9 REPORT OF THE DIRECTOR CORPORATE AND COMMERCIAL

9.1 Blue Haven Terralong Asset Condition Report

CSP Objective: Outcome 4.1 Public funds and assets are managed strategically, transparently and efficiently.

CSP Strategy: 4.1.2 Effectively manage assets and commercial investments, ensuring their relevance, lifecycle needs, and value are optimised in accordance with legislative requirements.

Delivery Program: 4.1.2.2 Develop a strategic plan for the future sustainability and direction for Blue Haven Terralong this will include development of an asset condition and capital works requirements over coming years.

Summary

This report provides the Asset Condition Report (aka Asset Dilapidation Report) for Blue Haven Terralong. The Office of Local Government, as part of the Varied Performance Improvement Order (PIO) Part B, requires the public release of this document. The report conveys facts that are not a complete surprise, but the extent of which and the required funding will no doubt be a shock to the broader community, as it was to Council.

In short, the report conveys that the asset condition is of poor standard, aged and requires significant financial investment to bring it from a condition of “poor” to a standard of “average”. The report also highlights that many of the assets need replacement and renewal, most critically end of asset life conditions are expected to double from 2026 to 2027 if no action is taken. By the end of a 10-year period, 74% of assets by replacement cost will be in Poor-End of Life condition. Findings such as this warrant immediate action be taken. However, the quantum of costs for this work is beyond the means that Council can provide given its financial and operating position, and limited rate base.

The forecast costs over 10 years are as follows (note the report shows fire safety works at $7.5M based on estimates at that time however have increased since to $10M.

Capital upgrade	$35M	
Building rectification / Fire Safety Compliance	$10M	
		$45M
Capital maintenance	$3.8M	
Refurbishment	$2.4M	
		$6.2M
Total		**$51.2M**

***** noting operational costs or staffing costs are excluded above.***

Financial implication

The report shows a need for funding in the order of $45M for capital upgrade and building fire safety rectification works, achieving only a move from “poor” to “average”. This quantum of funding has significant financial implications that will need to be addressed and worked through. Last year Kiama Municipal Council (KMC) included $20M in the Long Term Financial {lan (LTFP) over the next 10 years which was originally intended to be spent on asset replacement and renewal for Blue Haven Terralong. These funds will now need to be diverted from the more strategic asset renewal focus to upgrade and compliance but more importantly increased. Maintenance and refurbishment costs of similar value to the report were also included in the LTFP.

The immediate capital costs required to continue to operate Blue Haven Terralong re summarised in the section above but it is important to note that the asset condition report **does not include** associated costs such as project management, staff time, vacancy costs, alternate accommodation costs.

Bridging the unplanned maintenance/capital costs from $20M to $45M is challenging and may require a whole of government solution, as it is beyond Council’s capacity to fund exclusively. This situation presents a complex challenge for a local government at a time when Council is already struggling to demonstrate financial sustainability and to keep pace with existing service demands for core essential local government services.

When the required maintenance costs are combined with additional capital costs, renewal and operational costs, it becomes evident that innovative future thinking and consideration about Council’s role in the provision of this service is required.

This consideration needs to include whether retirement villages are an essential local government service for KMC to deliver with ratepayer’s funds. Or, if in fact there might be a better option/future if Council re-considered partnering, leasing, joint ventures or divesting. That question needs to be centered on an understanding of what is in the best interest of the residents and ratepayers, and what is financially sustainable for a local government of KMC’s size and scale.

This current situation including the unexpected building compliance fire safety issue is impacting Council resources, both staff and financial. The magnitude of this issue is diverting funding from general operational funding such as rates and fees and diverting staff resources from general operational core council services such as waste, roads and parks, amongst other things.

Staff acknowledge and respect the prior resolution of Council in February 2023 to retain Blue Haven Terralong, which was counter to the professional recommendation and the conclusion of the business case. The role of public servants is to give frank and fearless advice to Elected Representatives, and our staff diligently always perform this task, often in the face of community criticism and reactions.

Whilst it may be possible to secure a loan or approach NSW IPART and apply for a Special Rate Variation (SRV) for the purposes of funding this maintenance work, the community would need to be consulted on their support for an increase to their rates for the purpose of funding the retirement village works. An SRV application can take at least one year to manage and given the PIO requirement to meet a balanced budget this financial year, critical decisions need to made.

Noting that residential rates per capita in Kiama are already at the very high end of the 128 councils across NSW and when considering the general cost of living challenges impacting communities and households at this time, it is highly probable that any proposed increase to rates would be resisted and may not garner community support. For reference KMC receives approx. $23M in general and business rates each year, so a 10% increase yields $2.3M. The average residential rate per household is $2,000 and a 10% increase equates to an additional $200 per household.

Risk implication

Every situation contains inherent risk and this asset condition audit exposes the organisation and community to risks. Noting the PIO requires the release of this information publicly there is a need for both Council and the community to be aware of the risks, and to manage and understand these accordingly. Identified risks include:

- Building compliance and safety
- Financial risk
- Community reaction to the quantum of costs and uncertainty of funding and future delivery models
- Reputational risk
- Operational risk in meeting service expectations and regulatory requirements
- Asset and equipment failure risk
- Destabilising and causing stress / adverse reactions amongst the resident community at Blue Haven Terralong
- Potential need for increases in weekly resident fees
- Potential need to prepare a special rate variation application
- Potential need to proceed to a market sounding conversation on future management models, leasing arrangement, joint venture or divestment options for consideration
- Potential need to partner with State and Federal Governments or discuss funding solutions at a time when government funding is limited
- Increased uncertainty amongst retirement village community which leads to increased vacancies / higher turnover in resident population requiring deposit refunds from immediate cash flow
- Ageing asset base and resident reaction to significant historic underspend on maintenance of council owned assets, and broader equity issues with other council owned facilities that may also require significant funding for maintenance, renewal and replacement
- Cash flow risks negatively impacting sustainability of KMC.

Policy

Varied Performance Improvement Order (May 2022)

Strategic Finance and Governance Improvement Plan

Consultation (internal)

Audit, Risk and Improvement Committee

Finance and Major Projects Advisory Committee

Mayor and Councillors

Office of Local Government

Executive Leadership Team

Management Leadership Team

Communication/Community engagement

Continued resident communication will need to occur on this issue, both with the broader community and the retirement village community. Staff have developed a communication plan and will implement this. Meetings with State and Federal Government representatives will be sought to discuss the issue and ongoing communication with the Office of Local Government will occur.

Attachments

1 Blue Haven Terralong Asset Condition Report⇩

Enclosures
Nil

RECOMMENDATION

That Council:

1. Notes the findings of the Asset Condition (Dilapidation) Report and makes this report public as per the requirements of the Office of the Minister's Varied Performance Improvement Order (PIO), Part B.
2. Notes the report states that the order of capital works and building safety rectification required at Blue Haven Terralong in the next 10 (ten) years is projected to be $45M to bring the condition of the asset from poor to fair with additional maintenance and refurbishment costs of $6.2M resulting in a total of $51.2M
3. Recognises the complex challenges and critical funding required to support the operation, renewal and maintenance at Blue Haven Terralong and delegates to the CEO to undertake the following tasks:
   (a) utilise the planned funding projected in the Long-Term Financial Plan towards the costs of maintenance at Blue Haven Terralong instead of a strategic asset renewal focus.

(b) meet with key stakeholders including retirement village residents and State and Federal Members to discuss this situation and explore future options for funding solutions.

(c) proceed to market testing processes in line with the *Local Government Act 1993* regarding future leasing, joint venture and divestment options for Blue Haven Terralong, and Old havilah vacant site and provide a future report to Council on options for consideration.

(d) ensure ongoing community engagement with the residents of Blue Haven Terralong concerning this report and future considerations, as this council facility is also their home.

Review of PIO requirements

Part B of the Performance Improvement Order (PIO) states the following:

1. *Address issues associated with Blue Haven Terralong including but limited not 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.*
   - *Examine options to retain and refurbish Terralong to confirm with contemporary independent living units.*
   - *Establish 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.*
2. *Complete plan of management for Blue Haven Terralong.*
3. *Monitor and report on compliance with the Aged Care Act 1997, Retirement Villages Act 1999 (NSW), Retirement Villages Regulation 2017 (NSW) and other relevant legislation relating to Blue Haven Terralong.*

General comment

KMC engaged AssetFuture to prepare the asset condition (dilapidation) report (attached). This report assesses the condition of site assets, plant and equipment providing 10 year cost forecasts for asset capital upgrade and maintenance.

KMC engaged Vision (Lifestyle Projects) to prepare a Strategic Review. This work is currently in a draft form and will be considered at the April or May ordinary meeting.

Comment and update for Part B item 1

Asset Condition Report

The report considered the infrastructure, assets, plant and equipment that could be visibly seen (excluding sub-structure works). In summary due to historical underspending, and the advanced age of the various assets noting the most recent Stage 5 is 18 years old, the report shows:

- $35M required over the next 10 years for capital maintenance upgrade
- fire safety upgrade costs of $7.5M and now updated to $10M.
- maintenance and refurbishment costs of $6.2M.

Incorporating $45M into KMC's LTFP additional to maintenance and refurbishment of $6.2M is complex as there is insufficient cash at hand to be able to undertake this immediately. A combination of loans and future options may need to be considered.

It is important to note that being a strict Asset Condition Report, the Report **does not include** further considerations such as project management, contingencies, alternative accommodation, sequencing of works and potential alternate resident accommodation. These and other potential resulting costs are excluded.

Options for Havilah Place

The demolition of the old residential aged care facility is nearing completion. Havilah Place is a catalyst site and strategic consideration of options for this and other catalyst sites have had preliminary discussions and a further update will be provided to Council in a separate report in this agenda.

Establish a Restricted Reserve to meet replacement / renewal costs

This reserve was commenced with the target of $2M per annum. However, due to the building compliance fire safety issue, costs, delayed unit sales and resulting cash flow constraints, the reserve has been utilised.

True costs and whether general rate revenue is subsidising

The strategic review report and any review of Blue Haven highlights that historical financial records showing each of Blue Haven Terralong and KMC separately does not exist beyond 2021-22. That said, KMC now has good financial records and based on recent years' performances indicate that Blue Haven Terralong has been cash positive by an average of $1.3M per annum.

The legacy of aged care and the more recent experience with the Blue Haven Bonaira development have left a significant gap in KMC's balance sheet cash position that is impacting the whole of Council's operations. KMC's rate revenue, fees and charges is relatively small and cannot support and replenish these cash reserves. The cash contribution noted above is beneficial but underspending in asset and facilities maintenance that now requires significant capital expenditure cannot be absorbed by that cash contribution and will place further significant pressure on KMC's cash position. Ratepayers and KMC generally will continue to be impacted by the capital and operational aspects of Blue Haven Terralong.

The 10 year capital upgrade works and building fire safety works of $45M, general maintenance/refurbishment of $6.2M will clearly place significant pressure on future cash flow. This means that unit price increases, sales processes and high occupancy is critical. This will be a major strategic and operational focus and needs to be well resourced to ensure cash flow risk is managed over the next 5 years in particular as the operating position of Council is delicate and marginal.

Maintenance fees

An internal Management review has shown that maintenance fees are low compared to competitors. Low recurrent fees provide a sense of security for residents but Blue Haven Terralong is notably lower than similar retirement village providers, including not-for-profit providers, by circa 20%. It is recommended that options to increase fees be considered. This has been considered in the draft budget in the context of legislative requirements governing fee increases with a first strategy being to increase fees for new future residents. This has been discussed with the external consultant and will form part of the Strategic Review.

The consultant has also indicated that unit prices and the pricing model appears reasonable against the competition and that price increases implemented in recent years have been appropriate and justified. This too will form a part of the Strategic Review.

Refurbish to contemporary standards

The consultant will consider the ‘fit for future’ aspect of the unit stock at Terralong (and not the specific matters in the Asset Condition Report). Initial discussions clearly highlight Stage 1 as a key priority but also the industry trends and requirements for improved accessibility as ‘ageing in place’ expectations are sought by consumers when considering accommodation design, logistics and environment . The focus and redirection of planned funding to capital works and safety rectification works will delay and stop progress for renewal and replacement of aged stock. This will impact the marketability and competitiveness of the asset and present financial and operational risk as the age of the buildings increase.

Comment and update for Part B item 2 - Plan of Management

The need for this has been clarified with the Office of Local Government and it has been confirmed that the Strategic Review will meet this requirement. The Strategic Review report covers strategic and operational aspects of Blue Haven Terralong including governance, risk and financial performance. This will be considered by Council at its ordinary meeting in April or May.

Comment and update for Part B item 3 - Compliance with Retirement Village Act and Regulation

The Strategic Review will address this.

Conclusion

The Asset Condition Report presents a significant challenge for KMC and managing the cash flow implications in the Budget and LTFP will be extremely difficult. The Office of Local Government requires that this information is publicly released. Council staff will engage with the residents and broader community on this situation.