



**IPART review**  
**The development of a funding framework for Local Land Services**

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## **1. Introduction**

NSW Farmers welcomes the opportunity to provide input to the IPART draft report on the development of a funding framework for the Local Land Services (LLS). The establishment of the LLS is one of the biggest structural changes to support and service delivery in NSW agriculture for over 60 years. The merger of the three organizations, the Livestock Health and Pest Authorities, Catchment Management Authorities and Department of Primary Industries extension services also combines a number of different services, providing benefits to a range of consumers and raising revenues from different sources. It will be the balance of these services and how the revenues are raised that will be of major concern for the farmers in NSW.

NSW Farmers recognizes that IPART has been given a terms of reference to develop a funding framework. As such much of the content in the issues paper is reflective of theoretical funding frameworks, to an extent based on the assumption of autonomy of the local boards and flexibility and freedom to set funding arrangements according to a decision matrix. The reality however is that there will be limitations and externalities that will affect the ability of the local boards to fully employ the funding framework. Furthermore the government funding allocations have already been identified and a commitment has been provided that rates will remain unchanged. This raises the question of how influential this funding model will be and the extent to which local boards will have the ability to apply the framework.

Interestingly chapter 2 of the draft report contains a break down of the current revenues and expenses for the three organizations that will form the LLS. Information on the Livestock Health and Pest Authorities is clear on the revenues and expenses for the organization. Information on the Catchment Management Authorities is much more general without an aggregated expense or revenue line item. Revenues and expenses for the DPI extension component however are non-existent. NSW Farmers would expect in the interests of transparency this information would be made available to allow for comparison between the current and future arrangements.

As part of this submission, NSW Farmers has made comments pertaining to the content and in particular the recommendations of the draft report produced by IPART. The comments made by the NSW Farmers in its original submission to the review still remain current.

## **2. Draft Funding Framework**

The cost recovery framework as outlined in Table 4.1 of the draft report appears reasonable. However at this stage it is theoretical and the full comprehension of its effects will not be understood until the new boards conduct the recommended review of existing activities and implement the cost recovery framework. Only at that time, and following the application of the framework will we be able to fully comprehend the effectiveness and accuracy of the framework. Generally costs should be apportioned by a foundation arrangement or by recourse to established plans such as the biosecurity plan or the local LLS strategic plan.

It is expected there will be some limitations on the ability to implement the cost recovery framework completely. Given the historically defined regulatory functions that will be performed by LLS and the prescribed funding commitments from government in their budget forward estimates which are based on previous contributions, available funds and cost savings

exercises, it is expected that there will be limited flexibility in assigning cost recovery to some functions.

NSW Farmers is comforted that IPART draws the distinction between the regulatory and the non regulatory approaches for the draft funding framework. However we note that the design phase outlined in the funding framework are exactly the same for the regulatory and non regulatory approaches. Commentary provided on pages 30 and 31 explains that in the case of the regulatory approach the hierarchy of funder categories will be more focused towards risk creators where as the non regulatory approach would focus more on the beneficiary.

While noting IPART's position, we draw attention to the Productivity Commission's<sup>1</sup> comments on cost recovery and that "the case for recovering the costs of administering regulation is complex." Furthermore the Commission also states that,

*The complex issues surrounding cost recovery for both information and regulatory activities suggest that the onus should be on the government and its agencies to demonstrate that there would be net benefits to the community from introducing cost recovery for particular products or activities.*

As such it should be recognized that the regulated functions could just as easily be attributed to the beneficiaries. It would only appear fair that if the community imposes some productive limiting regulation such as native vegetation legislation that they should be required to bear some of the costs. It would be unfair for a landholder who bears the opportunity costs of the legislative instrument through foregone production to also bear the regulatory costs associated with implementing and enforcing it.

NSW Farmers does have a general concern surrounding all cost recovery frameworks applicable to government agencies and statutory organizations. The draft report states on page 21 that "the main objective of cost recovery . . . is to improve the allocation of resources in the economy, thus contribute to allocative efficiency". While improving the information and cost transparency of a monopolistic market, externalities or public goods, for truly efficient allocative efficiency there is a presumption that cost recovery frameworks are using competitive cost structures. Traditionally allocative efficiency is determined by the intersection of marginal costs and marginal benefits. Under a competitive market situation these costs are competed down. However under a regulated environment in the provision of a public good or accounting for an externality there is no such competition. How does the payee know that the cost recovery structure is based on the most competitive costing?

NSW Farmers recognizes that a cost recovery framework is possibly the most appropriate system under a regulated market however the onus is on the service provider to justify these costs and demonstrate they are reflective of competitive markets.

The examples of public goods provided on page 36 are useful in the explanation of the definitions. However it would be of even further value if examples of LLS functions could be used as part of the explanation. For example how would the IPART classify the management and provision of property identification codes (PICs)? PICs provide benefits to industry as a management of health and disease. As an individual number they could be considered rivalry as only one property can have one PIC, however as a system it could be considered non-rival as the use of the information (through the appropriate agencies) by one party does not exclude

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<sup>1</sup> Productivity Commission, *Cost recovery by Government Agencies*, Report no. 15, AusInfo, Canberra, August 2001 (p. 32)

use by another party. It may be argued that there is excludability in the sense that it is a database of information held by an authority and therefore access is restricted however as it is set up for the public benefit it is unclear whether there would be price excludability given there is no charge in accessing the information.

### 3. Funding and Costing

In considering the IPART proposal that LLS boards follow a hierarchy approach in regards to who should pay the costs of regulatory and non-regulatory activities, thought should be given to the interpretation between risk creator and beneficiary. Depending on personal persuasion either side could see the other as the risk creator. For example paddock trees in native vegetation. The legislation could be interpreted such that the risk creator is the farmer for possibly clearing trees and therefore they should pay for the native vegetation services. On the other hand the landholder might see the legislation as the risk creator. The same could be applied in assessing the beneficiary scenario. It is very generic to apply the assumption that because there is a legislated requirement, the landholder or property right holder, generate a cost on others and therefore as the impactor should have the costs internalised.

The comments in the draft report on the allocation of costs presuppose the ability of LLS boards to have a degree of persuasion over government funding on behalf of the community. It is expected that there will be a range of activities undertaken by the LLS that will infringe on the nexus between direct landholder benefits and indirect community benefits. As such there will be times where certain activities might need government funding to proceed however predetermined government contributions may restrict this. It would be favourable if the IPART are recommending the cost recovery framework with a hierarchy approach to assigning benefits and costs then all parties to the funding mechanism must have sufficient funding flexibility so as not to impose severely limiting revenue streams on the LLS activities and therefore their ability to meet their defined plans.

Government should fund the cost of governance that arises from regulatory requirements placed upon the LLS.

NSW Farmers has some concerns about IPART's comments on the costing the activities of the LLS. It is noted that on page 54 of the draft report the Productivity Commission's position is cited that "a regulatory agency should recover the full cost of administering regulation". It is not noted however that the Commission goes on to state in justifying the beneficiary and risk creator application that "firms can then pass on some or all of this charge to purchasers, down the production chain to final consumers."<sup>2</sup> This does not occur in a primary production industry where the price taking situation of farming does not allow the costs to be passed on to the consumer. In a sense this is creating a perverse effect in that the beneficiary does not appreciate the costs of their requirements. For example Australia has one of the highest wage rates in the international economy. Along with the other workplace relations costs associated with our standard of living this adds to the cost of producing agricultural produce yet consumers of food and fibre expect our food prices to be competitive with the rest of the world who do not

<sup>2</sup> Productivity Commission, *Cost recovery by Government Agencies*, Report no. 15, AusInfo, Canberra, August 2001 (p. 173)

have these same costs. Without consumers being aware of the impact their expectations and standards of living impose there will not be a true reflection of the cost of regulation.

Notwithstanding the comments in the draft report about the fact that the regulatory functions of the LLS contribute to its existence and that without internalizing the costs the risk creator will continue to consume, it should be noted that many of the regulated functions serve to benefit the community. As stated above, without the ability to pass these costs on to the beneficiary, the community will not suitably pay for these regulations. It should also be noted that the LLS had its origins in localism with the eradication of pests and disease which has since evolved into a much more regulatory orientated role.

While recognizing IPARTs terms of reference and the discussion on page 58 of the draft report, there remains a concern amongst NSW Farmers and our members that the recommendation that government be a funder where they are an identified beneficiary or impactor or as a funder of last resort potentially alleviates some of the duties of the government and their funding commitments to LLS. NSW Farmers is concerned that through the application of the risk creator approach and full costing there will be opportunities for the government to reduce current and past funding commitments it has provided to LLS and its predecessors.

The State Government should provide appropriate and sufficient financial assistance to LLS. This financial assistance would help to fund the increasing regulatory functions required by ongoing State legislation which are imposed on LLS and consequently on farmers and land managers.

#### **4. Use of rates and levies**

NSW Farmers agrees that LLS boards should retain the ability to charge a general rate and specific purpose rates. However in the discussion through chapter 7 of the draft report, in addition to the current general rate, animal health rate and specific purpose rates pest insect and meat industry rate, it is proposed that local boards also have the ability to charge flood mitigation levies, biosecurity rates and natural resource management rates. NSW Farmers cautions that while acknowledging the points on page 70 about the approach for establishing specific purpose rates, too many rates may become cumbersome, confusing and administratively difficult in a centralised rating collection system. Furthermore it could lead to transparency issues with complexity possibly compromising the matching of revenue collection and expenditure allocations. Consideration must be given to the regulated roles of the LLS and the functions performed under that role and therefore what actions would be captured under the collection of a general rate.

Recommendation 9 should not be allowed to be an open invitation for the LLS boards to develop a range of specific purpose rates to simply collect additional revenue. Rather as the cost recovery principles apply due consideration must be given to the services performed and the justified revenue collection.

In regards to recommendations 15 and 16 on the establishment of a biodiversity rate and a natural resource management rate, NSW Farmers flags that it may be difficult to disaggregate activities and costs between the general community and the individual therefore possibly making it more difficult to use the rates to target a specific section of the ratepayer base and should possibly be more focused on the wider community.



On page 64 of the draft report it notes that “ideally the variable amount should be linked to the risk created or benefit received by identified impactors or beneficiaries”. Given the statements in chapter 6 about full cost recovery, does IPART have any position on the allocation of the capital or fixed costs versus marginal costs and how they might apply to a rating structure that include fixed and variable amounts?

NSW Farmers would like the statement on page 66 stating that “NSW Farmers proposed that . . . intensive livestock operations should pay a higher variable amount” to be corrected. In our original submission we stated that “intensive industries should have a separate rate that accommodates that they have large numbers of livestock but relatively small parcels of land.” In making a separate rate it does not necessarily mean that it should be a higher rate. This rate, as per the IPART rating framework, should reflect the relative risk creation or benefits received from LLS services for intensive industries.

NSW Farmers suggests that there should be a review of the allocation of notional carrying capacity to intensive industries. We have suggested that intensive industries have a separate rate to acknowledge the different circumstances under which they operate compared to traditional extensive livestock operations. Trying to apply a notional carrying capacity based on dry sheep equivalent to an intensive operation involving pigs or chickens may be an unreasonable process.

NSW Farmers welcomes the recommendations that in the case of the meat industry levy and the pest insect levy, the LLS be able to recover an administration charge for the collection of these funds. However transparency must prevail to ensure that any administration costs are not simply passed back to the levy payer through higher levies.

NSW Farmers welcomes the recommendation that the minimum ratable land area should be reduced to 2 hectares. Smaller properties have just as much responsibility as larger properties in the management of pests and diseases and therefore should contribute to the LLS. It is noted however as recorded in the IPART report that these landholders need to be engaged in this process to understand their responsibilities. Further that this engagement needs to be in proportion to their funding contribution and risk creation.

An equitable rating system for LLS should have the following principles:

- a. That notional carrying capacity be used as the preferred primary function for determining rates
- b. That all holdings greater than 2 ha pay a base rate
- c. That all holdings less than 10 ha pay a base rate only as determined by each Authority
- d. That all public land managers pay rates
- e. That the rate structure be:
  - A base rate
  - Animal health rate
  - Pest animal rate
  - Intensive livestock industries rate

LLS should be able to recoup expenses from the NSW Food Authority for the collection of the Meat Industry Levy.

The Government fund the plague locust control program and that no charges are recovered through the LLS

The NSW Government should pay for NSW contribution to the Australian Plague Locust Management Commission, as happens in Victoria, South Australia and Queensland, as opposed to funding this through the Pest Insect Levy. If continued funding through LLS ratepayers occurs, this should:

- (a) Be applied as a special rate upon all LLS ratepayers across all regions of NSW
- (b) Should not accrue as a debt against the LLS
- (c) Provide income to the LLS to recoup expenses from Government spent in collecting the Pest Insect Levy.

## 5. Most efficient rating base

NSW Farmers believes that rates should be based on the notional carrying capacity of the land. Different land types will have different carrying capacities depending on their pasture, soil type, rainfall and other characteristics regardless of their size. For example a 50 hectare property on the coast with improved pastures could carry 1,250 sheep (dry sheep equivalent). A 50 hectare property on the northern plains area with natural pasture could carry 100 sheep. The different carrying capacities mean different shares of the risk or benefits, particularly those related to livestock. As a minimum, all rating referencing livestock or revenue raising operations for livestock related matters, the NCC should be used as an indicator of the landholders risk created or benefit received.

It is recognised that through the formation of 11 new LLS areas there will be a transition from the 14 LHPAs and 11 CMAs. While cognisant that rates will possibly be different within the boundary of a new LLS as a legacy of previous structures, NSW Farmers questions the process of standardising rates before implementing the cost recovery process. Will this result in two changes of rates for some landholders and possibly a longer process? Would it not be simpler to standardise all the rates under the IPART cost recovery proposed process?

Given the size of the LLS boards has IPART given consideration to different specific rates or different ad valorem rates within general rates across an LLS area? It may be the case that landholders have different issues in different areas and therefore LLS boards may see fit in application of the cost recovery framework that there could be reason for different rates within an LLS area, particularly in reference to the larger LLS areas in the west of the state.

NSW Farmers position is that there should be a separate intensive livestock industries rate. However at the current point in time the poultry meat industry have requirements under the *Poultry Meat Industry Act 1986* that set out food safety, biosecurity and environmental requirements of poultry meat growers.

The *Poultry Meat Industry Regulations 2008* state that:

- *The processor is to develop and implement effective quality assurance procedures relating to food safety, environmental management, animal welfare and biosecurity.*



- *The grower is to develop and implement effective quality assurance procedures relating to food safety, environmental management, animal welfare and biosecurity, having regard to any information provided to the grower by the processor in relation to those procedures.*

These activities are funded through the formation of the poultry growing agreements. The Poultry Meat Industry Act 1986 states that

*8(1) within one month after a processor and a grower enter into a poultry growing agreement, the processor:*

*(b) must pay a notification fee to the Director-General.*

*(3) The notification fee referred to in subsection (1) (b) is to be of an amount determined in accordance with a scheme established by the Director-General.*

The procedures that poultry meat growers currently perform under the act are in line with the procedures under the LLS act. As such, while the Poultry Meat Act is in place it is understandable that the poultry meat industry is exempt from LLS rates given the same procedures they perform under their own legislation.

NSW Farmers would also like to clarify the statement included in the draft report on page 87. The statement currently reads that:

*NSW Farmers held a similar view to the LHPA, arguing that exemptions would impact both the efficiency and transparency of the system*

While it is true that NSW Farmers believes that exemptions lead to complications and impact on efficiency and transparency. It is not the case that we hold the same view of the LHPA as reported in the draft report as opposing exemptions. There may be some justifiable reasons why exemptions should be provided such as the poultry meat example above or in the case of drought where exemptions may be provided on the basis of reduced services or hardships.

NSW Farmers recognise the need to encourage people to complete the stock returns however there will be scepticism that increasing the penalty is a revenue raising opportunity. LLS boards should be encouraged to demonstrate the benefits to landholders of completing the return and therefore provide incentives rather than penalties to encourage people to complete the returns.

## **6. Implementation and auditing**

NSW Farmers is generally supportive of the proposed implementation timeframes. Although we do propose that landholders be widely consulted and heavily involved in this process to ensure consideration of local issues and support local understanding on rating decisions.

In line with recommendation 26, NSW Farmers supports the conducting of a comprehensive third party specialist review to address rating issues from a technical and economically sound position. Through this process it is hoped that the operation of the LLS is transparent and accountable.

In addition to the audit process identified by IPART NSW Farmers believes that there should be an independent oversight committee which is mandated to ensure that any cost shifting

between NSW Government and LLS be reported to ratepayers annually with public disclosure of steps taken for rectification.

As the information contained in chapter 2 of the draft report illustrates the level of reporting for the 3 agencies that will make up the LLS has made the compilation of information and accountability difficult. The lack of financial information on the costs of services provided and income received prevents landholders and ratepayers from gaining a full understanding of the services provided and therefore having confidence in the bodies and their administration. It is imperative that this reporting be clear, accurate and regular to afford ratepayers full disclosure. Furthermore during this time of transition efforts must be made to provide an annual comparison of previous funding and service provision to provide clarity of ongoing services and charges.

Local Land Services must be made accountable to ratepayers

Authorities be required to make readily available to ratepayers annual reports and budgets for levies raised from LLS ratepayers including the Pest Insect Levy

An independent ombudsman type body be established to audit the effectiveness of the newly formed LLS