CITY OF
HOLDFAST BAY

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25 May 2022

Mr Sean McComish
Economic Regulatory Advisor
Essential Services Commission
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ADELAIDE SA 5001

Via email: rates@escosa.sa.gov.au

Dear Mr McComish

Local Government Rates Oversight Scheme – Draft Framework and Approach

The City of Holdfast Bay (Council) thanks ESCOSA for providing the opportunity to comment on the proposed draft of the Scheme.

Council is concerned that the proposed Scheme represents administrative burden and cost, rather than appreciable value to our community. Nevertheless as a scheme is legislated, Council seeks to ensure as much benefit for our community as possible from the final design.

It is noted that the provisions which have now commenced under which the proposed Scheme will be established was a negotiated compromise in response to the State's proposal to cap rates as part of local government reforms. While rate capping proposals were strongly opposed, during consultations Council acknowledged its commitment to effectiveness, accountability and transparency:

"Council is amenable to the principle of an 'independent umpire' to review decisions considered problematic. However, Council strongly believes that the definition of 'problematic' must be the choice of the relevant community."

Council maintains the position that local communities are the most appropriate arbiters of what services they receive.

Many services and infrastructure provided by councils is discretionary. While capacity to pay is a mathematical calculation, willingness to pay is not.

As ESCOSA's draft framework notes, "the intention behind the scheme is to give ratepayers greater confidence that the rates they pay are those necessary for their councils to provide *the services they value*" (emphasis added).

Historical mathematical trend assessments will not adequately account for community expectations, nor how they change over time or in response to macro-economic and other environmental conditions.

Also, questions as to the future planning of new capital works and initiatives are absent. Councils traditionally only borrow for new capital – this in turn impacts the NFL ratio and in turn depreciation. All the asset related expenditure questions appear to be focussed solely on asset renewal, not asset upgrade. In practice most asset renewal are upgrades reflecting the community requirement to improve its amenity.

The draft framework suggests that long term plans "would not be expected to exhibit significant variation through time (replacement/renewal expenditure should not materially vary due to policy cycles, or short-term transient operational or financial concerns)". This assumption is incorrect in practice, as community expectations can change substantially and often quickly. Notably, the legislation limits "relevant matters" for ESCOSA's consideration as being:

- material amendments made or proposed to councils' plans and the reasons for them;
- revenue sources outlined in the Long Term Financial Plan; and
- other matters prescribed by Regulation (of which there are currently none).

Given the primary relevant matters relate to amendments of plans, it can be assumed that variations to plans *should* be expected and that neither "program stability" nor static plans are an inherently good indicator of financial sustainability. For example, new capital is one type of expenditure that does vary due to political cycles and can exhibit significant variations through time, as well as ongoing impacts. Often this type of expenditure is tied to capital grants from other tiers of government.

Additionally, one of the big drivers affecting the indicators is asset valuation and the impact of revaluations. Councils have policies and methodologies for asset valuation cycles in accordance with the accounting standards. Increased replacement costs directly affect depreciation, and any long-term modelling needs to take this is into account. Depreciation is an accounting function and a broad based indicator – it is affected largely by re-valuations and expenditure on new capital including changes in service standards associated with those new assets.

Furthermore, economic system shocks are not uncommon, along with service and cost-shifting from other tiers of government. In the period proposed for evaluation by ESCOSA, there has been a global financial crisis as well as a global pandemic, both of which resulted in swift and substantial industrial dislocations and restructures. Also in that period, there have been government decisions that have increased the cost of councils doing business, such as the waste levy and the cost of local government reforms, including this proposed Scheme. If these conditions are not accounted for, trend data can be skewed.

Another issue for the analysis of historical information is the impact of the timing of Government grants – in particular FAG grants and LRCI grants which substantially distort the operating ratio from one year to the next. The recent decision by the Commonwealth Government to pay 75% of the 2022/23 FAG grant in April 2022 is a good example.

Council also owns and operates a large self-funded Aged Care Complex – Alwyndor. The historical results and long term financial plan for this complex can impact Council's consolidated results and forecasts, even though Alwyndor is self-funded. To be meaningful for ratepayers, Council would prefer to use both Municipal only activities as well as providing consolidated results.

Council agrees there could be some value in having an independent body give assurance of long term financial sustainability, but believe this can be done more effectively by reviewing financial policies and principles and evaluating their reasonableness, rather than relying on historical trend data.

Forward-looking plans are based on assumptions and policy position parameters a Council (and Audit Committee) has considered and endorsed. For example the City of Holdfast Bay has a number of financial management targets and ratios published in its Annual Business Plan. These inform the LTFP. It is suggested that ESCOSA's advice be based on an assessment of the reasonableness of these targets. Managing cost control, affordability and sustainability risk can be subjective in uncertain economic conditions such has been experienced in the past two years – hence any advice needs to be understood and explained in the context of assumptions and Council policies. Historical trends are a part of the evidence, however future trends are based on assumptions, financial targets and principles that need to be considered for reasonableness. Council's policies, financial management principles and targets are the most crucial for forecasting. A community may accept a higher debt level if it knows that major improvements will be made to its infrastructure resulting in a better community standard.

To this end, Council has a preference for qualitative assessments that take into account local conditions, rather than a standardised quantitative approach as currently proposed in the draft framework.

Given that the role of the Scheme is not to compare councils against each other, we do not believe a standardised quantitative approach is needed.

There is no such thing as a 'standard' council. A rural council maintaining hundreds of kilometres of roads has very different issues, concerns and community expectations than an inner-city council which entertains 90%+ of the State's visitors. Therefore assessing the sustainability and reasonableness of Council decisions requires a qualitative assessment that takes into account the particular conditions of, and community expectations within, each area.

There are many drivers for increased maintenance and renewal needs due to additional service requirements. For example the City of Holdfast Bay is a tourist destination. Council facilities including parks, reserves, public amenities and streetscape cleanliness require a higher standard of maintenance and renewal costs due to increased use of assets. Property growth is just one factor in assessing scale of requirements for a City and not all factors are relevant across all councils.

Council is aware that the Local Government Association is submitting a whole-of-sector response and concurs with the general intent expressed. In particular, Council supports the view that assessments should be scaled up if and when needs are identified, preferably using a local value and/or risk-based approach. If historical data is used, the timeframe it relates to should only go back so far as is relevant to inform the future, and should be data that is publicly available which does not need to be re-formatted by councils. When considering future plans it is considered that a 10 year time horizon is too long for meaningful decision making and forecasting. A shorter time period of five years is preferred to forecast and model more accurately costs and revenue requirements.

Council also strongly believes that the use of the term 'CPI constrained' and the application of CPI in general is inappropriate and will potentially create misunderstanding and unnecessary mistrust. At a time in history where trust in governments in general is at a record low and misinformation is rife, it does not serve any tier of government to pursue reductionist arguments for populist ends.

Historical budgets and results have been prepared and measured based on plans that have been provided to the community through the annual consultation process that include assumptions, financial management principles and targets and, where applicable, new capital and operational initiatives. Community consultation, feedback and outcomes have been historically considered by both the Audit Committee and Council. To use historical CPI as a comparative measure does not present a useful picture given the historically approved expenditure plans and outcomes that have been consulted on.

CPI is a broad based measure only and ESCOSA has noted the existence of a council specific index used within the local government sector called the Local Government Price Index (LGPI). The draft Framework comments that this is not relevant for the purposes of the scheme, however, Council consider LGPI to be extremely relevant, as it measures a more appropriate basket of goods and services. The fact that it is developed in conjunction with the South Australian Centre for Economic Studies provides credibility and robustness to this measure.

In any case, there are many reasons why a council may introduce a rate rise above CPI or LGPI, most of which are rooted in community expectations. To suggest, either by inference or directly, that rates should never rise above CPI ignores the realities of community expectations and undermines the extensive engagement processes that council are legislatively required to abide by.

As submitted during engagement on local government reforms, Council suggested a different scheme to that proposed, whereby:

> "Rather than all councils being required to submit their plans for annual independent evaluation, ….the designated authority be tasked with providing independent advice on plans only where 51% of the number of people who voted in the last election of that council lodge an objection against their proposed plan.
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> Such a mechanism would keep the power over local decisions within communities, while providing assurance of remedy where a substantial number of citizens believe a decision to be incorrect. It should also increase engagement with the annual business planning process as councils will have greater impetus to ensure their communities are invested in the content of their plans and citizens will feel like they have a regular (annual, as opposed to four-yearly at the ballot box) and direct line of influence, should council be making decisions they are unhappy with. The proposed percentage also ensures that the numbers are representative and achievable, thereby improving accountability, efficiently."

As it did then, Council now also strongly objects to administratively burdensome processes being imposed on all councils due to the questionable decisions of some.

As such, Council's strong preference is for the State to bear costs of the proposed Scheme, since it's of the State's making. It is also noted that the costs associated with the proposed scheme are far in excess of what was anticipated.

However, given the legislation allows for costs to be shifted to councils, it would be more equitable to distribute costs on a pro-rata basis relating to population, rather than a flat fee. Council does not consider it equitable that councils with very low rating bases to bear the same costs as a Council who can leverage greater resources.

In any case, the scope of the proposed scheme should be reduced to address costs as much as possible. The scope of the proposed Scheme and the information requested should be directly relevant to and used for the purposes of the narrow scope outlined in the legislation, not the expansive interpretation set out in the draft Framework.

[redacted]