Draft Submission to IPART – Review of Rate Peg Methodology

Council's preferred stance in relation to the rate peg is that rate-pegging should be discontinued, in line with submissions made in relation to the Review of the Local Government Rating System and the previous review of the rate peg methodology. There should be a governance framework that permits a certain range of increase from year to year, without the need for a Special Rate Variation.

It is Council's view that the determination of the appropriate annual rates increase should be made by each council with the objective of ensuring that the community's expectations are met in a financially sustainable manner, over the long term. Increases would be in line with the required amount as identified in Council's Integrated Planning and Reporting (IP&R) documentation, developed through community consultation.

Setting rates within a range over the four-year Delivery Program timeframe would enable councils to smooth the impact of rate increases and reduce volatility, which reduces the cumulative impact to ratepayers over the long term and enable improvements to services, as demanded by the community.

The application of a State-wide rate peg, based on the average costs of predetermined set of council costs, does not reflect the costs and expectations of each individual council's community. Because of this, it does not enable councils to provide appropriate service levels in a financially sustainable manner.

Adjustments to enable councils to respond to external forces (e.g., pandemics, sharp economic changes, natural disasters, and changes in legislation) should be initially financed through grant funding and then incorporated into future rates increases through the governance framework established.

IPART's role would be to develop an appropriate governance framework and to monitor and approve rates increases in line within this framework set initially as part of Delivery Programs and then adjusted via annual applications, if required to respond to external forces.

Council also notes that some amendments to the Local Government Act, 1993 made in May 2021 are yet to be implemented through the Local Government Regulations (General), 2021. Some of these amendments will help in the flexibility of the local government rating system.

The responses to the specific questions posed within the Issues Paper are provided in the following section.

1. To what extent does the Local Government Cost Index reflect changes in councils' costs and inflation? Is there a better approach?

Comment: *The main issue is that the Local Government Cost Index is not recalculated with sufficient regularity to ensure that it is reflective of the average councils' cost and inflation. Additionally, it fails to capture the cost of increased demand for enhanced services by the community, increased costs associated with changes in legislation, specific contractual obligations, or impacts of external forces. Finally, very few councils reflect the 'average council' and subsequently, the LGCI can be a poor reflection of the actual change in councils' costs and inflation.*

A more effective approach would be for councils to have a detailed four-year plan in line with the Delivery Program timeframe that builds in the impacts of the aforementioned factors and provides a buffer for effective response to external forces. This would enable councils to improve services, accommodate increased demand outside population increase and apply price-smoothing techniques to reduce the cumulative impact of rates increases over time. This approach is similar to how annual charges in relation to Sewer and Domestic Waste are currently determined by councils.

2. What is the best way to measure changes in councils' costs and inflation, and how can this be done in a timely way?

Comment: *The best way to determine historic changes to councils' costs and inflation is through the data collected under the Financial Data Return. However, this again is a lagging indicator and does not enable improvement of services. There is limited availability for leading indicators that could be reliably used, particularly in the current volatile economic conditions, to be able to broadly apply to all NSW councils.*

Therefore, it is more effective for councils to determine the costs to be covered and consult with the community on a range of rate increases for the services agreed over the Delivery Program timeframe.

3. What alternate data sources could be used to measure the change in councils' costs?

Comment: *This is covered by the response to Question 2.*

4. Last year we included a population factor in our rate peg methodology. Do you have any feedback on how it is operating? What improvements could be made?

Comment: *The population factor does seem to be reflective of the population growth experienced by Hawkesbury Council. However, as this only accounts for residential population growth, it does not capture the increased cost of demand for commercial, employment and tourism sectors. Additionally, there are a range of costs greater than those captured within developer contributions that require funding prior to the point of increased population.*

As outlined above, each council has unique growth and changes in demand associated with growth and therefore should be responsible for determining the appropriate range of rating increases over the Delivery Program timeframe.

5. How can the rate peg methodology best reflect movements in productivity and the efficient delivery of services by councils?

Comment: *Most productivity enhancements are generally linked to being able to achieve more, using the same resources and very rarely results in financial savings. For example, reducing the time to produce planning certificates will result in staff being able to reduce backlogs and respond more quickly to customer requests. There will be no savings in employee costs. Additionally, generally any savings that arise from automation are offset by increased technology costs.*

Each council should measure the outputs of services and aim for enhancements (i.e. reduced time taken to produce certificates, increased number of certificates generated etc.). The focus should be on enhancing services, not on reducing budgets to gain false economies.

Again, each council has the detailed knowledge required to develop the appropriate service delivery matrix on which to measure productivity improvements on and outline enhanced services provided from these improvements. This could be captured in Annual Reports and form the basis for determining rate increase ranges in future Delivery Programs, with possible reductions in cumulative increases over the timeframe.

6. What other external factors should the rate peg methodology make adjustments for? How should this be done?

Comment: *External factors that should be included in the rate peg:*

- *Increases in costs associated with changes in legislation*
- *Reductions in overall NSW-wide grant allocations available for local government*
- *Increases in costs set by the NSW Government and passed to Local Government (Emergency Services Levy, Election Costs, Planning Commission Costs)*
- *Increases in costs associated with net zero targets*
- *Increases in costs associated with enhancing community resilience to natural disasters and pandemics*
- *Costs associated with responding and recovering from natural disasters that are not funded by grants and under Natural Disaster Funding Arrangements.*

Again, the external factors that impact and the level of impact will differ from council to council and therefore makes the inclusion within a rate peg system ineffective. For example, the cost of the COVID-19 Pandemic on some councils was significant, but this was not the experience of some councils depending upon their reliance on income generated from the hire of assts, commercial inspections, and rental properties.

Each council has the business knowledge to be able to factor in appropriate buffers to external shocks based on appropriate analysis. This again will give a mechanism for smoothing rates increases over the long term and reducing the overall cumulative impact to ratepayers, while enabling improvements in services and enhanced resilience to external factors.

7. Has the rate peg protected ratepayers from unnecessary rate increases?

Comment: *The rate peg has protected ratepayers from unnecessary rate increases, but at the cost of not receiving enhanced quality and range of services, lower levels of asset renewals, limited additional infrastructure and increased volatility in rates increases due to insufficient levels of rates income to enable proactive responses to external factors. This has been exacerbated by the rate peg not covering additional costs of programs initiated by State Government and passed to Local Government for administration or delivery.*

8. Has the rate peg provided councils with sufficient income to deliver services to their communities?

Comment: *The rate peg does not generate sufficient income for councils to deliver services to their communities. The data presented on page 12 of the Issues Paper shows that Council reduce their overall operating expenses to meet Operating Performance Ratios and remain within Operating Income totals, not that the full range and quality of services the community expects is being delivered.*

Additionally, this clearly indicates that infrastructure renewal and capital enhancements are constrained, as there is very little gap between operating income and expenditure to increase this expenditure. This also constrains councils' ability to weather external shocks (e.g., natural disasters) and to implement new programs, particularly in relation to net zero targets and building resilience, which is becoming more of a focus across the industry.

Most social media platforms of local government will clearly see that more are demanded by constituents than is currently being delivered.

9. How has the rate peg impacted the financial performance and sustainability of councils?

Comment: *The rate peg impacts financial performance of councils by reducing the overall income able to be invested in providing services to the community and ensuring infrastructure is at the level required to ensure sound economic, environmental, and social outcomes.*

As stated above, programs that councils should be progressing and investments that have potential to reduce social, environmental and economic costs in the long term are unable to be progressed, as operating expenditure is kept aligned with income, predominantly driven by the rate peg.

Over the long term, delays in appropriate asset maintenance, renewals and replacements results in increased costs and degraded services to the community and costs more.

10. In what ways could the rate peg methodology better reflect how councils differ from each other?

Comment: *As the communities, environments, costs, income sources and contexts of each council differ, the only way to be able to truly account for these differences is to enable each council to determine a set range of rates increases to be applied over a Delivery Program timeframe, with oversight by IPART.*

11. What are the benefits of introducing different cost indexes for different council types?

Comment: *The benefit would be to better reflect the cost drivers and align these to the likely experience of different council types. However, this does not account for the different service expectations and council specific objectives that councils strive to achieve as part of developing their Community Strategic Plans.*

12. Is volatility in the rate peg a problem? How can it be stabilised?

Comment: *The issue with volatility in the rate peg is that is currently reactive, based on lagging indicators, whereas Delivery Program and Operational Plans are derived off assumed rate pegs. Services, programs, and asset planning are set based on the assumed income and where the rate peg sharply differs, this results in cutting of programs and deferral of planned asset expenditure, which cost more over the long term and reduces services to the community.*

To stabilise volatility, ideally a council should determine the services, programs and optimal asset expenditure over the four-year Delivery Program horizon and determine a range of rate increases to enable responses to externalities, using appropriate price-smoothing techniques.

This could be applied within a rate peg context, by establishing a minimum and a range the rate peg will be within over the Delivery Program timeframe, based on cost indexes for the council type. The population factor would then be applied on top of this rate peg minimum/range.

13. Would councils prefer more certainty about the future rate peg, or better alignment with changes in costs?

Comment: *To support the Integrated Planning and Reporting framework and establish service levels with respect to programs, services and asset expenditure, the rate peg needs to be more long-term in its approach, enabling increased certainty, greater coverage for externalities and service enhancements to communities.*

Ideally, there would be a range rates would be within over a Delivery Program timeframe, with potential for annual applications to increase either by councils, or initiated by IPART, to accommodate for unforeseen circumstances.

14. Are there benefits in setting a longer term rate peg, say over multiple years?

Comment: *There are benefits in relation to being able to plan effectively for delivery of projects and planned asset expenditure, provided there is a mechanism to adjust based on unforeseen external shocks. This is optimised if councils themselves can establish the rate peg range for their council of this timeframe, based on the demands of the community, the outcomes to be achieved within the Delivery Program and optimal asset expenditure.*

15. Should the rate peg be released later in the year if this reduced the lag?

Comment: *The rate peg within the current context is issued at the optimal time in terms of being able to plan effectively for its impact on the Delivery Program within the development of the annual draft Operational Plan. Any delay would result in ineffective budgeting processes and sub-optimal investment decisions and changes to costs could still occur in any case.*

16. How should we account for changes in efficient labour costs?

Comment: *The Local Government Cost Index should include the NSW State Government Award, which more closely reflects the costs of employees in Local Government. The changes in the superannuation guarantee also needs to be included in the calculation of the rate peg.*

In relation to accounting for efficiency gains, as outlined above, it is rare that councils' overall Full Time Equivalent staff reduces, it is more that service levels are improved, or positions / activities of positions change to incorporate changes in legislative reporting, technological improvements, improved data capture, or are diverted to new programs and services, depending upon the outcomes to be achieved as part of each council's Community Strategic Plan.

17. Should external costs be reflected in the rate peg methodology, and if so, how?

Comment: *This is covered by the response to question 6.*

18. Are council-specific adjustments for external costs needed, and if so, how could this be achieved?

Comment: *Council-specific adjustments for external costs are needed, to enable councils to expand their services and increase service levels from historical levels (particularly in relation to asset expenditure). This should be based on the detailed planned expenditure developed in consultation with communities within the Delivery Program. A range of rates increases should be included within the community consultation and then approved by IPART.*

Annual changes required due to substantial changes to the assumptions included within the Delivery Program outside this range, should then be via a streamlined, efficient application process with IPART, after community consultation.

19. What types of costs which are outside councils' control should be included in the rates peg methodology?

Comment: *This is covered by the response to question 6.*

20. How can we simplify the rates peg calculation and ensure it reflects, as far as possible, inflation and changes in costs of providing services?

Comment: *The benefits of simplifying rates peg calculations is better achieved, not by simplifying the calculation itself, but by determining a range rates can be increased by over a Delivery Program timeframe. This would enable price smoothing and planned expenditure to be optimised on a individual council basis, where the best knowledge of the community, environment and cost that the council is operated within.*