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13 May 2022

9/3/6

Mr Adam Wilson
Chief Executive Officer
Essential Services Commission
GPO Box 2605
Adelaide SA 5001
rates@escosa.sa.gov.au

Dear Mr Wilson,

Re: Local Government Rates Oversight Scheme - Draft Framework and Approach

Thank you for the opportunity to comment on the Essential Services Commission of South Australia's proposed *Local Government Rates Oversight Scheme*.

Council considered the draft framework and approach at its May meeting and resolved to provide the following feedback:

Overall framework
Overall, the seven principles underpinning the analytical framework appear sound and will provide for a comprehensive assessment. The use of existing information and financial performance indicators will help streamline the process and improve a council's ability to integrate the information in its planning and business processes.

However, while the framework reflects some consideration of its administrative impact on Council operations, the detail of the information requested appears to extend beyond the minimum requirements as per the *Local Government (Financial Management) Regulations 2011* to the full suite of information available in the Model Financial Statements and seek historical information dating back to 2007/08.

The requested additional extracts from a council's *Statement of Financial Position* and *Note 2* in councils' annual financial reports are not referenced within the Uniform Presentation of Finances. Such detailed information is also not commonly referenced in council LTFPs. Adding this information will add significantly to the administrative burden worn by councils.

Considering the significant changes not just in our financial management but also in elected council priorities and services provided to our communities over a span of 15 years, it is difficult to see what value such historical data can hold for informing the Commission's assessment.

It is instead proposed that only the high-level information available from the Model Financial Statements included in business and long term financial plans, and data for a period of four years, aligning with a full review cycle, be provided by councils.

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Specific questions (questions 17 and 29) regarding any indication of financial and service sustainability, cost control or affordability risks emerging, appear to sit outside of the scope envisaged by the legislation. Though they may provide some assurance to elected members and community, this assurance will come at significant cost to ratepayers (more below) and similar assurance is already provided through other processes, the external audit of council finances for example or CEO report on the sustainability of the council.

CPI vs LGPI

The Commission proposes to use the Consumer Price Index (CPI) to compare the growth rate in a council's operating income and operating expenditure data "*given the context and purpose set out in the second reading speech. (…)*
The Commission notes that there is a council-specific index used within the local government sector: the Local Government Price Index (LGPI), developed by councils in conjunction with the South Australian Centre for Economic Studies. The LGPI measures price movements faced by councils in respect of their purchases of goods and services. Although it may be considered a robust tool for that particular purpose, given the focus of the second reading speech, it is not as relevant for the purposes of this scheme." (Page 21 of the Framework)

The Commission itself describes the second reading speech (Page 4) as stating the scheme's two key purposes as firstly, supporting councils to make decisions relating to their annual business plans and budgets in the context of their long-term financial plans (LTFP) and infrastructure and asset management plans (IAMP), and secondly, ensuring that the decisions councils make on financial contributions made by ratepayers to the provision of services and infrastructure (mainly through general rates) are appropriate within the context of those long-term plans. The second reading speech also notes there is a reasonable expectation that councils will seek to ensure value for money for their ratepayers through finding efficiencies, rather than ratepayers continually paying for increased costs through increased rates.

Neither the first, nor the second purpose appear to support the Commission's dismissal of the LGPI. In fact, the entire framework is concerned with a council's sound long term planning, and sound assumptions underlying such planning, only to then disregard a well-established and researched cornerstone of this planning, the LGPI.

The *Local Government Act* leaves at a council's discretion to determine reasonable assumptions to be used in the development of the LTFP. The Rates Oversight Scheme does not authorise the Commission to constrain councils to any particular indices. In attempting to only give weight to one inflation index and discounting any others, the Commission inappropriately limits the discretion bestowed upon councils under the Act.

It may be useful to examine the Commission's proposed adoption of the CPI for the comparison of operating income and expenditure growth rates when translated to a non-government context:

An engineering/metal fabrication business purchases a range of goods and services, steel purchases making up 40% of the business' operating expenditure. Steel prices have gone up 50% since December 2020. If we were to adopt the Commission's view that "*the* *underlying measure of inflation is most relevant to* customers *(= ratepayers)*" the business would increase its prices by CPI, rather than the much more relevant price of steel. Though the business' prices would ensure happy customers, it would very likely find itself unable to pay its bills in short order.

While local government may purchase a slightly more diverse basket of goods than an engineering/metal fabrication business, we also do not buy a consumer basket of goods and services, and CPI does not reflect the price movements we face.

Reflecting on general price movements faced by consumers is without a doubt important when ensuring rates remain affordable. It does not provide a sound basis for assessing a council's expected cost increases and related need to raise revenue.

Depreciation vs AMPs
"*The Commission notes that councils have moved from using depreciation as the denominator in the asset renewal funding ratio, to using the IAMP figure for replacement/renewal expenditure. The Commission is proposing to consider the asset renewal funding ratio using both approaches. This is because:*

- *Using both depreciation and the IAMP replacement/renewal expenditure approaches for the asset renewal funding ratio provides a way of comparing whether the asset lives assumed in each case are broadly consistent and, if not, why this is the case. A council operates in perpetuity, it does not face competition in providing its services and provides public goods, so there does not appear to be any immediate reason why implied asset lives with respect to depreciation and IAMP replacement/renewal expenditure should vary significantly. (…)*" (Page 25)

While it is useful to compare both, the expectation that depreciation and AMP replacement/renewal expenditure will always mirror each other overlooks the 'lumpy' nature of infrastructure asset management. A Community Wastewater Management Scheme for example may have an asset life of 55 years. It will depreciate over the term of the LTFP in accordance with its expected asset life but, considering its long life, will likely not be replaced within the 10-year term of the LTFP or AMP, resulting in what may seem to be a misalignment in respect to depreciation and AMP replacement/renewal expenditure.

Publication
The Commission proposes that all advice provided should be published in full. The publication of the advice is positive and may provide assurance to ratepayers that their councils are responsible service and asset managers. However, by its very nature the advice will likely be lengthy and difficult to follow. Its inclusion in an existing plan, Tatiara District Council's current annual business plan at 43 pages is one of the shorter ones, increases the risk that the advice may become inaccessible in practice.

It is therefore proposed that the advice be prefaced by a plain English executive summary and supporting infographic, and that instead of including the advice in full, the annual business plan include this summary and provide a link to the full report and Council response, if any.

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Cost of the Scheme

The costs of administering the scheme are to be recovered from each council, as a debt due from the council to the Commission.

The Commission's indicative total cost, over the first four-year cycle of the scheme is $3,545,001, or $52,133 per council, based on Commission staff effort per council being the same, irrespective of council size or location. (Page 51)

This is more than double the cost indicated to Parliament by then Minister Chapman, which was in the order of $20,000 per council, and directly related to the significant – and unwarranted - increase in the scheme's scope proposed by the Commission.

In the context of the cost of the scheme, it is worth noting that 30 of the 68 South Australian councils raised less than $10m dollars in general rates in the 2019/20 financial year, according to the last available Grants Commission report. The Essential Services Commission proposes to raise almost $1m in revenue for its assessment of councils every year in the first three years, compared to seven councils raising less than $2m in general rates. Though the costs will be felt much more dearly by these councils than by those on the other end of the scale, sharing the costs based on size rather than number would mean that ratepayers in one local government area would effectively subsidise another.

For the avoidance of unnecessary administration, it is suggested that the Commission invoice councils directly for an equal share.

The second reading speech notes there is a reasonable expectation that councils will seek to ensure *value for money* for their ratepayers through finding efficiencies, rather than ratepayers continually paying for increased costs through increased rates. The scheme currently does not appear to provide for an evaluation of its own effectiveness compared to its costs. Such an evaluation should be planned for and included from the outset to ensure that the scheme achieves what it is setting out to do.

Conclusion

While there may be value to councils in receiving high level advice on strategic management plans, the framework proposed by the Commission is overly onerous in terms of information provision by councils and the costs are far more than what was anticipated.

I would be pleased to provide further information and can be contacted by email to [redacted] or mobile [redacted]

Yours faithfully,

[redacted]