Advice

Local Government Advice - Attachment

District Council of Lower Eyre Peninsula

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

Table of contents

A The Commission's approach

In providing the Advice for the District Council of Lower Eyre Peninsula (**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]

- 2023-24 Annual Business Plan adopted 19 July 2023
- Asset Management Plan 2023-2032 adopted 19 July 2023
- 2023/24 Declared Rates
- Long Term Financial Plan 2021-2030 Review 2 (April 2023)
- Long Term Financial Plan 2021-2030 Review 1 (March 2022)
- Strategic Plan 2020-2030

The Commission notes that the Council's asset base is covered by its existing asset management plan (**AMP**), and that most asset revaluations for those assets have been carried out within the last four years. The Commission further notes that the Council has not met its legislated obligation of providing a long-term financial plan for ten years in accordance with Section 122(1)(a) of the *Local Government Act 1999*.

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 financial plans (**LTFPs**),[4] it has also considered the Council's performance in that context. Findings regarding the content of the District Council of Lower Eyre Peninsula'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 2023-24 LTFP forecasts for 2023-24 to 2029-30, as well as its 2022-23 LTFP forecasts, and historical financial data and number of rateable properties and council staff (Full Time Equivalent (**FTE**)) numbers from 2012-13 onwards.[6] [7] All charts and tables in the Advice are primarily sourced from these datasets, (noting that the seven year forecast rather than the required 10 year forecast, leaves some graphs incomplete). In addition, the Commission has reviewed the Council audit committee reports, and other public information, as appropriate.

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*. 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.

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

7 The Council's estimates for the 2022-23 financial year, relied on at the time of preparing this advice, were unaudited.

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 2012-13, and then projections of this series from 2023-24 based on the Reserve Bank of Australia (**RBA**) (Australia-wide) inflation forecasts (to the June quarter 2026), and the midpoint of the RBA target range (2.6 percent) thereafter.

Finally, in formulating this Advice, the Commission has had regard to the circumstances of the District Council of Lower Eyre Peninsula, including its location as a regional council, its income level ($16.8 million) and the size of its rates base (more than 4,207 ratepayers).[8]

Summary of the District Council of Lower Eyre Peninsula's financial sustainability performance and the Commission's risk assessment

Financial sustainability indicators:	Last 10 years from 2012-13 (Actual performance)		2022-23 estimate	Next 7 years from 2023-24 (Council forecasts)
Operating surplus ratio (target 0-10%)	Ratio met historically ---------------------------->		Ratio met unaudited	Ratio met but risks------->
Net financial liabilities ratio (target 0-100%)	Ratio met historically --->			Ratio projected within target ----------------->
Asset renewal funding ratio (target 90-110%)	ratio below range	Volatility with some years below range----------------->	Renewals below target range ------------->	
Identified Risks:				
Cost control risk	Operating expenses per property average growth 4.0% pa to 2021-22 (CPI 2.0%)---------->		Projected operating expenses per property average growth 1.8% pa to 2029-30 (CPI 2.6%)	
Affordability risk	High rates revenue per property average growth of 4.4% pa to 2021-22 (CPI 2.0%) ------------------------------->		Projected rate revenue growth 3.6% pa to 29-30 - slightly above CPI (2.6%)	

Ratio outside suggested LGA target range or higher risk

Ratio close to suggested LGA target range or medium risk

Ratio within suggested LGA target range or lower risk

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

B Material plan amendments in 2023-24

The District Council of Lower Eyre Peninsula has made various amendments to its 2023-24 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 2022-23 and 2023-24 LTFPs, the Commission has reviewed the seven overlapping years' statistics: 2023-24 to 2029-30 and identified material amendments accordingly.

Selected Financial Item	Sum of 2023-24 to 2029-30 estimates in 2023-30 LTFP ($ million)	Sum of 2023-24 to 2029-30 estimates in 2023-24 LTFP ($ million)	Change in 2023-24 estimates ($ million)	Change in 2023-24 estimates (percent)
Total operating income	110.4	124.8	14.4	13.1
Total operating expenses	105.0	124.2	19.2	18.3
Operating surplus / (deficit)	5.3	0.6	-4.8	-5.2
Capital expenditure on renewal of assets[10]	21.9	27.7	5.8	26.6
Capital expenditure on new and upgraded assets[11]	24.3	23.7	-0.6	-2.4

B.1 Changes to operating performance

The District Council of Lower Eyre Peninsula has budgeted (in 2023-24) a decrease in its operating surplus, with a surplus of $0.6 million compared to a surplus of $5.3 million in the 2022-23 LTFP. In aggregate, the projections in its current and previous LTFPs (that is, over the seven-year comparative period to 2029-30, as shown in the table above) indicate the Council's cumulative operating performance decreased by $4.8 million. This reflects the Council's efforts to achieve an average positive operating surplus over the next seven years following their material revision of inflation affecting income and expenditure.[12]

For the 2023-24 budget year, the Council has stated that the decrease in the operating surplus (compared to the LTFP) is mostly a result of actual and projected inflation for 2023-24.[13] Some of the amendments, compared to the LTFP, include:

- Material adjustments to interest earning percentages.
- Higher inflation estimates and growth in expenses resulting in increased cost pressures for 'materials, contracts and other' expenses, as well as 'employee' expenses, as discussed in section B.2.

9 This table shows only selected financial items to demonstrate the material amendments made by the Council in its 2023-24 estimates. It excludes various financial items and individual items do not sum to totals.
10 The capital expenditure estimates are based on the 2023-30 LTFP estimates provided by the Council to the Commission (in an Excel template).
11 Footnote 10 applies.
12 Lower Eyre Council correspondence dated 26.9.2023, "2023-24 Local Government Advice Scheme – Financial Reporting Commentary".
13 Footnote 12 applies.

- An increase in annual Financial Assistance Grant allocation that was more than assumed inflation.

The Council's historical and projected operating performance is discussed further in section C.1.

B.2 Indexation adjustments

The Council applies CPI-based inflation adjustments to its cost and revenue estimates. It assumes CPI inflation increases of 8.6 percent in 2023-24 and 4.75 percent in 2024-25 with 3.25 percent in 2025-26 followed by 2.75 percent annually from 2026-27.[14] This is an upward revision to its assumptions in its 2022-23 LTFP estimates (of average CPI growth of 1.75 percent over the life of the plan).[15]

Based on updated inflation assumptions in its 2023-30 LTFP[16], the Council has increased its cost estimates by 18.3 percent and revenue estimates by 13.1 percent over the 2023-24 to 2029-30 forecast period,[17] compared with the same estimates in its 2022-23 LTFP.

The Council has factored unexpected revenue into its LTFP projections, discussed in section C.1. However, its current inflation forecasts, at levels higher than RBA forecast inflation, do still present a risk to its cost and income projections in the current inflationary environment. The RBA currently forecasts the CPI (Australia-wide) to increase by 3.6 percent in the year to the June 2024 quarter and by 3.1 percent in the year to June 2025. Thereafter, it is reasonable to anticipate a return to long-run averages (and growth of 2.6 percent per annum from 2026-27, based on the midpoint of the RBA's 2 to 3 percent target range).[18]

The Commission notes that the Council's stated assumptions for indexation in its 2023-30 LTFP are transparent and based on its annual review of these forecasts, but notes that there is uncertainty around the assumptions. 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:

1. Review its inflation forecasts in its budget and forward projections from 2023-24 to align more consistently with RBA inflation forecasts, given the potential for higher short-term inflation outcomes, followed by a return to long-term averages.

B.3 Increase to capital expenditure estimates

The Council's 2023-30 LTFP indicates an increase in capital expenditure for asset renewals (by $5.8 million or 26.6 percent), and a decrease for new and upgraded asset expenditure (by $0.6 million or 2.4 percent), compared to the previous year's LTFP. Over the remaining 7-year projections in the 2023-30 LTFP, the Council has factored in a total of $45.1million in capital renewal and replacement works and $37.9 million in new and upgraded capital works, accounting for 54.3 percent and 45.7 percent of the total capital expenditure program respectively.

The Council's transport assets (mainly road assets) represent the largest asset class, and is a major focus of its renewal investment, projected to account for 71.3 percent (or $32.2 million) of the total asset renewal budget over the next 7 years of the forecast capital asset renewal works program.[19] The renewal budget incorporates $4.9 million of deferred renewal expenditure[20] and notes issues with sourcing materials and external validation of its sealed road pavement renewal works.[21] The Council

14 Lower Eyre Council correspondence dated 26.9.2023, "2023-24 Local Government Advice Scheme – Financial Reporting Commentary", p7.
15 District Council of Lower Eyre Peninsula long-term financial plan 2021-2030 Review One, p2.
16 Lower Eyre Council correspondence dated 26.9.2023, "2023-24 Local Government Advice Scheme – Financial Reporting Commentary", p7.
17 The overlapping set of seven years forecast in both the 2022-23 and 2023-24 LTFP projections.
18 RBA, Forecast Table - August 2023, available at: https://www.rba.gov.au/publications/smp/2023/aug/
19 District Council of Lower Eyre Peninsula asset management plan 2023-2032 adopted April 2023, p53.
20 District Council of Lower Eyre Peninsula asset management plan 2023-2032, adopted April 2023, p3.
21 Lower Eyre Council correspondence dated 26.9.2023, "2023-24 Local Government Advice Scheme – Financial Reporting Commentary", p5.

advises it is working to resolve these issues with state government departments and third party contractors.[22]

For new and upgraded assets, the Council is projecting a decrease in expenditure of $0.6 million (or 2.4 percent). The Council's capital expenditure outlook is discussed further in section C.3.

B.4 Changes between 2023-24 LTFP and annual business plan

The District Council of Lower Eyre Peninsula adopted its annual business plan and budget in July 2023, three months after it adopted its LTFP 2023-30 in April 2023. The Council proposed further material amendments to its 2023-30 estimates for the financial year, from those proposed in its LTFP.

The Commission notes that the District Council of Lower Eyre Peninsula's annual business plan includes budgets for 2023-24 that vary from the adopted LTFP 2023-30. While there is no current regulatory requirement for it to publish its LTFP projections with its annual business plan and budget, it might be useful for it to republish adjusted annual budget estimates for 2023-24.

To this end, the Commission considers that it would be appropriate for the District Council of Lower Eyre Peninsula to:

2. Update its most up-to-date long-term financial plan projections in its annual business plan and budget to provide more transparency to the community about any changes to forward projections, including rate projections, and the longer-term impacts of its short-term decisions.

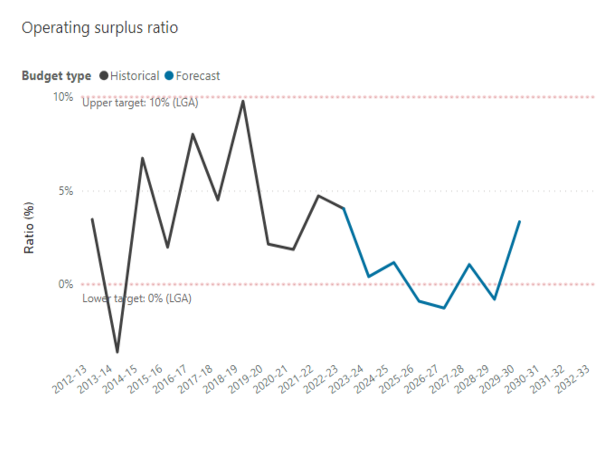
22 Meeting with District Council of Lower Eyre Peninsular 24.11.2023.

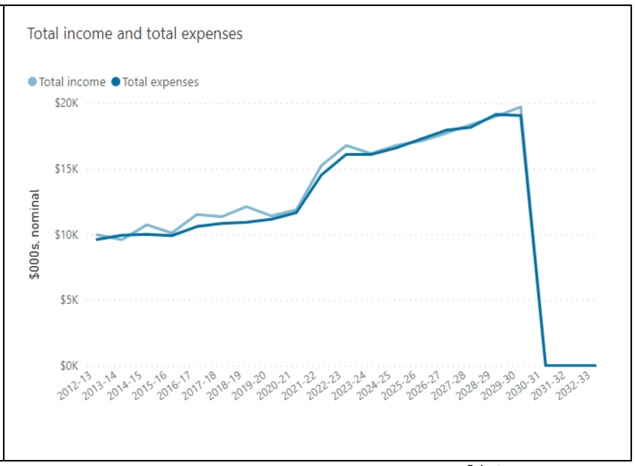
C Financial sustainability

C.1 Operating performance

The District Council of Lower Eyre Peninsula has predominantly run operating surpluses from 2012-13 to 2021-22 with the operating surplus ratio[23] averaging 4 percent and growth of 3.5 percent over this period. In its forward projections, the operating surplus ratio is forecast to be 0.4 percent on average and remain within the suggested LGA target range of 0-10 percent in the period 2023-24 –2032-30 for three of the seven years.

Operating income growth averaged 4.8 percent per annum from 2012-13 to 2021-22, with a similar rate of operating expense growth (averaging 4.7 percent per annum). The Council received a combination of additional rates, statutory charges, user charges and 'grants, subsidies and contributions' income to generate its relatively strong historical operating income growth.





Rates revenue has increased on average by 5.1 percent per annum from 2012-13 to 2021-22[24] (when rateable property growth averaged 0.7 percent and CPI growth averaged 2 percent). Over the same period 'grants, subsidies and contributions' (accounting for 5.8 percent of total operating income) increased by an average of 10.9 percent per annum. Grants income has been 'lumpy' from year to year, and the three-year average of $589 per ratepayer in 2019-22 compares with the three-year average of $485 in 2016-19, which reflects an increase in value in real terms.

The Council's operating expense growth (from 2012-13 to 2021-22) was due to an average annual increase of 6.3 percent in 'employee' expenses, 3.8 percent in 'materials, contracts and other' and 5.4 percent in 'depreciation, amortisation and impairment' expenses (see the changes by expense type in specific time periods in the left chart over the page).

Looking forward, the Council is projecting average annual rates revenue growth of 4.7 percent to 2029-30 which is above the forecast long-term inflation,[25] and represents a real terms increase in rates. This average growth in annual rates revenue is also higher than expected expense growth (rates are discussed in more detail in section D).

The forecast average expense growth of 2.9 percent per annum is higher than the RBA-based forecast inflation growth[26] but represents a change from the Council's past performance (with average annual

23 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).

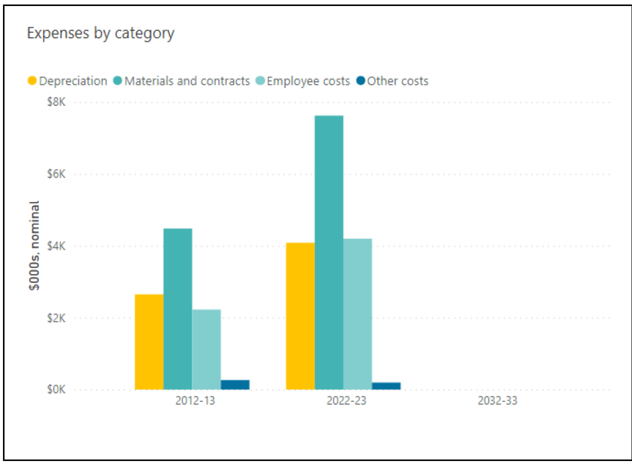
24 Based on the compound average annual growth rate formula (which is the adopted approach to calculating average annual growth rates throughout the Commission's advice).

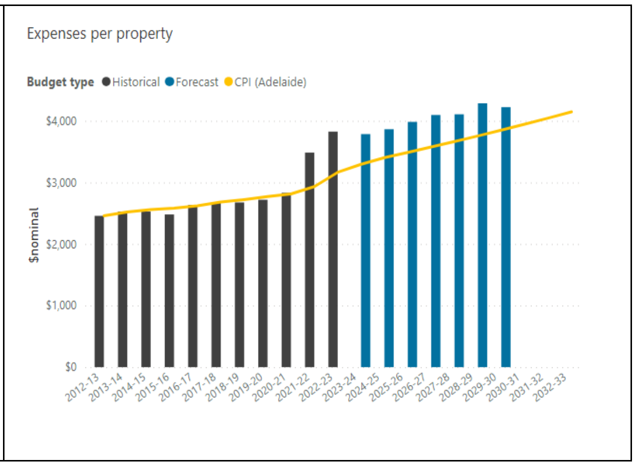
25 The forecast average annual growth in the CPI from 2023-24 to 2032-33 is estimated to be 2.6 percent based on the RBA forecasts for the CPI (Australia-wide) to December 2025 (and the Commission's calculations of average annual percentage growth) and the midpoint of the RBA's target range (2.5 percent) from 2025-26.

26 Footnote 24 applies.

growth of 4.7 percent in the 10 years to 2020-21). The Council anticipates that it will achieve savings in materials and contracts expenditure by capitalising works undertaken in-house and by decreasing staff numbers as short-term contracts conclude.[27]

Expenses per property (a metric which also accounts for growth) are expected to increase by an average of 1.8 percent per annum over this period, which would represent a cost reduction in real terms (based on current inflation projections) (see the right chart below) over the longer term.





The Council's correspondence to the Commission[28] advises that it does not forecast the number of rateable properties nor employee numbers but instead has assumed a flat 1 percent growth per annum in rateable properties and a flat 0.15 FTE growth per annum in employee numbers. Some of its operating income and expense lines indicate negligible change in real terms or growth below current inflation forecasts. For example, grants income represents a forecast of $2.3 million per annum (on average in nominal terms), compared to a historical average of $1.9 million per annum.[29] In addition, 'employee' expenses and 'materials, contracts and other' expenses are forecast to increase by an average of 2.2 percent and 2.7 percent per annum respectively, from 2023-24 to 2029-30. Overall, this would reflect modest growth, closely aligned to forecast inflation. While this is a positive trend, if the anticipated growth in rateable properties does not occur, the Council may have to further increase rates revenue or provide less services. The Council's financial sustainability looking forward does rely on 'cost constraint'.

The Commission notes the practice of the District Council of Lower Eyre Peninsula in conducting regular service level reviews of its operations, focused on achieving increased productivity, efficiency, and effectiveness, and aligning services to customer demand.[30] The Council advises that it reviews the AMP annually prior to setting budgets and does make adjustments for depreciation and changed conditions, and that it is considering implementing rolling condition forecasts for transport assets,[31] however, formally reviews the AMP on a five-year basis at present which may pose the risk of understated projected capital expenditure.

The Commission also notes that the Council has provided its LTFP forecasts for only seven years. Given the long-term nature of the Council's asset base and that the AMP forecasts expenditure until

27 Lower Eyre Council correspondence dated 23.11.2023, "2023-24 Local Government Advice Scheme – Response to Questions Prior to Onsite Meeting" p3.

28 Lower Eyre Council correspondence dated 26.9.2023, "2023-24 Local Government Advice Scheme – Financial Reporting Commentary", p1.

29 Based on the Council's Excel template provided to the Commission. Historical average is based on the 10-year period from 2012-13 to 2021-22; and forecast average is based on the 7-year period from 2023-24 to 2029-30.

30 Lower Eyre Council correspondence dated 26.9.2023, "2023-24 Local Government Advice Scheme – Financial Reporting Commentary", pp2-3.

31 Meeting with District Council of Lower Eyre Peninsular 24.11.2023.

2032, the LTFP should also meet the legislated minimum requirements for a LTFP that relates to a period of at least 10 years.[32]

To ensure the Council is positioned to achieve the real terms reduction in its cost base that it has forecast, and improve its operating performance (without the need for further rate increases above inflation), the Commission encourages it to:

3. Monitor cost growth in its budgeting, to keep costs constrained within the long-term financial plan forecasts, including related to depreciation expenses.
4. Report any actual and projected cost savings in its annual budget (and long-term financial plan, as appropriate), to provide evidence of constraining cost growth and achieving efficiency across its operations and service delivery.
5. Revise and publish the long-term financial plan with 10-year forecasts pursuant to section 122(1)(a) of the *Local Government Act 1999.*

C.2 Net financial liabilities

With the Council's frequent operating surpluses from 2012-13 to 2021-22, its net cash flow after operating and investing (that is, capital-related) activities has averaged $0.07 million annually for the period. (This is different to the top left chart over the page left which shows cash held by the Council at the end of each year, including financing activities, which has averaged $4.2 million).

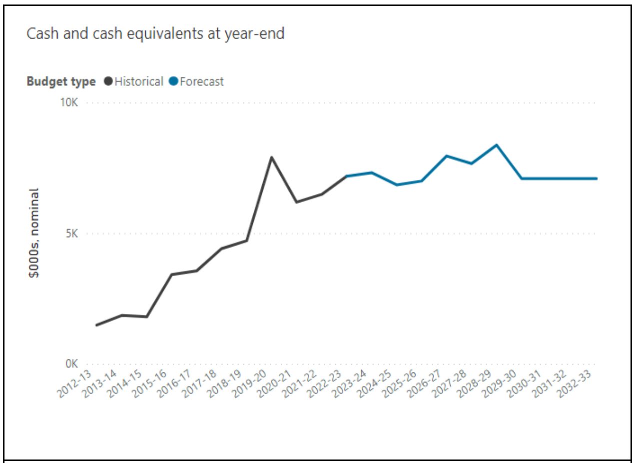
The District Council of Lower Eyre Peninsula has used loan borrowings between 2012-13 and 2020-21 to fund its renewal of existing assets and acquisition of new and upgraded assets. Enacting its new treasury management policy, the Council is projecting no new borrowings after 2024-25 up to 2029-30[33] (see bottom right chart over the page).

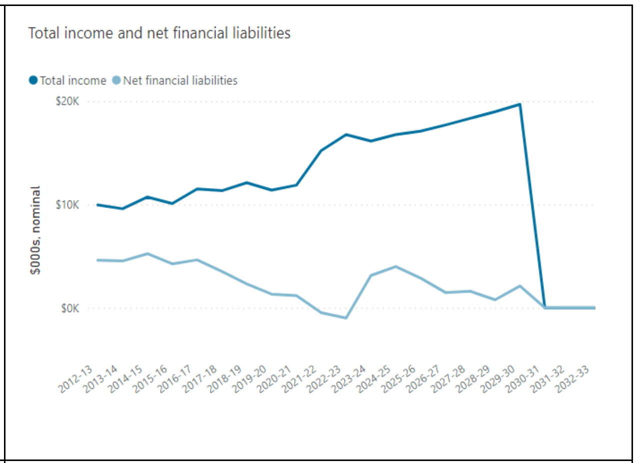
The Council's net financial liabilities ratio has trended between 48.8 and -3.1 percent between 2012-13 and 2021-22 (see bottom left chart left over the page). This is within (or below) the suggested LGA target range for the indicator of between zero and 100 percent (averaging 29.3 percent over this period) and is at a level which demonstrates that the Council is only accumulating liabilities that its operating income can reasonably service (see bottom right chart over the page).[34]

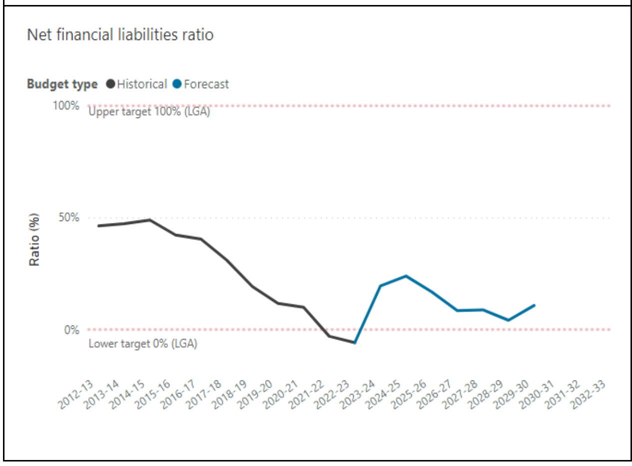
The Council has estimated that the ratio will peak at 23 percent in 2024-25, then decrease to 10.7 percent at the end of this LTFP (see the chart left overleaf).

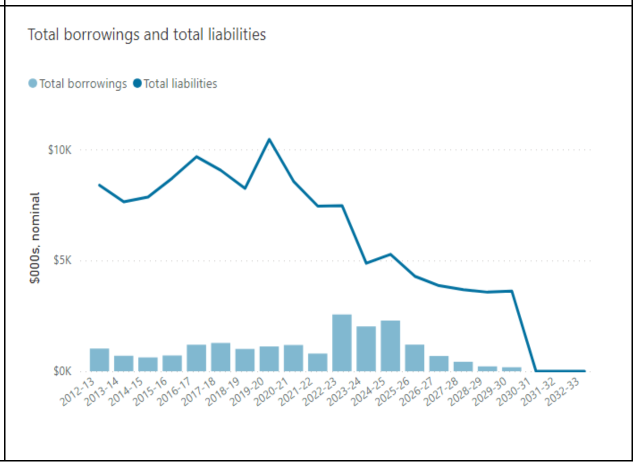
As previously stated, the Council is relying predominantly on further rates revenue growth and lower growth in operating expenses to improve its overall financial sustainability.

32 As required under s122(1a) of the LG Act.
33 Lower Eyre Council correspondence dated 26.9.2023, "2023-24 Local Government Advice Scheme – Financial Reporting Commentary", p2.
34 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).









Based on the Council's projected repayment of borrowings, and relatively low forecast net financial liabilities ratio in the longer-term, and treasury management policy, the Commission notes that it might have the opportunity to utilise its cash holdings to further address its asset renewal expenditure requirements.

C.3 Asset renewals expenditure

The Council has underperformed on its asset renewal funding ratio[35] between 2012-13 and 2021-22. The 2022-23 unaudited estimates and forecasts indicate slight average improvement in asset renewal spending priorities (see the top charts over the page) however, volatility continues through the forecast period. The Commission notes that the Port Lincoln Airport Asset expenditure may distort asset renewal ratios, given that it requires significant periodic expenditure (normally co-funded by grants), and that the asset is managed as a separate entity within the Council and has no real effect on rates and other expenditures.[36]

Between 2012-13 and 2021-22, the asset renewal funding ratio (under the 'IAMP-based' approach) averaged 78 percent,[37] signifying a substantial underspend on the renewal and rehabilitation needs of its asset stock over this period. The Council's spending on renewal and rehabilitation of assets averaged $2.9 million each year (over this period).

35 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).

36 Meeting with District Council of Lower Eyre Peninsular 24.11.2023.

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

From 2023-24 to 2032-33, the ratio is forecast to average 80.7 percent, reflecting some additional expenditure to address previous years' deferred renewal expenditure however remains below the LGA target range for this ratio. Average annual spending on renewal or rehabilitation of assets is projected to increase to $4 million (in nominal terms). The Commission notes that the Council has financial capacity to further address renewal backlogs by using existing cash holdings.

The District Council of Lower Eyre Peninsula has marginally decreased its asset base over the past 10 years by 1.0 percent notwithstanding total capital expenditure averaging $5.3 million per annum (including $3 million per annum on new or upgraded assets) between 2012-13 and 2021-22 (see the bottom right chart over the page). This has led to an average decrease in the value of the asset stock per property of $355 or 1.7 percent for each year over the 10 years to 2021-22 (see the bottom left chart over the page). By implication this indicates the Council's asset stock has declined in real terms (or the increase is lower than historical inflation) or assets revaluations are out of date.

The Council is forecasting higher spending on new or upgraded assets between 2023-24 and 2029-30, estimated to average $3.4 million per annum, however at least 44 percent of this relates to airport capital expenditure which if excluded, reduces average annual spending on new/upgraded assets to $2.2 million. The Council has noted receipt of unusually high levels of grant funding in the past two to three years which is increasing new asset funding in the short term.[38]

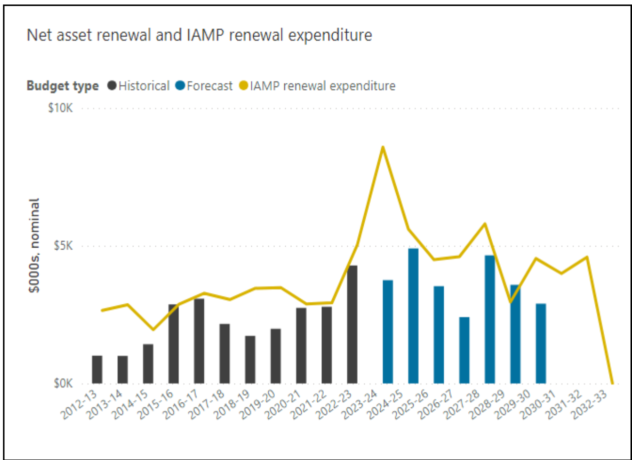
The Council has recognised that its historical capital spending profile has given rise to an accumulation of deferred asset renewals (indicated by actual asset renewal expenditure being lower than required under the AMPs). In addition, the Council has experienced materials and staffing resource issues that have impacted its ability to achieve all planned asset renewals but has strategies in place to mitigate outcomes.[39]

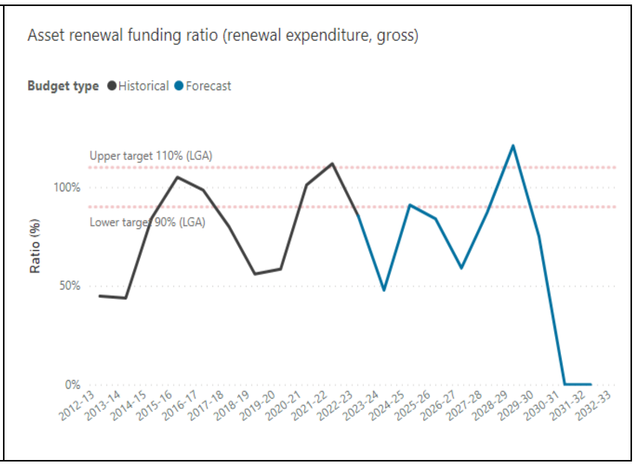
Over the next six years of its LTFP from 2023-24 to 2028-29, the Council is forecasting a volatile asset renewal funding ratio in the later periods of the LTFP projections partly caused by a significant new/upgraded capital expenditure related to the Port Lincoln airport in 2029-30 (see the top right chart over the page).

Acknowledging the proposed asset spending priorities by the Council, which is reflected in its LTFP projections, and to reduce any further accumulation of asset renewal backlogs, the Commission considers that it would be appropriate for it to:

6. **Provide** more funding to the renewal of its assets, rather than prioritising initiatives which involve new or upgraded infrastructure.

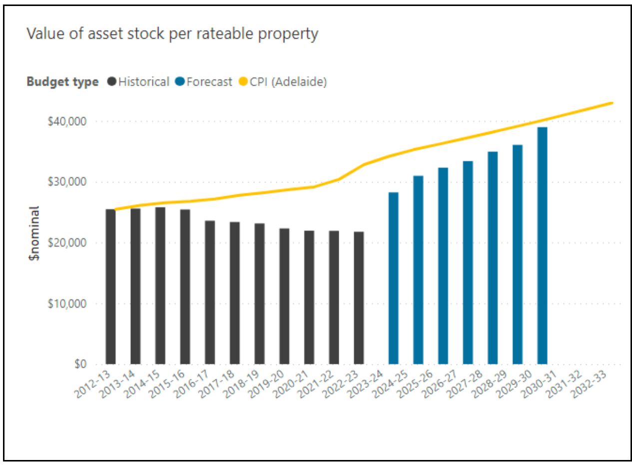
7. **Address** the backlog of asset renewal in the near to medium term using cash reserves to mitigate the risk of future asset failure or higher levels of deferred asset renewals.

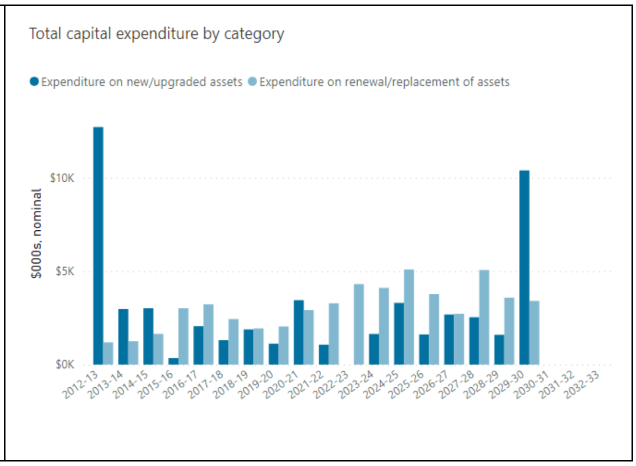




38 Lower Eyre Council correspondence dated 26.9.2023, "2023-24 Local Government Advice Scheme – Financial Reporting Commentary", p4-5.

39 Meeting with District Council of Lower Eyre Peninsular 24.11.2023.



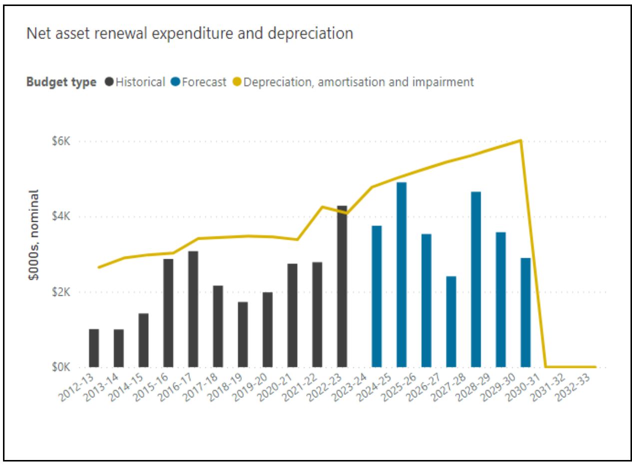


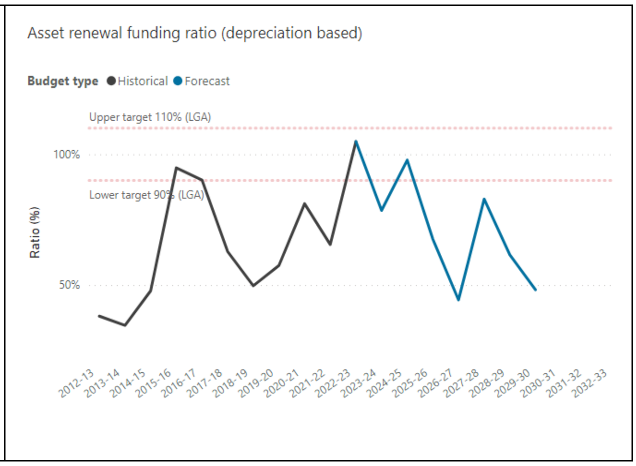
Asset renewals can also be evaluated by the depreciation-based asset renewal funding ratio,[40] which is projected to track lower than the recommended minimum level (for the IAMP-based ratio) of 90 percent, averaging 68.7 percent per annum to 2032-33 (see charts below). While the ratios reflect a small shift in the Council's asset spending priorities towards asset renewals rather than new and upgrade asset expenditures, the amount of spending is below the LG target range of 90-110 percent.

Historically (between 2012-13 to 2021-22) depreciation expenses have outpaced renewal capital expenditure by a significant margin (totalling $10 million over ten years) and the gap is set to increase over the forecast period to $20 million indicating that assets may not require renewal as often as the depreciation schedule predicts, or that significant under expenditure may be occurring, or that at least a proportion of the gap relates to airport assets. This trend may indicate an intergenerational equity[41] risk, as the Council had partly funded capital expenditure (through depreciation) but had deferred or under invested on its asset renewal needs.

For these reasons, the Commission considers that it would be appropriate for the Council to:

8. Continue to update the valuation and useful lives of assets to reduce risk to intergenerational equity.





The Council currently has an AMP for transport, buildings and other structures, major plant, CWMS, stormwater and water infrastructure assets. This covers most of the Council's asset base and reflects

40 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.

41 'Intergenerational equity' relates to fairly sharing of services and the revenue generated to fund the services between current and future ratepayers.

asset valuations that have been carried out within the last four years; all asset classes excluding Machinery, Plant & Equipment and Furniture and Fittings were revalued at 1 July 2021.[42] In formulating its AMP, the Council has considered several matters such as customer levels of service, utilisation and demand of its assets, life cycle management, and risk management planning. These matters (among others) have informed the Council's planned operating and maintenance budgets, and asset renewal needs over the period to 2030. The Commission notes that the asset renewal capital expenditure funding forecasts (in its 2023-30 LTFP) do not align with its AMP renewal targets however, some of the reasons for this are noted above.

The Commission's review of the AMPs has found that, on balance, the timing of the District Council of Lower Eyre Peninsula's strategic planning processes and the LTFP do not align well. Ideally, asset revaluations would also align with AMP reviews and update.

The Council's planned renewal expenditure is mainly attributed to transport assets (covering sealed roads, sheeted roads, kerbs, and footpaths), and accounts for approximately 71.3 percent of total renewals from 2023-30 to 2031-32.[43] Aside from transport works, the Council has planned renewals for tourist infrastructure, plant and equipment, the airport and other service facilities.

As previously noted, the Council has identified an accumulation of deferred renewals and a corresponding funding shortfall, referred to as a 'renewal funding gap', across all asset classes in its AMPs. This gap is estimated to be $20 million at 2029-30 as per LTFP projections. The Commission notes the Council has forecast under expenditure on its sealed and unsealed road network pending locating of additional rubble sources and external validation of sealed road pavement renewal works.[44] The Council indicated to the Commission that it is proposing several amendments to its AMP and other strategic documents in 2023-24, as follows:[45]

- Review of Strategic Plan
- Development of a new 15-year Capital works Plan (2025-2040)
- Development of a 15-year asset management Plan (2025-2040)
- Development of a 10-year LTFP (2025-2034).

The Commission recommends that the Council:

9. **Align** the proposed expenditure in its asset management plans with its long-term financial plan to reduce the risk of inaccurate forecasting.
10. **Achieve** the reviews of strategic documents and asset management plans as it has proposed.

42 Lower Eyre Council correspondence dated 26.9.2023, "2023-24 Local Government Advice Scheme – Financial Reporting Commentary", p2.
43 District Council of Lower Eyre Peninsula asset management plan 2023-2032, p54
44 Lower Eyre Council correspondence dated 26.9.2023, "2023-24 Local Government Advice Scheme – Financial Reporting Commentary", p7
45 Provided in an email to the Commission on 10 October 2023.

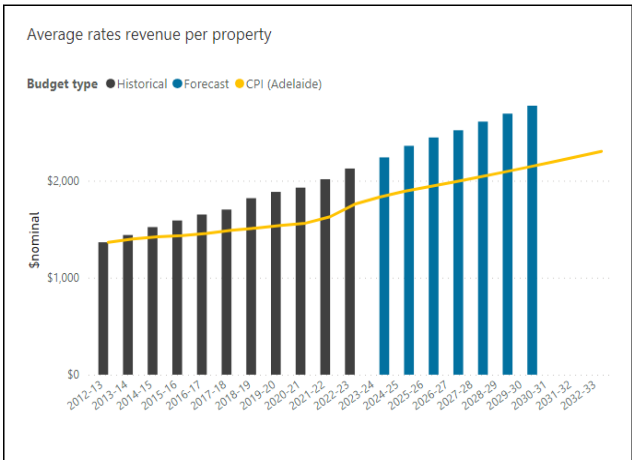
D Current and projected rate levels

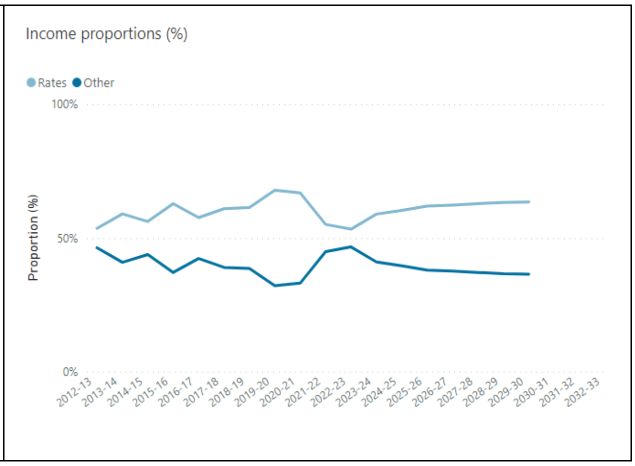
D.1 Historical rates growth

The District Council of Lower Eyre Peninsula's rate revenue per property growth has averaged 4.4 percent or $65 per annum for each property over the past 10 years,[46] to reach an estimated $2,016 per property in 2021-22 (see the left chart below). This has exceeded CPI growth of an average of 2 percent per annum over this period, but also encompasses 0.7 percent average annual growth in rateable property numbers.[47] Current rate levels partially reflect its recent history of spending growth, predominantly on higher employee-related costs, and depreciation expenses and the Council's focus to improve its operating performance.

The Council remains reliant on its rate base for its operating sustainability. As the chart below indicates (to the right), rates revenue is forecast to remain consistent with rates averagely accounting for 61.9 percent of budgeted operating income in 2023-24 to 2029-30, compared with an average of 60.2 percent of income in 2012-13 to 2021-22. To assist in maintaining sustainability, the Council is considering differential rates for bulk handling facilities.[48]

The Commission notes that the District Council of Lower Eyre Peninsula has relatively low average rates, reflecting its relatively low-rate levels for both residential and rural categories.[49]





D.2 Proposed 2023-24 rate increases

The District Council of Lower Eyre Peninsula has budgeted for an average rate increase of 3.6 percent or $93 per property per annum for its existing ratepayers in 2023-24 to 2029-30,[50] which includes a significant increase of 12.6% for 2023-24 between estimates in 2022-23 LTFP and 2023-24 LTFP. The rates increase reflects higher short-term inflation (estimated by the Council to be 8.6 percent).[51] While the Council does not forecast growth in rateable properties, it has assumed 1.0 percent as a minimal rate and is not an important determinant in 2023-30 rates revenue.

---

46 From 2012-13 to 2021-22.

47 ABS data historical time series available at https://www.abs.gov.au/statistics/economy/price-indexes-and-inflation/consumer-price-index-australia/sep-quarter-2023#capital-cities-comparison

48 Meeting with District Council of Lower Eyre Peninsular 24.11.2023.

49 Refer to Councils in Focus rates data for 2019-20 available at: https://councilsinfocus.sa.gov.au/councils/district_council_of_lower_eyre_peninsula.The Commission is not relying on these rate comparisons for its advice; the data source provides one indicator, among many, which has informed its advice on the appropriateness of the rate levels.

50 Based on the Council's Excel template (with the 2023-30 forecasts) provided to the Commission.

51 Lower Eyre Council correspondence dated 26.9.2023, "2023-24 Local Government Advice Scheme – Financial Reporting Commentary", p7.

Different rate categories are applied based on the locality of land and all rateable properties are subject to a fixed charge. Other than 'general rates' revenue, the Council collects income from waste collection,[52] the CWMS charge, the Regional Landscape Levy and receives annual dividends from its airport asset of approximately $2 million per annum[53] that provide an effective discount to rates.[54]

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 4.7 percent per annum from 2023-24 to 2029-30.

In total, the LTFP effectively projects a cumulative increase of $93 per annum per existing ratepayer (to $2,774 per annum) by 2029-30, which is consistent with the Council's assumed inflation growth over this period, but above the RBA-based long-term inflation forecast of an average of 2.6 percent per annum[55] (refer back to the previous page chart on the left side). This long-term average trend is impacted by the Council's projected rates increases in the first three years of its LTFP (from 2023-24 to 2025-26) being above the RBA forecast rates.[56]

The percentage of the Council's total income contributions from ratepayers is projected to average around 61.9 percent – a marginal increase on the historical average of 60.2 percent.

D.4 Affordability risk

Affordability risk among the community for these 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 for the District Council of Lower Eyre Peninsula area,[57]
- the current relatively low average rates without further forecast increases above inflation for ratepayers,
- the effect of cumulative increases in expenses per existing ratepayer of approximately 2.0 percent per annum to the period 2031-32, below the RBA forecast rate of inflation, and
- the overall financial sustainability risks of the Council based on asset renewal backlogs that could be mitigated by utilising existing cash reserves.

However, as the current economic environment is putting more pressure on most communities' capacity to pay for further rate increases, including those of the District Council of Lower Eyre Peninsula, the Commission considers it would be appropriate for the Council to:

11. Consider limiting future increases in rates to no more than expected inflation, to help reduce any emerging affordability risk in the community.

52 The Commission notes the increase in the solid waste levy over the last 10 years, which has impacted waste management costs in the local government sector.

53 Lower Eyre Council correspondence dated 26.9.2023, "2023-24 Local Government Advice Scheme – Financial Reporting Commentary", p2.

54 Meeting with District Council of Lower Eyre Peninsular 24.11.2023.

55 The forecast average annual growth in the CPI from 2023-24 to 2032-33 is estimated to be 2.6 percent based on the RBA forecasts for the CPI (Australia-wide) to December 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.

56 Lower Eyre Council correspondence dated 26.9.2023, "2023-24 Local Government Advice Scheme – Financial Reporting Commentary", p8.

57 The District Council of Lower Eyre Peninsula area is ranked 64 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 (eg, 1) denotes relatively lower access to economic resources in general, compared with other areas, available at Socio-Economic Indexes for Areas (SEIFA), Australia, 2021 | Australian Bureau of Statistics (abs.gov.au)

ESSENTIAL SERVICES COMMISSION OF SOUTH AUSTRALIA