IPART Independent Pricing and Regulatory Tribunal | NSW

Responses to Questions on Notice

Carmel Donnelly PSM, Chair IPART

Inquiry hearing - Ability of local governments to fund infrastructure and services – 17 May 2024

This document provides responses to two questions taken on notice by Carmel Donnelly PSM, Chair of IPART, when appearing before the Standing Committee on State Development on Friday 17 May 2024 for the Inquiry into the ability of local governments to fund infrastructure and services.

Question on notice 1

The CHAIR: How much growth in council revenue per capita has the rate peg methodology allowed for over the last 10 years, would you say?

CARMEL DONNELLY: I am sure we have the answer to that. It might be one that I take on notice and give you some data.

Source: Report on proceedings before Standing Committee on State Development – Inquiry into the ability of local governments to fund infrastructure and services – Uncorrected, 17 May 2024, pp 7-8.

1 How much growth in council revenue per capita has the rate peg methodology allowed for over the last 10 years, would you say?

1.1 Response

We estimate that the rate peg (before the impact of any special variations) would have allowed council revenue per capita to increase by about 28% over the 12-year period from 2010-11 to 2022-23, including from when IPART began setting the rate peg.[a] We also estimate that actual income from rates per capita including the impact of special variations increased by about 54% over the same period.[b] The difference is due to the impact of special variations, which is excluded from our estimate of income from the rate peg but included in actual income from rates.[1] Both measures include income from supplementary valuations.

[a] This reflects the maximum increase in income from the rate peg. We note that councils can choose to increase their rates income by a lower percentage than the rate peg, or not at all. We have included the full duration from when the rate peg function was transferred to IPART by the NSW Government.

[b] We obtained income from rates from the Office of Local Government (OLG) time series data and have estimated the 2022-23 income from rates as this is not yet available. We converted this to income from rates per capita using Australian Bureau of Statistics (ABS) data on estimated residential population by local government area (LGA).

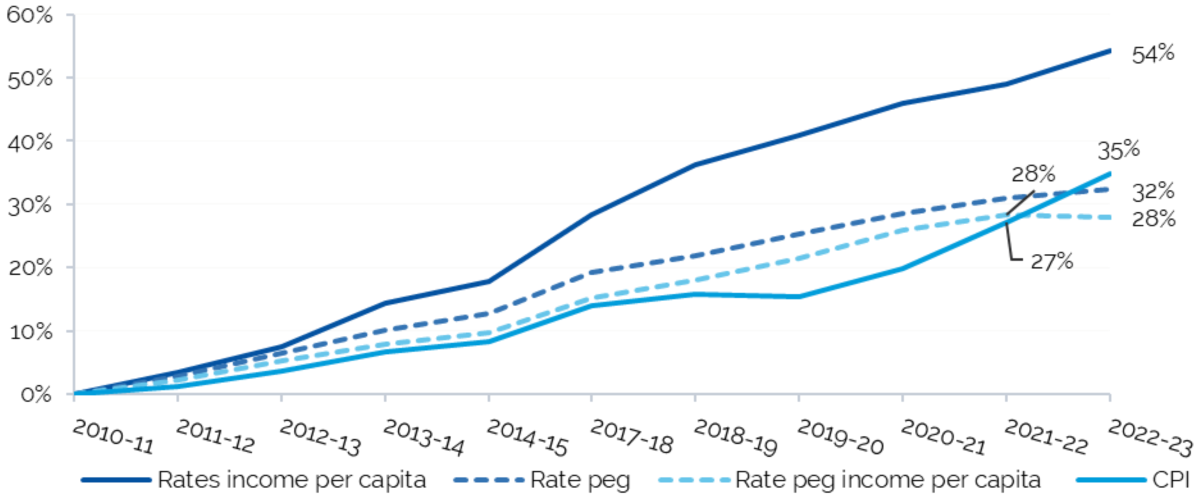
Figure 1 shows that, compared to CPI since 2010-11:

- Until 2021-22, rate peg income per capita allowed by the rate peg (excluding the impact of special rates variations) increased by slightly more (28%) than the increase in CPI (27%).
- In 2022-23 high inflation meant a CPI increase of around 7%[c], however due to the 2-year lag in how the rate peg was calculated at that time, the rate peg only increased by 0.7% (before the population factor).[d] The net effect is that rate peg income per capita (excluding the impact of special rates variations) increased by less than CPI (35%) over the period to 2022-23.
- The increase in income from rates per capita (including the impact of special rates variations) (54%) was more than CPI (35%) over the 12-year period to 2022-23.

Figure 1 also shows that rate peg income per capita (excluding the impact of special rates variations) increased by less than the rate peg (32%) over the period. Until 2021-22, the rate peg did not capture additional increases in costs due to population growth. Councils are partly compensated for higher population growth through higher rates revenue from the supplementary valuations process (see below for more information about supplementary valuations).

Prior to 2021-22 the legislation required us to produce a single rate peg that applied to all councils. In 2022-23, following legislative change in 2021 which allowed for different rate pegs to be set, we introduced the 'population factor'. This factor was designed to allow growth councils to maintain real rates income per capita over time.[2] However, there is a 3-year lag in the population factor methodology. For example, for the 2024-25 population factor we used the change in population over the year to June 2022.[3]

Figure 1 Cumulative percentage increase in per capita rates income and rate peg income[a], 2010-11 to 2022-23



a. Rates income per capita includes the impact of special variations. Rate peg income per capita excludes the impact on rates income of special variations. It estimates what per capita income from rates would have been if rates income had increased by only the rate peg plus supplementary valuations.
Source: Office of Local Government time series data, Australian Bureau of Statistics data on estimated resident population by LGA, and IPART data and analysis.

c This refers to the change in the Sydney CPI over the year to June 2023.
d This in large part led to the changes in our rate peg methodology.

We calculated rate peg income per capita (excluding the impact of special rates variations) by:

- obtaining total income from rates in 2010-11 from the OLG time series data
- increasing that amount by the 2011-12 rate peg then adding the additional income received from supplementary valuations in that year to give total income from the rate peg (excluding the impact of special rates variations) in 2011-12
- repeating the process for each year until 2022-23
- dividing the total rate peg income in each year by the population, using the Australian Bureau of Statistics data on estimated resident population by LGA.

We calculated rates income per capita by dividing actual rates income, obtained from OLG time series data, by the population using ABS data on estimated resident population by LGA. Rates income for 2022-23 is estimated as this information is not yet available. In 2022-23, the rate peg included the population factor. We captured the impact of population factors in the rate peg as a weighted average, weighted by the total income from rates.

Supplementary valuations

Supplementary valuations are additional valuations of land that are issued by the Valuer General NSW, outside the usual 3 to 4-year general valuations cycle, when changes to property are recorded on the Register of Land Values. Supplementary valuations can be due to subdivision, zoning changes or an amendment to land value. Supplementary valuations can result in land values increasing or decreasing, impacting the rates income received for the affected properties. Councils' general income can be reduced where supplementary valuations result in a reduction in rates income or vice versa.[4] Where supplementary valuations lead to an increase, this can increase council rates income above the rate peg. The supplementary valuations process can capture some population growth that results from subdivision and re-zoning which can lead to increases in rates income.

Unlike supplementary valuations, changes in land value in the general valuation cycle do not impact a council's total permissible rates income.[5] The council's total permissible income is limited by the rate peg or a percentage determined by IPART in a special variation. This is why a routine increase in a ratepayer's land value by the Valuer-General does not necessarily mean that a ratepayer's rates will automatically increase. The impact on rates depends on whether the land value has increased or decreased compared to others in the ratepayer's local government area.

Question on notice 2

The Hon. EMMA HURST: I've just got one final question about the special variations. I note in your submission that the majority of those special variations were processed. However, 10 were declined. I'm not asking for any specific details about those specific 10, but I am just wondering what aspects, or what problems, would there be in that application to refuse a special variation?

CARMEL DONNELLY: We look at each one case by case. We get the applications. We publish them. We call for submissions—obviously it's expected that the council will have done its own consultation as well and we take that into account—and then we assess them against criteria that are set by the Office of Local Government. We're looking for evidence of a financial need—which doesn't mean there's financial mismanagement or sustainability, but is there a case for financial need that we can look at?

Is the impact of the rate increase reasonable on ratepayers? So we will look at affordability, we will look at—compared to similar councils, neighbouring councils—the income levels, how many people are pensioners, how many people own their own homes, a number of those factors, and the community feedback. We'll look at what productivity cost containment the council has already done and how well they consulted because we're not required to show that the community supports, but they must have been informed about the need. They must have been accurately informed about the extent—like how large those rate increases that are proposed are.

The short answer is that some councils will not meet those criteria. We'll have gone through a thorough assessment and then we will say, "No, you don't meet the criteria." We may come to the view, as the tribunal, that they might have asked for an increase that's going to go on for five years of continued increases, but they've only shown that the need is there for two. And after that their numbers will be improving, and so we may say, "We'll give it to you partially." We'd be happy to take it on notice if you would like to get a bit more information about the sorts of factors without going into detail about particular councils.

The Hon. EMMA HURST: That would be great.

Source: Report on proceedings before Standing Committee on State Development – Inquiry into the ability of local governments to fund infrastructure and services – Uncorrected, 17 May 2024, p 10.

2 About special variations (SVs)… 10 were declined… what aspects, or what problems, would there be in that application to refuse an SV?

2.1 Response

When elected councillors pass a resolution to increase their general income by an amount greater than the rate peg, they can apply to IPART for a special variation (SV).[e] Councils may also apply to increase the amount of their minimum rate, above the statutory limit,[f] if a minimum rate is in place in their local government area.

[e] If IPART approves an application for a special variation, it will issue an instrument under section 508(2) or 508A of the *Local Government Act 1993* specifying the amount by which the council may increase its general income and the year(s) to which it applies.

[f] IPART assists the Office of Local Government, Minister for Local Government, and the Governor in amending clause 126 of the *Local Government (General) Regulation 2021* each year, which prescribes the maximum minimum amount of a rate. If IPART approves a minimum rate application, it will issue an instrument under section 548(3)(a) of the *Local Government Act 1993* specifying a minimum amount of a rate that is greater than the amount prescribed in the regulations.

In 2010, special variation and minimum rates determinations were delegated to IPART by the then Minister for Local Government.[g]

Special variation assessment

IPART assesses SV applications against the 6 criteria in the guidelines issued by the NSW Office of Local Government (OLG).[h] IPART can approve an SV for a single year or a specified period of 2 or more years, up to 7 years.[i] Over that time, the council can set its own rates as long as its total general income stays within the approved increase.[j]

The criteria for assessing special variation applications include that the council has identified the need and purpose of the special variation, can demonstrate the impact on ratepayers is reasonable, and has provided evidence the community is aware of the need for and extent of the rate rise. Councils are required to actively engage residents in discussions about the proposed increase above the rate peg and can do this with public hearings or other community engagement tools that suit their population.

Of the 198 SV applications received since 2011 (excluding the 86 ASVs in 2022 – see below), 11 applications were declined and 41 SV applications were approved for a lower percentage or fewer number of years than the council applied for.[k] The reasons for these decisions are specific to each individual SV application but were anchored in IPART's assessment of the applications against the OLG criteria.

Some issues identified by IPART which may contribute to an application being declined, or approval of a lower increase than what the council applied for, include:

- Lack of community awareness of the need for and extent of the council's proposed SV. This can include the council not providing ratepayers and the community with sufficient information to enable them to understand what is proposed so they can effectively engage with the council and provide feedback on the proposal.
- Insufficiently establishing a financial need. For instance, if the council's financial performance as presented in its Long-Term Financial Plan meets the prescribed OLG benchmarks, IPART may determine there is not a sufficient financial need for an SV, such as if the council's Operating Performance Ratio (OPR) is significantly above 0% without the SV. IPART may still approve an SV in these circumstances if the council provides evidence that the increase is for a special purpose that cannot be funded without impacting current or planned services and the community is willing to pay for the rates increase.
- Lack of consideration of alternatives to the proposed SV. This can include the council not adequately considering alternative revenue streams or the potential for reductions in its costs that may eliminate the need for the SV or reduce the size of the SV needed.

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[g] The Minister for Local Government has delegated to IPART the power to grant SVs. By delegation dated 6 September 2010, the then Minister for Local Government delegated to the Tribunal the Minister's functions under sections 506, 507, 508(2), 508(6), 508(7), 508A, 548(3) and 548(8) of the *Local Government Act 1993 (NSW)*, pursuant to section 744 of that Act.

[h] The NSW Office of Local Government may update these criteria and they may not always be identical from year to year. The most recent criteria was published in 2020.

[i] This does not prevent councils from applying for, or IPART approving, a special variation that takes effect immediately after a 7-year period.

[j] An SV allows a council to increase its general income above the rate peg and can be temporary or permanent. For a temporary SV, the impact of the SV will be removed from the council's rate base once the temporary period expires.

[k] Each of the special variation applications that IPART has received and assessed can be found on the IPART website. The final determinations detail the reasoning for the decision.

- A failure to adequately demonstrate the impact of the proposed SV is reasonable. This may include not considering the impact on some of the affected ratepayer categories, or on particularly vulnerable groups within the community, or not sufficiently taking into account the extent of the impact on affected ratepayers in considering whether it is reasonable.
- Not identifying and detailing the need for the SV in the Integrated Planning and Reporting (IP&R) documents. This can include omitting the proposed SV from the relevant IP&R documents, or shortcomings with the quality of information in key documents such as the Long-Term Financial Plan.

Additional special variations (ASV) process

In 2022 (for the 2022-23 financial year) there was a one off 'additional special variations' process.[l] This was in response to the 2022-23 rate peg being set at 0.7% (excluding population growth factors).[6] The rate peg for the 2022-23 financial year was determined after the low inflation environment at the beginning of the COVID-19 pandemic. However, the following period of high inflation and global uncertainty increased councils' costs. Some councils demonstrated that without additional funds they would not be able to deliver the projects they had already consulted on and included in their budgets.

The additional special variation process gave councils an opportunity to apply to increase their rates above the level of the rate peg for 2022-23, to a maximum of 2.5%. A separate process and criteria for assessing these additional special variations were developed by the NSW Office of Local Government.

IPART approved applications by 86 NSW councils to increase their rates above the level of the annual rate peg through this process.[7]

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1 Office of Local Government, Time Series data, accessed 23 May 2024 & IPART analysis.
2 IPART, Review of the rate peg to include population growth – Final report, September 2021.
3 IPART, Information Paper – Rate peg for NSW councils for 2024-25, November 2023, pp 7-8.
4 IPART, Review of the rate peg to include population growth – Final report, September 2021, pp. 65-66.
5 IPART, Review of the rate peg methodology – Final Report, November 2023, p 26.
6 IPART, Review of the rate peg methodology – Final Report, November 2023, p 117.
7 IPART, NSW councils increase rates – Media Release, June 2022.

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l Applications for an additional special variation are assessed against guidelines provided by the NSW Office of Local Government.