

# Review of Kiama Municipal Council

Report to the Minister for Local Government

January 2024

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Review of Kiama Municipal Council

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# Executive summary

The Hon Ron Hoenig, MP

Minister for Local Government

and

Mr Brett Whitworth

Deputy Secretary Office of Local Government

Department of Planning, Housing and Infrastructure

Dear Sirs,

Re: Kiama Municipal Council

It is with pleasure that I submit my report in response to your request for advice on whether:

- A. Council has recognised its financial and budgetary challenges and is moving appropriately to address the challenges for the long-term benefit of its community.
- B. Council has made the appropriate decisions on asset sales, particularly:
  - i. Whether the assets should be disposed or whether they could be retained, and
  - ii. Whether there is a longer-term value to retaining the assets.
- C. If Council is right to dispose of the assets, is it getting the best value for the assets.
- D. Whether the Minister should appoint a Financial Controller to oversee the financial decisions of the Council, using the provisions of the Local Government Regulation to frame the advice.

The review was undertaken by:

- examining documents made available to me by Office of Local Government (OLG)
- holding discussions with and obtaining clarifications from the Mayor and CEO, Kiama Municipal Council (KMC)
- holding discussions with the Chairperson Audit, Risk and Improvement Committee, Chairperson Finance Advisory Committee (a volunteer) Chairperson Blue Haven Advisory Committee (a volunteer)
- examining Council reports and decisions.

Access to confidential Council information was not sought nor provided. This summary is supported by the following more detailed report.

## Background

In December 2021 the Chief Executive Officer (CEO) to the Council, self-reported the Council's financial and governance issues to the Office of Local Government, including:

- An inability to produce 20/21 annual financial statements.
- A negative trend of increasing liabilities and trading losses.
- Council's Aged Care facility/service (Blue Haven) running at a loss.
- Poor understanding of the loss, efficiency and compliance of the Blue Haven Aged Care facility.
- Concerns whether Council's Auditor would certify Council as a going concern.
- Restricted funds had been illegally applied to general use.

In November 2022 the then Minister for Local Government issued a Performance Improvement Order (PIO) on the Council and appointed a Temporary Advisor under the Local Government Act. The Council was required to address the financial issues it faced including:

- Review Council's compliance with accounting principles.
- Review Council's strategies to improve its immediate financial circumstances.
- Develop strategies to ensure its long-term financial security.

Plus, a range of requirements to improve regulatory compliance and financial viability of Blue Haven Aged Care facility.

Kiama Municipal Council is small in terms of area, population, and financial capacity and flexibility. In fact, of the Councils outside of the Metropolitan area and to the east of the Great Dividing Range, Kiama Municipal Council is one of the smallest. Therefore its ability to find innovative solutions to its circumstances are extremely limited.

Also, it is the only Council east of the Great Dividing Range operating an aged care facility.

The Long-Term Financial Plan (LTFP) proposes Council reach financial sustainability in 2031/32 however this report proposes this is achieved by FY 2026/27.

It is evident that the Council has for many years and continues to 'live beyond its means'. In the past it has operated and taken decisions without proper financial accounting, records and reports.

The current Council has been made aware of and recognises past failures but is moving too slowly to achieve surplus budgets and become financially sustainable.

## Response to the Brief

### *A. Whether Council has recognised its financial and budgetary challenges and is moving appropriately to address the challenges for the long-term benefit of its community*

The Council's financial position is dire!

It is not meeting the principles of sound financial management as set out in the Local Government Act. Past financial reporting has been such that adequate financial management was not possible.

#### Analysis

Council has accepted responsibility for the financial situation and is taking steps to address its circumstances. Evidence of its financial situation is provided through:

- the Council relying on asset sales to produce a surplus and without asset sales the FY 23/24 budget will be in deficit of approximately \$12m.
- the Capital Works Program relies on grants and external funding.
- Council does not have discretionary funds to finance additional capital works or unplanned maintenance.
- Council not having the funds to install the necessary infrastructure if it was to introduce paid parking.
- Council not having unlimited assets it can divest so this income stream will soon run out.
- the sale of Blue Haven Bonaira being essential to reduce debt and improve liquidity.

A significant Special Rate Variation (SRV) may be required but this should not be pursued until all other options are exhausted or if it becomes evident that a SRV is required to meet the financial sustainability target.

Whilst Council has been made aware of its financial challenges, the structure of the FY 2023/24 Budget demonstrates the Council is not addressing its financial challenges with the urgency required. Expenditure must be reduced.

The balance of Council's unrestricted cash varies from month to month and when liquidity is low, cash is boosted through transfers from the Land Development Reserve.

Good progress is being made on updating information technology (IT) systems to improve financial reporting and governance arrangements.

Council is facing litigation over the sale of Akuna Street (Mitre 10 site) and if this is successful and not covered by insurance, Council will be at significant financial risk. A negotiated settlement will also severely impact on Council's finances.

*B. Whether Council has made the appropriate decisions on asset sales, particularly.*

- i. Whether the assets should be disposed or whether they could be retained, and*
- ii. Whether there is a longer-term value to retaining the assets.*

To address its critical financial situation and challenges, Council has adopted Strategic Improvement Plan 2 which guides Council in actions to improve its immediate financial circumstances and look to its long-term financial sustainability.

Council is pursuing the actions in close consultation with the Office of Local Government, its Audit, Risk and Improvement Committee and its Finance Advisory Committee.

Key actions include:

- Divestment of selected assets including Blue Haven Bonaira
- Achieving savings and efficiencies
- Business and service reviews
- Exploring revenue opportunities

The latter three actions will not achieve the turn around necessary to improve Council's liquidity.

Council has adopted a Property Plan which commits Council to:

- seek the best value from its property holdings to provide community and economic benefits.
- utilise returns from land holdings to supplement revenue sources and minimise the demand for increasing rates above rate-pegging or reducing services.
- hold returns from property sales in a Property Reserve to seed other property developments or acquisitions.
- undertake business cases to assess and compare relative outcomes through financial tools such as NPV, return on investment and potential dividends or yields, together with relative impacts on Council's finances and services.

Whilst the commitments include holding sales returns in Reserve to seed other property developments or acquisitions, it is also being used to meet cash flow requirements.

Under the Property Divestment Plan, Council has taken decisions to sell three land holdings, Akuna Street (2 properties) and Irvine Street currently on the market, plus the loss-making

business, Blue Haven Bonaira. The 2023/24 Budget lists a number of additional land holdings to be sold.

The Budget shows an overall surplus of \$18.5 million due to a predicted \$31.2 million from the gain or profit from asset sales, primarily the forecast sale of Blue Haven Bonaira.

Excluding sale of assets, the budget is in deficit by \$12.7 million, however if predicted asset sales are not achieved the deficit could be higher.

Council's Cash Flow and Sustainability Strategy, adopted 28 February 2023, identifies asset divestment as a key element in its financial recovery.

Of the sales to date and upcoming sales the following amounts have been/will be transferred to the Land Development Restricted Reserve, in accordance with one of the commitments in the Property Plan:

- Akuna Street (Mitre 10) \$8.4m
- Akuna Street (Car Park) \$2m
- Irvine Street - all net funds will be applied to the Reserve however, this Reserve is also used to meet liquidity issues.

## Blue Haven

Paul Sadler Consultancy and Stewart Brown were engaged by Council to undertake the review of Council's Aged Care Facility Blue Haven.

The review found that the residential aged care operation at Blue Haven Bonaira was in deficit to the value of \$5.26m in FY22, offset by surpluses in other sections of Blue Haven. The amount of the loss in previous years had never been understood as the financial position of Blue Haven had always been reported as part of Council's consolidated accounts. This was confirmed by The Auditor General for New south Wales in her letter to the Minister for Local Government on 16 August 2022.

Council is now able to provide more accurate reports on the financial performance of Blue Haven.

It was reported to the July 2023 Council meeting that the Blue Haven Bonaira Residential Aged Care "continues to operate at a substantive loss, currently \$5.34M as of 31 May 2023 compared to \$4.34M at 30 April 2023".

NB: Council's rate revenue is in the vicinity of \$26m.

The September 2023 Monthly Financial Report for Residential Aged Care suggests a \$1m net deficit for the first quarter compared to a budgeted loss of \$591k.

The Paul Sadler review also highlights the increasing requirements for residential aged care which is the major focus for aged care reform in Australia. The higher standards of care, the



challenges in staffing and the reliance on agency staff is unsustainable. The community care services suffer from the same agency cost overheads.

The review's analysis of the 'Keep', 'Partnership' and 'Sell' options overwhelmingly rated the 'sell' option as the preferred way to improve Council's liquidity, reduce risk and enable quality care and accommodation.

Council will consider tenders for Blue Haven Bonaira at an Extraordinary Meeting in early February 2024.

## Conclusion

Whilst there is a level of community ownership and sentiment towards Blue Haven, Council cannot take the financial and operational risk to maintain ownership and operation of Blue Haven Bonaira.

The asset divestments have been supported by the ARIC, the Finance Advisory Committee and the Temporary Advisor appointed by the then Minister.

Council has been diligent in its analysis of the options for Blue Haven and in identifying the potential of holdings through the Property Plan.

Adherence to the Property Plan answers the question of whether the assets should be disposed or whether they could be retained.

The only two sales to date, the Akuna land holdings, have been disposed of as originally intended providing immediate and necessary financial benefit being applied to boost Reserves, reduce debt and supplement income.

Local government and particularly Kiama Municipal Council, is not resourced and does not have the skills and expertise to manage the ever increasing complex and regulated residential aged care facility. The sale of Blue Haven Bonaira will bring immediate and ongoing financial benefit and Council will have disposed of a loss-making business.

In normal operating circumstances it is preferable for a Council to retain property assets, particularly if those holdings are generating a revenue stream. The land holdings sold or planned to be sold by the Council were/are not generating income and were/are absolutely necessary to improve liquidity and to reduce debt.

Without the sales Council would not be able to maintain liquidity.

Many of Council's financial problems can be traced to the lack of adequate reporting on Blue Haven. Now that better financial measurement is available and there is closer scrutiny on the operations of Blue Haven Bonaira, it is obvious Council does not have the skills and expertise to manage residential aged care or to meet the standards now required by government.

Council cannot retain the loss-making business Blue Haven Bonaira which has only a two-star Clinical Quality rating.

*C. If Council is right to dispose the assets, is it getting the best value for the assets.*

Property divestments are conducted strictly in accordance with the Property Plan and for significant sales, probity advisors are appointed.

Prior to going to market, a valuation is obtained but the real value of a property is what the buyer is prepared to pay at the time.

- Akuna Street (Mitre10) sold for \$8m above valuation.
- Akuna Street (Car Park) sold slightly below the lower end of the valuation range but at a price deemed satisfactory to the Council considering the market at the time.
- Blue Haven Bonaira and Irvine Street sales have yet to be finalised.

Under the Property Plan the Council will also 'undertake business cases to assess and compare relative outcomes through financial tools such as NPV, return on investment and potential dividends or yields, together with relative impacts on Council's finances and services'.

It is considered Council has to-date obtained the best value for its two completed sales.

*D. Whether the Minister should appoint a Financial Controller to oversee the financial decisions of the Council, using the provisions of the Local Government Regulation to frame the advice.*

Ministerial intervention with Kiama Municipal Council has occurred through the issuing of a Performance Improvement Order (PIO) in November 2022 and the appointment of a Temporary Advisor at that time.

The Temporary Advisor's appointment concluded in June 2023.

The financial and governance issues facing the Council were a result of failures of previous Councils. The current Council is aware of the challenges and has commenced addressing them.

The recommended option is to issue a new or vary the current PIO.

Subject to the progress Council makes, the Minister can then consider whether a Temporary Advisor and/or a Financial Controller should be appointed or more extreme intervention.

The suggested PIO recognises the progress to date but proposes to emphasise the urgency required to address the finance and governance issues faced by Council.

The PIO would inform the current Council, candidates for election in September 2024 and the incoming Council, that the Council's operating expenses must be reduced and that there are no discretionary funds available for additional capital projects.

The attached detailed report reviews Council's response to the existing PIO under each requirement. The report also suggests the actions which could be included in the varied or new PIO.

#### **Financial Controller/Temporary Advisor**

It is recommended that at this time neither a Financial Controller nor a Temporary Advisor be appointed and that the response to a new or varied Performance Improvement Order be monitored by the Office of Local Government through reporting requirements.

The Minister would be able to intervene at any time should progress be deemed to be unsatisfactory, particularly if Council is not on track to reach a point of financial sustainability by 2026/27.

John Rayner PSM

17 January 2024

# Purpose

The Minister for Local Government, through the Office of Local Government, is specifically seeking advice in the form of a short, written report on whether:

- A. Council has recognised its financial and budgetary challenges and is moving appropriately to address the challenges for the long-term benefit of its community.
- B. Council has made the appropriate decisions on asset sales, particularly:
  - I. whether the assets should be disposed or whether they could be retained, and
  - II. whether there is a longer-term value to retaining the assets.
- C. If Council is right to dispose the assets, is it getting the best value for the assets, and
- D. Whether the Minister should appoint a Financial Controller to oversee the financial decisions of the Council, using the provisions of the Local Government regulation to frame the advice.

The review was undertaken by:

- examining documents made available by Office of Local Government.
- holding discussions with and obtaining clarifications from the Mayor and CEO, Kiama Municipal Council.
- holding discussions with the Chairperson Audit, Risk and Improvement Committee, Chairperson Finance Advisory Committee (a volunteer) Chairperson Blue Haven Advisory Committee (a volunteer) and former Temporary Advisor Peter Tegart.
- examining Council reports and decisions.

Access to confidential Council information was not sought, nor was it provided.

# Background

In responding to the brief, it is important to consider the dire financial standing of the Council.

In December 2021 the Chief Executive Officer (CEO) to the Council, self-reported the Council's financial position to the Office of Local Government (OLG). The financial and governance issues facing the Council included:

- An inability to produce 20/21 annual financial statements.
- A negative trend of increasing liabilities and trading losses.
- Questions raised about Council's liquidity and viability.
- Council's Aged Care facility/service (Blue Haven) running at a loss.
- Poor understanding of the loss, efficiency and compliance of Blue Haven.
- As a result of changed accounting systems Council was unable to produce reliable financial reports.
- Concerns whether Council's Auditor would certify Council as a going concern.
- Significant cost overrun in the establishment of Blue Haven Bonaira.
- Restricted funds had been illegally applied to general use.

In November 2022 the then Minister for Local Government issued a Performance Improvement Order (PIO) on the Council and appointed a Temporary Advisor under the Local Government Act.

The PIO required council to address the following:

- Council's financial management
  - Review Council's current financial circumstances against Council's Strategic Improvement Plan (SIP).
  - Revise the SIP as necessary.
  - Implement actions of the SIP.
  - Review Council's compliance with accounting principles.
  - Review Council's strategies to improve its immediate financial circumstances.
  - Develop strategies to ensure its long-term financial security.
  - Undertake a strategic review of its property holdings and investments.

- Blue Haven Aged Care Facility
  - Review Council’s management and operation of Blue Haven.
  - Develop an Operational Plan of Management for Blue Haven.
  - Revise the Operational Plan of Management.
  - Prepare a comprehensive business case outlining options for Blue Haven including lease, sale, joint venture or retention.
  - Review Council’s compliance with relevant legislation including:
    - the use of funds, deposits and bonds,
    - the financial circumstances of the facility,
    - strategies to improve the financial performance,
    - any response to the facilities’ accreditation audit.
- Council’s Financial Accounting and Management Systems
  - Review Council’s current financial accounting and management systems and implement changes.

The PIO required Council to provide four reports of its actions addressing the PIO.

The reports have been completed; the final report lodged 30th June 2023.

In considering Council’s ability to address its financial and governance issues, Council’s relative position needs to be taken into account.

Kiama Municipal Council is small in terms of area, population and financial capacity and flexibility. In fact, of the Councils outside of the Metropolitan area and to the east of the Great Dividing Range, Kiama Municipal Council is one of the smallest. Therefore, its ability to find innovative solutions to its circumstances are extremely limited.

Also, it is the only Council east of the Great Dividing Range operating an aged care facility.

It is evident that the Council has for many years and continues to ‘live beyond its means’. In the past it has operated and taken decisions without proper financial accounting, records, and reports.

The current Council has been made aware of and recognises past failures but is moving too slowly to achieve surplus budgets and become financially sustainable.

# Response to Brief

## A. Whether Council has recognised its financial and budgetary challenges and is moving appropriately to address the challenges for the long-term benefit of its community

The Council's financial position is dire!

It is not meeting the principles of sound financial management as set out in the Local Government Act. Past financial reporting has been such that adequate financial management was not possible.

However, through the actions undertaken and proposed in the Strategic Improvement Plan and this report, the financial standing of the Council can be improved.

The financial position and challenges are evidenced through:

- The self-reporting of the financial issues in December 2021.
- The State of the Organisation Report (December 2021) to the new Council highlighted *“that the matters facing KMC are not unusual to local governments, cash flow, asset management, lack of governance are all issues that councils experience, however the added complexity of the aged care business presents an unusual circumstance.*

*It is worth noting that many of the matters that are impacting on the business have taken decades to arrive at their current state. Across the board there has been a lack of planning, governance, resourcing and quality systems and procedures to help inform quality Council decisions”.*

- The fact that the then Minister for Local Government issued a Performance Improvement Order on the Council in November 2022 with an emphasis on financial issues including those emanating from the Blue Haven facility. A Temporary Advisor was appointed at that time.
- The Forsyths' Forensic Report, March 2022 stated, *“The current cash position poses a significant risk to Council's ability to fund its significant debt obligations into the future”* and *“Council has consistently spent outside of its original budget parameters during the period under review meaning that the budgeting process is not achieving its objectives of planning and monitoring expenditure”.*
- The Forsyths' Report made it abundantly clear to Council that it has many challenges and risks, including;

- the inappropriate use of Developer Contributions and non-compliance with EP&A Act.
- unbudgeted project expenditure (Blue Haven) from restricted funds.
- deterioration in Council's cash position.
- risk to Council's ability to meet debt obligations.
- an unfunded component (\$26.5m) of Refundable Accommodation Deposits (Blue Haven).
- a liability of \$92.5m for Independent Living Unit (ILU) deposits.
- Council consistently spending outside its budget parameters.
- the increase in externally restricted funds as a percentage of overall cash poses a risk to Council.
- shortfall of \$18.8m in loan repayments to TCorp.
- risk that council may not have spent sufficient funds on infrastructure.
- Council's budget and monetary process is ineffective as Council is failing to adequately manage funds within budget.
- failure to meet benchmarks set by OLG in key financial indicators.
- August 2022 letter from Auditor General for NSW to the then Minister for Local Government advising of liquidity issues, the key source relating to construction of Blue Haven Bonaira, the unfunded liability of employee entitlements, the adequacy of Council's books and accounts and confirming that Council has never maintained separate ledgers for Blue Haven.
- In considering the FY 20/21 Financial reports the Auditor issued disclaimers of opinion over everything in the financial report being unable to obtain evidence for any balance that was reported.
- For the FY 21/22 the Auditor was able to verify most balances but issued disclaimers of opinion on the value of Property, Plant and Equipment and could not verify the split between restricted and unrestricted cash.
- The recently completed FY 2021/22 Annual Financial Statements:
  - report a net operating loss of \$18,699.
  - Operating Performance Ratio (containing operating expenditure within operating revenue) outside benchmark.



- Unrestricted Current Ratio (adequacy of working capital) outside benchmark. The reason given is “*significant balance of Blue Haven current liabilities and no sufficient cash balance to offset it*”.
- negative performance indicators for Buildings and Infrastructure Renewal Ratio and Infrastructure Backlog Ratio.
- As of 30 June 2022 Council reported payables of \$139,339 as part of its current liabilities. The majority of the payables comprise the aged care accommodation bonds and lease liabilities attached to the independent living units.
- The November 2023 Statement of Investments reports on Cash and Investments held:
  - Externally Restricted \$30,022,634
  - Internally Restricted \$11,766,587
  - Unrestricted Funds \$ 2,563,061
  - Total \$44,352,282

Of concern is that the Total Cash drops to \$40.33m in April 2024 and to \$39.59 in May 2024.

It will be reported that the Unrestricted Funds will be \$4.8m on 31 December 2023.

The Land Development Reserve is being used under the Restricted Funds Policy to meet financial obligations and requirements of Council’s Long Term Financial Plan and emergencies with a resolution from the Council.

Whilst part proceeds of sales may be transferred to the Reserve, it has been drawn on in 2023 when cash flows have been low or unbudgeted expenditure occurs.

The Council has committed to address the financial situation through a range of strategies and actions, however under the Long-Term Financial Plan Council will not be financially sustainable until 2032/2033.

Those strategies and actions include:

- Council adopted its initial Strategic Improvement Plan (SIP) in April 2022 and has:
  - received accreditation for the Blue Haven Residential Aged Care Facility.
  - sold property at Akuna Street to partly restore reserves and working capital.
  - established the basis of improving its financial position through liquidity, property and cashflow plans.
  - opted to pay down \$30m of the debt to TCorp leaving a balance of \$15m.
  - resolved to progress reviews of business units and services, governance arrangements and technology.

- Strategic Improvement Plan 2 which updated the original SIP was adopted by Council in April 2023 with actions including:
  - providing monthly reports to Council on financial position and bimonthly on the SIP.
  - Liquidity Plan adopted.
  - Cash Flow Plan adopted.
  - Long Term Financial Plan adopted.
  - distribution and returns from property divestment used to respond to financial issues.
  - updating Property Plan identifying holdings to be divested.
  - reviewing Council's management and operation of Blue Haven Residential Aged Care Facility.
  - exploring options (lease, sell, joint venture or retain) for Blue Haven.
  - implementing recommendations of Forsyths Forensic Report
  - implementing TechOne finance, HR and Assets systems.
  - improving financial systems and reporting.
  - undertaking service reviews, initially waste, leisure centre, pavilion and holiday parks.
  - exploring revenue opportunities, including paid parking.
  - working with and taking advice from Audit Risk and Improvement Committee and Finance Advisory Committee, both with independent community representatives.
  - selling Blue Haven Bonaira to reduce debt and improve liquidity.
  - transforming organisation and improving governance arrangements.
  - restoring negative restricted funds, replenishing unrestricted and replenishing and strengthening infrastructure reserves.

## Long Term Financial Plan

Long term financial plans are inherently uncertain and become visionary past the first few years. Assumptions need to be made and given the time span for the Plan. Those assumptions may need to be reviewed regularly.

Council's Plan states *"The current Long Term Financial Plan was prepared based on the Strategic Improvement Plan (SIP) and parameters defined in Council's Liquidity Plan and Financial Sustainability and Cash Flow Strategy adopted by Council on 28 February 2023 with the key strategies being:*

- *Asset Divestment in the 2023/24 financial year including sale of Bonaira site and services component of Blue Haven at the end of next financial year.*
- *Refinancing \$15 million TCorp loan with the repayment of the loan tied to sale of Bonaira site and associated business.*
- *Capital Works Program focus on reserve funded projects with minimum allocation from unrestricted cash.*
- *Replenishment of unrestricted funds (working capital).*
- *Achieving operational efficiencies starting from 2024/25 financial year".*

The Long-Term Financial Plan proposes that with the implementation of the strategies summarised above, Kiama Council (consolidated) will achieve a balanced budget with the positive unrestricted cash movement by 2026/27 financial year. It is claimed the positive unrestricted cash movement will continue in future years. *"This will allow Council to build-up its unrestricted cash balance to a sustainable level by 2032/33 financial year".*

The Long-Term Financial Plan (LTFP) recognises the sale of Blue Haven Bonaira will improve the annual income by some \$2 million initially and up to \$4 million per annum thereafter.

Operational efficiencies identified through services review of the general fund operations will result in 3% reduction in expenditures in 2024/25, 5% in 2024/25, and 2% in 2026/27 and 2027/28 (total savings of \$6.6 million).

The LTFP demonstrates three scenarios and their implications of financial performance of Council.

Scenario 1 – Base Case. This scenario represents the Council's preferred outcome and projects a balanced budget by the 2026/27 financial year and an operational surplus by 2031/32.

Scenario 2 – 10% Special Rates Variation (SRV). Improves the Council's financial performance more quickly than scenario 1 and achieves a balanced budget in 2024/25.

Scenario 3 – Status Quo. This scenario demonstrates that the continuation of Council operating Bonaira, including care facilities and ILUs, is unsustainable. The LTFP forecasts ongoing Council deficits and no achievement of a balanced budget in the next 10 years.

## 2023/24 Budget

The Budget shows an overall surplus of \$18.5 million, due to a predicted \$31.2 million from the gain or profit from asset sales, primarily the forecast sale of Blue Haven Bonaira.

Excluding sale of assets, the budget is actually in deficit by \$12 million.

The \$13.9 million Capital Works Program is mainly financed from external sources such as grants.

## Analysis

Council has accepted responsibility for the financial situation and is taking steps to address its circumstances. Evidence of its financial situation is provided through:

- the council relying on asset sales to produce a surplus and without asset sales the 23/24 Budget will be in deficit of approximately \$12m.
- the Capital Works Program relies on grants and external funding.
- Council does not have discretionary funds to finance additional capital works or unplanned maintenance.
- Council not having the funds to install the necessary infrastructure if it was to introduce paid parking.
- Council not having unlimited assets it can divest so this income stream will soon run out.
- the sale of Blue Haven Bonaira being essential to reduce debt and improve liquidity.

A significant Special Rate Variation (SRV) may be required but this should not be pursued until all other options are exhausted or if it becomes evident that a SRV is required to meet the financial sustainability target.

Whilst Council has been made aware of its financial challenges, the structure of the 2023/24 Budget demonstrates the Council is not addressing its financial challenges with the urgency required. Expenditure must be reduced.

The balance of Council's unrestricted cash varies from month to month and is boosted through transfers from the Land Development Reserve.

Good progress is being made on updating IT systems to improve financial reporting and governance arrangements.

Council is facing litigation over the sale of Akuna Street (Mitre 10 site) and if this is successful and not covered by insurance Council will be at significant financial risk. A negotiated settlement will also severely impact on Council's finances.

**B. Whether Council has made the appropriate decisions on asset sales, particularly:**

- I. Whether the assets should be disposed or whether they could be retained, and**
- II. Whether there is a longer-term value to retaining the assets.**

To address its critical financial situation and challenges Council has adopted Strategic Improvement Plan 2 which guides Council in actions to improve its immediate financial circumstances and look to its long-term financial sustainability.

Council is pursuing the actions in close consultation with OLG, its Audit, Risk and Improvement Committee and its Finance Advisory Committee.

Key actions include:

- Divestment of selected assets including Blue Haven Boronia
- Achieving savings and efficiencies
- Business and service reviews
- Exploring revenue opportunities

The latter three actions will not achieve the turn around necessary to improve Council's liquidity.

Council has taken a decision to focus on achieving operational efficiencies and service reviews before considering a Special Rate Variation (SRV).

Over past decades governments and Councils have sold assets to generate boosts to revenues, offset expenditure or to change the method of service delivery.

A current example is Central Coast Council where asset sales is a key element in Council's financial recovery. Sales to date are valued at circa \$85m.

Ideally Councils should establish a Property Reserve/Fund which acquires and protects income earning assets, generates an income stream and finances the purchase of assets which will add to the annual yield of the Fund.

In February 2023 Council unanimously adopted a working draft Property Plan/ Property Divestment Strategy which will be continually worked on by staff and which was reviewed by Council in August 2023.

After considering the status of each property Councillors have given clear direction on assets to be sold. The Property Divestment Strategy goes hand in hand with Council's liquidity strategy aimed at addressing financial issues.

The Property Plan *"tabulates Council's operational holdings and considers scenarios to retain, refurbish, redevelop, recycle, repurpose, partner, sell or lease with future assessment to outline the associated net present value (NPV) or return on investments (ROI) of those scenarios"*.

The Property Plan commits Council to:

- seek the best value from its property holdings to provide community and economic benefits.
- utilise returns from land holdings to supplement revenue sources and minimise the demand for increasing rates above rate-pegging or reducing services.
- hold returns from property sales in a Property Reserve to seed other property developments or acquisitions.
- undertake business cases to assess and compare relative outcomes through financial tools such as NPV, return on investment and potential dividends or yields, together with relative impacts on Council's finances and services.

Under the Property/Divestment Plan, Council has taken decisions to sell three land holdings, Akuna Street (2 properties) and Irvine Street currently on the market, plus the loss-making business, Blue Haven Bonaira. The FY 2023/24 Budget lists a number of additional land holdings to be sold.

The FY 23/24 Budget shows an overall surplus of \$18.5 million, due to a predicted \$31.2 million from the gain or profit from asset sales, primarily the forecast sale of Blue Haven Bonaira.

Excluding sale of assets, the budget is in deficit by \$12.7 million, however if predicted asset sales are not achieved the deficit could be higher.

Council's Cash Flow and Sustainability Strategy, adopted 28 February 2023 identifies asset divestment as a key element in its financial recovery:

*"KMC recognises that asset divestment is simply the first piece of the overall financial sustainability strategy and the second component requires operational efficiency improvements from July 2024 and ongoing. Strategic Improvement Plans, Management focus and leadership with aligned sound governance decisions by Councillors (with advice and recommendations from its supporting ARIC and FAC sub-committees) can and will rectify KMC financial sustainability"*.

Of the sales to-date and upcoming sales the following amounts have been/will be transferred to the Land Development Restricted Reserve, in accordance with one of the commitments in the Property Plan:

- Akuna Street (Mitre 10) \$8.4m.

- Akuna Street (Car Park) \$2m.
- Irvine Street all net funds will be applied to the Reserve however this reserve is also used to meet liquidity issues.

## Blue Haven

Paul Sadler Consultancy and Stewart Brown were engaged by Council to undertake the review of Council's Blue Haven Aged Care Facility.

The review found that the residential aged care operation at Blue Haven Bonaira was in deficit of \$5.26m in FY22, offset by surpluses in other sections of Blue Haven. The amount of the loss in previous years had never been understood as the financial position of Blue Haven had always been reported as part of Council's consolidated accounts. This was confirmed by The Auditor General for New South Wales in her letter to the Minister for Local Government on 16 August 2022.

Also, true costs have not been attributed to Blue Haven Terralong, nor have the Terralong assets been depreciated.

Council is now able to provide more accurate reports on the financial performance of Blue Haven. It is difficult to project the loss for Blue Haven Bonaira for FY23 and the current financial year.

The financial reports for 2022/23 will not be available until April 2024. It was reported to the July 2023 Council meeting that the Blue Haven Bonaira Residential Aged Care *"continues to operate at a substantive loss, currently \$5.34M as at 31 May 2023 compared to \$4.34M at 30 April 2023"*.

NB: Council's rate revenue is in the vicinity of \$26m.

The September 2023 Monthly Financial Report for Residential Aged Care suggests a \$1m net deficit for the first quarter compared to a budgeted loss of \$591k. (Council Meeting 21st November 2023).

The Paul Sadler review also highlights the increasing requirements for residential aged care which is the major focus for aged care reform in Australia. The higher standards of care, the challenges in staffing and the reliance on agency staff is unsustainable. The community care services suffer from the same agency cost overheads.

The consultants acknowledged that the retirement villages, independent living, are a comparative success however, there remains a number of financial and other issues at Blue Haven Terralong.

The review's analysis of the 'Keep', 'Partnership' and 'Sell' options overwhelmingly rated the 'sell' option as the preferred way to improve Council's liquidity, reduce risk and enable quality care and accommodation.

Having resolved to explore all options for Blue Haven, Council considered the report from Paul Sadler on 28 February 2023 and decided unanimously to accept the consultant's recommendation and reaffirmed an earlier decision to divest all aged care assets located on the Bonaira site, including the residential aged care facility, community transport, independent living units and home care services.

Council will consider tenders for Blue Haven Bonaira at an Extraordinary Meeting in early February 2024.

## **Conclusion.**

Whilst there is a level of community ownership and sentiment towards Blue Haven, Council cannot take the financial and operational risk to maintain ownership and operation of Blue Haven Bonaira. The level of community support for the status quo does not suggest other ways to meet the financial challenges facing Council. This is evidenced in the submissions to the Public Inquiry into the reclassification of the Boronia site. Whilst the objections were numerous there were no viable alternatives suggested.

The asset divestments have been supported by the ARIC, the Finance Advisory Committee and the Temporary Advisor appointed by the then Minister.

Council has been diligent in its analysis of the options for Blue Haven and in identifying potential of holdings through the Property Plan.

Adherence to the Property Plan answers the question of whether the assets should be disposed or whether they could be retained.

The only two sales to date, the Akuna land holdings, have been disposed of as originally intended providing immediate and necessary financial benefit being applied to boost reserves, reduce debt and supplement income.

In normal operating circumstances it is preferable for a Council to retain property assets, particularly if those holdings are generating a revenue stream. The land holdings sold or planned to be sold by Council were/are not generating income and sales are absolutely necessary to improve liquidity and to reduce debt.

Without the sales Council would not have the finances to continue.

Many of Council's financial problems can be traced to the lack of adequate reporting, poor decision making and unsustainable policies for Blue Haven. Now that better financial measurement is available and there is closer scrutiny on the operations of Blue Haven Bonaira



it is obvious Council does not have the skills and expertise to manage residential aged care or to meet the ever increasing, complex and regulated standards now required by government.

Council cannot retain the loss-making business Blue Haven Bonaira which has only a two-star Clinical Quality rating.

### **C. If Council is right to dispose of the assets, is it getting the best value for the assets.**

Given its dire financial circumstances Council must dispose of some of its assets, in particular the loss-making business Blue Haven Bonaira. It has taken the decision on Bonaira following consideration of expert advice and recognising the increasing care standards required and that Council does not have the expertise to operate in the residential aged care sector.

Property divestments are conducted strictly in accordance with the Property Plan and probity advisors are appointed for significant sales.

It is noted that litigation has commenced in relation to the Akuna Street (Mitre 10) sale.

Prospects advice will be received by Council in February 2023.

Prior to going to market, a valuation is obtained but the real value of a property is what the buyer is prepared to pay at the time:

- Akuna Street (Mitre10) sold for \$8m above valuation.
- Akuna Street (Car Park) sold slightly below the lower end of the valuation range but at a price deemed satisfactory to the Council considering the market at the time.
- Blue Haven Bonaira and Irvine Street sales have yet to be finalised.

Under the Property Plan the Council will also *“undertake business cases to assess and compare relative outcomes through financial tools such as NPV, return on investment and potential dividends or yields, together with relative impacts on Council’s finances and services”*.

It is considered that Council has to-date obtained best value for its two completed sales.

### **D. Whether the Minister should appoint a Financial Controller to oversee the financial decisions of the Council, using the provisions of the Local Government Regulation to frame the advice.**

Ministerial intervention with Kiama Municipal Council has occurred through the issuing of a Performance Improvement Order (PIO) in November 2022 and the appointment of a Temporary Advisor at that time.

The Temporary Adviser was required to review aspects of Council's financial circumstances and the operation of Blue Haven and to generally advise Council on the implementation of the Strategic Improvement Plan and other financial matters.

The Temporary Advisor's appointment concluded in June 2023.

Whilst the reporting requirements of the PIO have been met, the Order remains in place.

The Minister has a number of intervention options available; the most extreme being the suspension of Council and the appointment of an Interim Administrator or dismissal of the Council (after a public inquiry) and the appointment of an Administrator.

The financial and governance issues facing the Council were a result of failures of previous Councils. The current Council is aware of the challenges and has commenced addressing them.

Extreme options may need to be considered if Council does not urgently advance the actions required to become financially sustainable by 2026/27.

The recommended option is to issue a new or vary the current PIO. Subject to the progress Council makes, the Minister can then consider whether a Temporary Advisor and/or a Financial Controller should be appointed. The suggested PIO recognises the progress to date but proposes to emphasise the urgency required to address the finance and governance issues faced by Council.

The PIO would inform the current Council, candidates for election in September 2024 and the incoming Council that the Council's operating expenses must be reduced and that there are no discretionary funds available for additional capital projects.

In addressing the brief, it is important to review the Council's response to the existing PIO under each of the 13 actions.

### **PIO action 1 - Review Council's current financial circumstances against Council's Strategic Improvement Plan**

Since self-reporting the Council's financial circumstances in December 2021 Council has taken steps to improve its financial standing and to place its significant loss-making business on the market.

Poor financial systems and reporting has led to serious delays and inadequacies in completing Annual Financial Statements.

The FY 2021/22 Financial reports have been completed recently and the 2022/23 Financial Reports should be available by April 2024.

In considering the FY 20/21 Financial reports the Auditor issued disclaimers of opinion over everything in the financial report, being unable to obtain evidence for any balance that was reported.

For FY 21/22 the Audit was able to verify most balances but issued disclaimers of opinion on the value of Property, Plant and Equipment and could not verify the split between restricted and unrestricted cash.

Council is receiving monthly reports on its financial position and bi-monthly on performance against the Strategic Improvement Plan.

- **PROPOSAL: REGULARLY AND CONTINUOUSLY REVIEW COUNCIL'S FINANCIAL SITUATION WITH A VIEW TO BECOMING FINANCIALLY SUSTAINABLE BY 2026/27.**

**PIO action 2 - Revise Council's Strategic Improvement Plan as necessary taking into account the review of Council's current financial circumstances, any findings or recommendations from the FY21 audit and the FY22 audit and the Aged Care Quality and Safety Commission's response to the Section 9-3 Notice for Information.**

The Strategic Improvement Plan 2 contains 74 actions several which have been completed. The actions cover both financial and governance issues. The governance matters included in the FY22 Audit letter can be added to the SIP.

With so many actions monitoring becomes challenging, and it is suggested that an updated Plan with a focus on key financial and governance issues be developed. To draw a line in the sand the new plan could be titled 'Financial and Governance Improvement Plan'.

- **PROPOSAL: REVIEW AND UPDATE THE STRATEGIC IMPROVEMENT PLAN 2 WITH AN EMPHASIS ON THE URGENCY TO ADDRESS THE FINANCIAL AND GOVERNANCE ISSUES COUNCIL IS FACING.**
- **PROPOSAL: TO FOCUS ON THE CHALLENGES FACED BY COUNCIL, CONSIDER BRANDING THE UPDATED PLAN FINANCE AND GOVERNANCE IMPROVEMENT PLAN**

**PIO action 3 - Implement the actions identified in Council's Strategic Improvement Plan and report progress monthly to Council.**

This action has been partly complied with. Financial updates occur monthly and reporting on the Strategic Improvement Plan 2 is bi-monthly.

- **PROPOSAL: IMPLEMENT THE ACTIONS IDENTIFIED IN COUNCIL'S STRATEGIC/FINANCE AND GOVERNANCE PLAN AND REPORT MONTHLY TO COUNCIL ON THE FINANCIAL POSITION AND BI-MONTHLY ON THE GOVERNANCE AND OTHER ACTIONS IN THE PLAN**

**PIO action 4 - Review Council's current compliance with accounting principles including the Act, Local Government (General) Regulation 2021 and Code of Accounting Practice.**

With the implementation of systems and with the recruitment of an experienced CFO, Council's compliance with this requirement is improving. This is evidenced by the Audit Office.

- In considering the FY 20/21 Financial reports the Auditor issued disclaimers of opinion over everything in the financial report being unable to obtain evidence for any balance that was reported.
- For the FY 21/22 the Audit was able to verify most balances but issued disclaimers of opinion on the value of Property, Plant and Equipment and could not verify the split between restricted and unrestricted cash.

- **PROPOSAL: CONTINUE TO IMPROVE COMPLIANCE WITH ACCOUNTING PRINCIPLES INCLUDING THE LOCAL GOVERNMENT ACT, LOCAL GOVERNMENT(GENERAL) REGULATION 2021 AND CODE OF ACCOUNTING PRACTICE**

**PIO action 5 - Review Council's strategies to improve its immediate financial circumstances. Including development and implementation of its Liquidity Plan as per the resolution of Council on 23 May 2022.**

Council has improved its financial circumstances through property divestment improving Council's liquidity. The proposed sale of Blue Haven Bonaira will continue this improvement.

The FY 2023/24 Budget shows an overall surplus of \$18.5 million, due to a predicted \$31.2 million from the gain or profit from asset sales, primarily the forecast sale of Blue Haven Bonaira. However, excluding sale of assets, the budget is in deficit by \$12.7 million.

To properly improve its financial circumstances Council must break from its pattern of adopting and achieving deficit operational budgets. Deficit budget cannot continue, and Council will need to live within its means. Asset sales to prop up the Budget cannot go on forever.

- **PROPOSAL: TAKE ACTION OVER THE NEXT TWO BUDGETS (24/25 and 25/26) TO BREAK THE PRACTICE OF ADOPTING DEFICIT OPERATING BUDGETS WITHOUT RELYING ON PROPERTY SALES.**

**PIO action 6 - Develop strategies to ensure Council's long term financial security.**

Whilst Council has identified a number of areas where it will achieve efficiencies and boost revenue streams, there needs to be more urgency in progressing these actions. For example, service reviews were flagged in Council's initial Strategic Improvement Plan April 2022,

however only preliminary steps have been taken. Other revenue opportunities must be considered.

Council has engaged well qualified citizens to advise it on financial matters through its Finance Advisory Committee and Audit Risk and Improvement Committee (ARIC). The Finance Advisory Committee should be invited to present to Council Briefings and ARIC should present to Council in accordance with the new guidelines.

- **PROPOSAL: IMMEDIATELY REVIEW THE TIMING FOR SERVICE REVIEWS AND REVENUE OPPORTUNITIES TO ENSURE COUNCIL CAN MOVE TO SURPLUS OPERATING BUDGETS AND ENSURE ITS LONG-TERM FINANCIAL SECURITY.**
- **PROPOSAL: INVITE THE FINANCE ADVISORY COMMITTEE TO PRESENT BI-MONTHLY TO COUNCIL BRIEFINGS.**
- **PROPOSAL: PREPARE A THREE-YEAR FINANCIAL PLAN WHICH WILL CULMINATE IN COUNCIL INCREASING ITS UNRESTRICTED CASH BALANCE TO A SUSTAINABLE LEVEL BY FY 2026/27**

#### **PIO action 7 - Undertake a strategic review of its property holdings and investments.**

The review has been undertaken and Council is aware of the opportunities and constraints on the majority of its property holdings. The Property Plan contains policies and disciplines to be observed in deciding on the divestment of a property.

Sales of properties are partly applied to improve liquidity. A further review should be undertaken to examine whether the current Administration Centre, 11 Manning Street Kiama and its uses are appropriate for this valuable site.

- **PROPOSAL: CONTINUE TO INVESTIGATE AND PURSUE OPPORTUNITIES TO BENEFIT FROM PROPERTY HOLDINGS AND INVESTMENTS INCLUDING STRATEGIC HIGHLY VALUED SITES SUCH AS 11 MANNING STREET.**

#### **PIO action 8 - Review Council's management and operations of the Blue Haven Aged Care Facility**

Council has received expert advice on the management and operations of Blue Haven. A decision on the tenders received for Blue Haven Bonaira will be considered by Council in February 2024.

Attention needs to be given to Blue Haven Terralong to address issues including:

- There being no restricted reserve to meet the cost of replacements/renewal of assets.
- The potential to subdivide and sell former nursing home site at Havilah Place
- The appropriateness of the current caretaker model.

- The level of Terralong maintenance fees which are well below market.
- The actual financial result for Terralong when true costs and depreciation are applied and whether because maintenance fees are below market general rate revenue is subsidising its operations.
- Undertaking and making public a dilapidation/building report for Terralong and Havilah.
- Examine options to retain and refurbish Terralong to conform with contemporary Independent Living Units.

- **PROPOSAL: ADDRESS ISSUES ASSOCIATED WITH BLUE HAVEN TERRALONG INCLUDING BUT NOT LIMITED TO:**

- The true costs which should be applied and whether general rate revenue is subsidising its operation.
- The adequacy of current and proposed future maintenance fees.
- Completing and making public a dilapidation/building report for Terralong and Havilah.
- Examining options to retain and refurbish Terralong to conform with contemporary independent living units.
- Establishing a restricted reserve to meet the cost of replacement/renewal of assets.
- Examine the potential to subdivide and divest Havilah place in accordance with the criteria contained in the property plan.
- Review the level of maintenance fees.

**PIO action 9 - Develop an Operational Plan of Management for Blue Haven Aged Care Facility.**

Completed

- **PROPOSAL: COMPLETE PLAN OF MANAGEMENT FOR BLUE HAVEN TERRALONG (assuming the sale of Blue Haven Bonaira)**

**PIO action 10 - Revise the Operational Plan of Management, taking into account any finding or recommendation from the Aged Care Quality and Safety Commission accreditation assessment.**

Completed.

**PIO action 11** - Prepare a comprehensive business case for Council’s consideration, outlining options (lease, sell, joint venture or retain) for the Blue Haven Facility.

Completed

**PIO action 12** - Review and report on council’s compliance with the Aged Care Act 1997 and other relevant legislation regarding the management of Blue Haven Aged Care Facility including but not limited to the following:

- The use of funds, deposits and bonds
- The financial circumstances of the facility
- Strategies to improve the financial performance of the facility
- Any response to the facility’s accreditation audit

- **PROPOSAL: MONITOR AND REPORT ON COMPLIANCE WITH THE AGED CARE ACT AND OTHER RELEVANT LEGISLATION RELATING TO BLUE HAVEN TERRALONG**

**PIO action 13** - Review Council’s current financial accounting and management systems and implement any improvements to these systems.

This work is tracking well but all modules are yet to be installed. Transparency in budgeting is important for the community and the Council. The published draft budget and adopted budget limits transparency in relation to Council’s functions and only contains a table which summarises Income and Expenditure. There is a list of capital projects.

### Budget Summary 2024

Consolidated Revenue	\$
Consolidated Rates and annual charges	28,134,335
User charges and fees	23,002,301
Other revenues	9,086,546
Grants and contributions-operating	15,825,626
Grants and contributions-capital	11,445,385
Interest and investment income	2,387,133
Other income	3,129,931
Net gain from disposal of assets	31,218,368
Total Revenue	124,229,624
Consolidated Expenses	
Employee benefits and on-costs	37,517,824
Materials and Services	39,473,293
Borrowing costs	386,926
Depreciation and amortisation	14,608,055
Other expenses	2,271,786
Total Expenses	94,257,884
Surplus/(Deficit)	29,971,739

Surplus/(Deficit) before capital grants and cont.	18,526,335
S/(D) before capital grants and cont and one-off sales	(12,692,013

The draft and published Budgets should be structured so that councillors and the community can see detail of Council’s programs and activities, funding sources for each capital project and when possible, compared with current and previous year.

- **PROPOSAL: FULLY IMPLEMENT TECHNOLOGY ONE BY MID TO END 2025.**
- **PROPOSAL: RESTRUCTURE THE PRESENTATION OF THE DRAFT AND PUBLISHED BUDGETS TO DETAIL PROGRAMS AND ACTIVITIES COMPARED TO CURRENT AND PREVIOUS YEARS AND FUNDING SOURCES FOR EACH CAPITAL PROJECT.**
- **PROPOSAL: IMPLEMENT THE GOVERNANCE RECOMMENDATIONS FROM THE HOPWOOD REPORT AND THE AUDITOR’S LETTER FROM THE 2021/22 AUDIT.**

## Financial Controller/Temporary Advisor

Currently there is no Financial Controller or Temporary Advisor in place and the Council continues to address the requirements of the Performance Improvement Order. Council is being offered sound advice from the community representatives on its Finance Advisory Committee and the Audit Risk and Improvement Committee.

The CEO and staff are progressing improvements to governance and Council’s liquidity; however, improvements are not proceeding with the urgency the financial situation demands.

The Office of Local Government is monitoring the progress of the Council.

It is recommended that at this time neither a Financial Controller nor a Temporary Advisor be appointed and that the response to a new or varied Performance Improvement Order be monitored by the Office of Local Government through reporting requirements.

In making this recommendation the cost associated with appointing a Financial Controller and/or Temporary advisor is acknowledged. These funds could be applied to engage expertise to assist in meeting the requirements of the PIO, particularly in regard to 11 Manning Street and Blue Haven Terralong.

The Minister would be able to intervene at any time should progress be deemed to be unsatisfactory particularly if Council is not on track to reach a point of financial sustainability by FY 2026/27.

John Rayner PSM

17th January, 2024