Advice

Local Government Advice

Northern Areas Council

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

The Essential Services Commission is an independent statutory authority with functions in a range of essential services including water, sewerage, electricity, gas, rail and maritime services, and also has a general advisory function on economic matters. For more information, please visit www.escosa.sa.gov.au.

OFFICIAL

Northern Areas Council

AT A GLANCE

OVERVIEW

The Essential Services Commission finds the Northern Areas Council's current financial performance **potentially unsustainable,** but notes that it is taking steps to achieve a **mostly sustainable** position in the future, when taking into account the council's forecast moderate expense increase over the next 10 years and the planned average rate increases of 2.7% p.a. per property over this period

RISKS IMPACTING SUSTAINABILITY

- Asset management plans are significantly out of date
- Depreciation expenses related to assets may be understated impacting Operating Performance
- Low forecast expense growth is not realised and is underestimated
- No forecast expenditure for new or upgraded capital works from 2027-28
- Underestimation of future capital expenditure

CONTINUE

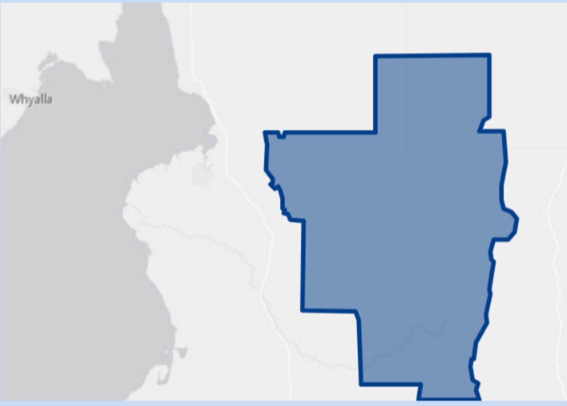
- Reporting actual and projected costs savings in its annual budget and long-term financial plan to provide evidence of cost constraint and achieving efficiency across its operations and service delivery

COMMISSION'S RECOMMENDATIONS

- Ensure updates to the long-term financial plan are reflected in key strategic management documents
- Update asset management plans and asset valuations regularly (at least every 4 years)
- Update asset management plans, and asset valuations within 12 months
- Immediately update the long-term financial plan following the asset management plans update and asset revaluations
- Review and update depreciation expenses based on revised asset management plans
- Provide more funding to the renewal of assets
- Manage its near-term forecast costs

KEY FACTS

- Population in 2021 was **4,559**
- Council covers **3,070 square kilometres**
- **4,257** rateable properties in 2022-23
- **$9.5 million of rate income** in 2022-23
- Value of assets held in 2022-23 equals **$113 million**



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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	Northern Areas Council
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 Paper 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 Northern Areas Council

The Essential Services Commission (**Commission**) finds the Northern Areas Council's (**Council**) short-term financial position **potentially unsustainable**. However, the Commission notes that the Council is taking steps to consolidate a **mostly sustainable** position in the medium to long-term. The Council's projected improvement to its financial performance is reliant on the renewal of its asset stock and a period of service consolidation, which would require at a minimum, continued cost control, and further rate increases.

Current financial performance:

Unsustainable	**Potentially Unsustainable**	Mostly Sustainable	Sustainable

Projected financial performance (future):

Unsustainable	Potentially Unsustainable	**Mostly Sustainable**	Sustainable

Previous financial performance (past ten years):

Unsustainable	**Potentially Unsustainable**	Mostly Sustainable	Sustainable

However, the Commission has identified that there are risks to the Council's sustainability with the major risks as follows:

- The Council's asset management plans are significantly out of date and 69 percent of asset valuations were undertaken at 1 July 2020 which creates a risk that depreciation expenses relating to its asset base are understated which could negatively impact the Council's Operating Surplus Ratio (**OSR**).
- The Council has predicted low growth in expenses to be below forecast inflation. If this forecast is not realised and its expenses are higher than anticipated, the Council may need to either increase rates, reduce service levels, or borrow further funds to maintain its forecast OSR.
- There is no forecast expenditure for new/upgraded capital works from 2027-28 where the Council risks understating its future new capital expenditure leading to an understatement of future depreciation expenses.

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, renews its asset base to meet sustainable service levels, plans its asset needs appropriately and constrains the extent of further rate increases.

Budgeting considerations

1. **Manage** its near-term forecast costs to ensure they are sufficiently constrained to enable achievement of the forecast operating surplus ratio.
2. **Ensure** updates to the long-term financial plan are reflected in key strategic management documents.

Continuing to provide evidence of ongoing cost efficiencies

3. **Manage** cost growth in its budgeting, where possible, including related to employee expenses and materials, contracts and other expenses.
4. **Review and update** depreciation expenses based on revised asset management plans.
5. **Continue** its good practice of reporting 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.

Refinements to asset management planning

6. **Adhere** to the principles underpinning its long-term financial plan projections to provide more funding to the renewal of its assets, rather than prioritising initiatives which involve new or upgraded infrastructure.
7. **Update** asset management plans and asset valuations regularly and at least every four years to ensure an accurate alignment between the asset valuation and renewal expenditure requirements in the asset management plans and the latest long-term financial plan projections.

Containing rate levels

8. **Update** its long-term financial plan immediately following each update of asset management plans and asset valuations to accurately forecast its financial position and provide transparency with trade-off options to ratepayers about potential higher rates.
9. **Complete** the update of asset management plans, assets valuations and a revised long-term financial plan within 12 months to provide ratepayers with more certainty about future rate increases.

2 About the advice

The Essential Services Commission (**Commission**), South Australia's independent economic regulator and advisory body, has been given a role by 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 Northern Areas Council (**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 the Commission 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 short-term financial position potentially unsustainable. However, the Commission notes that the Council has taken steps to consolidate into a sustainable position in the medium to long-term, following a period of volatile operating surplus results. The council has also struggled to meet the ongoing renewal needs of its existing infrastructure base.[10] This now presents a backlog of deferred renewal and rehabilitation it needs to address in the future.

The past rate increases above inflation have had the effect of increasing the Council's financial capacity to cover its operating and service sustainability requirements.

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).
10 ARFR renewal expenditure below recommended range.

Its forward projections from 2023-24 (in its LTFP) forecast an improving financial sustainability outlook due to the forecast rate of operating revenue growth set to outpace expense growth, but with:

- continued average rate increases below the Reserve Bank of Australia (RBA)-based forecast inflation rate,
- optimistic cost constraint with lower average cost growth than RBA-based forecast inflation,
- low spending on new or upgraded capital works with moderate asset spending on renewal and rehabilitation capital works, including to partially address the accumulation of deferred renewals over the next 10 years, and
- concerns about the accuracy of depreciation and capital expenditure forecasts.

The Council's past and projected operating surplus ratio, net financial liabilities ratio, asset renewal funding ratio and average rate revenue per property, together support these findings. However, the Commission notes the following significant risks to the LTFP forecasts:

- that uncertainty exists regarding Council's inflation assumptions,
- that AMPs are significantly out of date,
- that depreciation is not supported by current asset valuations,
- and that no new/upgraded capital expenditure has been forecast from 2027-28 which is inconsistent with past average expenditure of $0.7 million per annum.

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.[11]

2.2.1 Advice on material plan amendments in 2023-24

Key Points:

✅ The projected deficit is driven by grants received in advance which is a result of a timing issue (i.e. receiving a grant in advance of the financial year).

⚠️ The operating surplus forecasts were revised to be more moderate to account for higher inflation and to allow for additional renewal capital expenditure.

The Council's 2023-24 LTFP includes a forecast deficit in 2023-24 followed by an improvement to its projected operating performance from 2024-25, and a slight increase to its projected capital expenditure estimates.

- The forecast deficit is mainly driven by grants received in advance (2022-23) reducing the 2023-24 forecast grant value.

[11] The attachment will be available on the Commission's website with the Advice.

- An additional $0.5 million for new projects[12] not identified in the respective asset management plans (AMPs).

Operating Surplus forecasts have been revised to be more moderate, compared with the 2022-23 estimates, and in part, address the accumulation of deferred renewal expenditure and accounts for the current inflationary environment.

The Council has increased its operating income forecasts with a total operating income increase of 0.9 percent. The increase of 3 percent on 2022-23 rates accounts for higher inflation forecasts, based on an average of the Local Government Price Index forecast,[13] while grants income is decreased due to receipt of grants in advance. Expenditure is now forecast to increase by 2 percent, mainly driven by employee costs, compared to its 2022-2023 expenditure forecasts.

The Council has factored increased capital expenditure into its LTFP projections, discussed in the operating performance section below. However, its current inflation forecasts may 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 30 June 2024 and by 3.1 percent in the year to 30 June 2025. Thereafter, it is reasonable to anticipate a return to long-run CPI averages (and growth of 2.6 percent per annum from 2025-26).[14]

The Commission notes the Council's stated assumptions[15] for indexation in its 2023-24 LTFP but is of the view that there is considerable uncertainty around those assumptions. Notwithstanding the need for the Council to find savings and reduce any inflationary impact on its community, the Commission has found that it would be appropriate for it to:

1. **Manage** its near-term forecast costs to ensure they are sufficiently constrained to enable achievement of the forecast operating surplus ratio.

The Council adopted its 2023-24 annual business plan and budget together with its long-term financial plan in June 2023.[16] The Commission observes that the Council's LTFP identifies the risks to the financial estimates (due to economic factors, for example) and that the annual business plan also includes its 2022-2023 estimates (from the LTFP) to show any further budget amendments to those estimates. In addition, there is no current regulatory requirement for a council to publish its LTFP projections with its annual business plan and budget.

The Commission notes that the financials are aligned from 2025-26 forwards, however the annual budget 2023-24 was not updated to align with the LTFP forecast 2023-24. It would be better practice for the Council's annual business plan and budget to be republished with updated 2023-24 forecasts.

2. **Ensure** updates to long-term financial plans are reflected in key strategic management documents.

12 Northern Areas Council long-term financial plan 2023-24 – 2032-33 available at https://www.nacouncil.sa.gov.au
13 Northern Areas Council long-term financial plan 2023-24 to 2032-33
14 RBA, Forecast Table – August 2023, available at https://www.rba.gov.au/publications/smp/2023/aug/forecasts.html.
15 Footnote 13 applies, p8.
16 Northern Areas Council Minutes of the Special Meeting 27 June 2023 available at https://www.nacouncil.sa.gov.au

2.2.2 Advice on financial sustainability

Operating performance

Key Points:

- Operating deficits consistently observed between 2012-13 to 2021-22, with the operating surplus ratio averaging negative 2.3 percent in that time.
- 'Employee costs', 'materials, contracts and other' and 'depreciation' expenses all increased at conservative levels, averaging 1.8 percent per annum, from 2012-13 to 2021-22 which is 0.2 percent less than the CPI during that time.
- The operating surplus ratio is forecast to meet the suggested LGA target range from 2024-25 to 2032-33 averaging 4.7 percent per annum.
- Average operating expenses per rateable property between 2023-24 and 2032-33 are forecast to increase on average by 2 percent per annum, which is 0.6 percent less than the long-term RBA-based forecast inflation over the same period.

The Council has predominantly run operating deficits from 2012-13 to 2021-22, with the operating surplus ratio[17] averaging negative 2.3 percent over this period. However, in 2021-22, it achieved an operating surplus ratio of 14.3 percent (operating surplus over $2 million). In its forward projections, the operating surplus ratio is forecast to meet the suggested LGA target range from 2024-25 with an ongoing surplus averaging 7 percent.

The Council had experienced deficits of over $1m in each of the years 2012-13, 2013-14 and 2015-16 indicating it had difficulty in meeting its operating capacity requirements at that time. This is despite operating income growth averaging 5 percent per annum from 2012-13 to 2021-22, more than double the rate of operating expense growth (which was relatively conservative, averaging 2 percent per annum).[18]

For 2020-21, 2021-22 and the unaudited 2022-23 financial years, they show operating surpluses. However, there is a forecast operating deficit in 2023-24 which can be mostly attributed to the Financial Assistance Grant being received in advance (received in 2022-23 year for 2023-24). The most significant contributors to income growth over this period to generate the relatively strong operating growth were a combination of 'rates' and 'grants, subsidies, and contributions' income.

On the cost side, 'employee costs', 'materials, contracts and other' and 'depreciation' expenses all increased at conservative levels, averaging 1.8 percent per annum, from 2012-13 to 2021-22, related to annual CPI growth of 2.0 percent,[19] and there was a significant decrease in 'finance' costs due to a reduction in 'borrowings'.

The estimated rate of growth in operating expenses projected over the next 10 years, is an average of 2 percent per annum, which includes continuing reduction in total 'borrowings' across the period and is

[17] 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).

[18] 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).

[19] CPI Adelaide (All groups). Average annual growth in the LGPI published by the South Australian Centre for Economic Studies was similar (at 2.0 percent), available at https://www.adelaide.edu.au/saces/economic-and-social-indicators/local-government-price-index.

less than RBA-based forecast inflation.[20] When combined with rates, statutory and user charges revenue growth (slightly above or equal to the RBA-based forecast inflation), the Council's operating performance is expected to improve, generating an operating surplus ratio averaging 4.7 percent per annum. The Council has improved its position considerably in turning around from predominantly running deficits to forecasting predominant surpluses. However, the forecasts are optimistic when considered against RBA CPI forecasts and the Council has additional inherent risks because of outdated AMPs.

The associated impact on ratepayers is discussed further below.

The Commission notes that the Council is:

- planning to constrain expenditure within CPI,
- undertaking a review of its asset plans, and
- proposing no significant new projects to achieve savings.[21]

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

3. **Manage** cost growth in its budgeting, where possible, including related to employee expenses and materials, contracts, and other expenses.
4. **Review and update** depreciation expenses based on revised asset management plans.
5. **Continue** its good practice of reporting 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.

Net financial liabilities

Key Points:

- ✓ The net financial liabilities ratio has remained within the LGA target range between 2012-13 and 2021-22, averaging 40.6 percent.
- ✓ The net financial liabilities ratio in the 10 years to 2032-33 is forecast to be an average of 33.1 percent as a result of progressive repayment of debt.
- ⚠ A cautionary approach should be taken in relation to the net financial liabilities ratio forecast as it risks being understated because 69 percent of the Council's asset valuations were updated at 1 July 2020 with a subsequent period of high inflation.

Despite the Council's frequent operating deficits from 2012-13 to 2015-16 (including depreciation expenses), its net cash flows after operating and investing (that is, capital-related) activities has averaged $0.5 million per annum between 2012-13 and 2021-22. Over this period, growth in the Net Financial Liabilities Ratio was negative 18 percent as borrowing liabilities have decreased. The Council has relied primarily on rates revenue and supplementary grant funding to fund its capital expenditure program over this period.

The Council has also consistently used borrowings to finance (in part) its renewal of existing assets and acquisition of new and upgraded assets, and over time, borrowing has been within the suggested LGA

[20] 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.

[21] Northern Areas Council – 2023-24 - annual business plan.

target range for the Net Financial Liabilities Ratio (averaging 40.6 percent from 2012-13 to 2021-22).[22] The Council continues to meet the suggested LGA target range under its 2023-24 forecasts and projects a reduction in the ratio from a peak of 76.6 percent in 2013-14 to an average of 33.1 percent in the nine years to 2031-32. The Commission notes the reduction in borrowings at the end of 2026-27 to zero, and the intention of the Council to use cash reserves and short-term funding facilities to manage cash flow and fund projects as required.[23] The longer-term reduction in the Net Financial Liabilities Ratio from 2023-24 to 2032-33, comes from progressive repayment of total borrowings over the next ten years (to 2032-33) via operating income growth and deferral of capital projects expenditure. The NFLR may also be negatively impacted once Council has updated its asset valuations because of the impact of increased depreciation on the OSR.

Based on the Council's projected repayment of borrowings, and relatively low forecast Net Financial Liabilities Ratio in the longer-term, the Commission notes that the Council might have the opportunity to utilise more debt to further address its deferred asset renewal expenditure requirements subject to its capacity to repay.

Asset renewals expenditure

Key Points:

- Between 2012-13 and 2021-22 the Council's asset renewals and replacements expenditure averaged $3.8 million per annum, plus an average of $0.75 million per annum on new/upgraded assets, with an average annual asset renewal funding ratio of 86.9 percent.
- Asset renewals expenditure is expected to increase between 2023-24 and 2032-33 to average $5.9 million, with an average annual asset renewal funding ratio of 101.9 percent.
- The asset management plans are significantly out of date and may not reflect the requirements of their current asset stock renewal / repair / replacement, as a result of outdated condition assessments and estimated useful life of the assets.
- There is no new capital expenditure forecast in its long-term financial plan from 2027-28 onwards which is unrealistic based on past performance.
- Council is experiencing resourcing issues which may hinder its ability to ensure that asset renewals are on track and up to date as per its long-term financial plan.

Between 2012-13 and 2021-22, the Council's asset renewals and replacements expenditure averaged $3.8 million per annum plus an average of $0.75 million per annum on new/upgraded assets. However, expenditure fell short of the $4.7 million asset renewal and rehabilitation requirements specified in its AMPs. The Council's asset renewal funding ratio (IAMP-based) was below the suggested LGA target range of 90 to 110 percent, averaging 86.9 percent between 2012-13 and 2021-22.[24] This indicates that the Council underperformed in meeting its asset service sustainability requirements over this period, as it utilised increased rate and grant funding, and borrowings while it also sought to address its recurring

[22] 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).

[23] Meeting between Northern Areas Council and ESCOSA 19 Oct 2023.

[24] 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).

operating deficits. The Commission notes the advice of the Council regarding the timing of grant payments and the availability of staffing, contract and materials resources.[25]

From 2023-24, the Council is projecting to increase its asset renewals spending profile (with projected annual asset renewal expenditure averaging $5.9 million to 2032-33, in nominal terms). As a result, its Asset Renewal Funding Ratio (IAMP-based) is expected to trend within the suggested LGA target range (averaging 101.9 percent from 2023-24 to 2031-32). This coincides with much lower forecast spending by the Council on new or upgraded assets (estimated to average $.2 million per annum from 2023-24 to 2026-27, then cease).

The Council has forecasted no new/upgraded capital expenditure from 2027-28. The Commission notes that the Council has historically expended average new capital expenditure of $0.7 million per annum over the previous 10 years and could have reasonably made longer-term forecasts despite the absence of any known capital expenditure. Furthermore, the Commission also notes that the Council advised that new capital expenditure was frequently linked to grant funding, and that it had forecast grant funding for the same period in the absence of any new capital expenditure.[26] This may create a risk that forecast grant funding inflates the operating surplus ratio and understates the Net Financial Liabilities Ratio.

Acknowledging the shift in 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. Adhere to the principles underpinning its long-term financial plan projections to provide more funding to the renewal of its assets, rather than prioritising initiatives which involve new or upgraded infrastructure.

The asset management plans were last updated sometime between 2016 and 2017 and the information contained therein generally does not underpin the forward projections. In addition, the plans note the limitations of available data for confident forecasting. The Commission acknowledges the Council experienced resource issues that have contributed to the lack of updates, however notes that without frequent revaluation of assets and assessments of asset conditions, risks of asset failure and significant expense can occur. An additional key risk is that depreciation is understated which could potentially negatively impact OSR.

The Council's projected spending on asset renewals and the depreciation expenses (which represent the rate of asset consumption) are projected to broadly track in line. Renewal spending is forecast to account for 103.7 percent of depreciation expenses on average to 2031-32.[27] While this demonstrates a sound alignment between the average rate of consumption of its assets, as indicated by its depreciation and renewal expenditure, the validity of the underlying data is unknown due to the outdated asset management plans and asset valuations.

7. Update asset management plans and asset valuations regularly and at least every four years to ensure an accurate alignment between the asset valuation and renewal expenditure requirements in the asset management plans and the latest long-term financial plan projections.

[25] See footnote 23.
[26] See footnote 23.
[27] The Council's asset renewal funding ratio by the depreciation-based method (where asset renewal/replacement expenditure is divided by depreciation expenses) is forecast to average 103.7 percent to 2031-32. 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.

2.2.3 Advice on current and projected rate levels

Key Points:

- Rate revenue per property growth has averaged 6 percent per annum for each property in the period between 2012-13 and 2021-22 which is 4 percent above CPI for the same period.
- Forecasted rate revenue growth increase of 2.7 percent per annum per property from 2023-24 to 203-32 which is 0.1 percent above the RBA-based forecast of inflation over the same period.
- Affordability risk among the community for further rate increases appears to be high, given the council's approach to constraining operating costs is based on depreciation levels which may be inaccurate (based on its outdated asset management plans), and on ongoing deferral of renewal capital expenditure.

The Council's rate revenue per property growth has averaged 6 percent per annum per property in the period between 2012-13 and 2021-22, which exceeded CPI growth at an average of 2.0 percent per annum over this period. However, the Council has relatively high levels for rural ratepayer categories, compared to average rates of other councils for rural ratepayers.[28]

Its 2023-24 LTFP forecasts an average growth of 2.7 percent per annum from existing rates in total to 2031-32, which is broadly in line with the RBA-based forecast of average inflation (2.6 percent).

Affordability risk among the community for further rate increases appears to be high, given the council's approach to constraining operating costs is based on depreciation levels which may not be accurate, and on ongoing deferral of renewal capital expenditure (reducing associated materials and labour costs). The Council has optimistic forecasts and once AMPs and revaluations are undertaken, it may not achieve its planned reductions in operating expenses.

Given historical rate increases and the current economic conditions affecting many communities' capacity to pay, it would be appropriate for the Council to:

8. **Update** its long-term financial plan immediately following each update of asset management plans and asset valuations to accurately forecast its financial position and provide transparency with trade-off options to ratepayers about potential higher rates.
9. **Complete** the update of asset management plans, assets valuations and a revised long-term financial within 12 months to provide ratepayers with more certainty about future rate increases.

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:

- potential integration of its annual updates to its LTFP projections with its annual business plan process,
- ongoing performance against its LTFP estimates,
- achievement of cost savings and efficiencies and its continued reporting of these in its plans,

[28] Refer to Councils in Focus rates data for 2021-22 available at https://councilsinfocus.sa.gov.au/councils/northern_areas_council. The Commission is not relying on these rate comparisons for its advice; the data source provides just one indicator, among many, which has informed its advice on the appropriateness of the rate levels.

- reviews of capital expenditure (renewal and new/upgraded) based on updated asset management plan review, asset revaluations and asset condition assessments,
- reprioritisation of its capital spending towards asset renewal and rehabilitation works and how it has addressed the backlog of asset renewal expenditure, and
- how it has sought 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