

Council Submission
Proposed Methodology Consultation

Kiama Municipal Council

Council Name	Kiama Municipal Council
Contact Person	Jane Frawley
Position	Chief Executive Officer
Email	jane.frawley@kiama.nsw.gov.au
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1. Overall position

Please indicate your council's overall position on the proposed methodology: Support; Support with minor modifications; Support with significant modifications; Do not support; Unable to determine without further information.

Council's position: Do not support

Kiama Municipal Council supports reform of the Financial Assistance Grants methodology where reform results in improved horizontal fiscal equalisation and directs greater assistance towards councils with demonstrably lower revenue-raising capacity and greater unavoidable expenditure needs.

Council recognises that historical funding allocations should not be preserved simply because they are historical. Council also accepts the principle that councils with greater practical capacity to raise own-source revenue should generally require less equalisation assistance than councils with more limited capacity.

Council does not, however, support the proposed methodology in its current form.

The indicative outcome for Kiama is a reduction in its Financial Assistance Grant from approximately \$2.558 million to \$1.062 million, a reduction of approximately \$1.496 million or 58.5%.

Council's concern is not simply the size of that reduction. A substantial redistribution could be justified if it resulted from a comprehensive and demonstrably more accurate assessment of relative fiscal need. Rather, the magnitude of the indicative change provides a practical test of the methodology and raises questions as to whether all material factors have been adequately recognised.

Council is particularly concerned that insufficient consideration may have been given to:

- service population rather than resident population, particularly for accessible regional tourism destinations;
- minimum efficient scale and fixed service costs for smaller councils;
- the distinction between theoretical revenue capacity and practical revenue-raising capacity within NSW's rate-pegging framework;
- the distinction between land value, household income and municipal fiscal capacity, particularly for communities with an older demographic profile;
- regional supplier and service-delivery costs not necessarily captured by remoteness measures;
- infrastructure utilisation, particularly road usage, rather than infrastructure quantity alone; and
- interactions between variables that may compound rather than offset modelling limitations.

The proposed methodology may simultaneously underestimate Council's expenditure need and overestimate Council's practical revenue-raising capacity, resulting in an understatement of relative financial need.

Council also considers that greater transparency is required to understand how the proposed methodology produces individual council outcomes. Council therefore recommends further disclosure, modelling, refinement and consultation before a final methodology is adopted.

2. Alignment with principles

Consider whether the methodology aligns with key principles such as: Equity and fairness; Transparency; Simplicity; Consistency; Accountability.

Equity and fairness

Council supports directing greater funding towards councils with genuinely higher unavoidable expenditure needs and lower practical revenue-raising capacity. However, horizontal fiscal equalisation requires both sides of that equation to be appropriately measured.

For Kiama, resident population is an incomplete measure of service demand. The 2021 Census recorded 23,074 residents, while recent tourism data report more than 1.2 million annual visitors and approximately 1.8 million visitor nights. Overnight visitation alone is equivalent to an average daily visitor population of approximately 4,930 people, before day visitors are considered.

Council does not contend that every visitor creates the same expenditure demand as a resident. However, visitors make material use of Council-funded roads, parking, amenities, beaches, parks and reserves, coastal infrastructure, walking infrastructure and other public facilities.

This also creates an important interaction with remoteness. Kiama's proximity to Wollongong and Greater Sydney reduces its conventional remoteness, but that same accessibility drives substantial visitor demand.

A methodology that recognises accessibility as a proxy for reduced expenditure without recognising the additional service demand generated by that accessibility, risks producing inequitable outcomes.

Simplicity and consistency

Council supports simplification where it improves consistency and understanding. However, simplicity should not be achieved at the expense of adequacy.

Council is particularly concerned that population may not adequately capture minimum efficient scale. A council serving 25,000 residents does not require one quarter of the governance, financial management, planning, regulatory, asset-management, emergency-management or works capability of a council serving 100,000 residents.

There is a minimum institutional and service-delivery capability required to operate a council. Similarly, many community facilities cannot be scaled down proportionately with population.

Transparency and accountability

Council supports these principles but does not consider that the information published to date is sufficient to allow Council to reproduce or adequately explain its indicative outcome. This is addressed further under Topic 4: Transparency and Clarity.

3. Practicality and implementation

Consider: Ease of understanding; Availability of required data; Administrative burden; Implementation challenges.

Ease of understanding

Council supports a methodology based, where possible, on objective indicators and independently sourced data. At a conceptual level, the proposed methodology appears simpler than the existing approach. However, Council cannot readily determine from the published information how the model produces Kiama's indicative allocation.

A simpler formula will only improve practical understanding if councils can follow the calculation from published inputs through to the resulting allocation.

Availability of data and administrative burden

Council does not advocate replacing the proposed methodology with a complex return-based model or substantial new reporting requirements. Where additional indicators are warranted, preference should be given to independently collected and consistently available datasets.

For example, established tourism data could potentially support a service-population indicator without requiring councils to undertake separate population surveys. Similarly, any consideration of regional cost differences should, where possible, draw upon objective

procurement, tender or construction-cost information rather than subjective council assessments.

Implementation challenges

Any methodology producing substantial redistribution presents implementation challenges because councils prepare Long Term Financial Plans, workforce plans, asset-management strategies and service-delivery programs over multiple years.

If significant redistribution remains justified following further analysis, appropriate transitional arrangements should therefore be considered.

4. Transparency and clarity

Consider: Whether the methodology is easy to understand; Whether assumptions are clearly explained; Whether councils can understand how outcomes are determined.

Council considers that significant improvement is required in this area.

Council has not been able to identify from the published consultation material:

- the precise ARIA+ value attributed to Kiama;
- how council-level ARIA+ values have been derived;
- the coefficients and relative influence of individual expenditure and revenue variables;
- Kiama's modelled expenditure need;
- Kiama's modelled revenue capacity;
- the contribution of individual revenue-capacity indicators;
- the weighted-average financial-need threshold against which Kiama is assessed; or
- a calculation reconciling Kiama's model inputs to its indicative allocation.

These matters are particularly important where the proposed methodology produces an indicative movement of approximately 58.5%.

Simplicity should not be confused with transparency. A model containing fewer variables is not transparent if affected councils cannot reproduce or adequately explain its outcomes.

Council recommends publication of sufficient council-level information to allow the calculation to be understood and reproduced, including:

1. input data and variable definitions;
2. ARIA+ values and methodology;
3. relevant coefficients;
4. predicted expenditure and revenue capacity;
5. calculated financial need and applicable weighted-average benchmark;

6. resulting needs-based allocation; and
7. sensitivity analysis for material variables.

Council considers this information necessary both for informed consultation and for confidence in the final methodology.

5. Data sources and indicators

Consider: Appropriateness of the proposed data sources; Accuracy in reflecting local government circumstances; Data quality, limitations, or gaps; Currency and reliability of the data; Alternative assured data sources or indicators that should be considered.

Council identifies the following areas for further consideration.

Resident population and service population

Resident population is an appropriate core indicator but does not always accurately represent the population consuming council-funded services. This is material for Kiama because of its substantial overnight and day visitation.

Council recommends testing an independently sourced service-population indicator, using visitor-night and day-visitor data where sufficiently reliable. The methodology need not treat visitors as equivalent to residents. An appropriate weighting could recognise their narrower use of council services.

Population and minimum efficient scale

Council recommends testing whether the expenditure model adequately captures fixed costs and minimum efficient scale. Smaller councils must maintain core statutory, governance, operational and community-service capability despite having fewer residents across which to spread those costs.

Kiama is not a high-growth LGA and therefore has limited opportunity to achieve further scale efficiencies through a rapidly expanding population and rating base. Beyond a certain point, further expenditure reductions do not represent efficiencies. They represent service reductions.

Household income and revenue capacity

Council supports using household income where it is demonstrated to be a reliable indicator of municipal revenue capacity. However, the methodology should explain how household capacity to pay translates into Council capacity to raise revenue.

In NSW, councils cannot automatically convert greater household income into additional rate revenue. IPART sets the maximum amount by which councils may ordinarily increase aggregate general income, unless a Special Variation is approved. Kiama's 2026-27 rate peg is 3.2%.

Council therefore recommends that the Commission demonstrate the empirical relationship between household income and practical municipal revenue capacity within the NSW regulatory framework.

Land values

Council has similar concerns regarding land values. High residential land values do not automatically provide Council with additional revenue. Following revaluation, it is principally the distribution of the rating burden between properties that changes, rather than increases in land valuation simply flowing through to higher aggregate Council rates revenue.

Nor is property wealth equivalent to household liquidity. Kiama had a median age of 48 at the 2021 Census compared with 39 for NSW, with substantially higher representation in older age groups. Long-standing owner-occupiers may hold highly valued property while relying on comparatively constrained retirement income.

Property value, household capacity to pay and municipal revenue-raising capacity should be treated as related but distinct concepts.

Regional service-delivery costs

Council recommends that the Commission test whether remoteness adequately captures differences in regional procurement and service-delivery costs. Proximity to Sydney and Wollongong does not necessarily mean Kiama has equivalent supplier depth and competition to a major metropolitan council, particularly for specialised engineering, infrastructure and professional services.

Council does not suggest that a regional cost premium should simply be assumed. Rather, this should be tested against objective procurement, tender-participation and construction-cost evidence.

Local roads

Road length is a useful objective indicator but does not fully represent expenditure need. Road expenditure is also affected by utilisation, functional hierarchy, heavy vehicle movements, visitor traffic and physical conditions. Kiama's local government areas contain many roads that are historically disaster affected and are on topographically challenging terrain to build and maintain.

This is particularly relevant where a relatively compact network experiences substantial non-resident utilisation. Council recommends testing whether a reliable utilisation or functional-hierarchy indicator could supplement road length without materially increasing administrative complexity.

6. Potential impacts

Consider potential: Financial impacts; Service delivery impacts; Regional impacts; Equity impacts.

Financial impact

Kiama's indicative annual reduction is approximately \$1.496 million. Against Council's approximately \$23 million rates base, this is equivalent to approximately 6.5% of rates revenue.

For context, Kiama's 2026-27 ordinary rate peg is 3.2%. The proposed FAG reduction is therefore equivalent to approximately twice the value of one annual rate-peg increase, based on the \$23 million ordinary rates base.

Furthermore, Kiama Municipal Council is currently subject to a Performance Improvement Order issued by the NSW Government. The Order sets out actions that Council is required to undertake to improve its financial sustainability, governance and organisational performance, including an annual budget for FY 2027/28 that demonstrates an operating position at or above break-even. Given the constraints on revenue increases under the rate peg, Council is currently consulting with the community on a possible Special Rates Variation (SRV) of approximately 20% to meet the terms of the PIO by FY2027/28.

The impact of the proposed methodology change on Council's financial position would be drastic. This does not mean Council is proposing or would necessarily require a 6.5% rate increase on top of any proposed SRV. Council could respond through some combination of expenditure reductions, operational efficiencies, fees and charges, alternative revenues and rates. However, given the materiality of proposed change, the impact on the financial sustainability of Council could not be met without significant reductions in staffing and/or reduced services for the community

Service-delivery impact

A recurrent reduction of this magnitude cannot be accommodated through further efficiency measures alone, particularly if the methodology were to be implemented by FY28. Potential responses would ultimately affect staffing levels, community service levels, infrastructure and asset maintenance, facility operations, fees and charges, or Council's longer-term financial position.

Regional impact

Council is concerned about accessible regional councils which may receive limited recognition for remoteness while still lacking the scale, commercial revenue opportunities or supplier depth available to larger metropolitan and regional councils.

In addition, the necessary review of staffing and service levels from reduced grants would create a proportionally larger impact on a smaller regional community like Kiama LGA.

Equity impact

Council supports redistribution towards councils with demonstrably weaker fiscal capacity. However, equitable redistribution requires the model to distinguish appropriately between community socioeconomic circumstances and local-government fiscal capacity.

Timing of the financial impacts

Council notes that the financial impacts of any methodology change may be felt earlier than the formal implementation date due to the long-standing advance payment arrangements with Financial Assistance Grants.

Details of the new Federation Compact are yet to be released and this ought to be considered alongside the Grants Commission new methodology.

7. Risks and unintended consequences

Identify any risks, challenges, assumptions, or unintended outcomes that may arise from implementation.

Compounding model effects

Individual indicators do not operate in isolation. For a council such as Kiama:

- resident population may understate service demand;
- relatively high accessibility may reduce assessed expenditure need, while generating substantial visitor demand;
- a small resident population may not capture minimum service costs;
- high land values may increase measured revenue capacity without providing equivalent additional revenue;
- household income may indicate capacity to pay which cannot be directly translated into higher Council rates; and
- road length may understate infrastructure utilisation in a regional setting.

The principal risk is therefore that multiple effects operate in the same direction, simultaneously understating expenditure need and overstating practical revenue capacity. Council recommends that the Commission specifically sensitivity-test these interactions.

Threshold effects

Council is concerned about potential discontinuities around the weighted-average financial-need threshold. If relatively small movements in calculated financial need determine whether a council participates materially in the needs-based funding pool, modest changes in assumptions or inputs could produce disproportionately large changes in allocation.

The Commission should test and disclose the sensitivity of results around this threshold.

Financial sustainability

A methodology intended to improve financial equalisation should not inadvertently weaken the sustainability of councils whose genuine expenditure disabilities or practical revenue constraints are inadequately captured. This provides a further reason for testing the methodology against council-level outcomes before implementation. Consideration should be given to the unique situation faced by Councils like Kiama that have already shown financial sustainability improvements under a Performance Improvement Order.

8. Suggested improvements

Provide any recommendations that would strengthen the methodology or improve its application.

- (a) Retain the objective of genuine horizontal fiscal equalisation, directing greater assistance towards councils with demonstrably higher unavoidable expenditure needs and lower practical revenue-raising capacity.
- (b) Test a service-population indicator, using independent visitor-night and day-visitor data where material and statistically reliable.
- (c) Test for minimum efficient scale and fixed-cost effects, rather than assuming expenditure varies proportionately with population.
- (d) Demonstrate empirically the relationship between household income, land values and council revenue-raising capacity, having regard to the NSW rate-pegging framework.
- (e) Distinguish property wealth, household liquidity and municipal fiscal capacity within the revenue-capacity assessment.
- (f) Test regional procurement and service-delivery cost differences using objective evidence and determine whether ARIA+ adequately captures such effects.
- (g) Review the Local Roads Component to determine whether an objective utilisation or functional-hierarchy indicator should supplement road length.
- (h) Publish council-level inputs, assumptions and model outputs, including ARIA+ values, predicted expenditure, predicted revenue capacity and calculated financial need.
- (i) Undertake and publish sensitivity analysis, including the interaction of indicators and sensitivity around the weighted-average financial-need threshold.
- (j) Undertake further consultation once councils have sufficient information to reproduce and critically assess their indicative results.
- (k) Provide appropriate transitional arrangements if substantial redistribution remains justified following that further work.
- (l) Delay the implementation of methodology changes until they can be reviewed in the context of any proposed changes under the Federation Compact, which is intended to address the financial crisis facing Australia's local councils.

9. Additional comments and conclusion

Provide any other comments relevant to the proposed methodology.

Kiama Municipal Council supports the objective of improving the equity of Financial Assistance Grant distribution.

Council does not advocate preserving historical allocations simply because they are historical, nor does Council oppose additional assistance being directed towards councils with demonstrably greater fiscal need.

Redistribution of this magnitude should occur only where the methodology provides a comprehensive, transparent and empirically robust assessment of both unavoidable expenditure need and practical revenue-raising capacity.

The approximately 58.5% indicative reduction for Kiama is not, of itself, evidence that the proposed methodology is incorrect. It is, however, sufficiently significant to warrant confidence that the characteristics producing that result accurately reflect Council's fiscal circumstances.

On the information presently available, Council does not consider that confidence has been established.

In particular, further work is required to determine whether the methodology adequately recognises:

- material non-resident service populations;
- minimum efficient service-delivery costs for smaller councils;
- infrastructure utilisation;
- regional supplier-market conditions;
- statutory constraints on councils' ability to increase rate revenue; and
- the distinction between land value, household income and practical municipal revenue capacity.

Council's central concern remains that, for Kiama, these factors may interact in a manner that understates expenditure need while overstating revenue capacity. These changes are particularly impactful on Kiama Council, which is currently under a Performance Improvement Order issued by the NSW Government.

Council therefore does not support the proposed methodology in its current form and recommends further disclosure, modelling, refinement and consultation before a final methodology is adopted.

Council welcomes the opportunity to work constructively with the NSW Local Government Grants Commission and Office of Local Government to develop a methodology that achieves improved horizontal fiscal equalisation while appropriately recognising the diverse fiscal and service-delivery circumstances of NSW councils.


Jane Frawley
Chief Executive Officer
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