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IPART REVIEW OF LG RATE PEG METHODOLOGY
Submission from Murray River Council

This submission is based on the IPART Review of Rate Peg Methodology Issues Paper released by IPART in September 2022.

Murray River Council (**MRC**) does not believe a rate peg is necessary and strongly advocates for the abolition of the Rate Peg (**Peg**). Irrespective of what revisions that are done to the **Peg**, it would not be possible to come up with a methodology that will meet the individual needs and circumstances of each council while keeping the methodology simple and understandable by the average person. Having the IPART try and calculate a one-size fits all **Peg** is a waste of resources and energy when every Council has a "committee" (supported by an executive team) that is paid to look at their own specific circumstances and come up with the most appropriate **Peg** for that Council, i.e., the elected councillors.

Outlined below are several reasons why a single **Peg** across NSW will never be able to deliver on expectations.

- The circumstances of councils are varied, let's say a normal distribution. What a **Peg** can do, (irrespective of the methodology) is to come up with an average. Even if one assumes that the average caters to ± one σ (std. dev.), which is not necessarily the case, that still only caters to 66% of the population.
- It contradicts the principles of IP&R, which is based on establishing a "contract" with the community and then implementing the actions to give effect to the contract. That means those actions need to be funded, and the actions and funding requirements will always be different. If a single **Peg** is imposed, it becomes impossible to fund CSP activities. A fundamental assumption of the **Peg** is that it is a continuation of unchanged service delivery, impacted only by inflation. **If the State Government of NSw (State) continues with the Peg, then it should abolish the CSP requirements.**
- A limitation imposed by a separately elected body, the State, on another legitimately elected body is an affront to the democratic process. **Would the State favourably consider any limitations on its ability to raise revenue to be imposed by the Federal Government?** Councillors engage with the community through the CSP and are accountable for their decisions and actions (including decisions on rate rises) to the electorate every 4 years. IPART was set up to regulate for profit monopolies and protect the public from price gouging. Even if a LG raises more funding than required in a given year, that money is eventually reinvested back into the community (i.e., the very people who made the contribution in the first place). No shareholders will personally benefit from price gouging. QLD does not have a rate cap and there is no issue there of excessive rate increases.

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

A thorough review needs to be done on the components making up the LCGI, to ensure they are reflective of the costs. Once again, the issue of one size fits all comes into play; changes in input costs can vary significantly between different regions and different types of councils.

There is also a common misconception that LGCI = **Peg**. The **Peg** needs to consider much more than inflation (mere changes in the costs of continuing the current services at current service levels). The **Peg** also needs to take into consideration changes in other revenues (i.e., other than general rates), with the general rates needing to absorb any changes in those other revenues (e.g., FAGS not keeping up with inflation).

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

LGCI, by its very nature is a measure of historical cost changes (i.e., a price index). Measures that can be taken to improve it accuracy and relevance include:

- Reviewing the cost components and their weightings to ensure that they are reflective of the current cost base of councils. This should be a process that is undertaken on a periodic basis (say every 2-3 years).
- Calculating multiple LGCIs to cater to different categories of councils, where there is a significant difference is the cost components and their weightings.

Whether the LGCI (i.e., a historical price index) should be a component of the Peg (or whether a forward-looking forecast is more suited) is a different matter and discussion.

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

It is presumed here that the "changes in council costs" refers to the Peg and not to the LGCI.

The **Peg** needs to consider multilane factors that goes beyond just costs. IPART would need to explore what data sources would best suit to address these cost elements.

<u>Changes to other sources of revenue</u>

- The need to adjust general rates to accommodate changes in other revenue sources (e.g., FAGS not keeping up with inflation).

<u>Changes to cost of delivering current services</u>

- Increase in the LGCI, (historic or a forecast figure), noting that LGCI only addresses the costs of continuing to maintain current services at current service levels.
- Measure of changes to wages need to be specific to the LG industry.
- Mechanism to cater for costs that do not recur every year (e.g., LG elections). This should include gaps caused by DRFA and insurance payments not covering the full costs remediation and recovery after natural disasters.

<u>Additional services and obligations</u>

- Impacts of new initiatives stemming from the CSP.
- Impacts on cost due to addressing climate change requirements (e.g., improving surface drainage infrastructure to cater to more frequent and voluminous floods).
- Costs of changing legislation, standards, and compliance requirements (e.g., net zero requirements)
- Costs of delivering services/compliance activities that are moved from State to LG.
- Costs of delivering, operating and maintaining infrastructure required to cater to the changing technological landscape (e.g., smart cities initiatives, EV infrastructure, impact of AVs on town planning, and a bit into the future, the need to build infrastructure such as vertiports)

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?*

To calculate the general rates for next year (NY), the **Peg** should be applied the general rates raised from the properties existing at the start of the current year (CY) with any rates generated from new properties added to that total. That will automatically accommodate a factor for property growth, without having to resort to calculating population growth factors and other calculation methodologies. Noting that the reduction in the number of properties (even with declining population) is extremely rare, such an approach will not negatively impact regions with negative population growth.

Rates for NY = (Rates for CY from Properties at the start of the year x (1+**Peg**)) + Rates from additional (new) properties.

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

How any cost saving resulting from improvements in productivity is applied is best left to the individual councils. Most often when an investment is made to improve efficiency, such initiatives also include measures to improve effectiveness of services and efficiency gains are applied to generate those improvements in effectiveness (more service at the same cost).

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

Please see response to Question 3.

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

This is a loaded question and is totally dependent in the definition of “Unnecessary”. The more relevant question is “*Has the rate peg prevented councils from raising the rates required to maintain its service levels and deliver on its CSP commitments?*”. The response to that question is a resounding “YES”.

As indicated previously, “unnecessary” rate increases, (in the context of LGs, as opposed to say privately owned utilities) is mute as any surpluses in a given year can only be used to reinvest back into the community for the benefit of the ratepayers who contributed to the surplus in the first place.

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

NO. If you take a basic look at the difference between the **Peg** and simple CPI in the last 5 years, there is no need to even ask this question.

Under the IP&R framework, there is a requirement to have a workforce plan. This plan is designed to ensure succession is catered for. At present very few councils have the capacity to adhere to their workforce plans, creating a snowball effect, which is currently most visible in the town planning sector.

The **State** prescribes several performance indicators (ratios) that flag the financial sustainability of a council. The shortfall in rates revenue resulting from the inadequacy of the **Peg** has caused multiple councils to be below the target threshold for the Operating Performance Ratio, in addition to compromising forward looking requirements such as maintaining asset quality and succession planning. Another ratio is the Own Source Revenue Ratio, with a benchmark of 60%. The current **Peg** makes it impossible for most regional councils to meet that ratio. **What is the point of the State establishing performance indicators, and then have another arm of the State impose restrictions that make it impossible for councils to meet those benchmarks?** Is there any sanity in such an approach?

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

Once again, when there are councils whose mandated wage increases have been more than the increase in general rates (e.g., Hay, Carrathool), the answer to this can only be "Significantly". The shortfalls created by the **Peg**, has compromised the financial stability of multiple organsiations that deliver essential services to the community, and IPART needs to take fully responsibility for that situation. The primary method of impact is reduction is asset maintenance and renewals (due to depreciation not being fully funded). The impacts of such reductions are not immediately visible but will be felt in a few years to come when the backlog of asset maintenance and renewal requirements come home to roost.

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

The only way is to have multiple **Peg**s catering to the differing situations. Given the number of councils, that would mean a good dozen different **Peg**s. The ultimate would be to have an individualised **Peg** for each Council and the group best positioned to determine that **Peg** is the set of elected Councillors.

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

It's a customised approach taking into account the specific circumstances of that group, as opposed to a one size fits all approach.

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

The volatility in the **Peg** is not just having a different number for the **Peg** each year. The volatility of the **Peg** should be defined as the deviation of the **Peg** from the actual cost increases (and revenue changes) experienced by councils to deliver existing services at current levels as well as cater to changing external environment (CSP commitments, tech changes, legislation and cost shifting etc.)

Needless to say, when volatility is so defined, it is a major issue.

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

Better alignment with changes in costs.

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

NO. That is like asking the RBA whether they would commit to a single rate for a full year. The rate of change in the environment is increasing. Adaptability and agility is what is needed; setting longer term **Peg**s would only make the situation work, unless IPART has a tried and tested crystal ball.

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

Anything that reduces the lag and aligns the **Peg** with actual cost changes would be beneficial. The other aspect to be taken into account is that councils start their budgeting process at the latest in January, and has to complete by say March, to provide enough time for the budget to be open for public inspection, adjusted for any feedback stemming from public inspection and adopt the budget before the start of the financial year.

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

In the first instance, NSW public sector labour costs is **not reflective of the LG sector**, and a sector specific approach needs to be taken.

Productivity gains of labour cannot be looked at in isolation. There is no such thing as a free lunch. Labour productivity gains require investments in technology which in turn increase tech related operational and maintenance costs. As mentioned previously, such measures are also coupled with improving effectiveness (e.g., faster access to information by ratepayers).

The fact that IPART has failed to capture the increase in superannuation into the **Peg**, despite that being a legislatively mandated requirement that was well known in advance, indicates the extent to which IPART has been asleep at the wheel.

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

Reprioritising services (i.e., dropping one service to provide another) is not an option as it has never been acceptable to the community. **MRC** suggests that IPART conduct a survey of councillors across NSW to see how many councillors would be brave enough to go to the community with such a proposal. Go do a case study on the attempts by Campaspe Shire Council (Vic) to close a swimming pool and apply its savings to improve a more centralised pool facility.

User pays fees and charges can only be levied in certain circumstances. For a large proportion of Council services, it is not efficient and can cost more than it generates (e.g., charging users of a park each time they enter the park). Not only is it not efficient but is also undesirable as it will prevent those needing that service most to not use the service.

If SVs are to be a practical option, then IPART needs to significant change the approach used for such approval. Currently it is too costly and time consuming (may be that is a deliberate design element). If SV is to be a practical tool it needs to be on the following basis:

- Submission requirements for an SV needs to be simple and contained within a one or 2 templates
- SV submissions need to be deemed pre-approved (based on a council resolution)
- There should be a limited list specific circumstances (reasons) under which IPART can object to the SV.
- If IPART knocks back a SV, it needs to demonstrate that the reasons for knock-back aligns with the reasons pre-identified.

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

See response to Question 11. Response to Question 3 identifies the categories of costs that need to be addressed.

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

See response to Question 3.

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?*

You are trying to have the cake and eat it too. This is the overly simplistic approach that has caused the industry so much heartache in the first instance.

If you make the **Peg** calculation methodology simple and easy to understand, it will be relevant to a much smaller proportion of council (around the mean). If you want the **Peg** to be workable for a large number of Councils, there will need to be multiple categories of **Peg**s (at least) with most complicated calculations to cater for the differing cost elements.

The most efficient and effective way of "having the cake and eating it" is to have an individualised **Peg** for each council, and let the elected councillors determine what that **Peg** should be. IPART can have a supervisory role, with authority to intervene, under certain identified conditions (essentially where councillors are abusing that right). In such instances, the right of councillors to determine the **Peg** can be withdrawn for a certain period of time (IPART appoints a Rates Administer).

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