Summary of discussion at Rate Peg Methodology workshops for the local government sector

6 June 2023

1 Overview

We held 3 workshops with stakeholders from the local government sector:

- Online 30 March– 67 attendees.
- Queanbeyan 31 March – 21 attendees.
- Sydney 17 April – 22 attendees.

This paper presents a summary of the key issues discussed at the local government sector workshops including:

- Feedback on options we are considering for the rate peg methodology.
- Feedback on the broader regulatory framework.

2 Feedback on options we are considering

Key Theme	Summary of workshop views
Labour costs	• Some stakeholders favoured using the wage increases set by the Local Government (State) Award (the Award) over alternative measures such as wage price index (WPI) forecasts or the Fair Work Commission's Minimum Wage Increase because the Award includes known cost increases that most councils incur each year. • There was some concern that forecasts may not be as accurate as other measurements of labour costs. But others considered it a favourable measure of labour costs. Some indicated that they would support the use of a forecast if a true-up mechanism is included to adjust for changes in actuals. • Stakeholders did not support using the current measure of public sector WPI as it is impacted by the NSW government's wage cap. • Some councils favoured the Fair Work Commission's Minimum Wage Increase as an independent measure. • Some stakeholders raised that increases in the superannuation guarantee should be reflected in the measurement of labour costs. • Some stakeholders thought that a WPI forecast covering the public and private sectors would better allow councils to meet the rising costs of attracting and retaining staff when the labour market is tight. • Some stakeholders commented that using the Award would not reflect the need to pay above award wages to attract or retain staff. Some stakeholders commented that the gap between award and market wages is unlikely to close soon. • Many councils commented that they struggle to compete with the private sector and the NSW government for labour, particularly in regional and rural areas and for highly specialised roles. • Some councils stated that the increases in the rate peg may only cover their increases in labour costs for the same year and that all other cost increases need to be paid for out of their existing budgets.

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	• A stakeholder commented that using Award wage increases to set the rate peg may adversely impact negotiations with unions on the Award because the rate peg is an important consideration in award negotiations. • Stakeholders supported including increases in the superannuation guarantee in the rate peg
Depreciation	• There was some support among stakeholders for using a depreciation measure in the rate peg methodology. Some stakeholders were concerned about whether it would accurately reflect the differences between councils. There were also concerns about meeting the cost of regulatory changes and resilience and adaptation requirements. • There were also comments that depreciation expenses may not align with asset management requirements. • Some stakeholders were concerned that depreciation is a backwards looking measure and will not be forward looking. This would be exacerbated by a 3-year rolling average approach. They suggested considering forward-looking measures such as projections included in councils' Long Term Financial Plans. • Some stakeholders argued that depreciation represents a minimum requirement to replace current assets, not the optimal amount of expenditure to ensure assets are in line with future planning requirements and to address the infrastructure backlog. • Some stakeholders questioned the appropriateness of using councils' depreciation expenses because the quality of councils' asset management processes and documentation varies across the State. They proposed considering an alternative measure of asset costs such as the producer price index for the Construction industry published by the Australian Bureau of Statistics. Others considered that using depreciation would encourage councils to improve the maturity of their asset management processes. • Some stakeholders had concerns about using depreciation because it is an accounting measure and that the method for measuring depreciation could change over time. • Some stakeholders thought that using a per capita measure of depreciation would not capture the growth in expenditure required to provide services to other ratepayers such as businesses. • Some stakeholders commented about the differences between councils when it comes to depreciation expenses, particularly councils that are growing in population. These councils were concerned that a grouping for depreciation might not accurately reflect the differences between the councils within the group. • Some stakeholders were concerned about using a 3–year rolling average for depreciation expense due to the time it could take them to recover the costs of a large asset revaluation. • Some councils were concerned that councils with a particularly large asset base may be able to influence a depreciation expense component. • Some stakeholders were concerned that depreciation would include the indexation of cost but also partly incorporate growth. They felt that this made it unclear what the purpose of this component of the rate peg was. • Some stakeholders commented that Rural Fire Service and State Emergency Services assets are included in council's depreciation as assets. This can vary widely between councils based on whether their local government area (LGA) contains a facility or not. These stakeholders said that the current methodology provides the costs for an average council, but those with significant emergency services assets are not being compensated. • Some stakeholders also raised concerns with depreciation of emergency services assets because councils are unable to conduct full audits of the equipment. While the depreciation of the equipment is recorded in council financial statements it is controlled by the relevant emergency service.
Other operating costs	• A stakeholder expressed the view that the CPI is only relevant to capacity to pay arguments for households, and that the PPI is the relevant index for the cost of providing services for local government. • A stakeholder proposed using different CPI measures for different councils across the State – for example, cost changes for councils located close to the Queensland border could be more consistent with the CPI for Brisbane, and councils located around Canberra could refer to the CPI for Canberra.
Council diversity	• Councils were generally in favour of reflecting council diversity in the rate peg. • Some stakeholders were concerned about the differences within any groupings that IPART might establish, particularly regarding financial sustainability. • There was a discussion among stakeholders about the number of council groupings that could be used and the definition of the groupings. • Some stakeholders did not consider road length per capita to be an effective metric to group councils on. • There was support among stakeholders for a remote grouping along with the OLG council types. Others felt that the OLG council types were not accurate representations of councils. • Some councils noted that the difference in geography and topography create large differences in the cost to maintain, repair and replace assets such as roads. • Some councils were concerned about the basis on which the groupings were classified and whether differences between councils in the same grouping would not be reflected.

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	• Some stakeholders noted that councils across the State have a different mix of services that they provide to the community, and that groupings would not reflect this difference. They said that a rate peg for each individual council is the only way to truly reflect diversity in the sector. Others recognised that the rate peg is not suited to accounting for the unique circumstances of each individual council and that other funding mechanisms may be more appropriate for addressing these differences. • Some stakeholders were concerned about the additional community facilities that councils with high population growth need to provide. They argued that these facilities are not being provided by developers and that council has to build these facilities. Councils may fall under the same category (metropolitan, regional or rural), however population changes would lead to differences in their asset costs as some are growing while others are not and mostly focused on maintaining existing assets.
Population factor	• Councils argued that supplementary valuations should be removed from the population factor • Some stakeholders were concerned that deducting supplementary valuations was permanently reducing their rate base by not allowing the full population growth. • Some stakeholders felt that the population factor favoured the councils that are more financially sustainable to begin with and the councils that get more grants from State and Commonwealth governments. They felt that the population factor was widening the gap between some councils. • Some stakeholders disagreed with this and felt that the population factor was evidence that the supplementary valuations councils receive for property revaluations do not cover the cost of population growth and that more revenue is required to fund services for growing populations. • Stakeholders did not think that prisons were a significant cost to councils, apart from potentially increased wear and tear on council-maintained roads. • Some councils argued that declining populations can also increase their expenditure. These councils argued that the population factor should compensate for population decline as well as population growth. • Some councils were concerned that their population can increase due to residents on rating exempt land, such as social housing and community nursing facilities. They argued that reducing or removing the rating exemptions would help spread the impact of increasing rates due to population growth across more ratepayers. • Some councils felt that the population factor was less effective because unimproved value was being used instead of capital improved value (CIV) for rateable properties. They argued that CIV would spread the rating increases caused by population growth more equitably among ratepayers. • Some stakeholders argued that the population factor is not maintaining the average rate per property • Some stakeholders argued that rateable properties are a better measure of population growth than residents. They commented that the presence of intercensal errors reduces the accuracy of population estimates produced by the Australian Bureau of Statistics.
Productivity	• Some stakeholders questioned how IPART defines and measures productivity in the local government sector. They argued that councils shouldn't be compared to the private sector for productivity as they are not driven by profits. Productivity improvements in the local government sector more often lead to improved quality of services and longer-term value for money rather than short term cost savings. • Most councils seemed to favour removing the productivity factor. • Some councils suggested that if the productivity factor was to be retained councils should be provided additional income to recognise the additional imposts that local government carries such as the Emergency Services Levy (ESL). • Stakeholders noted that the introduction of audit risk and improvement committees and accompanying guidelines should lead to continuous reviews of council performance and councils having better and more efficient levels of service delivery. • Some councils also noted that their Integrated Planning and Reporting (IP&R) process includes requirements to introduce a program of service reviews which should promote productivity increases. • Councils discussed opportunities to use common service providers to address common issues such as cyber security and help avoid duplication of efforts. Some councils stated that they had approached the NSW Government to discuss programs to facilitate such an approach. They felt that if the NSW Government took a lead in negotiating with key service providers there could be opportunities to create efficiency. • Some councils were concerned that changing systems to meet a common standard would require significant investment and likely require a special variation because the funding would not be available in their existing budgets. Some councils said that they would prefer that any common service provider arrangements were on an opt-in basis.
Costs due to external changes	• Some councils were concerned about the financial impacts of the ESL and other costs associated with emergency services such as the Rural Fire Service.

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	• Some councils argued that in rural and remote areas they are the provider of last resort for their local communities. They provide services that other levels of government or the private sector are unable or unwilling to provide. • Some councils commented that there are differences in not only expenditure but the revenue that councils receive from additional services. New swimming pools in metropolitan areas may turn a profit for the council, but in regional areas they are run at a loss. • Some councils commented that increasing community expectations are a significant driver of costs that aren't being captured in the rate peg. When an asset is renewed or replaced today the community expects it to be to a higher standard, have more service capacity or provide higher quality service, etc. • Some councils were concerned about the additional costs of cyber security. • Some stakeholders were concerned about the policy of the State government regarding climate change could lead to further responsibilities for councils • Some councils raised concerns that the costs of Rural Fire Service and State Emergency Service assets are not included in the current methodology as part of the Emergency Services Levy recovery. • One council provided an example that the ESL is 3% of total ordinary rates and that if that funding wasn't being provided to the State government it could be invested in services and assets. • Some stakeholders were interested in an alternative process similar to the special variations process for considering external costs. Externals costs could be picked up and factored in the IP&R process. Through an alternative process there would be a need to think about external cost pressures and be rigorous. This would also foster transparency which may shed light on an accumulation of costs. Councillors might also find it easier to lodge an application because it is transparent. • Other stakeholders considered the need to get a regional view of external costs including examining cost shifting. • Some stakeholders consider that the ESL and companion animals should be out of the rate peg and charged as separate items. • A stakeholder recognised the need for defining the external costs and factors.
Ratepayer affordability	• Some councils raised concerns about how rating exemptions are currently applied and expressed that changes to the types of land exempt from rates would allow the rates burden to be spread across a greater number of ratepayers. • Stakeholders suggested that rates paid in other jurisdictions should also be considered when examining ratepayer affordability.
Our ratepayer survey	• Some stakeholders were concerned about the robustness of the survey and the representation of the sample of respondents. Some also questioned the engagement with farmland ratepayers.

3 Feedback on the broader regulatory framework

Key Theme	Summary of workshop views
Purpose of the rate peg	• Many stakeholders sought clarification on the purpose of the rate peg, as this determines what services should be included in the rate peg and what should be paid for by other sources of revenue. • Stakeholders commented that some councils may have been historically underfunded and that because of this, increases in the rate peg each year are not enough to bring the council up to the necessary revenue to fund the true cost of delivering services. • Some stakeholder raised the possibility of IPART setting a range for the rate peg, where councils would have the autonomy to pick their individual rate peg within the range. Stakeholders noted that councils would need to justify higher increases to their community. • Some stakeholders questioned whether the rate peg should be viewed from the point of being a tax on land or as a charge for the services provided by councils. They said either of these perspectives have to be factored into the principles of setting a rate peg.
Rating exemptions	• Some stakeholders felt that the impact of rating exempt land on council budgets should be considered. Such as national parks and forests, aged care facilities, community housing, etc • One stakeholder provided a specific example that if an aged care facility has only one social housing resident, the entire facility is exempt from rates. • One council provided a specific example that of the land within their LGA only 20% is rateable, the rest is national parks and state forests. Council provides 100% of the services to these areas, and that means the burden is spread over other ratepayers.

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	• One council stated that in their LGA they have a significant amount of housing provided by the Department of Housing. If all of these were to be transferred to rating exempt community housing this would mean other ratepayers would need to pay an extra 8% to keep the total rate revenue the same. • One council stated that pensioner rebates are currently 1.5% of the rate peg and this is continuing to grow which has a significant impact on revenue.
Statutory and other charges	• Several stakeholders raised the issue of statutory charges that have not been adequately indexed over time. This means that council has not been able to increase some fees and charges in line with the costs of providing the services. • Some stakeholders also noted that fees and charges are more efficient revenue source for larger councils that can recover the cost of providing services through fees to a much greater extent than smaller councils can. • Some stakeholders argued that ratepayers are effectively subsidising the cost of user fees and charges due to the indexation not keeping up with the cost of services.
Capital Improved Value (CIV) property valuations	• Some stakeholders felt that using CIV would be a more appropriate calculation of property values, and that it would more accurately capture growth within a council's area. They also argued that CIV is simpler and more easily understood. • Some stakeholders felt that CIV better aligns with the principles of taxation and that it would more equitably distribute the increasing cost of council services.
Council integrated planning and reporting process	• Some stakeholders commented that councils are required to undertake significant planning and reporting processes that involve considerable engagement with their communities. Rate pegging could be removed because these plans are already developed by the councils with public consultation and these democratic processes should determine rate decisions rather than the rate peg. • Some stakeholders questioned if the IP&R framework could be more closely connected to the rate peg methodology and if the planning and consultation already undertaken in that process could help inform the rate peg. • Some stakeholders felt that using the IP&R framework would help reflect the diversity among councils and allow the rate peg to be more individualised to each council. • Some stakeholders argued that if councils run a balanced budget and costs rise, they either have to withdraw services or increase rates. They considered that if their IP&R process was robust, they should be able to increase rates in line with the service delivery that was established with the community through the IP&R process. • Some councils commented on our initial survey results that ratepayers felt they were not being consulted enough. They stated that the IP&R process includes significant consultation and would hope that ratepayers have opportunities to engage with councils through that process.
Special Variations (SVs)	• Some stakeholders commented that SVs are being underutilised and that this may be partly due to the negative perceptions around SVs that prevent councils applying for them when they are in fact needed. • Some stakeholders stated that it is disappointing that SVs are viewed as a failure in financial management by ratepayers. • Some stakeholders raised a concern that these negative perceptions of SVs can make the process politicised which can lead to delays in seeking SVs that ultimately lead to higher increases in rates.
Financial sustainability	• Some stakeholders commented that some councils have a historically low-rate base that has not been increased through SVs and that these councils will continue to struggle financially because the rate peg is indexing up from this lower amount. • Some stakeholders commented that the rate peg doesn't account for changes in council's revenue. Such as councils will receive additional interest income through the high inflationary period that they may use to subsidise their budgets, but that after inflation returns to long term average there may be significant impacts on general revenue. • Similarly, as above, some stakeholders also commented that the rate peg doesn't factor in the provision of grants which can be withdrawn or can decline in real dollars as it doesn't keep pace with inflation. • One stakeholder raised a specific example about financial restrictions on councils. They started that the millions of dollars raised for the rural fire service and other emergency services is restricted to that purpose only and can't be used to fund other costs associated with natural disasters such as repairs and maintenance or increasing resilience.