

26 May 2022

Essential Services Commission
GPO Box 2605
ADELAIDE SA 5001

Sent via rates@escosa.sa.gov.au

Dear Commission,

Local Government Rates Oversight Scheme – Draft Framework and Approach

City of Port Adelaide Enfield is grateful for the opportunity to be able to provide feedback on the Local Government Rates Oversight Scheme draft framework and approach.

For your consideration, I have enclosed our response and comments on the above mention framework and approach that Essential Services Commission (ESCOSA) would like to take moving forward.

If you require further information or would like to discuss this matter, please contact [REDACTED]

Yours sincerely

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2.3.1 Overarching intent to the Legal Framework.

Do stakeholders agree with this interpretation of the legal framework? If not, why not?

ESCOSA recitation of the legal framework is substantially correct. City of Port Adelaide Enfield notes that s.122(2)(1g)(b) does provide ESCOSA with powers to seek additional information it considers relevant to providing its advice. However, it would be preferable that ESCOSA does this on a case-by-case basis, as needed, rather than in the fundamental design of the scheme from the outset. This risk-based approach may assist to reduce overall costs of operating the scheme.

City of PAE is concerned that ESCOSA's interpretation of the scope of the review will result in significant additional work by council administrations to create and supply additional information. This interpretation is also a primary driver for the significant additional costs that ESCOSA propose to invoice each council.

To the extent that ESCOSA does have a discretion the City of PAE submits that it should be exercised in a manner consistent with the limited scope of review contemplated in the Act and in Minister Chapman's second reading contribution.

2.3.2 The scope and context of the advice

Do stakeholders agree with this interpretation of the scope and context of the advice to be provided under the scheme? If not, why not?

City of PAE notes that Principle 3 (materiality) states that the focus of analysis should not be overly disaggregated with unnecessary detail. City of PAE would prefer to see analysis and advice based on aggregate revenue and expenditure categories, consistent with this principle.

4.2 The principles underpinning the analytical framework

Do stakeholders consider these principles appropriate for the analytical framework? If not, why not? How should they be changed and why?

PAE welcomes the high level independent review from ESCOSA which will strengthen councils existing 'review processes which includes: external audit; internal audit program, and oversight from the Risk and Audit Committee.

The focus of the review should be given to key overarching targets and measures. PAE is concerned that the scope of information required from councils indicates a more granular level of review. The proposed framework and approach appears to delve into a deeper level of operational data which, given the volume of required information outlined, adds complexity both to councils in terms of responding and ESCOSA in terms of analysis required.

City of PAE want to highlight the importance of maintaining the scope of the review in line with the intent of the legislation. In particular, we would like to see ESCOSA leverage the existing data sets reported to the SA Local Government Grants Commission to reduce the up-front administrative burden for individual councils.

The proposed DFA (Draft Framework and Approach) includes requirements for councils to provide information that will require a significant amount of work from councils to populate the templates provided.

4.3 Overarching analytical framework

Do stakeholders consider this an appropriate analytical framework?

If not, why not? How should it be changed and why?

PAE agrees that a focus on overarching financial sustainability, key financial indicators and model financial statements is appropriate. PAE notes that ESCOSA has given significant emphasis throughout the DFA to affordability (particularly in relation to ratepayer demographics) of the LTFP and IAMP. We believe this is certainly a key consideration for Elected Members, however, extending the scope of ESCOSA's review to this level of detail takes the advice beyond what is required to understand the 10-year LTFP and IAMP.

The DFA proposes a far more detailed analysis of each council's financial position. Therefore City of PAE has not seen evidence that a review considering this additional detail would provide greater overall benefit to the local government sector than a high-level' review.

4.4.1.1 The relevance of historical trends

Do stakeholders consider it necessary to consider historical trends when applying the analytical framework?

- **If not, why not? How should it be changed and why?**

PAE agrees that historical trends are one of many important factors to consider in forming a view regarding future revenue and expenditure projections. PAE is not opposed to ESCOSA obtaining access to data as old as 2007-08, but believes this information should be collected from existing centralised sources (i.e. SALGGC or State Library archives. Expecting individual council's to source and collate this information into a standardised template is extremely inefficient.

4.4.1.3 Accounting for scale

Do stakeholders agree that, where it is useful to do so, information should be normalised on a per rateable property basis?

City of PAE does not oppose ESCOSA analysing revenue and expenditure information on a per rateable property basis, provided appropriate consideration is given to the distribution of land uses within each individual council area. This may add significant complexity and cost to such analysis. PAE for example, has a higher proportion of commercial and industrial properties than many other council areas. What might appear to be a 'simple' normalisation methodology at first, may not actually enable meaningful conclusions to be drawn on this basis.

4.4.1.4 Accounting for inflation

Do stakeholders agree that use of the CPI is an appropriate index to utilise when considering a council's operating income and expenditure growth over time?

If not, why not? How should it be changed and why?

PAE agrees that due consideration needs to be given to measures of growth and efficiency in council expenditure. This is a key responsibility for Elected Members on behalf of their communities. However, ESCOSA's proposal to use Australia CPI as the benchmark/constraint for its analysis is unsound. Firstly, Adelaide CPI is a more accurate proxy for the general inflation pressures facing South Australian than Australia CPI. Though, this still does not reflect the true cost pressures faced by local government. This is better reflected in a historical analysis of LGPI relative to Adelaide CPI.

PAE notes that ESCOSA has given significant emphasis throughout the DFA to affordability (particularly in relation to ratepayer demographics). Analysis of future expenditure projections through this lens based on a generic inflation assumption appears to be an expansion of scope beyond the relevant matters and may lead to misleading conclusions about the council's LTFP and IAMP.

The Local Government Act provides discretion for councils to determine the reasonable assumptions to be used in the development of their LTFP. These issues were comprehensively reviewed as part of the (Local Government Review) Act 2021 and ultimately councils were not required to use specific indices. Rather, councils now have an obligation to include the assumptions used in the development of their LTFP.

In summary PAE believes ESCOSA should analyse the LTFP and IAMP relative to the LGPI.

4.4.2 The key questions to address

Do stakeholders consider these to be appropriate questions for implementing the analytical framework?

- **If not, why not? How should they be changed and why?**

The City of PAE believe that the first three key questions on page 22 capture much of what is required of a high-level review of the 'relevant matters'. A high-level review would satisfy ESCOSA's section 122 obligations whilst also providing councils with useful but not extraneous advice.

Under section 122, it is not ESCOSA's role to audit whether a council has 'successfully implemented' the LTFP and IAMP. However, ESCOSA should have 'regard to' the historical trends evidenced by the financial indicators.

The 'relevant matters' relate to the material amendments made or proposed to be made to the LTFP and IAMP (and the potential impact on the revenue sources outlined in the funding plan) not to the implementation of the plans.

The City of PAE agree that the implications of a council's long-term financial sustainability forms part of ESCOSA's scope however the LGA does not agree that a council's 'service risk profile' is a matter contemplated by s122.

The further factors which ESCOSA propose to review (ie. cost control, ratepayer demographics and practical implementation) descend into a level of detail beyond the scope of the legislation. Rather, these are matters for the democratically Elected Members of council, council administrations, council auditors and council Audit Committees.

The City of PAE agree that the three key financial ratios are an appropriate mechanism which should guide high-level advice however we do not believe it is the role of ESCOSA to verify or audit the information that feeds into the ratios.

Council proposes an approach consistent with the high-level review contemplated by s122. The Local Government (Financial Management) Regulations 2011 Regulation 5(1) outlines that a LTFP must include:

- b) a summary of proposed operating and capital investment activities presented in a manner consistent with the note in the Model Financial Statements entitled Uniform Presentation of Finances; and
 - c) estimates and target ranges adopted by the council for each year of the long-term financial plan with respect to an operating surplus ratio, a net financial liabilities ratio and an asset renewal funding ratio presented in a manner consistent with the note in the Model Financial Statements entitled Financial Indicators.
- 2) A long-term financial plan must be accompanied by a statement which sets out—
- a) the purpose of the long-term financial plan; and
 - b) the basis, including key assumptions, on which it has been prepared; and
 - c) the key conclusions which may be drawn from the estimates, proposals and other information in the plan.

The focus of ESCOSA's key questions should be on the information (that is required by the regulations to be included) in the LTFP (ie. what are the historical figures indicating about the validity and robustness of the assumptions used to predict the proposed high-level trends). Note that many councils provide more information in their LTFP than required by the regulations, however this should not expand the scope of the review contemplated by s122.

The City of PAE believe it is the role of ESCOSA to verify or audit the data contained in council LTFPs and/or the ratios. It should be noted that council financial statements are already audited by external auditors. Council does not support the scope of ESCOSA's review including any matter or any process which is already provided for in the legislative scheme governing SA councils (eg audits, comparisons of council data).

Material amendment

City of PAE agrees with ESCOSA that what is a 'material' amendment to a LTFP or IAMP will depend on the council being considered. We do not believe it is appropriate to further constrain the definition of materiality. Councils have an existing understanding around what is considered 'material' in the context of their financial statements, as guided by Australian Accounting Standards. This understanding should be drawn on to guide ESCOSA in this regard.

4.4.3 How the analytical framework can address the key questions and what information is required to do so

Do stakeholders consider this an appropriate approach to the analytical framework to assess the key questions in Table 5?

If not, why not? How should the approach be amended and why?

City of PAE are not supportive of the Methodological Proposal 3 which further expands the proposed scope of the review, adding additional analysis methods that will considerably increase council costs. Relevant information to be analysed should be limited to that which will assist a review of the Relevant Matters, to ensure the review scope (and related costs) are contained.

PAE is concerned about the inclusion of trend graphs in ESCOSA's advice which are 'constrained' by an inflation factor which is of questionable relevance to Council's primary expenditure exposures. The assessment of affordability for council's ratepayers is a primary obligation of the Elected Members, in consultation with their respective communities.

We accept that section 122(1e) enables ESCOSA to make guidelines relating to the provision of information by councils. We also understand this section authorises guidelines dealing with how relevant information is provided. However we do not consider that section 122(1e):

- expands the possible scope of a rates oversight scheme; nor
- does it authorise the acquisition of documents that are beyond the objectives of a review
- Section 122(1e) requires us to provide "all relevant information" on:
 - material amendments made or proposed to be made to the council's LTFP and infrastructure and asset management plan and the council's reasons for those amendments; and
 - revenue sources outlined in the funding plan (which is part of the LTFP).

The powers of ESCOSA to obtain information for section 122 reviews which means ESCOSA "may, by written notice, require us to give the designated authority, within a time and in a manner stated in the notice, information in the council's possession that the designated authority reasonably requires for the performance of the designated authority's functions under this section".

This power does not extend to information held by parties external to a council.

We are not supportive of the expression 'all relevant documents' authorises the inclusion in the review of a wide range of documents, which are not necessary for ESCOSA to understand and provide a high-level review of the LTFP or IAMP.

4.5.1 Content of the advice

10 Do stakeholders consider this an appropriate approach to developing the content of the advice that the Commission provides to each council?

- **If not, why not? How should the approach be amended and why?**

ESCOSA proposes to “provide an overarching picture of any potential cost control, affordability, and sustainability risk, based upon actual performance and forecast performance. Further, the advice can utilise available qualitative information regarding a council’s SMP, its current CEO sustainability assessment and its approach to setting rates to identify how any risks identified in the quantitative assessment are managed/mitigated, creating opportunity for further discussions on those matters”.

City of PAE believes that the proposed ‘Content of the advice’ goes beyond the advice contemplated by the section 122 scheme.

City of PAE position remains that the ESCOSA review is a high-level review, focused on the ‘relevant matters’.

4.5.2 Publication of the advice

Do stakeholders consider this an appropriate approach to adopt for the publication of the advice, given the legal framework?

- **If not, why not? How should the approach be amended and why?**

We accept that the legislation requires the publication of ESCOSA advice and that it is in the public interest for this advice to be made public. However, a very large ESCOSA report may impact negatively on the size and readability of Councils Annual Business Plan (ABP).

Therefore, we would suggest for an (ESCOSA-prepared) executive summary (ie. the findings and recommendations) to be published in the council’s ABP, together with an ESCOSA link to the full document.

This approach would ensure the full advice was available to council and all others who wished to access it; whilst keeping council ABP to a manageable size.

City of PAE is also concerned the proposed ESCOSA timeframes may impact on Council’s ability to meet ABP timeframes if there are matters arising from the advice which council wishes to respond to in the current annual planning cycle.

4.6.1 Alignment with the legal framework

Do stakeholders consider the analytical framework aligned with the legal framework?

- **If not, why not? How should the approach be amended and why?**

As stated earlier, City of PAE has concerns the proposed framework goes beyond the intent of the legislation. Council would prefer to see a risk-based approach which meets the intent of section.122 but limits the level of detail required based on a case-by-case risk assessment.

4.6.2 Alignment with the overarching principles for the analytical framework

Do stakeholders consider the analytical framework to be aligned with the overarching principles for its development?

- **If not, why not?**

As already outlined above, City of PAE believes that the analytical framework includes matters and a level of detail beyond the scope. In particular, the proposed analytical approach appears to be misaligned with the stated principles of Materiality and Simplicity and as a result, driving higher scheme costs for council's.

5.2 Guidelines and information provision

Do stakeholders consider publishing a revised set of guidelines and proforma Excel template no later than the start of each the Relevant Financial Year appropriate?

- **If not, why not? How should the approach be amended and why?**

City of PAE would like to see ESCOSA leverage existing centralised sources of council data, such as SALGGC to populate the historical data tables.

We note Principle 5 which proposes a scheme that leverages existing information and evidence. By contrast, the 'proforma Excel template' therefore indicates that council officers will be required to populate new datasets in new documents. The DFA contains several template documents which appear to require the inclusion of large amounts of data to complete. This will:

- Consume significant council resources in preparing; and
- Expand the scope of the ESCOSA review beyond the scope thereby increasing overall council costs.

PAE recommends that as far as possible, ESCOSA restrict the documents it compels councils to provide to those documents that already exist and which remain readily available.

5.3 Timing of information provision

Do stakeholders consider the proposed timing for information provision appropriate?

- **If not, why not? How should the approach be amended and why?**

A major concern with the first iteration of the Rates Oversight Scheme related to proposed timelines which were conflicting with council budget preparation cycles. The timeframe set out in s122 was drafted, based upon feedback from the 68 councils, taking into account workloads of financial teams and the timing, each year, when particular documents would become available.

PAE are not supportive that ESCOSA has a power to vary the statutory deadline set out in this section.

Any variation to ESCOSA timeframes may impact PAE's ability to meet ABP or other statutory reporting timeframes.

7.1 Cost recovery – Introduction

As set out above, several versions of rate capping and rates oversight schemes were put before Parliament. Ultimately, it was agreed that an ESCOSA review would focus on a council's 'long-term financial plan' (LTFP) and its 'infrastructure and asset management plan' (IAMP).

ESCOSA proposes a scope of review that is considerably wider than contemplated by section 122.

City of PAE acknowledges that the more information analysed, the more expensive the resulting report will be.

A high-level, limited scope review will provide council with sufficient information to make appropriate choices about their financial settings.

Councils are required to reimburse ESCOSA for the costs of each review. ESCOSA has indicated that the cost per review per council may be in the order of \$52,000.

As ESCOSA proposes to adopt the same review process for each council there is unlikely to be a significant variation in the amounts paid by different councils.

These costs are likely to fall on a council once every four years.

Council were previously advised by Parliament that the costs of an ESCOSA review were "likely to be in the order of \$20,000 per council.³". ESCOSA now propose a process that would cost each council \$52,000 per review.

The City of PAE is very concerned with the increase in cost the proposed scheme operating costs and the impact this would have on smaller councils.

The increase in the scope of rates oversight reviews, as proposed by ESCOSA, has obviously led to substantial increases in the costs of the scheme to the sector. A reduction in the scope would better align to the intent of s122 and reduce costs.

7.2 Reasonable Costs

Do stakeholders agree with the Commission's approach to addressing any material difference between its actual costs and its projected indicative costs?

If not, why not? How should the approach be amended and why?

Set-up and development costs should be borne by the State Government.

PAE agrees that ESCOSA should consider any material cost variance in the way it approaches the second review cycle. This should include a robust consideration of opportunities to simplify the scheme and reduce ongoing costs to council's ratepayers.

As there is no legislative authority to charge councils, fixed costs, overheads and establishment costs must be borne by the State Government.

7.3 Cost recovery

Do stakeholders agree that the Commission should bill the LGA the total yearly cost associated with the scheme, noting that any such scheme would require unanimous agreement between the LGA and member councils covering at least the first four-year cycle?

If not, why not?

The Act requires ESCOSA to invoice each council directly however ESCOSA is proposing an alternative arrangement whereby they send one bill to the LGA. Then LGA recover these funds from each council.

The LGA does not have statutory authority to act in the manner ESCOSA is proposing. As all 68 councils would need to agree that the LGA should act as their agent for the purpose of payment of ESCOSA invoices.

City of PAE recommends ESCOSA invoices directly to councils.

7.3.2 When should councils be billed and with what frequency?

Do stakeholders agree with the Commission's approach to the timing and frequency of billing? If not, why not? How should the approach be amended and why?

PAE would prefer to be billed and pay for its scheme costs in one lump sum, in its relevant year of review. This aligns with the applicable accounting treatment for the expense. This would also limit ESCOSA's billing/administrative costs to a nominal level annually.

7.3.3 How should costs be allocated between councils?

If the Commission were to bill each of the 68 councils separately, do stakeholders agree with its proposed approach to allocating the total yearly cost between councils?

If not, why not? How should the approach be amended and why?

PAE agrees that the operation of the scheme will require similar levels of effort from ESCOSA for each council, regardless of size. It is therefore a reasonable conclusion that each council incurs the same cost.

Section 122(2)(1k) stipulates a 'cost recovery' approach for the costs incurred in relation to a Council. PAE does not believe ESCOSA has the discretion to elect an alternative allocation methodology under this section.

If the scheme is implemented as proposed and the cost of \$52k maintained, this will represent a significantly larger proportion of rate revenue for smaller council's. Such council's may have no alternative other than to implement a separate general rate to cover this significant cost, similar to the approach used for recovery of the Regional Landscape Levy.