THE HILLS
Sydney's Garden Shire

THE HILLS SHIRE COUNCIL
3 Columbia Court, Norwest NSW 2153
PO Box 7064, Norwest 2153
ABN 25 034 494 656 | DX 9966 Norwest

4 July 2023

Independent Pricing and Regulatory Tribunal
PO Box K35
HAYMARKET POST SHOP NSW 1240

Dear Sir / Madam,

SUBMISSION - REVIEW OF THE RATE PEG METHODOLOGY

Thank you for the opportunity to provide comments on IPART's Draft Report concerning the Review of the Rate Peg Methodology.

Please find attached submission from The Hills Shire Council. Due to a short time frame between the release of the Draft Report and submission due date, this submission has been prepared at the officer level and has not been endorsed by the elected Council.

Please note that this submission will be reported at a Councillors Workshop held on 4 July 2023. Should there be any requested changes at the Workshop to this submission, a revised submission will be submitted to IPART no later than 6 July 2023.

If you have any questions in relation to this matter, please contact Ava Cheung on [redacted], Manager – Financial Strategy.

Yours faithfully

[redacted]

Chandi Saba

CHIEF FINANCIAL OFFICER
The Hills Shire Council

IPART DRAFT REPORT – REVIEW OF THE RATE PEG METHODOLOGY

SUBMISSION FROM THE HILLS SHIRE COUNCIL

1. What are your views on using one of the following options to measure changes in employee costs in our Base Cost Change model? How can we manage the risks associated with each option when setting the rate peg?

   a. Use annual wage increases prescribed by the Local Government (State) Award for the year the rate peg applies, adjusted to reflect any change in the superannuation guarantee rate.
   b. Use the Reserve Bank of Australia's forecast change in the Wage Price Index from the most recent Statement on Monetary Policy (averaging the changes over the year to June and December for the year the rate peg applies), adjusted to reflect any change in the superannuation guarantee rate.

- We support the use of the Local Government (State) Award as the inflator for employee costs, and the use of RBA's forecast WPI when the Award increase is not available. This gives assurance to councils that the rate peg will at least allow for the minimum increase in employee cost faced by councils under the Award. Where the Award data is not available in the first year, we believe that a true-up should be given should the RBA WPI be lower than the first year of the Award increase. This will ensure that councils can cover the minimum increase.
- We agree with the Draft Report that there are sufficient mitigating factors (such as the IP&R process, the power of ratepayers to elect council out of power, and the role of the NSW Industrial Relations Commission) to address ratepayers' concern around council having less incentive to negotiate lower wage increases, should Award be used as the inflator.
- With regards to the risk of councils having to pay above the Award to compete with the private and State Government sector in retaining and attracting talents, this risk is more difficult to mitigate as it is driven by the competition in the labour market. One recommendation would be for IPART to monitor the variances between the actual WPI and the Award increase year-on-year and allow for an adjustment if deemed necessary to address market wide labour shortages or wage rise. This will mitigate the risk of councils not being able to compete with the market for labour.

<u>Additional Feedback on Risk of the BCC Model:</u>

- Whilst we are supportive of the proposed BCC formula of using forecast indicators, it is recommended that IPART tracks the difference between actual price movements and the inflation forecasts applied in calculating the relevant year's BCC. Where significant variances are observed, e.g., from unforeseen magnitude of price movements (like those observed in FY22/23 and FY23/24), it is recommended that IPART allow for a true-up to account for such significant variances. Whilst lagged, true-up can help in mitigating significant forecast risk overall.

- When tracking actual vs forecast CPI and PPI movements, it is recommended that the most relevant indicators for each council group be considered, e.g., CPI Sydney and PPI NSW for Metropolitan, and CPI Australia and PPI Australia for Regionals etc.
- In terms of review timing, given that there are major changes from the current to the revised approach, it is recommended that consultation be conducted again within 3 years of implementation to assess how effective the revised methodology is, and then review every 5 years thereafter.

2. Are there any alternative sources of data on employee costs we should further explore?

- We are not aware of any other publicly available sources apart from those noted by IPART.

3. Do you support releasing indicative rate pegs for councils in September, and final rate pegs that are updated for councils' Emergency Services Levy contributions in May?

- No, we do not support releasing indicative rate pegs for councils in September and final pegs that are updated for ESL contributions in May for the following reasons:

    1. As noted in the Draft Report, rate affordability is the ratepayers' prime concern. Exhibiting the IP&R documents without a final rate peg would be misleading and creating a new problem. Releasing the final rate peg in May is too late as many councils would have exhibited their IP&R documents by then.

    2. ESL expenditure represents around 2% to 2.5% of The Hills Shire Council's total expenditure. It is not material enough to be the reason for delaying the release of the final rate peg till May. Whilst we agree to capture the actual increase in ESL by a separate ESL factor, we believe that the ESL factor should be a 'true-up' for prior year's actual increase instead of being the adjustment for the ESL contribution for the current rate peg year. See below for a proposed true-up formula.

    3. Councils have experienced the biggest increases in ESL contributions in 2023-24 and it is doubtful that there will be another increase of this nature in the near term. It is important that the ESL factor in 2024-25 reflects a 'true-up' of the gap between the 2023-24 rate peg and the actual increase experienced in 2023-24. IPART's current recommendation of applying same-year approach from 2024-25 will not address the shortfall in the 2023-24 rate peg, which will have a compounding impact on future Rates income for many councils.

- We recommend the below formula for the true-up (i.e., the difference between the actual ESL % increase in the previous year less BCC or LGCI for the previous year, expressed a % of the Notional General Income):

$$\text{ESL true-up factor} = \frac{\left[\left(\left(ESL_{(t-1)} / ESL_{(t-2)}\right) - 1\right) - R_{x(t-1)}\right] * ESL_{(t-2)}}{NGI_{(t-1)}}$$

Where:
ESL = Actual ESL contribution
R_x = Cost Component of the Rate Peg (i.e., BCC or LGCI) excluding ESL contribution
NGI = Notional General Income
t = the rate peg year

- Note that in the above formula, if $ESL_{(t-1)}$ and $ESL_{(t-2)}$ are substituted with $ESL_{(t)}$ and $ESL_{(t-1)}$ respectively, the resulting ESL factor will be the same as one calculated by IPART's proposed formula. A worked example in Excel is included in Attachment 1.

4. Do you have further information on arrangements between councils to share Emergency Services Levy (ESL) contribution bills including:
   a. what these arrangements cover (including whether they cover matters other than ESL contributions), and
   b. whether they apply to Rural Fire Service, Fire and Rescue NSW and NSW State Emergency Service ESL contributions, or contributions for only some of those services?

   - No comment as we do not have sharing arrangements with other councils.

5. Would councils be able to provide us with timely information on the actual ESL contribution amounts they pay including contribution amounts paid to the:
   a. Rural Fire Service
   b. Fire and Rescue NSW
   c. NSW State Emergency Service? For example, by providing us with a copy of any cost sharing agreement that sets out the proportion that each council pays.

   - No comment as we do not have sharing arrangements with other councils.

6. Would you support IPART establishing a process to develop adjustment factors for groups of councils to increase the rate peg to cover specific external costs?

   - We would support IPART establishing a process to develop adjustment factor, however it should be a process whereby councils can individually apply to increase the rate peg to cover specific external costs, rather than having to apply as a group.
   - However, it is recommended that the process be simple and straight forward, unlike the special variation process.

7. Would you support measuring only residential supplementary valuations for the population factor?

   - No, we would not support measuring only residential supplementary valuations for population factor. We do not see the need for splitting out residential supplementary valuations as we believe that population growth is one of the key drivers for supplementary valuations in other categories in our shire, e.g., the growth in population attracts more businesses to come.

8. If you supported using residential supplementary valuations, what data sources would you suggest using?

   - We do not support using residential supplementary valuations.

9. What implementation option would you prefer for the changes to the rate peg methodology?

   - The Draft Report suggested that the implementation cannot be postponed beyond 2025-26, even if economic continues to be volatile. Hence our preference would be the last option listed in the Draft Report, which is to implement all changes in the 2024-25 rate peg and include a true-up:
     — replace the LGCI with the 3-component BCC model and use 3 council groups
     — amend the population factor to remove prison populations
     — develop a separate ESL factor
     — include a one-off true-up adjustment for the differences between the LGCI and the BCC (excluding the ESL) so that councils would be no worse off under the new methodology compared to what they would have received under the existing methodology for 2024-25.
   - As noted above, we recommend the ESL factor to be calculated as a ‘true-up’ for the previous year rather than for the current year.

Attachment 1 - Proposed Alternative ESL True-Up factor

THSC Proposed Formula:

$$\text{ESL true-up factor} = \frac{\left[\left(\left(ESL_{(t-1)} / ESL_{(t-2)}\right) - 1\right) - R_{x(t-1)}\right] * ESL_{(t-2)}}{NGI_{(t-1)}}$$

The below example is based upon the data as per Table 4.2 (p.62) in the Draft Report, plus additional 2022/23 data inserted for the illustration of THSC's proposed prior Year true-up calculation.

	2022/23	2023/24	2024/25	
BCC or LGCI ex ESL factor (a)		2.0%	3.0%	
NGI	9,000,000	10,000,000		
Actual ESL Contribution	850,000	1,000,000	1,100,000	
Actual ESL increase % (b)		17.6%	10.0%	
Actual ESL Increase vs BCC or LGCI given, i.e. (b) - (a)		15.6%	7.0%	
ESL True Up $ Required		133,000	70,000	
THSC Propsed ESL True Up Factor (Prior Year True up Method)			**1.3%**	1.3% <-- See formula

The proposed formula can be used to arrive at IPART's ESL Factor if ESL(t-1) and ESL(t-2) are substituted with ESL(t) and ESL(t-1) respectively, i.e., Same Year adjustment method:

$$\text{ESL true-up factor} = \frac{\left[\left(\left(ESL_{(t)} / ESL_{(t-1)}\right) - 1\right) - R_{x(t-1)}\right] * ESL_{(t-1)}}{NGI_{(t-1)}}$$

	2022/23	2023/24	2024/25	
BCC or LGCI ex ESL factor (a)		2.0%	3.0%	
NGI	9,000,000	10,000,000		
Actual ESL Contribution	850,000	1,000,000	1,100,000	
Actual ESL increase % (b)		17.6%	10.0%	
Actual ESL Increase vs BCC or LGCI given, i.e. (b) - (a)		15.6%	7.0%	
ESL True Up $ Required		133,000	70,000	
IPART Proposed ESL True Up Factor (Same Year Adjustment Method)			**0.7%**	0.7% <-- See formula
			Agrees to IPART's Cal	