INVERELL
SHIRE COUNCIL

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4 November 2022

Independent Pricing and Regulatory Tribunal
PO BOX K35
Haymarket Post Shop
SYDNEY NSW 1240

Dear Tribunal

Re: Submission: Review of the rate peg methodology – Issue Paper

Inverell Shire Council welcomes the opportunity to provide a response to the 'Review of the rate peg methodology' Issues Paper. Please find below our responses to each of the questions IPART has posed.

Please do not hesitate to contact myself on [redacted] should you require any further information

Yours faithfully

[redacted]

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RESPONSE TO QUESTIONS PRESENTED IN THE IPART ISSUES PAPER

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

   The LGCI achieves what it is designed to do, which is to reflect the average costs across all NSW councils based on 26 cost components during periods of stable inflation. Where it fails is to reflect cost movements in periods with volatile inflations as experienced during the last 18 months. The LGCI does not provide for the individual cost movements of each council.

   The two-year lag has not been an issue during times of relatively stable inflation. In times of volatile and somewhat unpredictable inflation the effect can be (and has been) very dramatic and does not align with community expectations.

   Given the large variety of services provided by Councils the current 26 cost components do not reflect the services and/or service levels provided to individual communities. The LGCI cost components need to be expanded and should align with the service levels expected by individual communities. At a minimum, four LGCI should be delivered, one for Metro, Regional, Rural and Remote Councils. A far more accurate LGCI could be derived for each Local Government Area (LGA) via collecting data through the Financial Data Return due by 31 October each year. IPART could then release an individual rate peg per LGA by 1 December each year allowing Council's sufficient time to prepare future budgets.

   A portion of the LGCI must include some forward-facing indices or some judgement must be exercised on future inflationary pressures.

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

   Each council is significantly different in the way it services its community. Therefore, the number of cost components should be increased to better measure overarching costs of each Council.

   As noted in question 1, at a minimum, four LGCI should be delivered, one for Metro, Regional, Rural and Remote Councils. A far more accurate LGCI could be derived for each Local Government Area (LGA) via collecting data through the Financial Data Return due by 31 October each year.

   A portion of the LGCI must include some forward-facing indices or some judgement must be exercised on future inflationary pressures.

3. ***What alternate data sources could be used to measure the changes in council costs?***

As noted in question 1 above, an individual LGCI for an individual LGA would provide a far more accurate weighting of the basket of items in the index.

Other alternate data sources may include:

- The Local Government (State) Award provides known increases for a period of three years, this index could be used to forecast future labour costs.
- The Reserve Bank of Australia (RBA) produces forecast CPI.
- Forward facing indices (such as gold futures) could be used to predict future inflation.

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?***

No comment.

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

The productivity of councils and the efficient delivery of services to the community is a key concern of Councillors, Management and ratepayers.

Each council has different service levels and community needs, improvements in productivity are part of our Integrated Planning & Reporting (IP&R) process. Productivity gains are usually reinvested within Council's operations to improve existing services. That is, "productivity gains result in extra expenditure on the ground".

Penalising councils for efficiency gains is a disincentive for innovation and should be removed.

The ABS price indexes used to measure productivity do not reflect the large variety of services provided by different sized councils. A "one size fits all" approach does not adequately represent all councils.

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

Unique costs that have occurred in the last twelve months or that are predicable for the relevant LGCI period. For example, the additional 0.2% added onto the 2021-22 rate peg to account for the costs of conducting council elections, and its subsequent withdrawal in 2022-23 is appropriate. Similar instances of these types of costs should be included in the LGCI methodology.

If a new cost is identified by the IPART or the OLG and it is expected to have a uniform impact on the sector (as with above) then a factor should be applied in the relevant LGCI. The factor may only affect one year and therefore it is reasonable to expect a similar reducing factor in the following year. If the impact is permanent, i.e. the costs are going to have an effect infinitum the factor should not be removed in the following LGCI.

The revised LGCI should be agile enough to adapt to the changes to councils' costs driven by external factors:

- Global Economic Forecasts and delays in the Supply Chain,
- Changes in private sector costs and pricing trend where local government has a high degree of interaction or engagement (e.g. IT, building construction, waste management, specialist contractors, infrastructure, design etc.)
- Impact of natural disasters and severe weather events
- Resilience – cost in identifying how local government can support its community to be more resilient and how local government can itself be resilient. Cost to implement identified resilience outcomes.

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

In the short-term, rate pegging has protected ratepayers from unnecessary rate increases. However, over the long-term, this protection comes at a significant cost especially to the most vulnerable in the community when Councils are forced to seek large Special Rate Variation (SRV) to ensure financial sustainability.

NSW councils adhere to strict IP&R frameworks that require extensive community consultation that allows for intervention by the community and mandates numerous consultation steps. Council's that demonstrate financial sustainability – ie "Fit for the Future" through the IP&R process should be allowed to increase the IPART rate peg by a set margin to deliver on community expectations.

To this point we encourage IPART to consider some flexibility in the rate peg methodology that would allow for increases above the peg of up to 3%. The increase should align with the Community Strategic Plan (CSP) and the Long-Term Financial Plan (LTFP), Delivery Plan (DP) and the Operational Plan (OP). This concept was first proposed as an incentive for Councils to meet the NSW State Government "Fit for the Future" benchmarks.

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

No. Thus the reason for Special Rate Variations (SRV). Given every Council in NSW has now applied for at least one SRV indicating that the rate peg has not provided sufficient income for the delivery of services.

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

Following on from the NSW Governments 'Fit for the Future' investigation, a number of councils found it necessary to apply for significant rate increases to remain financially sustainable. Essentially, this situation leads to injustices in intergenerational equity as the current and future ratepayers are paying for mistakes by preceding councils that had not raised the appropriate fair and equitable land rates.

In the last 10 years:

- 178 councils applied for a SRV
- 165 applications were approved in full or in part
- 142 applications rationalised based on one or all of the following to address:
    - financial sustainability,
    - existing infrastructure backlogs,
    - future infrastructure expenditure obligations.

In addition to this, in the last 3 years:

- 79 councils reported an infrastructure renewal backlog of greater than 2%
- 56 councils consistently reported an infrastructure backlog of greater than 2%
- 99 Councils reported an infrastructure renewal ratio of less than 100%
- 33 Councils consistently (over 3 years) reported an infrastructure renewal ratio of less than 100%
- 74 Councils reported an infrastructure renewal ratio of less than 100% over a 3-year average

The above statistics clearly show that a large majority of NSW councils are balancing their operational budgets by underfunding its capital obligations.

Based on the number and size of SRV applications in the last 10 years and the deterioration of councils' asset sustainability indicators over the least 3 years, it can be said that the rate peg has prevented necessary rate increases.

Instances of "kicking the can down the road" for future generations to deal with should be considered and made easier to prevent.

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

Following from our suggestions detailed in question 1 above, a different rate cap should be calculated for councils falling in (at a minimum) the four main council categories of Metro, Regional, Rural and Remote, or an individualised rate peg per LGA. This will not only more accurately reflect the different operating environments facing councils, but also facilitates comparisons between the performance of local councils within each category. As a consequence, there will be greater transparency for local residents and more accountability for local councillors.

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

An individualised LGCI for each LGA may be more in tune with each council's actual costs of providing services to their communities. At a minimum, the LGCI should be employed for the main categories of councils (metro, regional, rural, and remote councils).

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

Yes. The IPART will be fully aware of the challenges councils recently presented with the 2022-23 LGCI being released at 0.7%.

To stabilise the LGCI the data used needs to align more closely with the current financial environment and possibly using a period of rolling averages. It would preferably be based on the future landscape rather than historical. Presently council applications for a SRV is assessed on where that council is heading and a proven lineage to the future needs being demonstrated in the council DP as part of the IP&R requirements.

Accordingly, when it comes to the bespoke application to go beyond the standard rate peg the IPART looks toward that councils' future costs and future financial position not what the historical costs were. If this principle could be incorporated into the LGCI it would be more easily understood by the community and more closely align the LGCI with the SRV process.

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

More certainty about future rate peg would allow Councils to adopt LTFP with greater confidence. IPART has for many years now suggested that Councils should use a 2.5% rate peg factor in their LTFP. IPART should consider setting a minimum rate peg of 2.5% and increase this rate peg as required through the LGCI process. The minimum rate peg could be set for each term of Council. Eg four years.

While a minimum rate peg will provide some certainty to councils it does not prevent the operating cost pressures on individual councils as a result of inflation volatility, pandemics natural disasters and State Government cost shifting.

A better alignment to actual costs is recommended and the use, where possible, of known future costs indexes (e.g. NSW Local Government (State) Award for labour costs) and the RBA forecast CPI.

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

More certainty about future rate peg would allow Councils to adopt LTFP with greater confidence. IPART has for many years now suggested that Councils should use a 2.5% rate peg factor in their LTFP. IPART should consider setting a minimum rate peg of 2.5% and increase this rate peg as required through the LGCI process. The minimum rate peg could be set for each term of Council. Eg four years.

While a minimum rate peg will provide some certainty to councils it does not prevent the operating cost pressures on individual council as a result of inflation volatility, pandemics natural disasters and State Government cost shifting.

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

Generally, no. Councils need to prepare their OP (budget) early in the new calendar year to meet exhibition timelines, the current release dates support this outcome.

A far more accurate LGCI could be derived for each LGA via collecting data through the Financial Data Return due by 31 October each year. IPART could then release an individual rate peg per LGA by 1 December each year allowing Council's sufficient time to prepare future budgets.

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

We believe accounting for actual labour costs should be aligned with changes in the NSW Local Government (State) Award to be more reflective of council's costs. The cost of attracting quality staff should also be factored in, these costs may be identified through sector-based advertising agencies.

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

Yes, all costs must be considered as part of the compilation of a rate cap. The LGCI cost components need to be broader to capture all costs impacting on council service delivery.

See question 18 below for further information.

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

Yes, all costs must be considered as part of the compilation of a rate cap. The LGCI cost components need to be broader to capture all costs impacting on council service delivery.

Examples of external costs include, but are not limited to;

- Tracking Federal and State imposed targets, and the cost to achieve them;
- Audit Risk and Improvement Committee (ARIC);
- NSW Audit Office fees;
- Increases in minimum superannuation guarantee rate;
- Councillors Superannuation;
- Compliance (pool inspections, food shop) and others;
- New compliance cost for UPSS regulations;
- Pensioner Rebates;
- Increase in Emergency services levy above CPI
- Stormwater Management Charge – charges set by regulations and unchanged since 2006-07,
- Cost-shifting has an impact on how income from land rates is allocated, we oppose all forms of cost shifting and the imposts on local communities;

Council prepares a significate amount of public facing information through the IP&R process, Financial Reporting (Statements) and data uploads to the OLG (Financial Data Return – FDR). It may be possible to access relevant information through one or more of these reports or by simply modifying current requirements without adding something new.

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

Local government has been subject to significant cost shifting from other levels of government. Recently we received information showing the mandating of the NSW Audit Office has seen an increase in audit fees of approximately 100% over 9 years.

Changes to legislation that affects all councils, often result in additional costs to the local community, examples include but are not limited to the mandating of the audit office, rather than competitive tendering, superannuation payments for elected councillors, increases in emergency services levies, and monitoring UPSS sites.

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

Where possible the LGCI should be future facing, as is the case with SRV applications.

Cost components in the LGCI that can be sourced from forward looking known variables, such as labour costs and RBA forecast CPI.

A portion of the LGCI must include some forward-facing indices or some judgement must be exercised on future inflationary pressures.

The LGCI cost components needs to be expanded and should align with the service levels expected by individual communities. At a minimum, four LGCI should be delivered, one for Metro, Regional, Rural and Remote Councils. A far more accurate LGCI could be derived for each LGA via collecting data through the Financial Data Return due by 31 October each year.