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Mr Chow
Local Government Division
Essential Services Commission
Level 37, 2 Lonsdale Street
MELBOURNE VIC 3000

Dear Mr Chow

Feedback on the Growth Study Report (by Arup)

Thank you for the opportunity to provide feedback on the *Arup Growth Study Report*, which was recently released for feedback by the ESC.

Having been involved with this project since late November 2016, and having now reviewed the Growth Study Report that was released on 20 September 2017, Casey has the following observations, comments and suggestions for consideration here:

Casey welcomes the findings that growing councils are required to spend more

Casey appreciates that the Growth Study has been commissioned and undertaken, which resulted from the ESC's own internal reviews (as advised by the ESC in late August 2016), as well as the October 2016 report from the external review on the year 1 implementation of the Fair Go Rates System (FGRS) undertaken by Mr Peter Brown.

Casey welcomes the finding, supported by clear evidence, that there are significant upfront expenditures and investment required as a result of population growth, presenting financial challenges for 'growth' councils. This finding is consistent with past submissions that Casey has made on this particular item.

Casey notes, in particular, the finding that greenfield infrastructure costs 24 times more than infill (p. 11).

Comments on Arup's findings, including gaps and weaknesses

No evidence that the additional costs of growth are 'self-funding'

Apart from the initial finding that growing Councils do require more financial resources compared to non-growth Councils, the most important claim in Arup's Report is that "we believe that it is possible to use debt financing to bridge the gap between capital expenditure today and the income to be raised from residential rates and charges in the future."

Unlike the first finding, however, there appears to be little or no evidence to support this "belief".

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Section 4.1 of the Report states that if there is a 'revenue gap' for desirable and efficiently delivered infrastructure and services, then "fundamentally the challenge of growth is one of timing"

However, this is only true of a *temporary* revenue gap.

If there is a permanent revenue gap between the additional costs of delivering new infrastructure and services to accommodate growth (including any finance costs), and the revenue that flows from that growth (e.g. DCP, grants, future rates and charges), then debt financing cannot be used to 'bridge the gap' – and would in fact exacerbate the problem.

As far as Casey can determine, there is essentially no evidence in the Report to demonstrate that the additional financial resources required for growing Councils is only a temporary gap. In other words, no evidence is presented that growth is 'self-funding' over the longer term.

In the Executive Summary, the finding from Section 4.1 of the report is said to follow the review of three development studies. In the body of the report, however, these Case Studies (in Appendix D) are considered in section 3.3.2 (p. 33) in relation to the sufficiency of DCPs.

Put simply, the case studies do not support the claim.

All three of the case studies show that DCPs (and grants) did not fully fund the new infrastructure required. No analysis was undertaken that the increase in rates as a result of the growth would cover the gap (plus any financing costs) over time.

Furthermore, as ARUP notes (citing a study by SGS, see p. 34), caution should be used in generalising from any case study of this kind. DCPs can vary significantly, so these 3 particular DCPs cannot be taken as a proxy for the position and impacts of all DCPs on all Councils, and it is not clear that the full value of any gaps here has been quantified or modelled.

The upfront investment for new infrastructure, including the items transferred from developers, also come with future operating cost, maintenance and renewal liabilities across their lifecycle. As a result, not all of the increase in Council rates and charges attributable to growth is available to pay for the upfront capital costs (including any finance costs) of development. This 'lifecycle analysis' has not been investigated or considered in the Report.

Considering the report as a whole, it is fundamentally unclear how there can be an indirect finding and conclusion that growth Councils can have higher up-front costs (or required investment) for infrastructure to service its growing communities, and then operate without any additional financial or service delivery impacts with the same rate cap as a 'non-growth' Council over the longer term.

Asset Management Processes

Casey understands and supports the importance of ensuring that there are effective asset management and resource allocation processes in place to manage growth. This has been a key focus of Casey to redesign and implement evolutionary improvements of Council's related and complementary processes.

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However, it is important to consider one of the early principles of the design of the FGRS, and in particular the intent that Councils should not have to do or create new processes to complete and submit a variation application.

Many Councils participate in the MAV Step Program and/or self-assess under the NAMAf. Casey would strongly suggest that these programs be used for this purpose, or be strengthened if required, rather than requiring Growth Councils to adopt new and higher standards such as demonstrating ISO compliance.

The proposed creation of different and increased criteria for growth based applications is in conflict with the administrative simplicity that should be guiding the operation of the FGRS. It would also be a perverse overall outcome from the report, that despite a legitimate need having been identified, that a stronger criteria and more questions would apply for a growth based application under the FGRS.

Utilisation of DCP/ICP funds

Casey notes the proposal in the report for the potential funding of temporary facilities and bridging finance costs within an approved DCP/ICP. Although a nice idea, this concept belies the reality of the current operation and development of DCP/ICPs.

Required infrastructure is already being reduced or not included in DCP/ICPs being developed. There are capped amounts for the level of DCP/ICP contributions that can be applied, so if these items were to be included, they would also need to come at the cost of something else that would otherwise have been developed within the capped amount allowed.

Council would welcome the inclusion of more items in DCP/ICPs, however, that would need changes to the current guidelines in this space, and also has a potential trade-off with housing affordability – as higher levels of upfront DCP contributions would feed into the price of the impacted land/residential lots.

Use of Debt

Casey acknowledges that debt can be part of the solution to assist with meeting the funding challenges of providing the required services and infrastructure for its growing community. However, based on our recent engagements with the Casey community, in late 2015 and early 2017, it is also clear that our community has a very conservative attitude to the use of debt.

As indirectly noted in the Report, Casey is currently taking out its largest loan ever, \$62M for the construction of the Bunjil Place project, and once this loan is paid off, plans to use further borrowings in the future to fund regionally significant projects at the end of its current Long Term Financial Plan.

Noting that the only published information on debt ratios is from VAGO, it is essential that the ESC, LGV and the sector workshop, discuss and agree on updated guidelines and parameters in relation to debt.

The concept of the preferred range for the level of debt being linked to impacts of repayments on operating budgets (pg 42) would be workable, and would also allow for changes in interest rates in the future.

Noting that 40% is the current “Low Risk” for levels of indebtedness, it is natural that Councils would then aim for that as their debt ceiling.

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It is also essential that any debt taken on is able to be paid-off in a reasonable timeframe, so that the property owners receiving the benefit are paying for it. As such, the financial cost of borrowings needs to be taken into account in assessing the full costs of capital works, and any resultant variation application.

Casey notes that, based on its previous modelling, and noting the growth period still before Council of over 20 years, combined with the significant cumulative impacts of a CPI rate cap, the use of debt will only be part of the solution and funding mix.

Access to GAIC funding for Council delivered assets

There is a suggestion that Councils could look to access GAIC funding for certain types of assets, including new regional facilities. Casey would note that the ability to potentially access funding for these types of assets has only been indirectly flagged in the revised GAIC guidelines that were released in March 2017, which was after Casey had had interaction with ARUP.

Prior to this, it was very clear in the guidelines, and it is still the primary scope, that GAIC would only be used for State provided items – although even at that level, it has only been sparingly applied so far.

Casey's summary of the most recent GAIC guidelines is shown below.

- The GAIC funds can only be used for the purpose of State Funded Infrastructure
- Growth Council and others can "propose" projects however the funding submission must be made by the relevant State Agency
- The Guidelines indicate the funds can be allocated for Regional Community facilities such as Libraries and Major Recreational Facilities
- Priority for transport related projects is targeted towards infrastructure that supports Public Transport, Walking and Cycling

It should be noted that there have been no GAIC funded initiatives proposed by Councils that have been successful so far. It is hoped that this funding mechanism can be further relaxed or opened up for the defined asset types for Councils to access to provide important and required infrastructure for their growing communities. However, this would only mitigate a small part of the funding and infrastructure provision gaps facing growth Councils.

Possible Application of s185D of the Local Government Act

Despite it being allowed for in the Part 8A - Rate Caps section of the Local Government, there was no canvassing or consideration in the report of the use of s185D of the LGA for the Minister to set a different cap for "a class of Councils", for which the Growth Councils could be considered a class.

Comments on the questions proposed to assist the ESC in assessing higher cap applications related to Growth

Question 1 – rate of population growth over the next four years?

On page 5 of the report, it is indicated that 3% population growth would be a circumstance that would potentially warrant a variation to the rate cap. There is a reference to section 2.1 of the report, however, in that section of the report, there is no discussion or basis for how this particular figure "3%" was arrived at, as compared to 2% or 2.5% for instance.

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Casey notes that the following items should also be considered here:

- There should be consideration of an absolute population increase threshold. For instance, Casey expects to be constantly increasing its population by 8,000 to 10,000 people (or the town of Gisborne) each year for the next 20+ years, so even if the “% increase” reduces, the requirements for ongoing development and capital investment will remain the same.
- Noting the backlog nature of some infrastructure and service provision for growing communities, or the need for growth to reach certain triggers for some facilities, past growth is also a definite and necessary consideration here.

Question 2 – Percentage of expenditure for capital works and asset management

Arup has proposed a rate of ‘at least 30%’, again without any apparent discussion or basis. Given that Arup notes that “capital works accounted for 20-25% of interface council budgets in 2015/16” (p. 11), a 30% threshold appears arbitrarily high.

Question 3 – Approach to asset management and delivery

Casey supports the principle that Councils should pursue effective and efficient approach to asset management.

Casey notes again, however, that applying a new and higher standard on Councils experiencing financial challenges as a result of growth is a perverse outcome and inconsistent with the FRGS.

Question 5 – Use of available income

The Report includes a suggestion about the potential use of Special Charge Schemes for some infrastructure items (pg 38, section 3.3.6). Casey does not support this proposal, as it would be a significant inequity for those property owners that would be subject to it.

Casey understands the proposal to be that the Special Charge Scheme would apply mostly to newer properties in the growth areas, as they would have the required nexus with the localised benefit required for a special charge scheme. However, these same property owners have already paid for the cost of DCP/ICP contributions (and GAIC) in the price of their house and land packages. This would be a further impost on these new residents, which would only result in them being able to access the types of infrastructure that have previously been provided without this targeted mechanism in other parts of the municipality.

Given that Arup noted that ‘barriers on the use of special rates schemes’ is an area for further investigation (p. 51), Casey requests that this not be considered as a factor until the outcomes of any such study.

Question 6 – Approach to debt

Further to Casey’s comments above on debt, Casey requests that the ESC provide further guidance on how the amount and use of debt will be assessed.

This matter goes to the transparency of the operation of the FGRS, and the need for all participants to have certainty about the scope and intent and assessment methodology of all of the criteria that apply.

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Comments on the process for the Growth Study Report

Casey is disappointed that the actual process followed for this Growth Study Report has been different to what was presented to participating Councils on 24 November 2016 by the ESC.

First, although it was indicated that the scope of the study would incorporate Councils' feedback raised at the workshop on 24 November, and would be circulated to participating Councils by 30 November, in Casey's view the scope was heavily influenced by what the ESC was seeking from the study. Additionally, the scope was only provided to the Councils after the RFQ was sent to the 3 consultants.

The second major area was the indication was that the consultant would test their findings with Councils. This did not occur with the main findings of the final report – many of which do not appear to be evidence-based, and/or are not reflective of the questions and requests for information put to the Councils by the consultant.

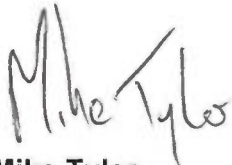
Thirdly, Casey notes that the Growth Study project was planned to be completed by 31 March 2017 (ostensibly to inform the 2017/18 Rate Cap Variation submission timelines), however the report was not released for consultation until 20 September 2017.

Conclusion

Thank you again for the opportunity to provide feedback on the *Arup Growth Study Report*. Given what Casey considers to be material gaps in the Report, Casey requests that the ESC provide timely advice on its next steps in relation to how Growth will be considered as part of the FGRS.

If you require any clarification or further discussion on the matters raised in this feedback, please contact Council's Chief Financial Officer, Mr Andrew Davis.

Yours faithfully



Mike Tyler
Chief Executive Officer

17/10/17