p. 45, available at https://www.salisbury.sa.gov.au/assets/downloads/Council/FINAL-Annual-Report-2021-22-v2-lowres.pdf.

40 City of Salisbury, *Finance and Corporate Services Committee 17 October 2022, Agenda Item 2.1.1 Council Finance Report – September 2022*, p. 14, available at https://www.salisbury.sa.gov.au/assets/meetings/2022/10-October/finance-and-corporate-services-17-oct-2022/agendas/17102022-Agenda-and-Reports-Finance-and-Corporate-Services-Committee.pdf.

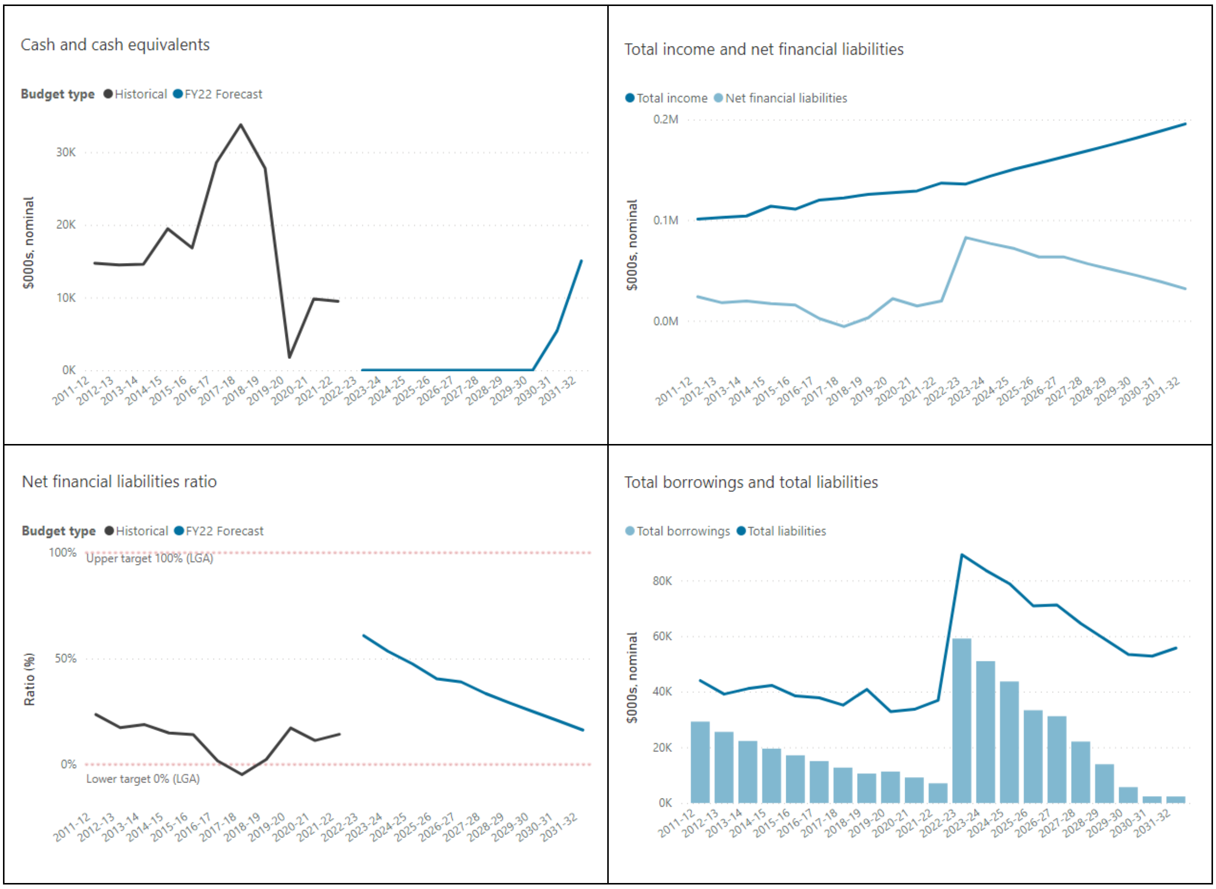
41 The net financial liabilities ratio is defined as: Net financial liabilities ÷ Total operating income. This ratio measures the extent to which a council's total operating income covers, or otherwise, its net financial liabilities. The suggested LGA target range is between zero and 100 percent of total operating income, but possibly higher in some circumstances (LGA SA Financial Indicators Paper, pp. 7-8).

suggests that the extent of rate increases over some of these years could be considered unnecessary to maintain financial sustainability for the Council.

The Council has estimated that the net financial liabilities ratio will peak at 60 percent in 2022-23, with additional borrowings of approximately $32 million to help fund the forecast peak in capital expenditure (representing a significant increase on its current borrowing liability of $7.1 million, based on the unaudited 2021-22 estimates) (see the bottom right chart below).

The LTFP projections include new borrowings which effectively provide funding for the Salisbury Aquatic Centre Redevelopment, the Council's largest capital expenditure item in 2022-23 (for $25.5 million in 2022-23, with the remaining spend in 2023-24). The Council will also receive grant funding of $7.2 million from the South Australian Government under the Local Government Infrastructure Partnership Program in relation to that project.

The Council's net financial liabilities ratio will decline to an average of 24.8 percent in the five years to 2031-32, which reflects both the marginally lower trend in borrowings and other liabilities, and the projected operating income growth (an average of 4.1 percent per annum).



The rate of reduction in borrowings after 2022-23 indicates that the Council may be accelerating the repayment of its new loans relative to the lifespan of its assets (for example the aquatic centre), and it may be appropriate for it to review these financing assumptions in its LTFP, so the loan costs are spread across a longer period.

The Commission considers that it would be appropriate for the City of Salisbury to:

6. **Review** its projected borrowing repayment plans in its long-term financial plan projections with a view to spreading the repayments over a longer time period, if possible, to reduce the extent of the required financial contributions from ratepayers to meet repayments in the short to medium term.

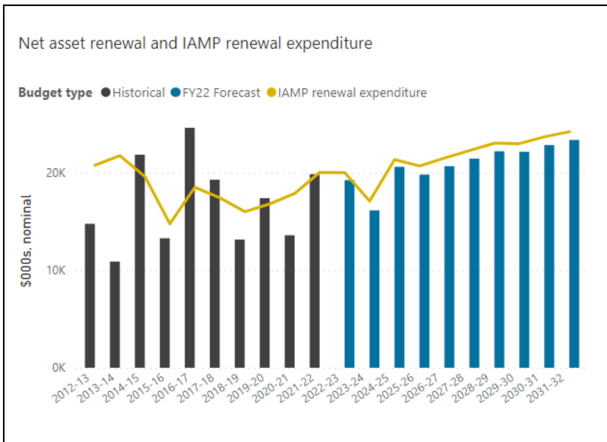
C.3 Asset renewals expenditure

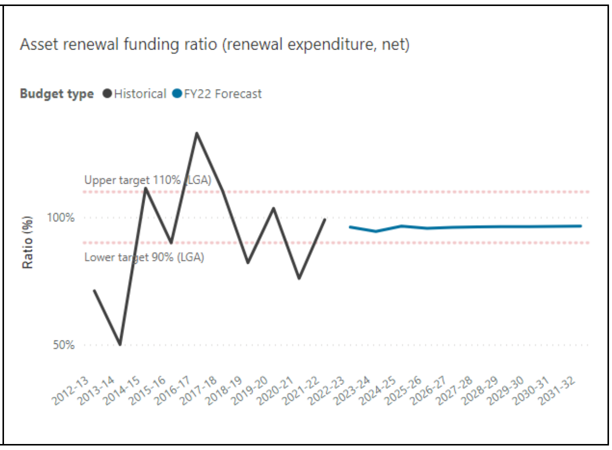
Over the period 2011-12 to 2020-21, the Council has generally improved the performance of its asset renewal funding ratio,[42] however in four of the last 10 years, it has underperformed on its asset spending priorities (see the charts below).

Between 2011-12 and 2020-21, the asset renewal funding ratio (under the 'IAMP-based' approach) averaged 91 percent,[43] signifying the Council has sufficiently spent (albeit towards the lower end of the suggested LGA target range) on the renewal and rehabilitation needs of its asset stock over this period. The Council's spending on renewal and rehabilitation of assets averaged $16.2 million each year (over this period).

From 2022-23 to 2031-32, the ratio is forecast to average 96.1 percent and remain consistently within the suggested LGA target range for the sector of between 90 to 110 percent. Average annual spending on renewal or rehabilitation of assets is projected to increase to $21.7 million (in nominal terms). The Commission encourages the Council to continue to prioritise the renewal of its assets, consistent with its projected performance.

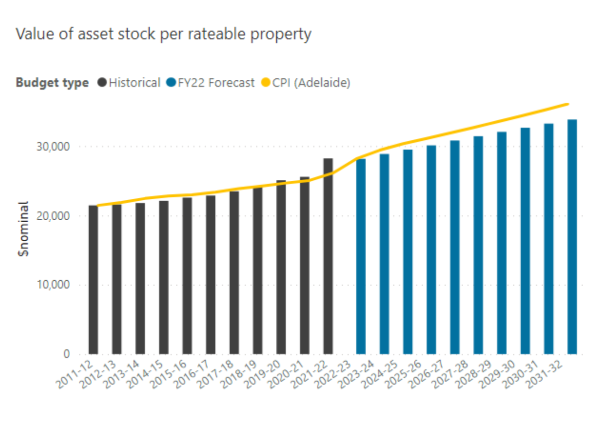
The City of Salisbury has grown its asset base over the past 10 years, with expenditure on new or upgraded assets averaging $20.4 million per annum between 2011-12 and 2020-21 (see the right chart over the page), which includes a portion of grant funding for certain projects. This has led to average growth in the value of the asset stock per property of $458 or 2.0 percent per annum in the 10 years to 2020-21 (see the left chart over the page). This growth is marginally above the rate of inflation (with average CPI growth of 1.7 per annum), which suggests a period of service consolidation.

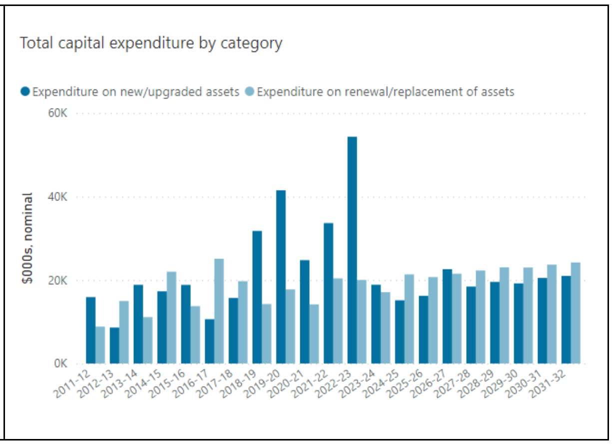




42 The IAMP-based method is the current industry standard whereby asset renewal/replacement expenditure is divided by the recommended expenditure in the IAMP (or AMP). Ideally, this will show the extent to which a council's renewal or replacement expenditure matches the need for this expenditure, as recommended by the plan. The suggested LGA target range for the ratio is 90 to 110 percent (LGA SA Financial Indicators Paper, p. 9).

43 The quoted averages for the ratio are based on 'net asset renewal expenditure' (after the sale of replaced assets) rather than 'gross asset renewal expenditure'.





The Council's planned renewal expenditure is mainly attributed to transport assets (covering roads, kerbs, and footpaths), and this accounts for approximately 50 percent of total renewals from 2022-23 to 2031-32.[44] Aside from transport works, the Council also has planned renewals for buildings and fleet assets (approximately 26 percent of total renewals). The Commission's review of the renewal expenditure in the AMPs indicates that the expenditure profile is generally consistent with that in the LTFP (when an allowance for inflation is considered). It is also noted that community consultation of the Council's AMPs has not identified any unsatisfactory levels of service (when the AMPs were developed in 2015).

Over the 2022-23 to 2031-32 period, the Council is projecting that new and upgraded capital expenditure will account for over half of its capital plan (including the Salisbury Aquatic Centre at $28.4 million). Of this new and upgraded asset expenditure, the Council has indicated that $15.1 million is uncommitted (or not fully costed) and spread across the 2025-26 to 2031-32 period.[45]

The depreciation-based asset renewal funding ratio,[46] is projected to track below the recommended minimum level (for the IAMP-based ratio) of 90 percent, averaging 53.5 percent per annum to 2031-32. This follows average performance of 67 percent for the ratio from 2011-12 to 2020-21 and indicates total depreciation expenses will continue be higher than the required expenditure on capital renewals under its various AMPs (see charts over the page).

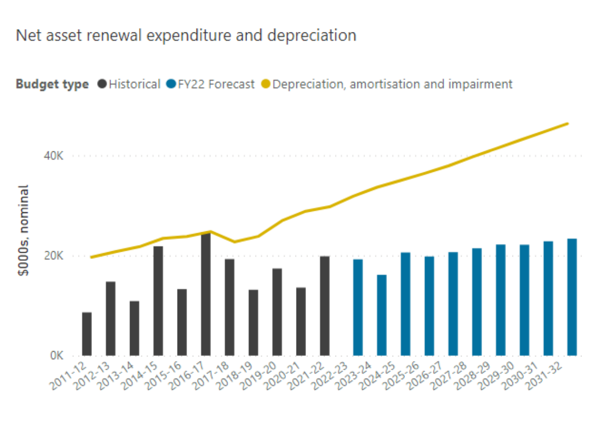
One area that might be leading to higher depreciation expense forecasts, relative to annual asset renewal expenditure needs, is the Council's recent accumulation of new assets following its capital expenditure projects. Another risk that arises when depreciation expenses exceed spending on asset renewals is that the asset lives are assumed to be shorter (in the depreciation calculation) than occurs in practice. The implication of projecting higher than necessary depreciation expenses is that higher operating income (and potentially higher rates revenue) is required to generate an operating surplus for the Council.

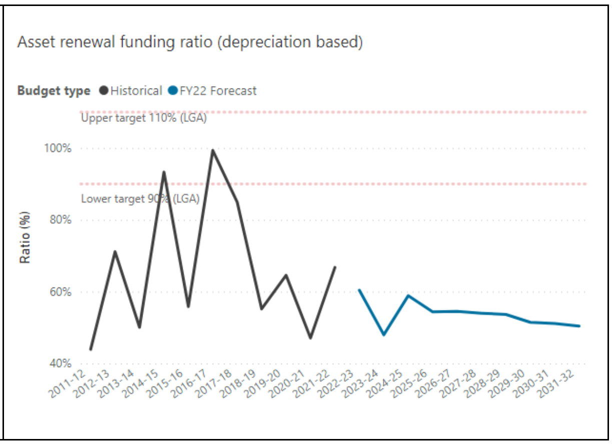
In general, it would be prudent for the Council to re-examine the key drivers of its depreciation modelling (such as average asset lives and asset valuations), as well as its projected increase in new and upgraded capital expenditure over the period of its LTFP.

44 Based on an analysis of the renewal expenditure forecasts (in real terms) in the Council's AMPs.

45 City of Salisbury, *2022/23 Long Term Financial Plan and Annual Business Plan*, p. 18.

46 The Council's asset renewal funding ratio by the depreciation-based method (where asset renewal/replacement expenditure is divided by depreciation expenses). This ratio shows the extent to which capital expenditure on the renewal and replacement of assets matches the estimated rate at which these assets are used or consumed.





The Commission has observed other matters between the Council's AMPs and its 2022-23 LTFP estimates, for example:

- It is not clear how the AMP projections (especially for new and upgraded works) align with the projections in the LTFP. For example, the Council's AMPs provide projections of new and upgraded capital expenditure averaging $3.7 million per annum (in real terms), whereas the 2022-23 LTFP projections average $22.6 million per annum (in nominal terms).
- As the AMPs were developed approximately seven years ago (in 2015), the information may include dated assessments of the Council's asset condition, service levels and community expectations.[47]

The Commission also notes that there can be legitimate budget reasons for adjusting capital expenditure from year to year, as well as additional inflation impacts, but encourages the Council to review this area to determine if there can be better alignment. To improve the robustness and consistency of the Council's asset management, the Commission considers that it would be appropriate for it to:

7. **Review** the assumptions underpinning its asset management plans to ensure those plans incorporate a more accurate picture of required asset expenditure and better align with the allocations in its long-term financial plan as necessary, including the estimates of asset lives and valuations feeding into the forecast rates of asset consumption and depreciation expenses.
8. **Review** the new and upgraded asset expenditure projections (as per **Finding 2**) with consideration of the service levels desired by the community.

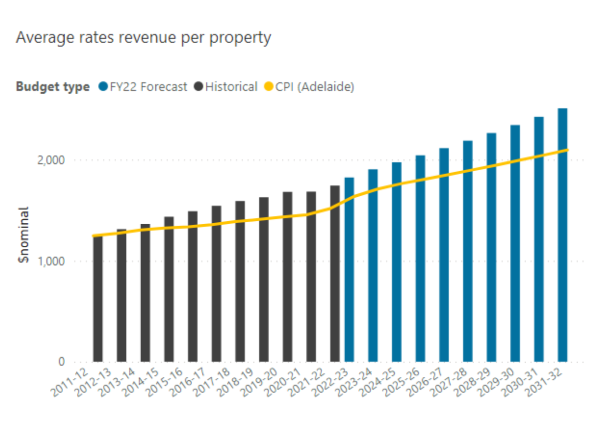
[47] Under s122(4)(b) of the LG Act, a council must undertake a comprehensive review of its strategic management plans within two years after each general election of the council. The City of Salisbury has also prepared an Interim Strategic Asset Management Plan (in 2022) which sets out its overarching asset management objectives, practices, and action plans (among other things).

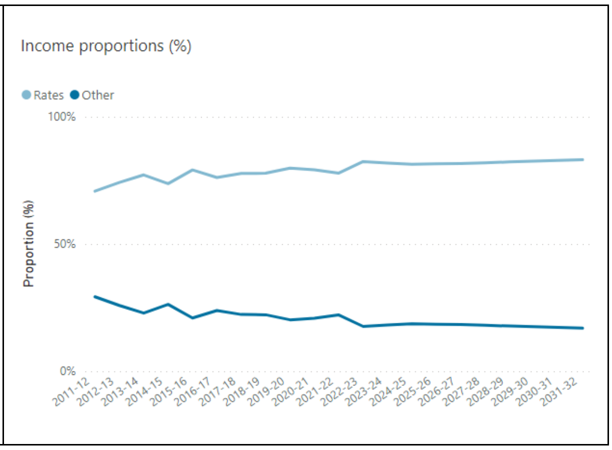
D Current and projected rate levels

D.1 Historical rates growth

The City of Salisbury's rate revenue per property increased on average by 3.4 percent or $49 per annum for each property over the past 10 years,[48] to reach an estimated $1,684 per property in 2020-21 (see the left chart below). This has exceeded CPI growth of an average of 1.7 percent per annum over this period, but also encompasses 0.6 percent average annual growth in rateable property numbers.[49] Current rate levels partially reflect its recent history of spending growth, predominantly on new and upgraded assets, which has resulted in additional maintenance, depreciation and other operating expenses.

The Council has become increasingly reliant on its rate base for its operating sustainability. As the chart below indicates (to the right), rates revenue is forecast to account for 82 percent of budgeted operating income in 2022-23, compared with 71 percent of income in 2011-12.





D.2 Proposed 2022-23 rate increases

The City of Salisbury has budgeted for an average rate revenue increase of 4.6 percent per property[50] or $80 for its existing ratepayers in 2022-23,[51] which was higher than it had anticipated charging for this year in its 2021-22 LTFP projections (that is, a 3.9 percent rate revenue increase was previously projected for 2022-23). The rates increase largely reflects the Council's financial sustainability assessment of its budget, and consideration of the financial impacts to the community.[52] It has

48 From 2011-12 to 2020-21.

49 CPI Adelaide (All groups). Average annual growth in the LGPI published by the South Australian Centre for Economic Studies was similar (at 1.9 percent). Available at https://www.adelaide.edu.au/saces/economic-and-social-indicators/local-government-price-index.

50 Based on the Council's Excel template data, comparing the 2022-23 budget figures to the unaudited 2021-22 estimates.

51 Individual rate level changes may be higher or lower depending on the rates category and property value. The Council has specifically budgeted (in 2022-23) average rate increases of 3.5 percent for residential rates, and 3.9 percent for commercial and industrial rates. City of Salisbury, *2022/23 Long Term Financial Plan and Annual Business Plan*, June 2022, p. 7.

52 During the 2022-23 budget development the Council assessed several scenarios of rate increase against each of the financial sustainability indicators and recommended a rate increase scenario in the range of 3.3 percent to 3.9 percent. City of Salisbury, *Audit and Risk Committee 12 April 2022, Agenda Item 7.1.7 Draft 2022/23 Long Term Financial Plan and Annual Business Plan*, p. 137, available at https://www.salisbury.sa.gov.au/assets/meetings/2022/04-April/audit-and-risk-12-apr-2022/agendas/12042022-Agenda-and-Reports-Audit-and-Risk-Committee_2022-04-12-010208_zxuo.pdf.

recognised higher short-term inflation (anticipated by the Council to be 3.3 percent based on the December 2021 CPI for Adelaide),[53] and an additional allowance for financial sustainability which, together with the operating cost pressures (discussed previously), results in a significantly reduced operating surplus ratio of 0.9 percent in 2022-23 (compared to 9.8 percent estimated in 2021-22). The Council's projected total rates revenue growth is higher (5.1 percent) and includes growth of 0.5 percent in rateable property numbers.

Different rate categories are subject to varying changes, with residential ratepayers (who make up 76 percent of total rates revenue) to pay a slightly lower increase of 4.1 percent or $58 per property on 2021-22 average rate levels.[54] Commercial and Industrial ratepayers (who together account for 21 percent of rates revenue) will pay the largest increase – an average increase of $331 or 4.6 percent more, which appears reasonable because these ratepayers are currently on relatively lower differential rates.[55] Ratepayers on the minimum rate, accounting for 17.6 percent of all ratepayers and likely to include the more vulnerable members of the community, will also pay 3.5 percent or $37 more (to $1,081) in 2022-23.[56] [57]

Other than 'general rates' revenue (which represents 97.8 percent of total rates revenue in 2021-22),[58] the Council has collected income from the Regional Landscape Levy (2.0 percent of total rates revenue), and minimal income on behalf of the Salisbury Business Association and Globe Derby Community Club[59] (around 0.1 percent of total rates revenue).

D.3 Projected further rate increases

Over the forward years of its LTFP, the Council is projecting average rates increases for its existing ratepayers of approximately 3.6 percent per annum from 2023-24 to 2031-32,[60] which includes a further 0.6 percent 'sustainability' allowance on top of inflation each year.[61] In total, the LTFP effectively projects a cumulative increase of $685 per existing ratepayer (to $2,509) by 2031-32, an increase of $224 above the Council's assumed inflation growth over this period (refer back to the previous chart on the left side).[62]

D.4 Affordability risk

Affordability risk among the community for these further rate increases appears moderate, on balance, when considering:

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53 City of Salisbury, *2022/23 Long Term Financial Plan and Annual Business Plan*, June 2022, p. 17.

54 The Council's residential impact assessment indicates that 44 percent of rateable properties are expected to experience an increase of greater than 4 percent. City of Salisbury, *2022/23 Long Term Financial Plan and Annual Business Plan*, pp. 126 and 135.

55 Rate in the dollar applied to the capital value of the property in the Council area.

56 City of Salisbury, *2022/23 2022/23 Long Term Financial Plan and Annual Business Plan*, p. 135.

57 Other ratepayers such as primary production, vacant land and other ratepayers will incur different rate variations including some rates reductions, City of Salisbury, *2022/23 2022/23 Long Term Financial Plan and Annual Business Plan*, p. 135.

58 Before discretionary rebates and penalties for late payment.

59 Income from the Regional Landscape Levy, and charges for the Salisbury Business Association, and Globe Derby Community Club are not retained by the Council.

60 Based on the Council's Excel template data submitted to the Commission.

61 City of Salisbury, *2022/23 Long Term Financial Plan and Annual Business Plan*, p. 16.

62 The CPI forecasts in the chart are based on RBA forecasts and then a return to long-term averages (2.5 percent per annum), which are broadly consistent to the Council's inflation forecasts (as was discussed in section B1).

- the Council's relatively low socio-economic indexes for areas (**SEIFA**) economic resources ranking for the City of Salisbury area[63]
- little to no community concern expressed about further rate rises in the 2022-23 budget process (only one submission noted the proposed increase in rates and considered it aligned with the level of deliverables in the budget)[64]
- the effect of cumulative increases in average rate revenue per existing ratepayer of 3.6 percent per annum to the period 2031-32, above the forecast rate of inflation
- the growing proportion of rates receivables (as a proportion of total rates revenue) increasing to 3.8 percent in 2020-21 compared to 2.4 percent in 2011-12, indicating potentially higher rate arrears than had occurred in the past,[65] and
- the overall higher risks associated with the Council's increasing operating and capital expenditure forecasts.

In addition, the current economic environment is putting more pressure on many communities' capacity to pay for further rate increases, including in the City of Salisbury. For these reasons, the Commission considers it would be appropriate for the Council to:

9. **Review** and **consider** limiting future minimum rates and average rates increases above inflation, particularly on rate categories which have lower capacity to pay, to help minimise affordability risk in the community.

63 The City of Salisbury area is ranked 17 among 71 South Australian '*local government areas*' (including Anangu Pitjantjatjara and Maralinga Tjarutja Aboriginal community areas and 'unincorporated SA') on the Australian Bureau of Statistics SEIFA Index of Economic Resources (2016), where a lower score (eg, 1) denotes relatively lower access to economic resources in general, compared with other areas, available at https://www.abs.gov.au/ausstats/subscriber.nsf/log?openagent&2033055001%20-%20lga%20indexes.xls&2033.0.55.001&Data%20Cubes&5604C75C214CD3D0CA25825D000F91AE&0&2016&27.03.2018&Latest.

64 City of Salisbury, *Finance and Corporate Services Committee 14 June 2022, Item 2.1.5 2022/23 LTFP and Annual Business Plan and Budget Public Consultation Report*, p. 59, available at https://www.salisbury.sa.gov.au/assets/meetings/2022/06-June/finance-and-corporate-services-14-jun-2022/agendas/14062022-Agenda-and-Reports-Finance-and-Corporate-Services-Committee_2022-06-10-022038_sxvo.pdf.

65 Based on an analysis of the City of Salisbury's General Purposes Financial Statements (included in its Annual Report) for the period 2011-12 to 2020-21. Refer to Note (2a) for Rates and Note (5b) for Trade and Other Receivables.

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