Advice

Local Government Advice

City of Onkaparinga

February 2024

Enquiries concerning this advice should be addressed to:

Essential Services Commission
GPO Box 2605
Adelaide SA 5001

Telephone: (08) 8463 4444
Freecall: 1800 633 592 (SA and mobiles only)
E-mail: advice@escosa.sa.gov.au
Web: www.escosa.sa.gov.au

City of Onkaparinga

AT A GLANCE

OVERVIEW

The Essential Services Commission finds the City of Onkaparinga's current financial performance **potentially unsustainable**, but is taking steps towards a position of becoming more sustainable with projected small future surpluses on a consolidated basis, total expenses projected to increase at a rate lower than inflation, and the planned average rate increases of 2.7% p.a. per property over the next 10 years

RISKS IMPACTING SUSTAINABILITY

- If cost growth exceeds Council's long-term planning forecasts (and forecast CPI)
- The long-term financial plan and infrastructure asset management plan are not properly aligned or updated regularly
- Asset renewals are not undertaken at sufficient levels to meet the required service standards or community expectations
- Maintaining and holding assets which are excess to requirements and do not provide benefit to the broader community

CONTINUE

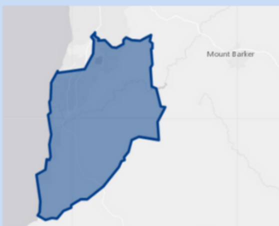
- Holding community consultations and conduct surveys to identify community priorities and desired service levels as part of the planning process for its strategic management plans
- Considering limiting any future increases in rates to no more than expected inflation

COMMISSION'S RECOMMENDATIONS

- Ensure that the long-term financial plan is prepared every year as required by the LG Act
- Update and coordinate the data in the long-term financial plan and annual budget by clearly identifying the annual inflation and other relevant assumptions as inputs to its projected revenue (including rates) and expenditure
- Provide an annual statement of financial sustainability as required by the LG Act
- Review the long-term financial plan annually including its 10-year projections and all relevant assumptions
- Consider options to increase income to move forward to a more financially sustainable position
- Monitor and report the growth in costs to ensure they are constrained within forecast levels
- Consider adopting cost savings targets and reporting the projected and actual cost savings in the annual budget and long-term financial plan
- Develop a staged plan and identify targets to reduce the high level of debt
- Identify and dispose of those assets that have reached the end of their useful lives, or are excess to requirements, to reduce debt and future liabilities
- Review the asset valuations, their remaining useful lives and corresponding depreciation schedules regularly to ensure that they reflect current values
- Develop and regularly update separate asset management plans for each asset group and coordinate the data in these asset management plans with the infrastructure asset management plans, budget and long-term financial plan
- Provide more funding for asset renewals rather than prioritising initiatives which involve new or upgraded infrastructure

KEY FACTS

- Population in 2021 was **175,204**
- Council covers **338 square kilometres**
- **81,989** rateable properties in 2022-23
- **$150.7 million of rate income** in 2022-23
- Value of assets held in 2022-23 equals **$2.52 billion**



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Glossary of terms

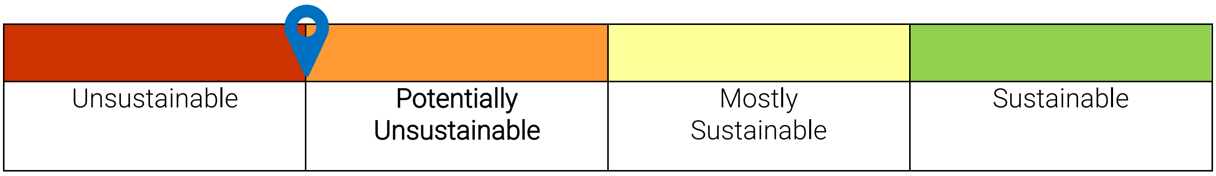
ABS	Australian Bureau of Statistics
AMP	Asset management plan (also called an IAMP)
Commission	Essential Services Commission, established under the *Essential Services Commission Act 2002*
CPI	Consumer Price Index (Adelaide, All Groups)
Council	City of Onkaparinga
CWMS	Community Wastewater Management System
ESC Act	*Essential Services Commission Act 2002*
F&A	Local Government Advice: Framework and Approach – Final Report
FTE	Full Time Equivalent
IAMP	Infrastructure and asset management plan (also called an AMP)
LG Act	*Local Government Act 1999*
LGA SA Financial Indicators Paper	Local Government Association of South Australia, Financial Sustainability Information Pa per 9 - Financial Indicators Revised May 2019
LGGC	Local Government Grants Commission
LGPI	Local Government Price Index
LTFP	Long-term financial plan
Regulations	*Local Government (Financial Management) Regulations 2011*
RBA	Reserve Bank of Australia
SACES	The South Australian Centre for Economic Studies
SEIFA	Socio-Economic Indexes for Areas
SMP	Strategic management plan
SG	Superannuation Guarantee
The scheme or advice	Local Government Advice Scheme

Legend: Low-risk Moderate-risk High-risk

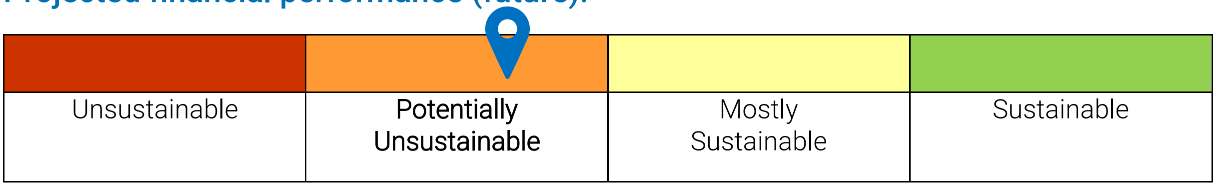
1 The Commission’s key advice findings for the City of Onkaparinga

The Essential Services Commission (**Commission**) considers the City of Onkaparinga (**Council**) to be in a **potentially unsustainable** financial position. However, the Commission notes that the Council is taking steps towards a position of becoming more sustainable, with projected small future surpluses on a consolidated basis, and total expenses projected to increase at a rate lower than inflation.

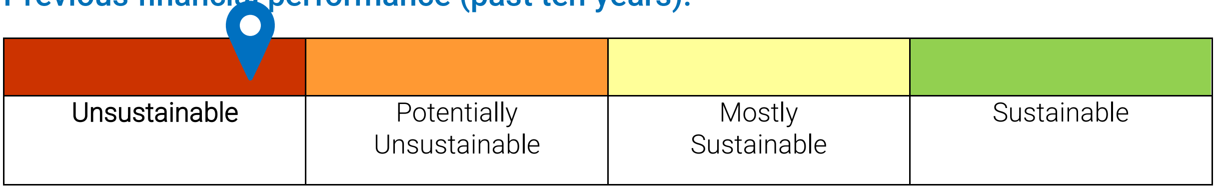
Current financial performance:



Projected financial performance (future):



Previous financial performance (past ten years):



Over the historical (10 year) period (from 2012-13 to 2021-22), the Council’s financial performance was considered **unsustainable**, due to it running an operating surplus for only three years during the 10-year period, with a negative average operating surplus ratio for this entire historic period.

The Council has also recorded an operating deficit for 2022-23, and has forecast another deficit for 2023-24, followed by its forecast of operating surpluses over the nine years from 2024-25 to 2032-33, which is anticipated to be achieved primarily through lower increases in operating expenses over that period.

Over the forecast period, the Council faces risks related to cost control and providing sufficient funding for infrastructure both to support the growth in rateable properties, and to undertake the asset renewal and replacement required to maintain the current level of services and/or higher levels of expenditure to address deferred asset renewal. Given these risks, its projected (future) performance is **potentially unsustainable**, with a forecast operating deficit in the short-term and the potential to return to an operating surplus in future.

Acknowledging the Council’s outlook, the Commission considers it would be appropriate for it to undertake the following steps to ensure it budgets prudently and transparently, continues to manage its cost base efficiently, plans its asset needs appropriately, renews its asset base to meet sustainable service levels, and continues to constrain the extent of further rate increases:

Budgeting considerations

1. Ensure that the long-term financial plan is prepared every year as required by the LG Act.
2. Update and coordinate the data in the long-term financial plan and annual budget by clearly identifying the annual inflation and other relevant assumptions as inputs to its projected revenue (including rates) and expenditure, to provide transparency to the community.
3. Start to provide an annual statement of financial sustainability as required by the LG Act.
4. Review its long-term financial plan annually (including its 10-year projections and all relevant assumptions (including for inflation)) to better inform its decision-making and any relevant consultation processes.

Continuing to provide evidence of ongoing cost efficiencies

5. Consider options to increase income to move forward to a more financially sustainable position.
6. Monitor and report the growth in costs, including employee expenses, to ensure costs are constrained to forecast levels to ensure the operating performance is not negatively impacted by a lack of cost control.
7. Consider adopting cost saving targets and reporting the projected and actual cost savings in the annual budget and long-term financial plan to provide evidence of controlling the growth in costs and achieving efficiencies across its operations and service delivery.
8. Develop a staged plan and identify targets to reduce the high level of debt, and report the achievements against targets in the annual budget and long-term financial plan.
9. Identify and dispose of those assets that have reached the end of their useful lives, or are excess to requirements, to reduce debt and exposure to future liabilities.

Refinements to asset management planning

10. Review the asset valuations, their remaining useful lives and corresponding depreciation schedules regularly to ensure they reflect current values, and incorporate this information into the strategic asset management plan and include these expenditure forecasts in the annual budget and annual long-term financial plan update.
11. Undertake the good practice of developing and regularly updating the individual asset management plans for each asset group and coordinate the data in these asset management plans with the infrastructure asset management plan, budget, and long-term financial plan.
12. Provide more funding for asset renewals rather than prioritising initiatives which involve new or upgraded infrastructure.
13. Continue to hold community consultations and conduct surveys to identify community priorities and desired service levels as part of the planning process for its strategic management plans.

Containing rate levels

14. Continue to consider limiting future increases in rates to no more than expected inflation to reduce any emerging affordability risk in the community.

2 About the advice

The Essential Services Commission (**Commission**), South Australia's independent economic regulator and advisory body, has been given a role by the State Parliament to provide advice on material changes proposed by local councils in relation to elements of their strategic management plans (**SMPs**), and on the proposed revenue sources, including rates, which underpin those plans.[1]

One of the main purposes of the Local Government Advice Scheme (**advice** or **the scheme**) is to support councils to make 'financially sustainable' decisions relating to their annual business plans and budgets in the context of their long-term financial plans (**LTFPs**) and infrastructure and asset management plans (**IAMPs**)[2] – both required as part of a council's SMP.[3] Financial sustainability is considered to encompass intergenerational equity,[4] as well as program (service level) and rates stability in this context.[5] The other main purpose is for the Commission to consider ratepayer contributions in the context of revenue sources, outlined in the LTFP.[6] In addition, the Commission has discretion to provide advice on any other aspect of a council's LTFP or IAMP it considers appropriate, having regard to the circumstances of that council.[7]

The first cycle of the scheme extends over four years from 2022-23 to 2025-26, and the Commission has selected 17 councils for advice in the second scheme year (2023-24), including the Council.

This report provides the Local Government Advice for the Council in 2023-24.

The Council is obliged under the *Local Government Act 1999* (**LG Act**) to publish this advice and its response, if applicable, in its 2024-25 Annual Business Plan (including any draft Annual Business Plan) and subsequent plans until the next cycle of the scheme.[8] It does not need to publish the attachment to the advice (these will be available with the advice on the Commission's website[9]), nor is it compelled under the LG Act to follow the advice.

The Commission thanks the Council for meeting with Commission staff and for providing relevant information to assist the Commission in preparing this advice.

2.1 Summary of advice

In general, the Commission finds the Council's current financial position to be **potentially unsustainable** but notes that it is taking steps towards a position of becoming more sustainable, with projected operating deficits or small future surpluses on a consolidated basis, and total expenses projected to increase at a rate lower than inflation. The Council faces risks in its journey to improve its operating performance over the forecast period which includes any unplanned increases in expenses which may arise, low levels of expenditure on the renewal and replacement of its existing assets, or increased maintenance and repair costs to maintain the level of services to deliver.

The Council ran an operating surplus for only three years during the 10-year historical period from 2012-13 to 2021-22, and has forecast an average operating surplus ratio for the forecast period from 2024-25 to 2032-33 of 2.83 percent. The Council is projected to achieve a return to surplus over the forecast period because total income is forecast to increase at an annual average rate of 2.6 percent (in line with

1 Amendments to the LG Act (s122(1c) to (1k) and (9)) specify the responsibilities for the Commission and local councils for the Local Government Scheme Advice. The Commission must provide advice to each council in accordance with the matters outlined in s122(1e), (1f) and (1g).
2 Commonly referred to as asset management plans.
3 The objectives of the advice with reference to a council's LTFP and IAMPs are presented under LG Act, s122(1g). LG Act s122(1) specifies the requirements of a council's SMP, including the LTFP and IAMPs.
4 'Intergenerational equity' relates to fairly sharing services and the revenue generated to fund the services between current and future ratepayers.
5 Commission, *Framework and Approach – Final Report*, August 2022, pp. 2-3, available at www.escosa.sa.gov.au/advice/advice-to-local-government.
6 LG Act s122(1f)(a) and (1g)(a)(ii).
7 LG Act s122(1f)(b) and (1g)(b).
8 LG Act s122(1h).
9 The Commission must publish its advice under LG Act s122(1i)(a).

average annual forecast inflation of 2.6 percent), and expenses at the lower annual average rate of 1.8 percent.

The main source of Council income over both the historic period and the forecast period is rates. Rates income increased at an annual average of 1.9 percent,[10] and contributed 79 percent of income over the historic period. Rates are forecast to increase at the average annual rate of 3.6 percent[11] (a full percentage above average forecast inflation) over the forecast period to contribute nearly 83 percent of income, indicating that the Council is relying more heavily upon rates for income over the 10-year forecast period.[12]

Over the historic period, the main contributors to expenses (at 39 percent of total expenses each) were employee costs (which increased at an annual average rate of 4.8 percent per annum), and 'materials, contracts and other' expenses (which increased at an annual average rate of 3.2 percent per annum).

Expenses are forecast to increase at an average annual rate of only 1.8 percent over the forecast period, with employee costs increasing at an average rate of 2.2 percent (to contribute over 40 percent of expenses), and materials to increase at an average annual rate of 2.5 percent (to contribute nearly 39 percent of expenses). Depreciation, which was 19.6 percent of total expenses over the historic period, is forecast to decrease by an annual average of 0.1 percent over the forecast period, and contribute only 18.6 percent of expenses.

The operating surplus ratio over the historic period sat below the target range for all but three years of the period, with an average of negative 0.01 percent for the 10-year period.[13]

The Commission has some reservations about the Council's ability to contain increases in expenses to these low forecast levels to return to, and maintain an operating surplus, especially because projections of the rate of increase to its expense categories sits below forecast inflation over the period. To achieve cost control, the Council should be developing cost reduction/control plans, with annual cost reduction targets for each area of its operations, and report achievements against these targets in both its budget and LTFP. The absence of cost control plans and targets in its current budget and LTFP increases the risk that the Council might be required to reduce the level of services it delivers to produce and maintain the operational surpluses over the forecast period.

The net financial liabilities ratio (a measure of the Council's indebtedness) sits within the LGA target range of 0 to 100 percent over both the historic and forecast periods.

Asset renewal expenditure was volatile throughout the historic period from 2012-13 to 2021-22, and the asset renewal funding ratio (net) sat within (or above) the target ratio range of 90 to 110 percent for only two years of the historical period.[14] The asset renewal funding ratio improves over the forecast period, with an average value of 92.1 percent, which sits at the lower end of the LGA target range of 90 to 110 percent, although planned asset renewal levels are less than those in the IAMP.

It is not clear from the budget and LTFP what strategies the Council plans to employ to reduce debt by such substantial amounts to achieve sustainability, while at the same time ensuring that the appropriate level of assets renewal expenditure is maintained.

It is understood that the Council is currently updating its LTFP, which ideally should include a range of strategies to reduce debt while not reducing service levels. Strategies should include the rationalisation

10 Which includes the low rates of growth in rates income over the period 2019-20 through 2021-22, when the Council provided rates relief during the pandemic.

11 Which includes an annual increase in rateable properties of 0.9 percent and an average annual increase in rates per property of 2.7 percent, only 0.1 percent above average forecast inflation.

12 This is despite the Council's stated intention to reduce its reliance for income on rates.

13 The main reason the operating surplus ratio sat below the LGA lower target of 0 over the later years is because of the pandemic rates relief, which meant that income from rates increased by an annual average only 1.2 percent during 2020-21 and 2021-22, which includes an increase of over 1.4 percent in the number of properties over the two years.

14 The Council has advised that from 2020-21, it used gross asset renewal expenditure (before the sale of replaced assets) in its assessment of its asset renewal funding ratio, which shows marginally better asset renewal performance.

and sale of assets, including the disposal of aged assets that incur high maintenance and renewal costs, over the term of the new LTFP.[15]

2.2 Detailed advice findings

The next sections summarise the Commission's more detailed observations and advice findings regarding the Council's material changes to its 2023-24 plans (compared with the previous year's plans), its financial sustainability (in the context of its long-term operating performance, net financial liabilities, and asset renewals expenditure), and its current and projected rate levels.

In providing this advice, the Commission has followed the approach it previously explained in the Framework and Approach – Final Report (F&A). The attachment explores these matters further.[16]

2.2.1 Advice on material plan amendments in 2023-24

Key Points:

⚠ A decline in operating performance in the updated draft long-term financial plan is projected with a surplus of $51.9 million compared to a surplus of $53.2 million in the approved 2022-23 long-term financial plan.

⚠ A deficit of $1.93 million is forecast in 2023-24 (an improvement of 57 percent from the projected deficit of $4.53 million in 2022-23 (unaudited). Total income is forecast at $204.33 million, and expenses at $206.27 million.

The Commission has compared the amendments to the Council's 2023-24 budget and forward projections that are included in its updated 2022-23 LTFP estimates.[17]

The Council budgeted for a decline in operating performance in the updated[18] 2022-23 LTFP, with a surplus of $52.9 million compared to a surplus of $53.2 in the approved 2022-23 LTFP. In aggregate, the projections in the approved and the updated 2022-23 LTFPs (that is, over the nine-year comparative period to 2031-32), indicate that the Council's cumulative performance deteriorates by $0.3 million or negative 0.6 percent.

The material changes are attributable to an alignment of rates income to the actual March 2023 (Adelaide) CPI of 7.9 percent, capital expenditure to the construction output price index,[19] increases in capital expenditure due to external funding, and an updated projected debt position.

The Council has planned for a deficit of $1.9 million in 2023-24, which is an improvement of 57 percent from the deficit of $4.5 million in 2022-23 (unaudited). Total income is forecast at $204.3 million, and expenses at $206.3 million.

The Council has aligned its rates increases to the most recent CPI of 7.9 percent for the 12 months ended March 2023.[20]

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15 As stated in the 2023-24 budget p. 41 and as required under the LGA Act.
16 The attachment will be available on the Commission's website with the Advice.
17 The last LTFP to be approved by the Council was the 2022-23 LTFP, which was approved in July 2022. The Council has not produced an approved LTFP since then because the newly elected members (in November 2022) placed a priority upon drafting and approving the 2023-24 budget.
The LTFP provided by the Council in the Financial Template is based upon the updated data aligned with the 2023-24 Budget.
18 But not approved, with the data included in the Annual Business Plan 2023-24, Appendix 8.
19 See https://www.abs.gov.au/statistics/economy/price-indexes-and-inflation/producer-price-indexes-australia/latest-release#construction. Construction costs usually increase at a rate higher than the CPI, e.g. 5.4 percent for the 12 months ended December 2023 compared to the consumer price index outcome of 4.1 percent.
20 See City of Onkaparinga Annual Business Plan 2023-24 p. 7.

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Some of the amendments, compared to the LTFP, include:

- An increase in income to adjust for inflation in March 2023, and higher income from user charges due to increased usage of facilities post COVID-19.
- An increase in employee costs in line with the higher CPI outcome for March 2023, and the reclassification of agency employees from 'materials, contracts and other' expenses to employee costs.
- An increase in expenditure on Infrastructure, property, plant and equipment due to significant asset revaluations to reflect increases in the building price index and replacement costs.
- Increased expenditure on new/upgraded assets with funding from the State and Federal Governments.
- An increase of $3.5 million in depreciation expenses.
- A reduction in borrowings and interest costs due to $30 million of grant funding received in advance.
- The inclusion in income for net gain– equity accounted Council businesses for the Council's 55 percent equity share in the Southern Region Waste Resource Authority (SRWRA - a joint venture with the City of Marion and the City of Holdfast Bay) not previously captured in the LTFP forecasts.[21]

The Commission notes that the Council's stated assumptions for indexation in its updated 2022-23 LTFP[22] are not fully transparent, because the assumptions included in the 2023-24 Budget Appendix 7 only relate to the current financial year. The key assumptions for the 2022-23 LTFP[23] (the last complete and adopted LTFP) are transparent (although outdated), and only the 2023-24 assumptions have been updated in the updated data included in Appendix 7 of the 2023-24 budget.

Given the need for the Council to reduce indebtedness and develop efficiencies to reduce expenses and the impact of inflation on the community, the Commission found it would be appropriate for it to:

1. Ensure that the long-term financial plan is prepared every year as required by the LG Act.
2. Update and coordinate the data in the long-term financial plan and annual budget by clearly identifying the annual inflation and other relevant assumptions as inputs to its projected revenue (including rates) and expenditure, to provide transparency to the community.
3. Start to provide an annual statement of financial sustainability as required by the LG Act.
4. Review its long-term financial plan annually (including its 10-year projections and all relevant assumptions (including for inflation)) to better inform its decision-making and any relevant consultation processes.

The Council adopted its 2023-24 Annual Business Plan and Budget on 17 July 2023, and updated the data included in the 2022-23 LTFP[24] approved on 4 July 2022,[25] rather than preparing a 2023-24 LTFP.

21 Council rejected a proposal to privatise their CMWS due to community opposition in November 2023.
22 As updated and included in the 2023-24 budget.
23 See Appendix 8 of the City of Onkaparinga 2022-23 LTFP.
24 The 2022-23 LTFP, which was approved in July 2023.
25 This includes an update for Phases 1 and 2 of the Local Roads and Community Infrastructure (LRCI) stimulus program, with Phase 3 works underway (to be completed by the end of June 2024). See City of Onkaparinga Strategic Asset Management Plan Update 2022-23 p. 8.

The Commission observes that the Council noted risks to its estimates arising from the impact of inflation upon expenditure. In addition, there are no current regulatory requirements for it to publish its LTFP projections with its annual business plan and budget, although the Council did not provide the updated LTFP projections for the 10-year forecast period elsewhere.[26]

2.2.2 Advice on financial sustainability

Operating performance

Key Points:

- ⚠ Operating surpluses experienced in only three years during the historical period 2012-13 through to 2021-22, with a forecast return to operating surpluses in nine years out of 10 in the forecast period (2024-25 through 2032-33).
- ⚠ The projected turnaround in forecast operating performance is as a result of increasing rates income by the forecast CPI plus growth in the number of rateable properties, and keeping the increase in expenses below the forecast inflation rate over the period.
- ⚠ From 2012-13 through to 2021-22, total expenses increased at an average annual rate of 4.3 percent, but are forecast to increase by only 1.8 percent over the next 10 years. It is noted that there are risks to the Council's operating performance if the anticipated moderate increase in expenses is not met.
- ✔ The Council has attempted to achieve budget savings of $8 million as referred to in its 2023-24 budget.

The Council ran an operating surplus for only three years during the historical period from 2012-13 to 2021-22 but forecasts a return to an operating surplus during the last nine years of the forecast period (2024-25 through 2032-33). The Council expects this will be achieved by increasing rates income by the forecast CPI plus growth in number of rateable properties,[27] while keeping the increase in expenses below the forecast inflation over the period.

The Council saw an annual average increase in operating income of 4.1 percent over the historic period. Its primary source of income over the period was rates, which was 79 percent of total income over the historic period,[28] which increased by an average of 1.9 percent per annum[29] (close to average inflation of 2.0 percent). This was followed by 'grants, subsidies and contributions' at 12.5 percent of income, which were volatile, and increased by an annual average of 7.3 percent.[30]

Over the historic period from 2012-13 to 2021-22, total expenses increased at an average annual rate of 4.3 percent, with employee costs and 'materials, contracts and other' expenses contributing an equal share of expenses at 39 percent. While employee costs increased by an average of 4.8 percent per annum,[31] 'materials, contracts and other' expenses increased by an average of 3.2 percent, both above average annual inflation for the period of 2.0 percent. At the same time, depreciation, which was nearly

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26 The Council did not publish an approved 2022-23 LTFP that contains the updates consistent with the 2023-24 budget data. The new Council is required by the LG Act to prepared and approve a new LTFP and IAMP within two years of the council election.

27 The number of rateable properties is forecast to increase at an annual average rate of 0.9 percent over the forecast period.

28 The Council's own source income was 88 percent of total income in the 2021-22 financial year, compared to the state average of 86 percent. See SA Local Government Grants Commission Report 2 – Sources of Operating Income by Council for 2021-22 Financial Year.

29 With the increases in income from rates due to only the growth in rateable properties in 2020-21 because the Council voted not to increase rates that year due to the pandemic.

30 As can be expected when funding is linked to specific projects.

31 As FTEs increased from 639 FTE in 2012-13 to 714 FTE in 2021-22, an increase of nearly 12 percent over the period.

20 percent of expenses, also increased at a rate above inflation, with an average of 6.2 percent per annum.

Over the forecast period of 2024-25 to 2032-33, total income is forecast to increase in line with the average forecast inflation rate, at an annual average of 2.6 percent, with income from rates increasing by an average of 3.6 percent per annum,[32] which includes growth in line with average inflation and growth in the number of rateable properties at 0.9 percent.

The income from grants, subsidies and other income is forecast to decrease by an annual average of 2.3 percent per annum, which shifts the source of income slightly away from grants, and towards rates and user charges.

While expenses increased at an average annual rate of 4.3 percent over the historic period (more than twice the rate of historic inflation), the Council has forecast that expenses will increase at an annual rate of only 1.8 percent, which is 0.8 percentage points below the forecast average inflation. This is due in part to forecast employee costs, which are over 40 percent of total expenses, increasing slightly below forecast inflation at an annual average rate of 2.2 percent, and by increases in the costs of 'materials, contracts and other' expenses (nearly 39 percent of expenses), forecast to increase at an average annual rate of 2.5 percent, and depreciation (at 18.5 percent of expenses), [33] which is forecast to decrease at an average annual rate of 0.1 percent.[34]

The Commission considers it problematic that the Council's expenses are forecast to increase at a rate lower than forecast inflation, when construction expenses increased historically at a rate higher than inflation[35] and are generally expected to continue to do so over the forecast period.[36] Combined with the continuing low levels of asset renewal, this suggests that the Council might be in a position where it is required to reduce the level of services it delivers, to maintain the operational surplus forecast from 2024-25 through to 2032.[37] This is due to it having not provided adequately for this expenditure in its budget and LTFP, or it being able to find further cost savings or efficiencies in delivering those services.

The operating surplus ratio fluctuated over the historic period, with negative values (i.e. below the LGA lower target of 0) for all but three years over the historic period, and an average value of negative 0.01 percent for the period, which indicates that the Council was not operating sustainably over the historic period.

The main reason the operating surplus ratio sat below the target range over the later years of the historic period, is because the Council did not increase rates (except for growth) in 2020-21 (at the start of the pandemic) and kept the increase below the inflation rate in 2021-22, while increasing expenditure with stimulus programs. Due to compounding effects, the deficit widened, which ensured that the operating surplus ratio remained below the lower target of 0 percent.

However, over the forecast period 2023-24 through to 2032-33, the Council has forecast a return to surplus from 2023-24 onwards, with an average operating surplus of 2.8 percent.

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32 The Council's rates increase policy over the three years 2019-20 through 2021-22, although it gave rates relief during the pandemic, was a major reason the Council had an operating deficit over those years.

33 The council has indicated in communications in December 2023 that depreciation has been a significant cost pressure due to 'significant asset revaluations over the last few years.

34 This seems counter-intuitive, because depreciation expenses should not be decreasing as expenditure on materials, contracts and other expenses increase, especially with expenditure due to the current externally funded projects. After decreases of negative 3.3 percent in 2023-24 and negative 7.2 percent in 2024-25, depreciation increases by an average of only 1.2 percent for the last eight years of the forecast period. This suggests that the levels of depreciation have not been updated and included in the current LTFP.

35 As per the construction price index see https://www.abs.gov.au/statistics/economy/price-indexes-and-inflation/producer-price-indexes-australia/latest-release#construction.

36 See https://www.propertycouncil.com.au/property-australia/labour-the-biggest-challenge-to-construction-costs-slattery#:~:text=Slattery%20expects%20costs%20escalation%20to,the%20back%20of%20infrastructure%20spend .

37 In communications in December 2023, the Council advised that they are 'aiming to break even within the next 2 years (before the current term of council)' and that that they are 'identifying opportunities to improve the operating position' using the strategies of 'reducing reliance on rates revenue and reviewing costs'.

The Council has attempted to achieve budget savings (e.g. the $8 million mentioned in the 2023-24 budget[38]), and it might be beneficial for the Council to develop cost reduction plans with annual cost reduction targets for each area of operations that is included in, and with achievements reported in its budgets[39] to hold itself accountable, and provide transparency to its ratepayers.

To ensure the Council achieves best practice in line with the LGA targets, the Commission considers it appropriate for the Council to:

5. **Consider** options to increase income to move forward to a more financially sustainable position.
6. **Monitor** and **report** the growth in costs, including employee expenses, to ensure costs are constrained to forecast levels, to ensure the operating performance is not negatively impacted by a lack of cost control.
7. **Consider** adopting cost saving targets and reporting the projected and actual cost savings in the annual budget and long-term financial plan, to provide evidence of controlling the growth in costs and achieving efficiencies across its operations and service delivery.

Net financial liabilities

Key Points:

- Between 2012-13 and 2021-22, the net financial liabilities ratio averaged 60.6 percent.
- Between 2023-24 and 2032-33, the net financial liabilities ratio is forecast to average 67.1 percent.

The net financial liabilities ratio[40] sits within the LGA target range for the entire historical and forecast periods, with an average value of 60.6 percent for the historical period, and 67.1 percent for the forecast period. Although the value of the ratio increased somewhat over these time periods, peaking at 83.7 percent in 2023-24, the ratio indicates that the Council was able to finance its financial obligations from operating income over both the historical and forecast periods.

It is not clear from the budget and LTFP what strategies the Council plans to employ to reduce debt by such substantial amounts to assist it to return to a sustainable position, while at the same time, ensuring that the appropriate level of asset renewal expenditure is maintained. The Commission notes that the Council is currently updating its LTFP, which ideally should include a range of strategies to reduce debt, while not reducing service levels. This should include the rationalisation and sale of assets, including the disposal of aged assets that incur high maintenance and renewal costs, over the term of the new LTFP.[41]

Along with the reduction in borrowings and total liabilities, cash and cash equivalents at year end, are forecast to increase from 2023-24 onwards at an average of 8.0 percent per annum, a rate stronger than forecast increases in both income and repayment of borrowings.

For the Council to strive towards achieving and maintaining financial sustainability, the Commission considers it appropriate for the Council to:

[38] See City of Onkaparinga Annual Business Plan and Budget 'From the Mayor' p. 4.
[39] Which is also linked to projects undertaken during each financial year.
[40] 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).
[41] As stated in the 2023-24 budget (p. 41) and as required under the LGA Act.

8. **Develop** a staged plan and identify targets to reduce the high level of debt and report the achievements against targets in the annual budget and long-term financial plan.
9. **Identify** and dispose of those assets that have reached the end of their useful lives, or are excess to requirements, to reduce debt and exposure to future liabilities.

Asset renewals expenditure

Key Points:

- Between 2012-13 and 2021-22, the asset renewal funding ratio averaged 78 percent.
- The forecast asset renewal funding ratio over the next 10 years is projected to average 92.1 percent.
- To facilitate an improved understanding of its asset base, current asset condition, and the service levels required, the Council should develop and regularly update separate asset management plans for each of its major asset groups that are linked to the asset register, and coordinate this data with the SAMP, budget and LTFP, which it does not currently have in place.
- The net asset renewal expenditure in the LTFP is not aligned to the IAMP renewal expenditure. This aspect of expenditure should be addressed in the current LTFP to ensure that the Council evaluates and addresses its asset renewal requirements.
- Council should identify assets that are obsolete or no longer required, with the intention of disposing of those assets to reduce maintenance and/or repairs costs and exposure to future liabilities.

The asset renewal funding ratio – renewal expenditure based (net), was volatile throughout the 10-year historic period, and averaged 78 percent over the period,[42] which lies below the lower end of the LGA target ratio of 90 percent. This indicates that the Council has failed to renew or replace its existing infrastructure assets to maintain the level of services over the historical period.

The Council must have a solid understanding of its asset base, with up-to-date condition assessments and knowledge of the service levels required for each asset.[43] Since the Council is also still growing, the Council faces the continuing need to service new subdivisions as well as the redevelopment of older subdivisions, and the LTFP forecast funding should accommodate these asset management requirements.

To facilitate an improved understanding of its asset base, current asset condition, and the service levels required, the Council should draft separate asset management plans for each of its major asset groups that are linked to the asset register, and coordinate this data with the SAMP, budget and LTFP.[44] These asset group management plans should then be updated regularly in line with the annual review and update of the SAMP.

Over the forecast period, the average value of the asset renewal funding ratio (net) improves, and the average for the period of 92.1 percent sits within the LGA target range of 90 to 110 percent. This means

42 The Council advised in communications with the Commission that it decided to defer capital expenditure in some historic years to assist with the budget position, which has impacted on the asset renewal funding ratio.

43 The Council is migrating its assets register data to 'One Council' and anticipates that this will assist in making informed decisions regarding maintenance, repairs and asset replacements. See City of Onkaparinga Strategic Asset Management Plan Update 2022-23 p. 2.

44 This is supported in the KPMG City of Onkaparinga Strategic Asset Management report September 2022 p. 6.

that the Council plans to undertake asset renewal at levels below that as set out in the IAMP.[45] The IAMP assists the Council manage its infrastructure and other assets to an agreed level of service, however, as the Council advised,[46] the net asset renewal expenditure in the LTFP is not aligned to the IAMP renewal expenditure, and this aspect of expenditure should be addressed in the current LTFP to ensure that the Council evaluates and addresses its asset renewal requirements.

Over the historic period, the asset renewal funding ratio (depreciation based)[47] has an average value of 71.1 percent for the period, and only sits within the target range of 90 to 110 percent for one year out of the 10 (in 2016-17).[48] Although it improves somewhat over the forecast period, it only sits within the 90 to 110 percent target range over the last four years. Along with the increasing levels of cash over the forecast period,[49] this indicates that the Council might be planning to spend too little from 2023-24 through 2028-29 to maintain the level of services, and risks incurring high repairs and maintenance expenses to maintain its existing assets, which is a continuation of the expenditure pattern over the historic period.[50]

This trend can also be seen in the relationship between net asset renewal and depreciation, where the values of net asset renewal expenditure remain below the levels of depreciation for all but two years of the historic and forecast periods (i.e., 2016-17 and 2032-33). This underspending on asset renewal is reflected in both the increasing levels of cash held at year end seen over the forecast period,[51] and in the renewal/replacement gap (both IAMP renewals based and depreciation gap), which covers 2013-14 through to 2032-33.[52]

Although the Council explained that the low levels of asset renewal expenditure planned over 2022-23 and 2023-24 are due to the Council prioritising the completion of projects funded by the State and Commonwealth Governments before the 30 June 2024 deadline,[53] this is followed by increased expenditure from 2024-25 on the renewal and replacement of assets, which does not compensate for the earlier low levels of expenditure, and the requirement to address the future stream of liabilities arising from the recent expenditure on new assets.[54]

The effects of the deficit of net asset renewal relative to IAMP renewal over the historic period continues into the forecast period, and is also seen as a drop in the asset value per property after 2025-26. It is

45 The Council advised in communications in December 2023 that the LTFP adopted in February 2021 and aligned to the financial forecasts in the SAMP, and in the 2022-23 update, a decision was made to reduce the capital forecasts for the Local Roads and Community Infrastructure Program stimulus funding, which has created a misalignment between the SAMP and LTFP.

46 In communications with the Commission in December 2023.

47 Where asset renewal/replacement expenditure is divided by the depreciation expenses.

48 As mentioned earlier, the Council advised that it deferred some capital expenditure to improve the annual budget outcome over the latter years of the historical period. Since the Council advised it has limited resources, it has now prioritised the state and federally funded projects that it had committed to deliver within a short timeframe (by the end of 2024-25). As a consequence, other planned capital expenditure was deferred until after 2024-25.

49 As discussed in the previous section and shown in the chart 'Cash and cash equivalents at the end of the period.'

50 Which, according to the Council, is due to a reduction in assets renewal expenditure in 2022-23. The Council recognises that the current LTFP and AMPs are now not consistent and expects that capital renewal expenditure will be re-aligned to the AMPs during the current update of the AMPs. See Materials Amendments Reasons for asset renewal funding ratio in the Financial Template.

51 Over the forecast period, the value of cash and cash equivalents at year end is forecast to grow steadily at an average annual rate of 8 percent, which sits well above the forecast annual growth in income of 2.57 percent. This can be attributed to the gap between depreciation and the lower levels of expenditure on the renewal and replacement of assets. Expenditure on the renewal and replacement of assets dropped by an average of 2.3 percent per annum over the historical period. Although this expenditure is forecast to increase by 4.8 percent per annum over the forecast period, it is calculated from a low base. New and upgraded capital expenditure declines in 2024-25 and 2025-26, and then has a value of '0' for the rest of the forecast period.

52 See above.

53 Funding made available to build new assets requires an increased maintenance budget, which is currently not funded, and these new assets will require renewal in the future.

54 Along with the initial expenditure on new assets (even those externally funded), the Council should consider the future stream of liabilities created.

imperative that an update of the IAMP is completed to enable the Council to reassess its asset renewal plans.

Along with the review of its assets, the Council should be mindful of identifying assets that are obsolete or no longer required, with the intention of disposing of any assets that are no longer required. This rationalising of assets will not only potentially add to Council revenue, but also reduce maintenance and/or repair costs that would have been incurred.[55]

To align the average rate of consumption of its assets, as indicated by its depreciation expenses, and the annual spending on the renewal of its asset base over time, the Commission considers that it would be appropriate that the Council to:

10. **Review** the asset valuations, their remaining useful lives and corresponding depreciation schedules regularly to ensure they reflect current values, and incorporate this information into the strategic asset management plan and include these expenditure forecasts in the annual budget and annual long-term financial plan update.
11. **Undertake** the good practice of developing and regularly updating the individual asset management plans for each asset group and coordinate the data in these asset management plans with the infrastructure asset management plan, budget, and long-term financial plan.
12. **Provide** more funding for asset renewals rather than prioritising initiatives which involve new or upgraded infrastructure.
13. **Continue** to hold community consultations and conduct surveys to identify community priorities and desired service levels as part of the planning process for its strategic management plans.

2.2.3 Advice on current and projected rate levels

Key Points:

Rate revenue per property increased at an average rate of 3.1 percent per annum over the 10-year historic period, which is more than 1.5 times the average rate of inflation (2.0 percent over the historic period).

The forecast rate increase between 2023-24 to 2032-33 is 2.7 percent per property per annum, which is generally in line with the RBA-Inflation forecast over the period.

Affordability risk among the community for the further rate increases appears to be low on balance, when considering:

- the Council's relative average socio-economic indexes for areas (SEIFA) economic resources ranking,
- the current relatively low average rates (across most ratepayers), and
- the forecast increases in rates of 2.7 percent per rateable property, which sits slightly above forecast inflation over the term of the LTFP.

The Council currently has rates that sit just below the average for the State of South Australia, with average rates per property in 2020-21 calculated at $1,663 per rateable property, compared to the state average of $1,665 per property.[56]

[55] Of course, any program for the disposal of assets will require community consultation, e.g., the Council's water assets decision in November 2023.

[56] As calculated by the SA Local Grants Commission and included in Finance Report 6 – Council Rating Arrangements for 2021-22 financial year.

The Commission notes that rates for the Council are close to the average for all councils in South Australia, and that the SEIFA[57] ranking for the Council community is in the middle of the ranking for advantage and disadvantage,[58] which means that the ratepayers may have the capacity to pay an average level of rates.

The Council's rate revenue per property increased at an average rate of 3.1 percent per annum over the 10-year historic period,[59] which is more than 1.5 times the average rate of inflation (2.0 percent over the historic period) and are forecast to increase by an average of 2.7 percent per annum over the forecast period, which is slightly above the rate of forecast inflation (of 2.6 percent). This means that average rates per property are projected to remain around the mid-range of rates in the State.

The Council stated that it intends to increase rates over the forecast period generally in line with the CPI,[60] with forecast rates increasing at an annual average of 2.7 percent over the 10-year forecast period.

While the current economic environment is putting more pressure on many communities' capacity to pay for further rate increases, including those of the Council, on balance, the affordability risk among the Council's community for these further rate increases appears to be low, when considering:

- the Council's relative average socio-economic indexes for areas (SEIFA) economic resources ranking for the Onkaparinga Council area[61] of 37 of 71, which places residents in the middle range of advantage and disadvantage,
- the historic average increases in rates of 3.1 percent per annum, which is above the average annual inflation increase of 2.0 percent per annum for the period,[62]
- the current average level of rates (across most ratepayers), which rank 32nd out of 72 Councils when ranked from highest to lowest rates in South Australia and sitting slightly below the average rates in the state,[63] and
- the forecast increases in rates of 2.7 percent per rateable property, which sits slightly above forecast inflation over the term of the LTFP.[64]

Given historical rate increases and the community's apparent capacity to pay, it would be appropriate for the Council to:

57 The SEIFA index is the relative socio-economic indexes for areas economic resources ranking, and the ranking for Onkaparinga is 37 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 (2021), where a lower score (e.g., 1) denotes relatively lower access to economic resources in general, compared with other areas, with information available at Socio-Economic Indexes for Areas (SEIFA), Australia, 2021 | Australian Bureau of Statistics (abs.gov.au)

58 See https://councilsinfocus.sa.gov.au/councils/city_of_onkaparinga for comparative rates information.

59 Which includes the low increases approved during the period 2019-20 through 2021-22 to provide relief during the pandemic.

60 See City of Onkaparinga Budget 2023-24 p. 39.
Note that the Council refers to rates income increasing by 'CPI plus growth', which means that the total income from rates is forecast to increase due to both increases in inflation and the growth in the number of rateable properties.

61 The Onkaparinga Council area is ranked 37 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 (2021), where a lower score (e.g., 1) denotes relatively lower access to economic resources in general, compared with other areas, with information available at Socio-Economic Indexes for Areas (SEIFA), Australia, 2021 | Australian Bureau of Statistics (abs.gov.au).

62 Which includes the rates relief granted by the Council during 2020-21 and 2021-22.

63 With average rates in Onkaparinga Council calculated at $1663 per property, compared to the state average of $1665 per property as calculated by the SA Local Government Grants Commission in Finance Report 6 – Council Rating Arrangements for 2021-22 financial year.

64 That is, an average annual increase per property of 2.69 percent compared to a forecast annual average rate of 2.6 percent.

14. **Continue** to consider limiting future increases in rates to no more than expected inflation to reduce any emerging affordability risk in the community.

2.3 The Commission's next advice and focus areas

In the next cycle of the scheme, the Commission will review and report upon the Council's:

- ongoing performance against its current LTFP estimates,
- the identification of opportunities for cost savings, including the disposal of assets that are surplus to requirements to reduce debt, and exposure to future liability streams,
- achievement of cost savings to reduce debt, including the sale of assets, and reporting savings achieved in its plans,
- the reassessment of its planned asset renewal and replacement expenditure, and
- the Council's efforts to minimise any emerging affordability risks.

The Essential Services Commission
Level 1, 151 Pirie Street Adelaide SA 5000
GPO Box 2605 Adelaide SA 5001
T 08 8463 4444
E escosa@escosa.sa.gov.au | W www.escosa.sa.gov.au