Introduction

In my response to the ESC Draft Rate Capping Recommendation I would like to highlight the impact of this on the Macedon Ranges Shire Council into the future.

Firstly what is the current strategy and long term borrowing of the Macedon Ranges Shire Council and its future debt level? Secondly how does this strategy impact future rate capping for our shire?

For the purpose of this discussion we will call it Debt financing.

What is the strategy and long term borrowing and intergenerational equity?

Sections 144 -150 of the Local Government Act 1989 govern a council's power to borrow. Subject to the principles of sound financial management, Council may borrow money to perform its functions and exercise its power.

The use of loans to fund capital expenditure is an effective mechanism of linking the payment for the asset to successive generations who will receive benefits over the life of that asset. This matching concept is frequently referred to as “intergenerational equity” because the costs of servicing debt through rate revenue and/or customer fees/charges enables the cost of the asset to be matched with the benefits from consumption of the services over the life of the asset, thereby promoting intergenerational equity.

However with the pending introduction of rate capping to CPI (currently 1.5%’ over the last twelve months) many councils because of low interest rates have previously taken out large loans to do these capital works expenditure for the community now and into the future and will be severely impacted on the way forward. In the Macedon Ranges Shire because of our Settlement Strategy and current strong population growth we have invoked this process through many key loans which have been taken up and yet to be. They are:

Itemised list of all budgeted loans in 2013/14, 2014/15 and 2015/16.

2013/14 Budget		
Gisborne Council Office Extension Part 1	$700,000	
Hanging Rock East Paddock Development Part 1	$550,000	
Kyneton Market Street Land Purchase (for Car Park)	$320,000	
Defined Benefits Superannuation Plan Liability	$3,638,000	
Gisborne Secondary College Stadium Contribution Part 2 (Note Part 1 in the 2012/13 Budget was $500,000)	$1,000,000	
Total		$6,208,000
2014/15 Budget		
Gisborne Council Office Extension Part 2 (Note: It will be recommended that the budgeted borrowings be reduced by $595,000)	$800,000	
Hanging Rock East Paddock Development Part 2	$450,000	
Total		$1,250,000
2015/16 Budget		
Gisborne Early Learning Centre Construction	$2,300,000	
Kyneton Landfill Rehabilitation	$1,775,000	
Total		$4,075,000
Grand Total		$11,533,000

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List of budgeted loans which have been taken up.

Kyneton Market Street Land Purchase (for Car Park)	**$320,000**	
Defined Benefits Superannuation Plan Liability	$3,638,000	
Total		$3,958,000

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List of remaining budgeted Loans, not yet taken up.

Gisborne Council Office Extension Part 1	$700,000	
Hanging Rock East Paddock Development Part 1	$550,000	
Gisborne Secondary College Stadium Contribution	$1,500,000	
Gisborne Council Office Extension Part 2 (Note: It will be recommended that the budgeted borrowings be reduced by $595,000)	$800,000	
Hanging Rock East Paddock Development Part 2	$450,000	
Gisborne Early Learning Centre Construction	$2,300,000	
Kyneton Landfill Rehabilitation	$1,775,000	
Total		$7,575,000

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Amount of outstanding loans as at 30 June 2013.

$3.9 million.

Amount of outstanding loans as at 30 June 2015.

$6.6 million.

Amount of outstanding loans as at 30 June 2016 – assuming that all budgeted loans will have been taken up.

$13.2 million.

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As you can see from previous council extract budget slides we are investing for the future in our shire with community support and expectations from a growing shire.

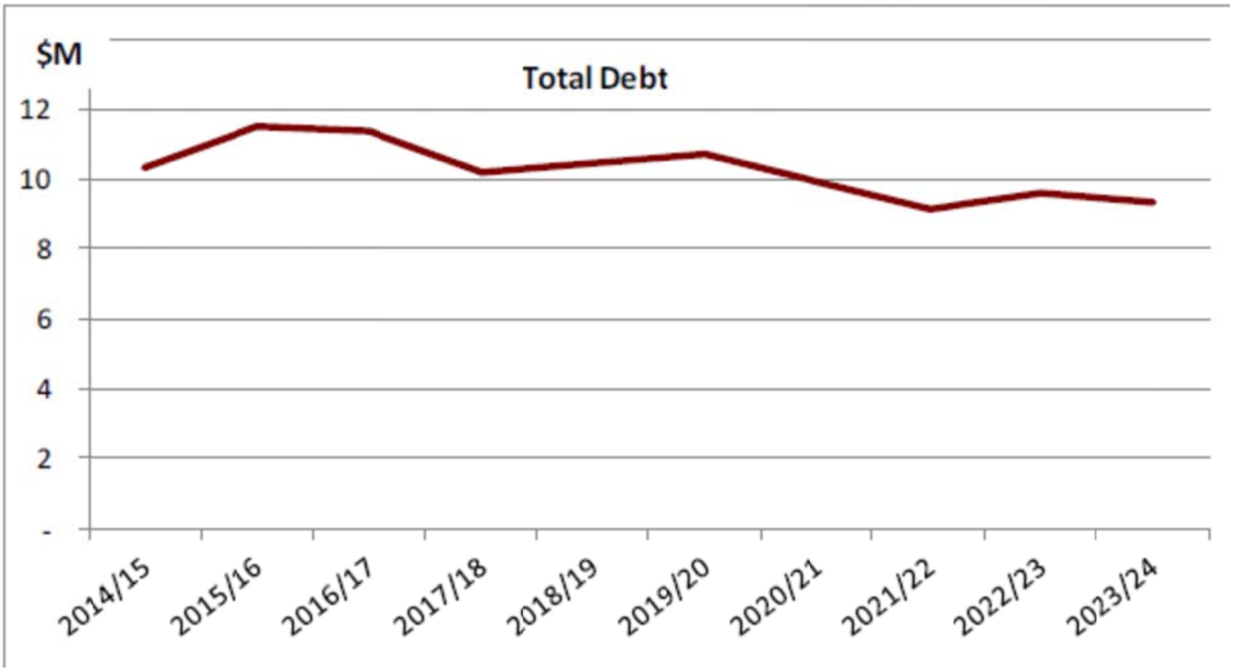
However with a significant shortfall in rates income because of rate capping to CPI our Council Plan and Strategic Resource Plan will all have to be revisited and changed for the ensuring years because our finance model and that of other councils has changed.

In determining an appropriate debt level, the following factors are seen as important: level of debt servicing costs as a proportion of rate revenue; ability to raise revenue in addition to rates; level of realisable assets to support the indebtedness; achieving the right mix of capital works and debt commitments; population growth and demographics; and community needs.

What is the Macedon Ranges Shires Council future debt level?

Council's Long Term Capital Works Guide covers the period up to 2023/24. The Guide aligns with the SRP financial assumptions in section 9 with respect to expenditure and revenue. The Guide predicts that in order to respond to the growing population there will be substantial capital investment in community buildings, community facilities and open space.

Because of the intergenerational nature of this type of capital investment, Council is willing to borrow money to fund capital investment works that may take place. The council graph below shows the estimated debt levels from 2014/15 to 2023/24.



The estimated debt levels in the preceding graph are based on the assumption that all projects within the Long Term Capital Works Guide will proceed. Of course this will now be impacted because of rate capping to CPI.

Whether all projects proceed or not will depend upon circumstances at that time, particularly the availability of government grants. If grants are available the projects may proceed and if they proceed Council may borrow money. For example our "Early Years" facilities are reaching capacity and will need to be expanded. Expansions of this kind are only required about once every 20 years or so. Therefore on the principle of intergenerational equity, it is proposed that borrowings would be used as opposed to funding these works through an abnormal rate increase in the year of construction.
However rate capping to CPI at a lower level will impact the opportunity to increase rate or take out further capital loans.

What is Council's Future Strategic Direction in terms of Debt?

1. Council will borrow funds for investment in capital projects of an intergenerational nature.

2. Council will retain its debt commitment (interest and principal repayments) at or below 6% of rate revenue.

3. Council will ensure its debt level does not exceed $14 million over the ten year financial forecast

Our Rating Strategy, which establishes a framework by which rates and charges will be shared by the community, can be found in our Strategic Resource Plan. Our financial forecast is based on the assumption that rate revenue will increase by 6.6%. This assumption is based on two contributing factors. Firstly, based on historical evidence, we will continue to experience 1.8% growth in rate revenue from new subdivisions and new constructions. Secondly to retain works and services at current levels and standards, we will continue to increase rates and the municipal charge by 4.8%. The proposed rates setting downward will now change this outcome as a result of rate capping.

Between, 1 January 2014 and 31 December 2014, the Consumer Price Index (All Capital Cities) rose by 1.7%.

The costs of providing services, infrastructure and facilities are closely linked to wage costs, construction costs, material costs and contract costs. These costs have nothing to do with the CPI. These costs often increase by more than CPI. There is no doubt that, if the State Government requires local councils to keep the annual increase in total rate revenue (rates, municipal charge and waste service charges) to no more than the annual CPI, then, over time, to remain financially sustainable, local councils will have to reduce their expenditure on services, infrastructure and facilities.

The total rate revenue that we need to generate (rates, municipal charge and waste service charge) in order to balance our 2015/16 draft budget is $41.9 million. This is almost a 6.6% increase ($2.5 million) compared to last year. This is because there is a 1.8% growth each year in our rate revenue due to new subdivisions and new constructions, this results in a 4.8% increase for the average Ratepayer.

Based on the 2015/16 draft budget, the difference between a 6.6% and a 1.7% increase in total rate revenue (rates, municipal charge and waste service charges) in 2016/17 should be -

6.6% increase = $2.7m
1.7% increase = $0.7m
Difference = $2m

In 1995, the Victorian Parliament gave the Minister (under section 185B of the Act) the authority to limit the amount by which councils are able to increase their total rate revenue (rates, municipal charge and waste service charges). The current Victorian Government has said that it will use this authority to restrict the annual increase in total rate revenue to no more than the CPI.

The Victorian Government has asked the Essential Services Commission to develop a “rates capping” framework to apply after 1 July 2016. The Essential Services Commission will take the following factors into account – federal budget cuts to core local government grants; cost shifting by other governments, such as the imposition of additional taxes or levies or increased statutory responsibilities; extraordinary circumstances such as natural disasters; other sources of income available to a council; the council’s overall financial position; and the need to maintain essential community services and infrastructure. The Government has asked the Essential Services Commission to prepare a draft report by July, invite comments from local councils and others and submit its final report by October.

If we make the assumption that rate capping will be set to the current annual CPI of 1.5% and the current minimum rates set by Macedon Ranges Shire Council is 4.8%

this is a shortfall of 3.3% which equates to $300,000 rate revenue per 1% equals $990,000 dollars in arrears in the first year of rate capping for a worse case scenario.

It is too early to make any predictions about taking out debt (future loans at a low interest rate) to support future major infrastructure projects now for our community as you can see our financial planning and modelling has been thrown a significant curve ball with rate capping which will impact our future finances.

However, if the Government accepts the ESC final report and recommendations, we should know what the impact will be on our total rate revenue in 2016/17, before we start preparing our 2016/17 Budget. The key ingredient is to ensure the future financial sustainability of council prior to incurring future debts for infrastructure projects which can wait until we can afford it but we need to ensure we have the rates income funding to all those capital works projects which we have previously committed in previous budgets to the community. Perhaps if the rate capping to CPI is set to low then may be as a council we will have to review our previous commitments to these projects with the community if as a council we cannot afford them.

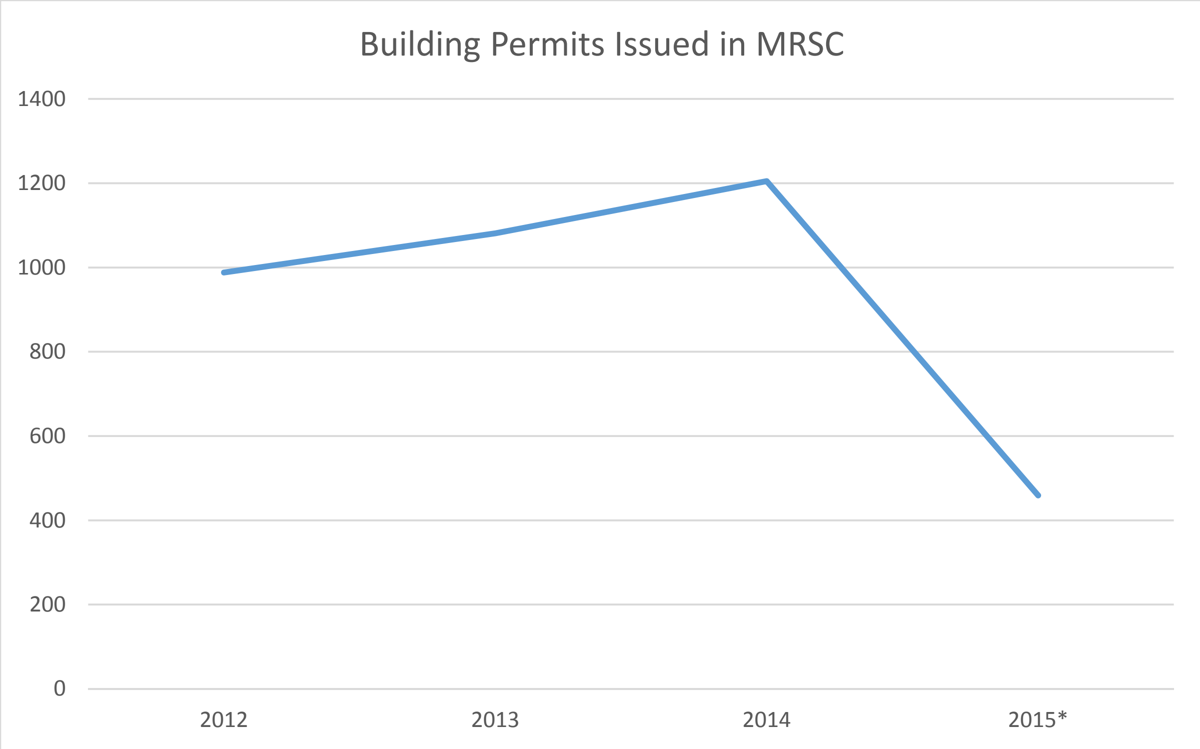
Below is supporting building permits issued in MRSC as evidence to our previous and current growth during my time on council as a positive outcome for our shire but opposed to this future trend is the shadow of rate capping looming overhead and its unknown impact.

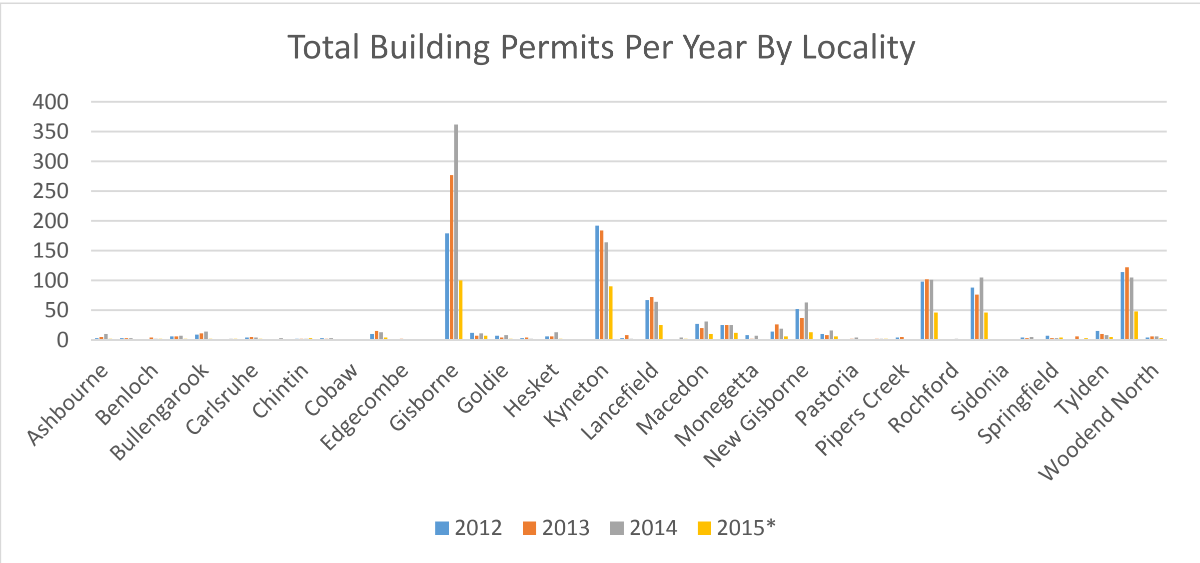
Building Permits issued in MRSC				
	Total	PBS	MBS	% issued by Council
2012	**988**	921	67	7
2013	**1081**	978	103	10
2014	**1205**	1050	155	13
2015*	**459**	387	72	16

* 2015 to 30/06/2015 only

PBS: Private Building Surveyor

MBS: Council's Municipal Building Surveyor





In summary I have grave fears that if or when rate capping is implemented then we as a council will have to look at other means to balance the books and ensure we keep paying our debts and maintain our current operational levels into the future.

Some of these considerations will be:

a) What is the core services of Council with a comprehensive review?

b) Undertake a ‘cost benefit analysis’ of those services deemed non-core.

Council has a finite income and outgoings to manage our current population needs and expectations and this will be significantly challenged as a shire whatever the ESC final recommendations with State Government endorsement sets as a future rating for our shire.

Therefore it is important for the State Government to seriously consider the impact of a future rate capping to CPI on our shire as previously stated with supporting evidence.

To ignore this may cause current and future state governments some consternation to again review this policy and its implications into the local government sector and community.

Regards

Cr Russell Mowatt

Deputy Mayor

Macedon Ranges Shire Council

To: localgovernment@esc.vic.gov.au
From: Cr Russell Mowatt
Date: 30/08/2015 12:05:34 AM
Subject: RE: ESC Rate Capping Submission - Addendum

To whom it may concern.

Below and attached is an addendum to my original ESC Rate Capping Submission dated 28th August 2015.

I'm submitting copies of the Southern Regional Strategic Plan Final and the Loddon Mallee South Regional Growth Plan as supporting evidence of my original submission to the ESC.

Fundamentally it is very important the ESC and State Government give these plans significant weighting prior to any future fixed rate capping to CPI for the Macedon Ranges Shire Council.

Why?

Because without the adequate monetary resources 'council allocated rates' our council and other councils in our region will not be in a financial position to deliver the outcomes planned for our communities future in these plans.

It would be remiss of the ESC and the current State Government to ignore these facts when determining any future fixed rate capping to 'CPI' in our shire and region.

It would be a reasonable assumption based on my original submission that when monies are taken out of the local government sector there is a considered risk to providing some future services, capital projects, asset renewal and intergenerational equity.

Perhaps there is also an argument that a recessionary economic climate may ensue with the loss of jobs in the local government sector as a result of a fixed rate capping to 'CPI'.

Therefore a SWOT Analysis would be strongly suggested by the ESC to ensure all options and there associated risks are considered prior to any implementation of any rate capping policy by the state government.

Regards

Cr Russell S Mowatt
Deputy Mayor MRSC