2 July 2013

Dr Peter Boxall
Chairman
Independent Pricing and Regulatory Tribunal
PO Box Q290
QVB Post Office NSW 1230

Dear Dr Boxall

Re: Review into the development of a funding framework for Local Land Services NSW

The Livestock Health and Pest Authorities (LHPA) are pleased to respond to the Issues Paper released, to inform IPART’s review into the development of a funding framework for Local Land Services. Please find enclosed our submission. Our submission does not contain any confidential information, and as such we are comfortable for IPART to publish it in full on its website and to the public.

This submission has been prepared by the State Management Council of LHPAs, with input from Director’s and General Manager’s of Local Authorities. It is the collective view of our organisation.

Directors and staff of LHPA who attended the recent public forums in Tamworth and Wagga have noted to me the success of these meetings. They noted the openness of Tribunal members and IPART staff to stakeholder views, and the value of dialogue in developing IPART’s understanding of our organisation and in exploring issues of importance.

We would welcome the opportunity to provide the Tribunal and IPART staff with a verbal briefing to discuss in further detail the points and views raised in our submission. We would also be pleased to provide IPART any further information or data you may require to support the next stage of the review.

In the first instance, please contact Tim Johnston, Acting Chief Executive Officer, Livestock Health and Pest Authority. Tim can be contacted on (02) 6391 3242 or by email Tim.Johnston@lhpa.org.au.

I look forward to further discussions between LHPA and IPART as this review progresses.

Yours Sincerely

[Signature]

Ian Donges
Chairman, State Management Council
Livestock Health and Pest Authority
Review into the development of a funding framework for Local Land Services NSW

Response to the IPART Issues Paper

Livestock Health and Pest Authority State Management Council
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Executive Summary

The Livestock Health and Pest Authorities (LHPA) are pleased to provide IPART with a response to the Issues Paper released to inform the Tribunal's review into the development of a funding framework for Local Land Services NSW (LLS).

Our focus in this submission is centred on the activities that are currently our responsibility, and will become core services to be delivered by LLS. These core services include biosecurity (livestock health and pest animal and insect management) and the management of travelling stock routes. Reflecting this focus, our analysis and views on key issues such as the ratings base concentrate on the recovery landholders' share of the costs to fund these services.

The Local Land Services Act 2013 was passed by the NSW Parliament at the end of June. Considerable effort is currently being focused on planning the transition period and establishing the appropriate policy and operational frameworks for the new organisation. The Act provides the statutory basis for LLS, its governance and planning. However, the nature of plans and how they will link to organisation budgets is yet to be fully developed. Furthermore, as yet there is no agreed timeframe for when the first plans should be completed.

Given this context, our view is that the cost recovery framework should:

- establish the key principles on which cost recovery should be based;
- determine the broad methodology for cost allocation and cost recovery;
- provide guidance as to how and when the cost recovery framework should be used in the development of plans and budgets; and
- provide guidance as to how the cost recovery framework should be used to determine rates and other fees and charges.

Our view is that the cost recovery framework should be flexible. Our view is that flexibility means the ability for the framework to:

- be adjusted on the commencement of LLS and over time, as the policy, planning and operating context of LLS is established and refined;
- account for regional differences in service offerings and costs, recognising that consistency of underlying principles is important;
- add new services or functions over time; and
- respond to changes in government policy over time.

Our view is that the cost recovery framework should be transparent. To maintain rate-payer confidence, there should be no cross-subsidisation between bundles of like services. For example, rate-payer contributions to biosecurity services should not be used to fund activities that deliver public environmental benefits.
Our view is that rating is an appropriate mechanism to recover the non-government share of costs associated with biosecurity and the management of TSRs for stock movement and grazing. Our view is that such rates should be:

- Determined on the basis of notional carrying capacity as this reflects the productive capacity of the land and as such “share of biosecurity risk”. In its essence, NCC is productivity measure that enables comparison of the productive capacity of properties within a district.
- Levied on properties greater than 2 hectares, as such properties are sufficiently large to carry stock that pose a biosecurity risk.

Our view is that, for efficiency, the audit of the cost recovery framework should be incorporated into the financial and performance audit program required by the LLS Act. It is important for audits to be focused not just on process and activities, but also on outcomes. Our view is that outcome focused audits will drive improvements in LLS over time, and also provide stakeholders with confidence that their investments are achieving their intended purpose.

In conducting this review, we urge IPART to be mindful of the broader implementation issues associated with the establishment of LLS. The development of strategic and local plans will be critical processes to consolidate the service offering and service level expectations of the new organisation. These planning activities must provide the context for the application of the cost recovery framework. To avoid multiple and potentially confusing changes to the ratings approach, our view is that the current model for recovering costs from ratepayers be maintained until key decisions relating to service delivery have been made and at least until the next rating period (i.e. Jan 2015). In this interim period, it is our view that LLS and Local Boards must be appropriately funded to maintain current service levels, recognising that LHPA’s have had a diminished ability to achieve this in the past few years.

This review is one of many considerations in the formation of the new agency. We encourage the Tribunal to ensure that its recommendations for a cost recovery framework are considerate of the broader strategic context of the reform process.

Our prevailing view is that it would be premature for IPART to recommend a rigid and fixed cost recovery framework. There is a considerable risk that a rigid and highly specified approach would result in a mismatch between the accepted framework and the ultimate needs of the agency. We recommend that the outcome of this review be a clear but broad cost recovery framework, with recommendations as to the methodology for determining cost shares and appropriate rating base and guidance as to how the framework could be applied to the planning and budgeting activities of LLS and Local Boards.
Overview

Introduction
The Livestock Health and Pest Authorities (LHPA) welcome the opportunity to respond to the Issues Paper prepared by IPART to inform its review into the development of a funding framework for Local Land Services NSW (LLS).

The integration of the current functions performed by LHPA into the new LLS will be of critical importance to our key stakeholders (ratepayers and users of our services, including governments). Our submission is predominantly focused on the services that are our core business, and our views on how the cost of the delivery of these services should be recovered from individual landholders, industry and government as representative of the broader community.

LHPA recognises that there is still considerable ground to be covered in the transition to the new LLS model. However, in developing the cost recovery framework, LHPA seeks that IPART more clearly articulates the intended outputs and outcomes of this review and how these may be adopted under the LLS model.

Due to the history of reform to the LHPA model, we have considered many of the issues raised by IPART in recent years, and our submission reflects this experience. We have considered a range of funding models and have conducted cost recovery analysis in the context of the 14 LHPA Boards. We are keen to share our experiences with IPART, and encourage the Tribunal to conduct more detailed analysis when developing the draft report in the next phase of this review. We would be happy to assist the Tribunal in the provision of relevant information and data to underpin such analysis.

Structure of this submission
This submission is structured into three parts. Part 1 examines the key policy and strategic issues facing the establishment and implementation of LLS. It is critical that the context, role and timing of the implementation of the cost recovery framework are clearly articulated to enable appropriate analysis and support considered discussion in this review.

Our view is that there are key strategic issues that have been omitted or inadequately addressed in the Issues Paper. These questions require further discussion with key stakeholders prior to the development of IPART’s draft report.

It is important that IPART takes a whole of organisation approach to these deliberations rather than discuss selected program or service examples. The cost recovery framework needs to be considered in a strategic planning and organisational budgeting process. The current treatment of selected services in this Issues Paper, while illuminating some principles, cannot be considered a strategic consideration of the wider issues arising from the application of a cost recovery framework.

Part 2 of this submission responds to the key issues and questions identified in the Issues Paper.

Part 3 provides more detail as to the current approach of LHPAs to planning and cost recovery.
**IPART’s Terms of Reference**

In preparing this submission, LHPA has focused on IPART’s terms of reference. The following table cross references IPART’s terms of reference to particular sections in this submission.

<table>
<thead>
<tr>
<th>Terms of reference</th>
<th>Relevant sections of LHPA’s submission</th>
</tr>
</thead>
<tbody>
<tr>
<td>1) Develop an efficient and transparent Cost Recovery Framework that LLS boards can use to set service fees for the different categories of services they provide to the different groups of beneficiaries. In undertaking this task, IPART will assess the strengths and weaknesses of cost recovery frameworks used by other similar service providers.</td>
<td>Strategic comments in Sections 2-6 Specific comments in Sections 7 &amp; 8</td>
</tr>
<tr>
<td>2) Advise on an efficient rating base for compulsory fee collection and an efficient fee collection mechanism.</td>
<td>Section 8.4 and 8.5</td>
</tr>
<tr>
<td>3) Develop an appropriate audit methodology for assessing the extent to which efficient cost recovery pricing has been applied to the services offered by LLS boards.</td>
<td>Sections 5 and 9</td>
</tr>
</tbody>
</table>
Part 1 – Key strategic issues

Introduction

LHPA recognises that there is still considerable ground to be covered in the transition to the new LLS model. However, in developing the cost recovery framework, LHPA seeks that IPART more clearly articulates the intended outputs and outcomes of this review and how these may be adopted under the LLS model.

The legislation (Local Land Services Act 2013, herein the Act) that enables the creation of LLS and Local Boards was passed by the NSW Parliament on the 27th June. Our submission is made in the context of the Act1.

Governance and strategic planning

Key principle:

- The cost recovery framework should be linked to the planning activities of LLS and Local Boards

The LLS Act emphasises that LLS and Local Boards:

- have the status of State agencies (Clause 9, Clause 28);
- are subject to the control and direction of the Minister (Clause 11); and
- are subject to the control of the Director General of the Department in specified circumstances of an emergency (Clause 12(2)).

The relationship between the Overarching Board of Chairs (the Board), LLS and Local Boards is also established in the Act. Our interpretation of this relationship is that:

- All decisions relating to the functions of Local Land Services are to be made by or under the authority of the Board (i.e. the statewide Board of Chairs) – or by authorised persons where such functions have been delegated (Clause 10(1), Clause 16, Clause 17).
- It is the responsibility of LLS to administer, deliver or fund all local land services (Clause 14(1)), including the making and levying of rates and the administration of grants, loans and subsidies (Clauses 14(1)(e) and 14(1)(f).
- Local Boards will make recommendations to the Board in relation to the making of rates, levies and contributions on rateable and other land in the region (Clause 29(c)).
- Decisions taken at a regional level are required to take account of State priorities for local land services (Schedule of Amendments No 3).

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1 Note: references to clauses in this submission refer to the text of the LLS Bill as introduced to the NSW Parliament. see http://www.parliament.nsw.gov.au/prod/parlment/nswbills.nsf/131a07fa4b8a041cca256e610012de17/818d82acd7727647ca257b79001efbce/$FILE/b2013-035-d18-House.pdf

Furthermore, the Act articulates a clear planning hierarchy for the delivery of LLS functions:

- LLS will prepare a state strategic plan to be approved by the Minister (Clause 37(1)).
- Local Boards are to prepare one or more local strategic plans to be reviewed by LLS (Clause 49) and approved by the Minister (Clause 46(1)). Such local plans must have regard to State Priorities and the State Strategic Plan (Clause 47(3)).

The Act does not specify the timeframe in which these plans should be developed. Such a timeframe would be established by LLS policy. It is also expected that LLS policy will establish the framework for the operational (annual) and business planning (3-5 yearly) activities required of local Boards.

The IPART Issues Paper is largely silent on the link between the planning processes of LLS and individual boards and the cost recovery framework. Furthermore, the Issues Paper does not adequately articulate how the cost recovery framework should be applied by LLS and Local Boards. In this respect, key issues that in our view have been inadequately addressed include:

- The scale at which the framework is to be applied. It could be applied at an organisational, regional, service offering or project scale, or all of these scales.
- When the framework should be applied. Is it during planning to inform prioritisation and decision making, to periodic budgeting processes or is in the design of programs or service offerings?
- The relationship between the cost recovery framework and standard agency planning and budgeting processes.

Our preliminary view is that agreed State and Local Strategic Plans should be the starting point for the development of any organisational budget and thus the starting point for the application of the cost recovery framework.

It is through the planning process that stakeholders such as risk creators and beneficiaries (including landholders and government as representative of the community) can articulate the types of services - and in turn the service levels - demanded of LLS and Local Boards.

Our view is that the cost recovery framework should account for the planning context for LLS services and for Local Boards. The planning hierarchy proposed by the LLS Act requires that the plans of individual boards be consistent with a Statewide Strategic Plan. Where a service or service level is imposed by the Minister through a planning process, consideration should be given as to the most appropriate funding mechanisms at this time. If the Minister agrees that a ‘service’ is worthwhile when approving a plan this could then influence whether the service is of a private, industry or public good.
Given this governance and planning hierarchy, our view is that in developing a draft report, it will be important for IPART to clearly articulate:

- the link between organisation planning and the cost recovery framework.
- to whom and to what the cost recovery framework should apply.
- the scale and when the framework should be applied.
- when the application of the framework should commence.

### Whole of organisation budgeting and cross-subsidisation

**Key principle:**

- The service mix of LLS is broad. For transparency, the budgets and cost recovery framework adopted for LLS must ensure that there is no cross-subsidisation between bundles of like activities.

The current service offerings of Catchment Management Authorities, Livestock Health and Pest Authorities and Department of Primary Industries' advisory services are very broad. Broadly, the types of services include:

- regulatory services (eg disease reporting, pest control orders, native vegetation clearing consents);
- program delivery services (eg Caring for Our Country investments, specific industry funded programs delivered by DPI);
- advisory services (e.g. disease diagnostic services, pest animal control support, DPI agronomic advice);
- training services;
- education and extension services; and
- emergency management.

As briefly identified in the Issues Paper, the current budgeting and cost recovery frameworks of the three organisations are also quite different. Given this, on transition, the budgeting process for the new organisation –both for the statewide LLS and for Local Boards will be a complex process.

In practice, a cost recovery framework should be applied to the proposed budget of an organisation or business.

The initial cost recovery framework for LLS must recognise the challenges associated with the transition to the new organisation and provide flexibility. The merging of budgets, systems and processes will take some time to settle as the new organisation establishes. Our experience with the reform of Rural Lands Protection Boards into LHPAs in 2009 highlighted the need for time for such a transition.

The capability of the new organisation's systems to inform the application of the framework must also be considered. While we see an opportunity for the new LLS to move to more sophisticated approaches – such as cost centre accounting – over time, in the intervening period, achievable steps should be taken to ensure that there is no cross-subsidisation of activity.
The LLS Act establishes the Local Land Services Fund which is to:

- receive all money by or on account of Local Land Services and the proceeds of any investment of money (Clause 20(1))
- pay all amounts required to meet expenditure incurred by Local Land Services in the exercise of its functions including the provision of loans etc (Clause 20(2)).

On commencement, it is proposed that the funds and reserves of individual LHPAs be transferred to the LLS Fund. These funds and reserves are the result of the management of rate payer contributions over time. It should be noted that currently, a significant proportion of reserve funds have been flagged by LHPAs to fund staff entitlements and the costs associated with any potential redundancies.

For transparency to government and ratepayers, the budgets and cost recovery framework of LLS or Local Boards should bundle like services. Our view is that rate payer confidence is essential for the new organisation to succeed. An overriding concern of LHPA is that we are transitioning from the current low-cost overhead model to a higher cost model of a government agency, and that an increasing proportion of rate payers’ contributions will go towards meeting higher management and administrative costs. For this reason, transparency in the application of rate payers contributions to the recovery of the costs associated with the delivery of LLS services is paramount to the early success of LLS.

Our view is that transparency of the application of rate payers contributions to recovering costs associated with the delivery of LLS services is paramount.

Our view is that the organisational budgeting and accounting and reporting practices adopted by LLS and Local Boards must be sufficient to ensure that there is no cross subsidisation of activities. Ratepayer contributions should be quarantined to the delivery of those services (such as biosecurity and emergency management) that have been identified in the cost recovery framework.

Our view is that the transparency resulting from the quarantining of funds should extend to the funds and interest generated from the reserves of LHPAs.

**Flexibility**

**Key principle:**

- The cost recovery framework should be flexible.

Implicit throughout the Issues Paper is that the cost recovery framework should be flexible. This principle is strongly supported by LHPAs. However, there needs to be a clear definition of what flexibility means in the context of the cost recovery framework. In our view, flexibility means:

- flexibility to adjust or fine tune the framework on the commencement of LLS and over time;
- flexibility to account for regional differences in service offerings and costs, recognising consistency of underlying principles is important;
- flexibility to adapt to seasonal needs and environmental influences;
- flexibility to adapt to emergency situations;
- flexibility to add new services or functions over time; and
- flexibility to respond to changes in government policy.

For example, at the Commonwealth level, there have been ongoing discussions about a levy to fund national biosecurity efforts.
There is still considerable uncertainty around the establishment, administration, focus and service offering of the new agency. Furthermore, the service offering may change over time as strategic plans are developed, government priorities change or as new risks emerge. Our view is that at this stage there is insufficient information available to support transparent consideration to establish explicit cost shares for each proposed service offering of the agency as a whole. Given this, it is our view that it would be problematic for IPART to make a rigid recommendation in relation to a cost recovery framework. The alternative would be for IPART to provide a policy framework, with recommendations as to the methodology for determining cost shares that should be adopted at some later date by LLS or the Minister.

Regional variation is driven by a number of factors. In terms of those services currently delivered by LHPA, some of the drivers of variation include:

- differing agricultural production systems (e.g. cropping versus grazing, prevalence of intensive industries);
- climate and biophysical characteristics (which influences risk of disease or prevalence of pest incursions);
- land use (e.g. prevalence of smaller blocks for lifestyle purposes);
- scale and land title; and
- population and number of landholdings.

Our past experience has shown that the diversity of production systems and landholding characteristics across the different regions of NSW make a “one size fits all” approach problematic. We encourage IPART to examine approaches that support flexibility in the application of the framework at regional scale.

Our view is that in making recommendations about the cost recovery framework, IPART should ensure that there is suitable flexibility so that its future application of the framework by LLS or Local Boards can be adjusted to account for key priorities and regional differences.

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4 for example leasehold lands in the Western Division
Audits

Key principle:
- The process for auditing the cost recovery framework should be fit for purpose and be cost effective.
- Audits should drive transparency and improved performance over time.

In relation to audit, the Act proposes that the:

- Minister is responsible for the arrangement of an audit to determine whether LLS is carrying out its functions effectively and efficiently and in accordance with the State Strategic and Local Plans (Clause 24(1)) and State priorities for local land services (Amendment No. 7)
- Minister is to ensure that the State strategic plan is audited, at intervals of not more than 5 years, to ascertain whether its provisions are being given effect (Clause 44(2)).
- Minister is to ensure that each local strategic plan is audited, within 3 years of its approval, to ascertain whether its provisions are being given effect (Clause 54(2) or at any time that the Minister considers it appropriate to do so (Amendment No. 11).
- Costs of such audits are paid for by LLS (Clauses 24(6), 44(4), 54(4)).

We support IPART’s concept of including the cost recovery framework in a broader audit program and welcome the Tribunal’s recognition that the level of proposed audits is potentially costly and in some cases overlapping.

Importantly, our view is that the audit program of LLS and Local Boards should focus on the achievement of outcomes, and not just activities and processes. Such a focus will drive improved performance in the agency over time and provide stakeholders with confidence that their contributions are leading to the achievement of planned outcomes.

Our preliminary view is:
- that the audit of the cost recovery framework should be embedded in the financial and performance audits of LLS and Local Boards.

Transition

Key principle:
- In recommending a cost recovery framework, IPART should recognise the implementation challenges associated with the establishment of LLS.

In preparing its draft report, LHPA suggests that IPART be cognisant of the broader implementation issues associated with the establishment of LLS. Considerable effort is currently being invested in the transition to the new organisation, including the establishment of a budget for commencement on 1 January 2014.
Once established, ongoing effort will need to be invested in merging teams, culture, systems and processes of three organisations into one. This effort will be important to the success of the new organisation, particularly in the eyes of our key stakeholders – rate payers.

As outlined above, the development of strategic and local plans will be critical processes to consolidate the service offering and service level expectations of the new organisation. Given this, in our view the development of a rigid cost recovery framework is premature at this stage of the development of the new organisation.

Currently, LHPA rates are calculated by local authorities in October/November. Rates are then approved by the Minister in January and dispatched in late January or February. Our view is that for the transitional period, the current approach to recovering costs from ratepayers be maintained until key decisions relating to service delivery have been made and at least until the next rating period (i.e. January 2015). In light of this, our view is that LLS and Local Boards must be appropriately funded to maintain current service levels, recognising that LHPA’s have a diminished ability to achieve this in recent years due to decisions associated with our revenue streams.

Our experience has shown that changing the rating methodology generates considerable inquiry from ratepayers, with the response requiring considerable resources. In our view, it would be preferable to dedicate time to establishing the logical basis for rate changes to reflect the service delivery of LLS, rather than changing the rating approach multiple times in the next 2 years. For this reason, our view is that the cost recovery framework should not be rigid, with fixed cost shares for specific services, but a high level framework to provide guidance to ongoing policy discussion.

Our view is that:

- The Cost Recovery Framework developed by IPART should take the form of guidance material for consideration by the Minister, and LLS and Local Boards once established.
- The current approach to rating be maintained until plans have been established by LLS and Local Boards.
- Until plans that articulate the service offering and service level have been developed, LLS should be appropriately resourced to maintain current service levels.
Part 2 – Response to specific questions

1 Cost Recovery Principles

The principles proposed by IPART are:

- Appropriate pricing strategies;
- Administrative efficiency;
- Institutional issues;
- Transparency; and
- Consistency.

LHPA broadly agrees with the principles espoused in Chapter 3 of the Issues Paper. This section explores in more detail our views on the concept of explicit rationale and the principles of institutional issues, transparency and consistency.

1.1 Key points

1.1.1 Explicit rationale for government involvement and funding

Our view is that IPART needs to further explore the concept of “explicit rationale” for government contribution. While the conceptual “risk creator / beneficiary pays” model may be broadly applicable, there are prudent and sound public policy reasons for government contributions to the types of services that are currently delivered by LHPAs.

Indeed, by the very nature of many of LHPA’s current services (i.e. regulatory services), Government has already made the decision that there is an explicit role for government in the conduct of these activities.

The wider implication of full cost of recovery of biosecurity services being left to rate payers is that there is a risk that funding of biosecurity services (and thus capability to respond to emergency outbreaks etc) will erode over time. Consideration should be given to government contributions to maintain a base level of capability to enable response to outbreaks/emergencies in the future. This could be explicitly addressed in the overall LLS strategic plan prior to the application of any cost recovery framework.

1.1.2 Institutional Issues

The Issues Paper highlights that the cost recovery framework should operate within statutory and legal constraints. In our view, this is a given.

However, our view is that this principle should be extended to also include government policy. LLS is a government agency, of which the relevant Minister has ultimate responsibility. It may be inappropriate for a Minister to be required to use a “hard wired” framework that contradicts the established policy of the day.

Furthermore, the framework should also account for national policy settings. By way of example, for number years, the concept of a “levy” to fund biosecurity activities has been discussed at a national level. If such a policy was agreed by the Council of Australian Governments, the state cost recovery framework should reflect such a change.
1.1.3 Transparency
It will be critical that transparency is maintained as the LLS is established.

As different services are integrated into the organisation, transparency will mean a much greater level of specification of services and allocation of resources to each service. If costs are allocated for core functions this will clear and defendable.

1.1.4 Consistency
Consistency in the underlying principles of the cost recovery framework, and how and when the framework is to be applied is essential. However, as articulated in Part 1, flexibility in the framework is desirable.

The degree of consistency or flexibility may differ, depending on how the framework is to be applied. For example, if considering core functions and resourcing, it may be impractical to have inconsistent treatment across boundaries. However, additional services that may in themselves vary between LLS regions, and indeed within regions, such as specific projects may have a more flexible approach to application of the framework.

IN RESPONSE TO IPART QUESTION 1
Our view is that the principles articulated by IPART are reasonable. However, it is important that transparency is defined and any process of budgeting and reporting addresses this principle explicitly by aligning services with revenue sources.

Our view is that that documenting the rationale for pricing strategies will require a joint effort between LLS and local Boards to ensure that pricing strategies can be assessed.
2 Cost Recovery Framework

2.1 Private and public benefits and the role of government

In this review process, it is important that stakeholders have a common appreciation of the terms private and public benefits.

Pannell (2006) provides an exposition of private and public benefits, particularly in the context of environmental benefits.

- ‘Private net benefits’ refer to those benefits that accrue to a private individual from taking action
- ‘Public net benefits’ refer to those benefits that accrue to everyone other than the individual taking the action (i.e. externalities)

A public good is a good which, because it cannot be withheld from one individual without being withheld from all, must be supplied publicly (Department of Finance 1991).

As highlighted by IPART (Box 5.1), under the competitive market model, market failure exists for four broad reasons:

1. market power leading to imperfect competition (eg monopolies);
2. lack of information / information imbalance;
3. presence of externalities; and
4. public goods or common pool resources.

The fact that market failure exists is not a reason for government action in itself. A secondary test is whether government action can actually see society better off from an action. For action to be justifiable from a public policy perspective there has to be a practical means of intervention and the potential efficiency gains (net of the costs of intervention) have to be a similar order of magnitude to other uses of public funds.

Natural resource management (NRM) is considered to be a key area for Government involvement as it is generally accepted that there are significant market failures. When there is market failure the output of natural resource or environmental ‘goods’ does not match the level that society wishes.

In 2011, the Productivity Commission examined the role of government and industry in rural research and development. This investigation has parallels with investment in biosecurity, as both R&D and biosecurity have individual (private), industry and whole of community benefits. The Productivity Commission (2011) concluded that the main rationale for public funding arises from the un-priced benefits for third parties (‘spillovers’) that often attach to investments in R&D. The Productivity Commission concluded that:

- even in the presence of spillovers, public funding support should only be justified where the expected benefits for a producer/industry are insufficient to motivate investment in research that is of net benefit to the community as a whole

• industry levies address free-rider problems and ensure that all producers who benefit from research contribute to its cost
• industry levies are unlikely to facilitate investment in research where the benefits are either spread thinly across a wide range of industries or mainly accrue to the wider community

It is apparent from examination of agency strategic plans, Catchment Action Plans and the various Acts that underpin NSW DPI, CMAs and LHPA, that the role of Government has been considered when the various services provided were established.

Investigations of market failure, beneficiaries and cost recovery frameworks have been applied in numerous investment decisions at an agency, program and project level across Australia. In general these have been a set of principles that are then embedded in a planning or negotiation phase.

The principles outlined by IPART are consistent with these approaches. However, the degree of formalisation of a process and methodology is almost unprecedented. The complexities of public policy and the problem of unintended consequences limit the effectiveness of an approach that is rigid and definitive. This is not to say such an approach does not aid sound policy and strategic planning, simply that any cost recovery framework should provide guidance and not simply tally a series of assumptions to produce a calculated outcome.

2.2 Identifying demand for services - beneficiaries and/or risk creators

The questions posed by IPART in the cost recovery framework with regard to demand for services will be fundamental to service provision and will be contentious for stakeholders, in particular beneficiaries. Decisions if applied without deep consideration of long-term outcomes could lead to negative outcomes.

During the planning phases, LLS must consider the most appropriate cost recovery mechanism or pricing strategy for services, so as not to generate unintended outcomes. For example, if LLS were to charge a fee for service for an activity such as on-farm disease surveillance, this may create a disincentive for farmers to report a suspected disease if they are then charged a fee. This would reduce the overall effectiveness of LLS staff in providing whole of district surveillance above and beyond the farm gate.

In our view, the examples raised by IPART highlight not the potential application of the approach, but the complexities that immediately arise.

1. Box 5.2 Travelling stock routes: ‘key questions’ to identify beneficiaries and / or risk creators

One of the key questions here is - what is a service? For example, LHPA manage a system to allow the utilisation of TSRs as highlighted. In some regions, TSRs are still heavily utilised for travelling stock and grazing. In others, traditional use of TSRs has declined, and in many cases, they are now seen as a ‘public resource’ with high conservation values. While this is recognised in the Issues Paper, this shared purpose clouds the framework as it is unsure who the risk creator is. In this case a more detailed rationale for ongoing service is required.

Control of wild dogs and other vertebrate pests has similar complexity, with the benefits accruing to graziers and to the community through reduced predation on livestock and native species.

2. Production efficiency programs: ‘key questions’ to identify beneficiaries and / or risk creators

A strict application of the framework may lead to outcomes which mean a reduction in required capacity for public good outcomes such as reduction in externalities and/or public health issues.
It is an implicit assumption that the framework is applied to a situation where the strategic outcomes of services are well established, clear and particularly in the case where designated as fee for service will not be retained if demand is low for a period of time.

3. Native vegetation: ‘key questions’ to identify beneficiaries and / or risk creators

This example raises a number of issues around the definition of service. This not a simple case as the PVP process aims to maintain or improve native vegetation outcomes. The CMAs are required to ‘provide’ regulatory services including the assessment of PVPs to issue clearing consents as part of the regulatory framework of the Native Vegetation Act and associated Regulation. An application of the overarching principle of recognising ‘Institutional issues’ would mean that this service should be funded by Government rather than a deemed’ risk creator and paid for through a fee for service. It is noted that the landholder does bear a cost to their business by applying and complying with these regulations. This issue of ‘risk creator’ is clouded by a change in the duty of care surrounding the introduction of regulation to restrict clearing.

There are approaches to defining individuals for fee for services charges. However, for rates and other broad based contributions, our view is that identifying sub-sections of the community will be difficult to achieve.

Defining an industry based on production type for rating purposes is considered fraught unless there is a very clear case and possible funding mechanism. As there are already existing methods to collect levies in most industries, any such contribution would be best pursued through co-contributions to a project. This approach is often adopted for animal health activities.

Identification of regional and other spatial amalgamations may be possible. This may be more suited to NRM activities where the risk creators / beneficiaries can be clearly identified. This is the case of the Hunter CMA where a high risk and key assets in Newcastle lend themselves to the implementation of a specific levy. Another example would be for the management of Fruit Fly in the Murrumbidgee Irrigation Area, which benefits citrus growers in that region in relation to market access. In most cases the key test of this approach will be alignment of the benefits arising from any levy to contributors (whether risk creators or beneficiaries).

In many cases it should be noted that Government contributions are also used to provide a way to leverage funds and increase the overall resources for action. The framework should note that this as a legitimate reason for government contribution, if there are wider public outcomes or there is significant underinvestment.

**IN RESPONSE TO IPART QUESTIONS 3&4**

Our view is that:
- In the medium term the demand for the existing services should be assumed to be unchanged. Over time the demand will change and this should be reflected in LLS strategic plans. These plans should be the starting point for the application of the cost recovery framework.
- The identification of parties that generate risk and/or receive benefit should be integral to the planning framework adopted by LLS and Local Boards. Over time, as services are delivered, knowledge of risk creators and beneficiaries will improve, resulting in adjustments to cost allocations.
2.3 Apportioning costs between parties

LHPA broadly supports the sliding scale approach (Approach 1) outlined by IPART. A key consideration in any approach is the availability of data and expert opinion to support analysis. The LHPA does not currently have the systems in place to enable the itemisation of services and costs (for example of staff effort) for the various services currently delivered.

The emerging context of LLS means that the extent to which service offerings (and as such the risk creators and beneficiaries) could vary at a Local Board level is still unknown.

Our view is that IPART should not seek to determine cost allocations as part of this review, but rather make recommendations about the broad approach and process that should be adopted by LLS. Our view is that the most appropriate process for determining cost shares would be through the use of expert panels, informed by available data. Such panels would examine each service offering or proposed program, and allocate cost shares appropriately. Our view is that this process should be coordinated by the new LLS with input from Local Boards once established. LLS should be appropriately resourced to ensure it has the necessary expertise to facilitate this process.

The application of a risk framework (Approach 2) as outlined in the Issues Paper across 30 or more services areas and 11 LLS Regions creates additional confusion and is in our view a potentially resource intensive process. Confusion will be compounded by a lack of data in many cases to justify risk assignments. In our view, the risk approach would add little to improving transparency over the sliding scale approach and as such is not supported. The risk model may be more useful for applying the cost recovery framework to an individual project or a special levy. In such cases the identification of parties may be easier and amenable to agreement.

LHPA does not support using the results of the Stakeholder Reference Panel to apportion costs (Approach 3). The primary reason for this position is the context in which the survey was conducted. Survey respondents were not aware that the information could be utilised to inform a cost recovery model. Appropriate and sufficiently detailed information was not provided to survey respondents to explain the services to be offered and the likely benefits that would arise from the delivery of the service to enable informed consideration of the question asked. It is also unlikely that survey respondents were sufficiently informed of the concepts of private and public benefits – key principles that should underpin any cost allocation methodology. A further question arises as to whether the survey population provided a representative cross section of the population of an LLS region.

IN RESPONSE TO IPART QUESTIONS 5,6,7,8,&10

Our view is that:

- We broadly support the sliding scale approach to apportioning costs outlined by IPART.
- A risk matrix approach would be unduly complex and not actually improve understanding of the cost recovery issues across the organisation. Such a method may be useful for a more specific funding agreement or special purpose rates. As such the approach is not supported by LHPA as the basis for apportioning costs.
- The stakeholder reference panel approach is flawed due to various bias including sample and information bias. Additionally the process was not designed for this purpose.
IN RESPONSE TO IPART QUESTION 9
Our view is that:
- It is important that the framework enable regional flexibility (see discussion in Part 1, section 4).

IN RESPONSE TO IPART QUESTION 11
Our view is that:
- We do not currently have the internal systems to itemise services and costs to inform the sliding scale approach.
- LLS and Local Boards should be appropriately resourced to ensure it has the necessary expertise to facilitate this process.

2.4 Funding options

2.4.1 A building block approach
Recognising the diverse range of risk creators and beneficiaries, our view is that – over the longer term - a building block approach be taken to budgeting and cost recovery for LLS and Local Boards. Such an approach underpins the principle of transparency and would support increased efficiency over time.

Our view is that broadly the building blocks of funding for LLS and Local Boards could comprise:

- An appropriation from government that provides the underpinning resources of the agency. These funds would support the governance, management and administration of the agency.
- A community service obligation (paid by government) that meets the “community share” of the cost of service delivery (e.g., biosecurity, natural resource management functions) – as determined by the sliding scale approach.
- A rate on landholders/occupiers to meet the “industry” share of the costs of the delivery of particular services (e.g. biosecurity).
- A community service obligation (paid by government) for any agreed landholder rate relief (e.g. a pensioner discount).
- Specific program contributions or project grants (e.g. those made by third parties such as the Commonwealth or R&D companies to fund discrete programs).
- Specific fees paid by individuals as a “fee for service” or “fee for product”.
- Specific charges imposed in the conduct of enforcing regulatory requirements such as those associated with mitigating specific biosecurity risks.

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8 for example LHPAs current charge for pest baits and NLIS tags
9 For example, under Part 11 of the RLP Act relating to pest control, the Minister or and Authority may impose an inspection charge to cover the reasonable expenses of actions taken by authorised officers as a consequence of an owner or occupier failing to act in relation to a pest control order.
Our view is that:

- Over the longer term, a building block approach be adopted by LLS and Local Boards to drive budgeting and cost recovery efforts.
- A building block approach would enable change over time as LLS knowledge and planning of the demand for service offerings improves.
- A building block approach will enhance transparency and ensure that there is no cross-subsidisation of service bundles.

2.4.2 Ratings Base

Our consideration of the issue of ratings base has focused on the most appropriate and equitable method to recover the share of costs from risk creators for biosecurity services and the management of TSRs for stock movement and grazing.

2.4.2.1 Notional carrying capacity (NCC)

Our view is that notional carrying capacity is the most equitable approach to determining the share of “biosecurity risk” of a particular landholding. In its essence, NCC is productivity measure that enables comparison of the productive capacity of properties within a district.

Currently, section 69(1) of the RLP Act requires the notional carrying capacity of “each holding” to be assessed at least every five years. While the regulation implies that assessments are to be made by visual inspection of the land itself, in practice LHPAs have adopted the practice of desktop assessments involving the use of computer maps, land descriptions etc to arrive at notional carrying capacity assessments. Physical inspections to review a determination of carrying capacity are conducted at the request a ratepayer within a specified period after the issuing of the rate notice.

We recognise that there is some confusion over the notion of carrying capacity among rate payers. The overwhelming anecdotal perspective of LHPA managers is that the majority of complaints received about rates notices are from small landholders about using carrying capacity as a basis for rating.

Our view is that there are opportunities to continue to use the concept of NCC as the broad basis for rating, but to improve the billing model and communication of rate purposes to improve clarity, particularly for small landholdings.

The LHPA Rates Working Group has been considering the issue of NCC and smaller holdings. The preferred option that was recommended by this working group is outlined in Box 1.
Box 1 A possible approach to rating

A minimum bill for landholdings that range in size from 2 to 40 hectares. This minimum bill would comprise:

- a general base charge; and
- an animal health supplement, where holdings carry 30 stock units\(^{10}\) or more

For holdings greater than 40 hectares, a bill would comprise:

- a general base charge;
- a charge based on notional carrying capacity; and
- an animal health supplement, where holdings carry 30 stock units or more.

Landholdings with intensive animal production (e.g. piggeries, poultry operations, horticulture etc) would be subject to a charge based on notional carrying capacity, regardless of size to reflect the biosecurity risks associated with intensive operations.

2.4.2.2 Area

Our view is that to charge a flat rate per hectare across an LLS Region would produce gross inequities in amounts charged on some properties, particularly for boards that cross the sheep/wheat and grazing zones. Such an approach would almost certainly involve some lands with a relatively low notional carrying capacity (and thus low productivity and low biosecurity risk) being subject to an inordinate increase in rates under an area based rating model.

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\(^{10}\) Stock units are defined under the RLP Act, with these provisions mirrored in the LLS Act (Schedule 9, Part 3). 30 stock units reflects
2.4.2.3 Unimproved capital value

The use of unimproved capital value (UCV) as a rating base for the provision of biosecurity services is problematic and is not supported by LHPA. UCV has very little relevance to productive capacity and as such biosecurity risk. UCV is influenced by many factors - proximity to urban centres or coastal views being two such factors that are unrelated to productivity.

Utilising UCV creates equity issues. Landholders within the same board area could pay substantially different rates, though biosecurity “risk” and the associated biosecurity services provided by LLS would be identical.

Furthermore, we have identified issues associated with the implementation of the UCV method. The process of the Valuer General means that properties within the same board area are not valued at the same time.

2.4.2.4 Other issues relating to the rating base

In Box 7.1 of the Issues Paper, IPART proposes that it may be practical to provide incentives (rate exemptions for specific rate components) for owners or occupiers who can demonstrate that they have mitigated the risk they pose.

LHPA does not support this model. Our view is that such an approach would be complex to develop, administer and monitor. If 2 ha is adopted as the minimum size of rateable property, LLS would have an estimated 289,000 landholdings to “service”. Our view is that significant resources would be required to process applications, conduct assessments and monitor compliance with any criteria, and that costs that would significantly outweigh any benefit of mitigated risk or efficiency.

There are numerous rating legacies of the former Rural Lands Protection Boards that were carried over into the LHPA model. On transition to LLS, there is an opportunity to address these legacies and anomalies. Examples of legacies include:

- differences in rates within a single board area. This was the result of RLPB rates being maintained when board areas were consolidated on the formation of the LHPAs; and
- exemptions such as those for properties designated for growing sugar cane and tree lots.

IN RESPONSE TO IPART QUESTION 12

Our view is that:

- The risk creator/beneficiary pays model is the best approach for levying charges.
- Over the longer term, a building block approach to budgeting and cost recovery for LLS and Local Boards should be adopted.
- Notional carrying capacity is the most equitable approach to determining the share of “biosecurity risk” for a fee collection system.
- Particular consideration should be given to the most appropriate methodology for measuring productive capacity for rating intensive animal production, to reflect the risk generated from such enterprises.
- A stepped approach to billing (similar to that outlined in Box 1) would support administrative efficiency and assist in communication with rate payers, particularly those on smaller properties.
IN RESPONSE TO IPART QUESTION 14

Our view is that:

- The exemption model proposed by IPART is impractical and would be prohibitively expensive to administer.
- Exemptions or reductions in charges should only be used in extremely rare cases with definitive reasons and criteria. The potential for abuse or gaming is often not worth the gains of such approaches given the scale of payments.
- Current exemptions, for example those for land for growing sugar cane should be removed.

2.4.3 Minimum rateable area

Minimum rateable area has been an issue of consideration by LHPA over the past few years. Our consideration of the issue of has focused on identifying a ratings base that recovers the share of costs of biosecurity services from risk creators. Our experience has been that blocks smaller than 10 hectares provide a biosecurity risk. For example, in the outbreak of equine influenza in 2007, 10,000 horses were identified from the land and stock returns from ratepayers of properties greater than 10 hectares in the Moss Vale Rural Lands Protection Board area\(^{11}\). However, during the outbreak, more than 100,000 horses from non-rateable properties (i.e. those less than 10 ha) were identified.

Similarly, in the Armidale RLPB, it was estimated that 800 horses would require vaccination. Following completion of the vaccination program, approximately 5,400 horses were treated. This was the experience of boards across the state, and it is again repeating itself with the management of Hendra virus in horses. LHPA veterinarians are called upon to diagnose all horses, and not just those located on rateable land.

The current 10 ha minimum fails to capture many intensive livestock operations which pose a biosecurity risk. For example LHPA staff have been a key component of the response to disease outbreaks such as Newcastle Disease and Avian Influenza in the poultry industry.

Our initial examination of land and property information data from 2012 shows that between 22% and 75% of properties in an LLS Region would not be rated if the minimum rateable area was established at 10ha (see Table 1). It should be noted that this analysis includes properties that are not likely to pose a biosecurity risk (for example schools, churches, industrial or council owned land). However, it highlights the magnitude of the potential risk creators that are not currently captured by the 10 ha minimum.

\(^{11}\) now part of the Cumberland LHPA

LHPA Submission 22
Table 1 Breakup of properties by size

<table>
<thead>
<tr>
<th>LLS Region</th>
<th>Number of properties &gt;= 2 &amp; &lt; 10ha</th>
<th>Number of properties &gt;= 10ha</th>
<th>Total number of properties &gt;= 2ha</th>
<th>% of properties &gt;= 2ha &lt;10ha</th>
</tr>
</thead>
<tbody>
<tr>
<td>Central Tablelands</td>
<td>7,270</td>
<td>17,061</td>
<td>24,331</td>
<td>30%</td>
</tr>
<tr>
<td>Central West</td>
<td>4,654</td>
<td>16,682</td>
<td>21,336</td>
<td>22%</td>
</tr>
<tr>
<td>Greater Sydney</td>
<td>32,544</td>
<td>10,989</td>
<td>43,533</td>
<td>75%</td>
</tr>
<tr>
<td>Hunter</td>
<td>11,353</td>
<td>20,456</td>
<td>31,809</td>
<td>36%</td>
</tr>
<tr>
<td>Murray</td>
<td>3,841</td>
<td>11,235</td>
<td>15,076</td>
<td>25%</td>
</tr>
<tr>
<td>North Coast</td>
<td>16,252</td>
<td>25,099</td>
<td>41,351</td>
<td>39%</td>
</tr>
<tr>
<td>North West</td>
<td>4,974</td>
<td>13,544</td>
<td>18,518</td>
<td>27%</td>
</tr>
<tr>
<td>Northern Tablelands</td>
<td>3,630</td>
<td>10,289</td>
<td>13,919</td>
<td>26%</td>
</tr>
<tr>
<td>Riverina</td>
<td>7,098</td>
<td>18,644</td>
<td>25,742</td>
<td>28%</td>
</tr>
<tr>
<td>South East</td>
<td>16,596</td>
<td>30,528</td>
<td>47,124</td>
<td>35%</td>
</tr>
<tr>
<td>Western</td>
<td>1,541</td>
<td>4,314</td>
<td>5,855</td>
<td>26%</td>
</tr>
<tr>
<td><strong>Total number properties</strong></td>
<td><strong>109,753</strong></td>
<td><strong>178,841</strong></td>
<td><strong>288,594</strong></td>
<td><strong>38%</strong></td>
</tr>
</tbody>
</table>

While there is evidence to justify the broadening of the rate base down to 2ha, consideration must be given to the level of service that would be expected or provided to smaller properties. The cost associated with meeting this expectation could easily outweigh the revenue generated. We have conducted preliminary analysis on the potential revenue benefits, using assumptions of the current rating model. This analysis estimates state-wide revenue benefits in the order of $6 million if properties between 2 and 10 ha were rated. The revenue benefits for individual LLS regions varied considerably with the Sydney region receiving the most benefit, and the Western Region the least benefit.

**IN RESPONSE TO IPART QUESTION 12**

Our view is that:

- Landholdings smaller than 10 hectares pose a significant biosecurity risk. Our experience indicates that properties of 2ha are sufficiently large to carry animals to generate such a risk.
- LLS planning should include consideration of the costs associated with servicing smaller properties, the resulting net revenue benefit
- A “minimum bill” concept would alleviate past issues associated with poor landholder understanding of rating.
- Additional efforts could be made to improve landholder understanding of the link between rates and biosecurity risk and expectations regarding service levels.
2.5 Collection mechanisms

2.5.1 The current system
Currently, LHPA rates are calculated by local authorities in October/November. Rates are then approved by the Minister in January. Following this State Council calculates individual rate files in January and the annual rate notices generated and mailed from late January to February. Debt recovery is the responsibility of individual authorities until rates have been unpaid for 120 days. After this, responsibility is transferred to a third party debt recovery company.

LHPAs also collect rates that are largely passed directly on to others. For example LHPAs charge the Special Purpose Rate (pest insects) - otherwise known as the Pest Insect Levy (PIL) to all ratepayers. This levy is then passed on to DPI in full. DPI pays a large proportion of the proceeds of the PIL to the Australian Plague Locust Commission as NSW’s contribution to its activities detecting egg beds, forecasting outbreaks and aerial spraying of bands of locusts in various states.

LHPAs collect a meat industry levy on behalf of the NSW Food Authority. LHPAs receive a small commission to cover the costs of the administration and collection from NSW Food Authority for the provision of this service.

2.5.2 Future options
Utilising local government as the collection mechanism for LLS rates is one option proposed by IPART in the Issues Paper. Our view is that all reasonable options should be open to consideration, and the most cost effective option be adopted. This would require detailed financial cost analysis that should consider the:

- administrative cost of the collection mechanism, including any commission;
- likelihood of unpaid rates and associated costs of debt recovery;
- costs of maintaining information services that are currently linked to rates billing database (for example land and stock returns);
- costs associated with maintaining accurate data records, including land transfers; and
- longevity of the system (for example, might councils change their mind about delivering the service to LLS, adding additional costs associated with change).

IN RESPONSE TO IPART QUESTION 13
Our view is that:

- a detailed financial analysis of the range of options be undertaken, and the most efficient collection method be adopted.
3  Audit

We support IPART’s concept of including the cost recovery framework in a broader audit program and welcome the Tribunal’s recognition that the level of proposed audits is potentially costly and in some cases overlapping.

The process for performance auditing for LLS is yet to be fully determined. In relation to audit, the Act establishes that the:

- Minister is responsible for the arrangement of an audit to determine whether LLS is carrying out its functions effectively and efficiently and in accordance with the State Strategic and Local Plans (Clause 24(1)).
- Minister is to ensure that the State strategic plan is audited, at intervals of not more than 5 years, to ascertain whether its provisions are being given effect (Clause 44(2)).
- Minister is to ensure that each local strategic plan is audited, within 3 years of its approval, to ascertain whether its provisions are being given effect (Clause 54(2)).
- Costs of such audits are paid for by LLS (Clauses 24(6), 44(4), 54(4)).

In the absence of a final policy position of the proposed audit process, our view is that detailed discussion of audit options for the cost recovery framework is somewhat premature.

IPART propose that the audits evaluate compliance with the following criteria:

- Cost Recovery Framework referred to in Chapters 4 to 6; and
- Funding sources and fee collection mechanism(s) referred to in Chapters 7 to 8.

Any audit of the Cost Recovery Framework will depend on how and when the framework is to be used. This could vary and it may also be used at various scales (e.g. organisational, regional, service offering or project). A critical step is the decision as to how and when the framework is to be applied, and expectations for its use. Our view is that this decision should be clearly documented, and could for example reside in the State Strategic and Local Plans.

Our view is that in making recommendations about auditing, the purpose of the audit should be clear. Does the audit relate to the implementation of the agreed budget and plans or does the audit examine the application of the framework to the strategic planning process? Is the audit to establish the appropriateness of the fees (as is implied by the cost recovery impact statement) or to examine compliance with the implementation of a fee schedule? In our view these are significantly different – with the former more a matter for a review than an audit process.

In the case of service fee pricing, the framework may be used to establish a schedule of agreed fees and charges that could then be audited.

Similarly, an audit of funding sources and the fee collection mechanism could logically fall into the scope of a financial audit, if the audit is focused on implementation of agreed processes. If the purpose of the examination is checking the appropriateness of a policy this could be reviewed and approved prior to implementation.

Our view is that it will take time for LLS and Local Boards to establish the compliance framework for the organisation, and that the integration of the cost recovery framework should occur as part of this process. In our view, the key determinant of the appropriateness of an audit process will be influenced by the system and process used to approve LLS budgets, cost recovery mechanisms and charges, and degree of flexibility that Local Boards may have in these decisions. As a policy question, this is yet to be resolved.
Importantly, our view is that the audit program of LLS and Local Boards should focus on the achievement of outcomes, and not just activities and processes. Such a focus will drive improved performance in the agency over time and provide stakeholders with confidence that their contributions are leading to the achievement of planned outcomes.

IN RESPONSE TO IPART QUESTION 16

Our view is that:

- The process for auditing the cost recovery framework should be cost effective and be included in other audit processes. At this initial stage our view is that the audit of the cost recovery framework should be embedded in the financial and performance audits of LLS and Local Boards.
- As a principle, audits should focus not just on processes or activities, but also outcomes. This will support improved performance in LLS over time.
- The process for auditing the cost recovery framework should be resolved once the responsibilities of different parties (i.e. The Minister, LLS and Local Boards) in applying the framework are known.
Part 3 – The current LHPA Approach

4 LHPA services and activities

4.1 Overview of LHPAs
LHPAs deliver the frontline livestock health service in NSW. Though in essence a regulatory agency, LHPAs work collaboratively with rural producers, government and industry to safeguard agriculture in NSW.

The Rural Lands Protection Act 1998 (RLP Act) constitutes each of the state’s 14 LHPAs and their governing body, the State Management Council, as bodies corporate. The State Management Council is responsible to the Minister for Primary Industries. There are 14 authorities, with staff at almost 60 locations across the state.

Core areas of responsibility are animal health, pest animal and insect control and the management of travelling stock reserves. We work in close partnership with NSW Department of Primary Industries and other government and industry agencies to carry out our goals.

LHPAs assist producers in ensuring they have correctly identified their livestock and that stock movement is carried out in accordance with requirements. They also assist with drought and natural disaster relief.

4.2 LHPA services and activities
The core services currently delivered by LHPA, which will ultimately become the responsibility of LLS are outlined in Table 2.

Table 2 Summary of LHPA services and activities

<table>
<thead>
<tr>
<th>Biosecurity (Livestock Health)</th>
<th>Biosecurity (Pest animals and insect management)</th>
<th>Natural Resource Management (Travelling Stock Reserves)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Disease surveillance and reporting</td>
<td>Regulatory services at the local level</td>
<td>Management of 600,000 hectares of TSRs</td>
</tr>
<tr>
<td>Emergency disease prevention, preparedness and response</td>
<td>Provision of advice on the most suitable and best practice methodologies for pest control</td>
<td>Issuing of access permits for TSR use</td>
</tr>
<tr>
<td>Advisory and diagnostic services</td>
<td>Promotion of working relationships between all stakeholders involved in pest control through groups</td>
<td>TSR infrastructure maintenance</td>
</tr>
<tr>
<td>Traceability systems</td>
<td>Provision of some materials used in pest control, including baits</td>
<td>TSR weed and pest animal control</td>
</tr>
</tbody>
</table>
4.3 Current approach to planning, budgeting and cost recovery

4.3.1 Overview of the business planning budgeting
In essence, each authority is a unique “business”. The board of each LHPA is responsible for the preparation of an annual function management plans\(^\text{12}\) and an associated budget for each financial year. These plans are approved by the State Council.

The State Council provides each board with technical expertise and guidance, support and service including:

- regulatory and compliance advice, communication and media advice, project management services, as well as general administrative and communication support;
- financial accounting services, including accounts payable, accounts receivable, treasury, payroll and financial reporting services;
- IT infrastructure, databases, applications and business systems and support;
- management of the annual rating process and Land and Stock return process; and
- Human Resources Management Services.

4.3.2 Rating and cost recovery
The RLP Act provides for each authority to establish a fund into which all monies received are deposited and from which monies required for any purpose allowed under the RLP Act or any other Act are paid. As required by RLP Act, the Board of each LHPA is required to prepare audited financial reports for each year.

Each LHPA’s primary source of income is generated from rates charged to landholders. The charging of rates by the LHPAs is required under the RLP Act, with rates charged on all parcels of land deemed to be rateable under the RLP Act. Each authority district has a minimum rating area for properties, which is generally 10 hectares on the coast and tablelands, and larger in more western districts of the state.

Rates are charged on a two-tier basis, including a general rate paid by all landholders and a supplementary animal health rate, which is payable in prescribed circumstances. Under the RLP Act, each authority determines the rates for its district based on local operational needs. Special purpose rates are charged for specified purposes, and for those liable to pay the animal health rate, such as the meat industry levy which is collected on behalf of the NSW Food Authority. The Minister for Primary Industries approves all rates.

\(^\text{12}\) RLP Act requires LHPAs to prepare function management plans for functions with respect to travelling stock reserves and animal health functions (s 44(1))
The cost of the delivery of State Council functions and services have traditionally been met by:

- a subscription charged to each individual authority by State Council;
- an operating grant provided by the NSW Government; and
- A capital grant - Stock Routes Capital Works Fund – provided by the NSW Government.

From 2010 to 2012 the LHPAs were directed by the Minister to cap total rate increases at the current Consumer Price Index (CPI) of 3.5%. For 2013, all rates\textsuperscript{13} were frozen by the Minister at 2012 levels.

Until the 2011-12 Financial Year, State Council received some government funding in the form of a departmental grant. This annual operating grant from the NSW DPI was not renewed in 2012-13.

In addition to the DPI operating grant, LHPAs may also receive grants for specific activities, for example the delivery of projects funded by CMAs or the Commonwealth under Caring for Our Country. These grants are generally received through a competitive tender process and are not assured.

An overview of the consolidated income streams of LHPAs for 2011/12 is provided in Table 3.

\textbf{Table 3 Overview of consolidated income streams (FY 2011/12)}

<table>
<thead>
<tr>
<th>Income stream</th>
<th>FY 2011/12</th>
<th>$</th>
</tr>
</thead>
<tbody>
<tr>
<td>General Rate</td>
<td>38%</td>
<td>19,108,447</td>
</tr>
<tr>
<td>Animal Health Rates</td>
<td>21%</td>
<td>10,602,850</td>
</tr>
<tr>
<td>Special Purpose Rate: Pest Insects</td>
<td>12%</td>
<td>5,894,558</td>
</tr>
<tr>
<td>Grant Income\textsuperscript{1}</td>
<td>3%</td>
<td>1,427,773</td>
</tr>
<tr>
<td>Other Income\textsuperscript{2}</td>
<td>26%</td>
<td>12,776,143</td>
</tr>
<tr>
<td>Total Income</td>
<td>100%</td>
<td>49,809,772</td>
</tr>
</tbody>
</table>

Source: LHPA Annual Report 2011/12

\textsuperscript{1} Grants include those from CMAs and directly from the Commonwealth under Caring for Our Country, (2) Other income includes interest income and income from the sale of goods (eg baits, stock permits, NLIS tags).

As outlined in our submission to the Ryan Review of LHPAs, there is a growing issue where deficits are becoming increasingly common as expenditure growth continues to outpace revenue growth. In 2010-11 analysis of financial data indicated that 12 of the 14 LHPAs had total expenditure (including depreciation) exceeding income.

Key factors that have influenced the ability of individual LHPAs to fully recover costs include:

1. a requirement to pay payroll tax;
2. rating model and restrictions (including minimum rateable size and rate caps);
3. costs associated with the collection of levies on behalf of others;
4. governance structure;
5. delivery of services for the public benefit (eg TSR management) that are “not paid for”; and
6. loss of DPI operating grant for the functions of State Council.

While LHPA recognises that some of these issues have been addressed by the creation of LLS, some issues (points 2, 3 and 5 above) are at the core of IPART’s current review.

\textsuperscript{13} general rate, animal health rate, pest insect levy and meat industry levy.
5 Conclusion

We appreciate that the Issues Paper and associated submissions are the first step in a lengthy process for this review. In this submission we have flagged our views on the strategic context of the cost recovery framework and on the key questions posed in the Issues Paper.

Our prevailing view is that it would be premature for IPART to recommend a rigid and fixed cost recovery framework. The policy and administrative frameworks for the new organisation are yet to be agreed and the plans that will establish the service offerings and service levels have not yet been developed. Our view is that there is insufficient information to establish explicit cost shares for each proposed service offering or for the agency as a whole. There is a considerable risk that a rigid and highly specified approach would result in a mismatch between the accepted framework and the ultimate needs of the agency. Given this state of transition, we advocate that IPART closely consider the ultimate outcome of this review.

In light of this, we recommend that the outcome of this review be a clear but broad cost recovery framework, with recommendations as to the methodology for determining cost shares and guidance as to how the framework could be applied to the planning and budgeting activities of LLS and Local Boards. Adopting a broad guidance approach would support flexibility, enabling the Minister and LLS to further consider the cost recovery framework once established.

To further support this flexibility, IPART could consider “unbundling” the terms of reference. We agree that a rating is a sound mechanism for recovering landholders’ share of costs. However, in the absence of key plans and government policy decisions, our view is that a rigid determination on the rating base and rateable area by IPART at this stage would lack appropriate context. In this submission, we have restricted our views to those on a possible rating approach to recover costs associated with biosecurity risk and the management of travelling stock routes for travelling stock and grazing purposes.

To inform the development of the cost recovery framework, in the next stage of this review we encourage the Tribunal to:

- be fully informed of the transitional arrangements for the establishment of LLS and Local Boards;
- seek briefings on the emerging policy and operational frameworks for LLS and Local Boards, including those to meet the audit requirements of the LLS Act;
- seek detailed information on the services that are currently delivered by LHPAs, CMAs and DPI to ensure the Tribunal has a sound appreciation on the breadth and complexity of the likely service mix of the new organisation; and
- conduct more detailed analysis – including likely revenue benefits associated with any expansion of the rating base, when considering possible options for ratings base and minimum rateable area.

It is our view that stakeholder confidence in the new LLS will be paramount to the success of these reforms. This review is one of many considerations in the formation of the new agency. We encourage the Tribunal to ensure that its recommendations for a cost recovery framework are considerate of the broader strategic context of the reform process.