

**INQUIRY INTO BUDGET PROCESS FOR INDEPENDENT
OVERSIGHT BODIES AND THE PARLIAMENT OF NEW
SOUTH WALES**

Organisation: Local Government NSW

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Draft Submission to the Legislative Council Public Accountability Committee

Inquiry into the Budget process for independent oversight bodies and the Parliament of New South Wales

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Opening

Thank you for the opportunity to make a submission to the Public Accountability Committee's Inquiry into the Budget process for independent oversight bodies and the Parliament of New South Wales.

Local Government NSW (LGNSW) is the peak body for local government in NSW, representing NSW general purpose councils and related entities. LGNSW facilitates the development of an effective community-based system of local government in the State.

This is a draft submission awaiting review by the LGNSW Board. Any revisions made by the Board will be forwarded in due course.

Purpose

The terms of reference establishing this inquiry are:

1. *That the Public Accountability Committee inquire into and report on the budget process for independent oversight bodies and the Parliament of New South Wales, and in particular:*
 - (a) *Options for enhancing the process for determining the quantum of funding of the following bodies, including the transparency of this process:*
 - (i) *Independent Commission Against Corruption*
 - (ii) *Law Enforcement Conduct Commission*
 - (iii) *Audit Office of New South Wales*
 - (iv) *NSW Electoral Commission,*
 - (v) *NSW Ombudsman, and*
 - (vi) *Parliament of New South Wales (Legislative Council and the Department of Parliamentary Services)*
 - (b) *Any other related matter.*
2. *That the committee report by the last sitting day in April 2020.*

LGNSW's brief submission will focus on the Budget process for the NSW Electoral Commission and the Audit Office of NSW.

NSW Electoral Commission

On 7 February 2019 the NSW Premier issued terms of reference for an Independent Pricing and Regulatory Tribunal (IPART) review into the costs of local government elections. IPART was requested to provide a report to the Minister for Local Government recommending a costing methodology to be applied in determining the amount the NSW Electoral Commission (NSWEC) charges councils which use the NSWEC to administer their ordinary elections.

The purpose of IPART's review was to ensure a robust methodology for determining costs is applied, in order to minimise the financial burden on councils and ratepayers and ensure local government elections are conducted efficiently and cost effectively.

IPART's final report to the NSW Government included figures provided by the NSW Electoral Commission, estimating the costs of the 2020 local government elections. (The NSWEC had forecast operating expenditure of \$62.4 million for the 2020 elections). However, IPART accepted findings of a review undertaken by consultants EY that found there was scope for significant efficiency savings, and that the total efficient costs of the elections should be \$48.5 million (i.e. – cost reflective pricing).

IPART further found that the market for local government election services is currently a near-monopoly, and that this, along with:

...the very sharp increases in costs proposed by the NSWEC highlights the need to review the efficiency of the NSWEC's proposed costs and to regulate prices, at least in the short term.¹

The NSW Government, in its 18 September 2019 response to IPART's report², committed to:

- Funding the NSWEC's core costs of \$19.9 million in relation to the administration of local government elections, thereby reducing councils' election costs.
- An indicative weighted average cost per elector of \$8.21, which will be passed onto councils, compared to a weighted average cost per elector of \$12.72 if no NSW Government contribution was provided.
- Reducing councils' election costs ensuring all councils, regardless of size, can afford to retain an electoral services provider to administer their elections
- More efficient, cost effective and cost reflective elections
- Ensuring a more equitable allocation of election costs, eliminating the need for larger councils to cross subsidise smaller councils' elections
- Reflecting the practice in other jurisdictions where State Governments fund their Electoral Commissions' core operations in relation to local government elections resulting in lower costs per elector compared to NSW.
- Further reducing the cost of local government elections.

Unfortunately, despite the commitments of the NSW Government, since October 2019 councils have been receiving from the NSWEC quote estimates for the 2020 local government elections that show significantly increases since the previous round of local government elections in 2016 and 2017, and per elector costs well above the \$8.21 average anticipated in the NSW Government's response to IPART's report.

Compared to the previous local government elections, councils are receiving quotes from the NSWEC that are up to (and in some cases more than) 100 per cent higher (i.e. more than

¹ IPART, Final Report – Review of local government election costs, August 2019, available at: <https://www.ipart.nsw.gov.au/Home/Industries/Local-Government/Reviews/Costs-of-Local-Government-elections/Review-of-costs-of-conducting-local-government-elections>

² NSW Government, Review of Local Government Election Costs: NSW Government Response to IPART Recommendations, 18 September 2019, available at: <https://www.olg.nsw.gov.au/sites/default/files/IPART-Review-of-Local-Government-Election-Costs-Government-Response-2019.pdf>

double).³ While the NSWEC's estimates for each council are not publicly available, it appears as though on the whole the NSWEC's estimate has increased by around 35% across all councils, but with a disproportionately higher increase for regional and rural councils and many councils seeing far higher increases. These increases cannot be explained by price inflation or population growth.

Further, it is unclear how the announced subsidy of \$19.9 million is being used (other than being fully absorbed by the NSWEC) – particularly given the dramatic increases in costs being passed onto councils. The NSW Government must ensure its \$19.9M subsidy to the NSW Electoral Commission is transparently accounted for, and applied to council costs so that councils do not face increases in the costs of local government elections by more than the rate cap imposed on local government rates.

Recommendation 1: The NSW Government must ensure its \$19.9 million subsidy to the NSWEC for the conduct of the local government elections is transparently accounted for and applied directly to council costs.

Rate peg and cost shifting

Councils in NSW operate in a constrained financial environment as a result of rate-pegging, cost shifting onto local government and state and federal funding arrangements that are no longer fit for purpose. If these election cost increases were to be imposed on councils and ratepayers, councils may be forced to cut other services for the community. The increase would be a significant additional cost shift by the State Government onto local government, a burden already estimated to exceed \$820 million per annum.⁴

The local government rate peg in recent years has been well below the price inflation evident in the NSWEC's election costs:

| Year | Rate peg |
|---------|----------|
| 2017-18 | 1.5% |
| 2018-19 | 2.3% |
| 2019-20 | 2.7% |
| 2020-21 | 2.6% |

Indeed, at LGNSW's 2019 Annual Conference councils resolved to call on the NSW Government to ensure that the NSWEC not be permitted to increase the cost of conducting local government elections for 2020 and all future local government elections by more than the rate cap limit imposed on local government rates.

³ Cobar, Leeton, Oberon and Snowy Valleys councils for example have all received quotes that are more than double the cost of their previous election, while for Dungog, Temora and Walgett the increase is greater than 75 per cent. Meanwhile, Canterbury-Bankstown's increase is more than \$350,000 and Central Coast Council's increase is greater than \$540,000.

⁴ LGNSW, Impact of cost shifting on local government in NSW, 2018, available at: https://www.lgnsw.org.au/files/imce-uploads/206/Cost_Shifting_Summary.pdf

Recommendation 2: The NSWEC must not be permitted to increase the costs passed to councils for conducting local government elections by more than the rate peg imposed on councils, and the NSW Government must take this into consideration in adequately funding the NSWEC's Budget.

The NSWEC has outlined some reasons for its increases, including salary raises for election workers, and a reduction in the number of ballot papers that each worker must process. The NSWEC has also explained that it has signed a memorandum of understanding with the NSW Department of Education which increases rental costs for using school halls for elections by between 80 and 330 per cent, depending on the size of the room or hall hired.

It is LGNSW's view that it is particularly inappropriate for the NSW Government to impose these immense fee increases for school hall rental. Councils across NSW provide substantially discounted fees to Department of Education public schools for the use of sporting fields and parks, saving the NSW Government millions of dollars each year. The NSW Government should also recognise the importance of local democracy as a public good rather than a revenue raising opportunity, and reverse the Department of Education's massive price increases for hall hire.

Recommendation 3: The NSW Government must reverse the Department of Education's massive price increases for hall hire for local government elections

Disproportionate impact on smaller rural and regional councils

There are also serious equity issues with the new funding model that will see those least able to pay (and particularly small and rural councils) hit with the largest cost per elector (as well as the largest increases in percentage terms). These increases come at a time when rural and regional communities are already enduring the impacts of extreme drought.

Elections and democracy are a fundamental public good that should not be more expensive for some ratepayers than others. LGNSW would welcome a sensible approach to funding the NSWEC that does not result in ratepayers in rural and regional NSW being penalised. The need to ensure equity to overcome the economic disparities across the state justifies maintaining centralised NSW taxpayer funding of a substantial proportion of local government election costs.

Recommendation 4: The NSW Government must adequately fund the NSWEC to minimise the financial burden on councils and ratepayers and ensure local government elections are conducted efficiently and cost effectively and do not result in inequities between ratepayers and communities in the price of maintaining democracy.

No ability for councils to meaningfully reduce costs

The bulk of council election costs are made up of staffing costs and councils are unable to take action to meaningfully reduce these costs. Polling place staffing costs, ballot paper costs and call centre costs are largely set in proportion to the number of electors in each local government area, which councils of course cannot influence.

While councils can suggest alternative venues for polling places, including council owned venues, the council will need to convince the NSWEC that polling places are suitable and that changing polling places compared to previous state and federal elections will not confuse electors and result in a reduced level of voting. It is then a matter for the NSWEC to agree to any changes in polling places.

LGNSW understands that a number of councils have also sought NSWEC approval to reduce the pre-poll period to one week but that the NSWEC has rejected these requests. At LGNSW's Annual Conference in 2017 (and again in 2018) councils resolved that LGNSW petition the NSW Government to shorten the pre-poll voting period. A reduced pre-poll period would go some way to decreasing the overall cost of running an election. Further, for candidates who have full time employment it can be very difficult to make available the time to be present at pre-polling stations. Importantly, those who are unable to attend a polling place on election day still have the further option of postal voting available to them to ensure voting is accessible.

Recommendation 5: The pre-poll voting period should be reduced to one week (Saturday to Friday in the week before election day), for all local government elections whether the election is administered by the NSW Electoral Commission or by a private election services provider.

Fine revenue from non-voting

The NSW Government collects significant fine revenue for non-voting in local government elections. LGNSW has long called for this revenue to be used to offset the costs of local government elections, rather than being returned to NSW Government consolidated revenue. Most recently, councils again resolved at LGNSW's 2019 Annual Conference to call on the NSW Government to address this matter.⁵

In 2014 the Joint Standing Committee on Electoral Matters also supported the concept of returning fine revenue to councils for electors that fail to vote in elections, stating:

Councils currently use the State Debt Recovery Office for fines issued by Councils for breaches of local by-laws and receive the corresponding revenue. Given that councils are paying for the conduct of their elections, they should similarly receive any corresponding fine revenue that accrues from this exercise.⁶

Recent annual reports of the NSWEC indicate that:

- In 2017-18 the NSWEC issued almost \$26 million in fines for failure to vote and received almost \$5 million in paid fines.⁷
- In 2016-17 the NSWEC issued almost \$24 million in fines for failure to vote and received more than \$4 million in paid fines.⁸

⁵ LGNSW Annual Conference Resolution 114 of 2019.

⁶ Joint Standing Committee on Electoral Matters, Report on the 2012 Local Government Elections, March 2014 p. 27.

⁷ NSW Electoral Commission, Annual Report 2017-18, p. 105

⁸ NSW Electoral Commission, Annual Report 2016-17, p. 89

While the NSWEC annual reports do not elaborate on which elections resulted in these fines, given there were no State Government general elections during this period, it is reasonable to assume that the bulk of this revenue was generated from the 2016 and 2017 local government elections.

Even noting that a substantial proportion of fines appear to remain unpaid, paid fine revenue for the 2016 and 2017 local government elections appears to amount to \$9 million, which would represent a substantial proportion of the cost of local government elections.

Recommendation 6: Significant fine revenue from non-voting at local government elections must be used to offset the costs of local government elections, rather than returned to NSW Government consolidated revenue.

It is clear that the Budget process for the NSWEC is no longer fit for purpose. While the NSWEC has an almost unfettered ability to pass on any and all costs to councils and ratepayers, it has limited incentive to ensure that its costs are efficient.

As part of the Intergovernmental Agreement signed between the NSW Government and LGNSW in October 2019, the NSW Government made a commitment to alleviate budgetary impacts of cost shifting to local government where possible.⁹

Councils support professionally run elections that safeguard public confidence in the democratic process. However, councils have extremely limited revenue raising opportunities. In line with the Intergovernmental Agreement between the NSW Government and LGNSW, it is essential that the Budget process for the NSWEC ensures that costs of local government elections are minimised and that any increases in excess of the rate peg imposed on councils must be borne by the NSW Government – for the 2020 elections and beyond.

Audit Office of NSW

As part of its Fit for the Future reform program, the NSW Government amended the *Local Government Act 1993* to include provisions for the Auditor-General to oversee the audit of councils' annual financial statements and to conduct performance audits of a council, or the sector.

Under the amendments, the NSW Government funds the Audit Office to conduct performance audits, while councils pay the Audit Office for the cost of auditing their financial statements. Previously, councils were required to engage commercial audit services through an open tender process every six years.

⁹ NSW Government and Local Government NSW, Intergovernmental Agreement to Guide NSW State-Local Government Relations on Strategic Partnerships, Clause 6.10, 14 October 2019, available at: <https://www.lgnsw.org.au/policy/intergovernmental-relations>

Increased cost of audit function

As the Audit Office has contracted to private audit firms a large part of the audit task, while maintaining an oversight role, many councils have found themselves being audited by their former auditor, but they're being charged more – in some cases, a lot more, with no discernible change in service standard.

When the transfer of the audit function was proposed by the Independent Local Government Review Panel, LGNSW recognised the potential to improve consistency and we supported the proposal provided the Auditor-General's role was limited to setting the sector wide audit standards. LGNSW did not support the Auditor-General undertaking the actual audits. LGNSW also expressed concern that it would be more costly for councils¹⁰.

At that time, the Audit Office suggested, based on its experience, that councils' audit fees would increase on average by approximately 10%. Unfortunately, this has not been the case.

Instead, in the first audit conducted under the new arrangements, councils incurred an average increase in their audit fees of 23.5%, with five councils having increases of over 100%.

LGNSW would argue that the legislative amendments are fundamentally flawed, in that they:

1. establish the Auditor-General as the monopoly provider of local government financial audit services, and
2. give that monopoly provider full control over the fees charged to a council¹¹.

We believe the provision of audit services is very similar to the provision of land valuation services and a similar pricing approach should apply. That is, the NSW Government recognises that the Valuer General is the monopoly provider of valuations to councils and it would not be appropriate in that context for the Valuer General to determine fees. Instead, IPART is responsible for making a pricing determination on a five-yearly basis. While councils and LGNSW may not always agree with IPART's methodology, there is at least the opportunity to raise any concerns in a transparent and open process.

Recommendation 7: The NSW Government should implement, through the Independent Pricing and Regulatory Tribunal, a transparent price determination approach for the cost of audit services, similar to the model used for land valuation services.

¹⁰ LGNSW Submission on the Independent Local Government Review Panel's Revitalising Local Government, April 2014

¹¹ Section 422(3) of the Act states: *The costs confirmed in writing by the Auditor-General as having been incurred by the Auditor-General in auditing a council's financial reports (including any audit of a council entity) or in any other inspection or audit carried out by the Auditor-General under this Division (or at a council's request) must be paid by the council. Note: An example of confirmation is an invoice.*

Disproportionate impact on small rural and regional councils

Like election costs, the increase in audit fees has disproportionately impacted those councils that can least afford it. For the following 10 councils, audit fees now consume over 1 per cent of their total annual operating revenue¹²:

| Council | Audit fees as percentage of total annual operating revenue |
|------------------|--|
| Central Darling | 2.8% |
| Balranald | 2.5% |
| Brewarrina | 2.4% |
| Bourke | 2.0% |
| Walgett | 1.4% |
| Liverpool Plains | 1.1% |
| Lockhart | 1.1% |
| Cobar | 1.1% |
| Weddin | 1.1% |
| Bland | 1.0% |

Level of service

LGNSW acknowledges that the Audit Office has been on a learning curve as it familiarises itself with councils. As a result, some councils have experienced conflicting advice, delays and late requests for information. Specific examples can be provided.

Worse still, some councils have found themselves being charged for additional time relating to undertaking the audits, the value of such extra time being questionable.

Last year 40 councils were late in submitting their statements, which is an unprecedented number of councils missing the deadline, as well as evidence that the audit process is not operating smoothly and that councils are paying extra under this model.

Overlap with internal audit function

LGNSW also argues that the Audit Office has not sufficiently defined or managed the scope of external audit, having regard to Internal Audit, which is also resulting in increased costs to councils and scope creep.

The NSW Auditor-General and the NSW Government have both emphasised the importance of well-functioning council internal audit functions and council Audit, Risk and Improvement Committees (ARICs). Indeed, councils are now required by the Local Government Act to have ARICs. However, there is little evidence of a coordinated or collaborative approach to planning audits, undertaking audits, sharing data or reliance of findings by the External Audit Team.

As a result, the effective functioning of council internal audit is potentially being compromised by outsourced external audits that are not being coordinated with Internal Audit. Impacts include uncertainty regarding roles and responsibilities between the two functions particularly

¹² For the average council, audit fees consume 0.17% of total annual operating revenue.

with audit planning, audit action follow up and validation of audit recommendations; and potential duplication of audit coverage and reports from both functions – and resultant costs to councils.

Recommendation 8: The NSW Auditor-General should modify its auditing practices to reduce duplication between external and internal audits of councils and avoid unnecessary costs.

Recommendation summary

In summary, LGNSW makes the following recommendations:

NSW Electoral Commission

Recommendation 1: The NSW Government must ensure its \$19.9 million subsidy to the NSWEC for the conduct of the local government elections is transparently accounted for and applied directly to council costs.

Recommendation 2: The NSWEC must not be permitted to increase the costs passed to councils for conducting local government elections by more than the rate peg imposed on councils, and the NSW Government must take this into consideration in adequately funding the NSWEC's Budget.

Recommendation 3: The NSW Government must reverse the Department of Education's massive price increases for hall hire for local government elections

Recommendation 4: The NSW Government must adequately fund the NSWEC to minimise the financial burden on councils and ratepayers and ensure local government elections are conducted efficiently and cost effectively and do not result in inequities between ratepayers and communities in the price of maintaining democracy.

Recommendation 5: The pre-poll voting period should be reduced to one week (Saturday to Friday in the week before election day), for all local government elections whether the election is administered by the NSW Electoral Commission or by a private election services provider.

Recommendation 6: Significant fine revenue from non-voting at local government elections must be used to offset the costs of local government elections, rather than returned to NSW Government consolidated revenue.

Audit Office of NSW

Recommendation 7: The NSW Government should implement, through the Independent Pricing and Regulatory Tribunal, a transparent price determination approach for the cost of audit services, similar to the model used for land valuation services.

Recommendation 8: The NSW Auditor-General should modify its auditing practices to reduce duplication between external and internal audits of councils and avoid unnecessary costs.

* * *

LGNSW would welcome the opportunity to assist with further information during this review to ensure the views of local government are considered.

To discuss this submission further, please contact LGNSW Strategy Manager Damian Thomas