Submission No 20

INQUIRY INTO ABILITY OF LOCAL GOVERNMENTS TO FUND INFRASTRUCTURE AND SERVICES

Organisation: NSW Revenue Professionals

Date Received: 24 April 2024

C/- Mr A Butcher
President NSW Revenue Professionals

24 April 2024

Inquiry into the ability of local governments to fund
Infrastructure and services
Standing Committee on State Development
6 Macquarie Street
SYDNEY NSW 2000

Dear Committee members

Submission - Inquiry into the ability of local governments to fund infrastructure and services

Thank you for the opportunity to make this submission on behalf of the NSW Revenue Professionals Inc. (NSWRP).

The NSWRP is the peak body of NSW Local Government revenue employees and was formed to:

- unite in a common organisation, those Local Government employees who are engaged in rating and revenue functions.
- improve and elevate the technical and general knowledge of Local Government employees who are engaged in rating and revenue functions.
- distribute amongst its members, and the regional NSWRP groups, information on all matters affecting or pertaining to the profession of rating and revenue management within Local Government by way of meetings, newsletters, conferences, or any other method available to the Committee.
- promote a professional image of Rating and Revenue practitioners in Local Government New South Wales
- promote quality services to Local Government in New South Wales through the dissemination of best practice.
- encourage members to keep up to date with finance related activities and legislative changes through continuing professional development.
- identify the skills and knowledge needed by employees and facilitate training and education.
- make the expertise of members available to professional bodies and government departments as required.

It is our view that the terms of reference are quite broad making it difficult to prepare a targeted specific response, we have prepared our submission based on previous reviews and the experiences of practitioners in the rates and revenue sector of local government. We have not applied any specific council-based scenarios, we have relied upon information available to us in the public domain and the technical skills and knowledge of our members.

This review has nuances to numerous reviews conducted in the past, one of which aligns very well with the Committee Chair for this review who stated;

> *'This inquiry will examine the level of income councils require to adequately meet the needs of their communities, and give consideration to the current levels of service delivery and financial sustainability in local government.'*[1]

Similarly, the terms of reference for the Commissioners Inquiry into Rating and Taxation by Local Government in NSW in 1989 were;

> *'To review the rating and other revenue powers and resources available to local government in NSW to finance the services for which councils are responsible, and report on the changes, if any, which are necessary to enable councils to provide those services more effectively.'*[2]

What we have learned from these past reviews is that recommendations for improvements are often overlooked and keep recurring in subsequent reviews that target the same issues.

The most prevalent of recent reforms have been in the Revitalising Local Government review conducted in 2013 and the Independent Pricing and Regulatory Tribunal (IPART) report December 2016. Of the five terms of reference in the Revitalising Local Government review three align with the current inquiry's terms, one aligns with the 2015 terms of reference provided to IPART.

One of the most important and powerful tools available to local communities is the Integrated Planning and Reporting (IP&R) framework. The suit of IP&R documents encourages participation and involvement in the way works, services, facilities, and activities are funded should replace the government's rate pegging policy.

Councils have revenue raising issues not to dissimilar to other levels of government. We note that the state is currently concerned about the distribution of GST revenue resulting in a $11.9 billion over the next four years. NSW Treasurer Daniel Mookhey warned there will be spending cuts but not to "must-have" policies to help with the cost of living.

Similarly, local councils budget annually by determining their expected revenue against expenditure to achieve a balanced budget. Shortfalls result in similar spending cuts, however with no significant alternative sources of revenue, either land rates need to increase cuts in expenditure are needed to achieve a balanced budget.

---

[1] Media Release - State Development - Local Governments - 18 March 2024

2 Report of the Committee of Inquiry into Local Government Rating and other revenue powers and resources – April 1990

Submission

1. The level of income councils require to adequately meet the needs of their communities

This will vary from council to council and be significantly impacted by the council's ability to charge user fees and its rate base. Other influences such as the ongoing maintenance of regional facilities and natural disasters or significant upswings in operating costs will result in income being short of the expenditure need.

It is a requirement under Section 8A(1)(c) and 8A(1)(d) that councils;

- *should plan strategically, using the integrated planning and reporting framework, for the provision of effective and efficient services and regulation to meet the diverse needs of the local community*
- *apply the integrated planning and reporting framework in carrying out their functions so as to achieve desired outcomes and continuous improvements.*

Furthermore, Section 8A(3) requires each council to, actively engage with their local communities, through the use of the integrated planning and reporting framework and other measures, and that spending should be responsible and sustainable, aligning general revenue and expenses (section 8(B)).

The IP&R framework is mandatory and provides the pathway for each council to reach the level of income required to adequately meet the needs of their community. However, income is restricted to the amount of the rate peg which restricts the flexibility and agile decision making that can only be overcome by a protracted and costly special variation process.

The IP&R framework begins with the community's, not councils, aspirations for a period of at least 10 years. The Office of Local Government (OLG) says the IP&R framework '*includes a suite of integrated plans that set out a vision and goals and strategic actions to achieve them. It involves a reporting structure to communicate progress to council and the community as well as a structured timeline for review to ensure the goals and actions are still relevant.*'[3]

The IP&R framework is a powerful tool for the community to have greater access to decision making and visibility of the outcomes that they identify as their main priorities and aspirations for the future and for councils to plan strategies to achieve these goals. We would like to see stronger ties to the objectives of the IP&R framework so that sufficient resources, time, money, assets and people are available to actually meet on balance ratepayer expectations.

The Resourcing Strategy for each council provides public visibility of the council spend, the document must include three components;

- Long term financial plan (10years)
- Workforce management plan, and
- Asset management plan.

[3] Office of Local Government – website https://www.olg.nsw.gov.au/councils/integrated-planning-and-reporting/

The Resourcing Strategy is the point where the council explains to its community how it intends to perform all of its functions, including implementing the strategies set out in the Community Strategic Plan.[4]

For a council to meet the requirements of the Local Government Act and align general revenue and expenses decisions will need to be made on how this can be achieved, the following represents those options.

- Apply for a special variation to increase revenue from land rates,
- Find savings in efficiencies or business improvement,
- Cut services,
- Reduce the spend on infrastructure maintenance.

User fees and charges are another avenue to raise revenue, many of which are regulated (planning) and others are often subsidised fees for community facilities or activities.

An emerging concern for local government is the Build to Rent (BTR) housing strategy. BTR housing is large-scale, purpose-built rental housing that is held in single ownership and professionally managed. The consequence of single ownership is a single rate assessment rather than separate rate assessments for each residential apartment/dwelling.

Developments of this nature thereby result in significant losses in land rates and will impact the ability of councils to fund their growing communities. This is despite the NSW Government supporting the IPART recommendation that councils land rates increase as their communities grow which has manifested into the population growth factor.

In the case of land rates, the amount calculated on the unimproved land value (ULV) is significantly less than what it would be under a strata division. In addition, the uplift in ULV is not recognised until the next general valuation cycle, meaning that a change will be diluted with other changes in the cyclical movement from one base date to the next and there will no one off uplift based on the change in carrying capacity.

Losses in revenue can be substantial and has the potential to exceed estimates of around $500,000 per annum in land rates, dependent on the size of the development.

The population factor should realise a higher percentage in the rate peg when residents move into BTR developments. However, this will simply result in rate increases for non BTR ratepayers and not achieve the population growth factor outcome the factor is designed to achieve.

According to IPART, 'As local communities grow, councils need to provide additional services to meet the demand of their residents and businesses. Allowing rates to keep pace with population growth enhances councils' ability to provide services and improves their financial sustainability. In response to a request from the NSW Government we have recommended a methodology that enables councils to maintain per capita general income over time as their populations grow. Maintaining per capita general income will help councils to maintain existing service levels and provide the services their growing communities expect.'[5]

---

[4] Office of Local Government Integrated Reporting and Planning guidelines September 2021 page 16
5 IPART Review of the rate peg to include population growth, September 2021 page 1

With BTR developments resulting in a high number of residents concentrated on land with a disproportionately low land value the revenue uplift will result in the remaining community paying higher rates.

In the case for waste collection charges, council may only raise a single domestic waste management charge on each rateable parcel of land and we are concerned with the charging for domestic waste management on sites with 150+ units and potentially >300 people and only one domestic waste management can be raised.

2. Examine if past rate pegs have matched increases in costs borne by local governments

The IPART found in its Review of rate peg methodology that council's costs have aligned with their revenue and concluded that this was because '*It is also possible that councils have referred to the rate peg when setting their budgets and planning their expenditure, which would explain why councils' total expenses per capita and the rate peg have grown at a similar rate.*'[6] This process aligns with the guiding principles for local government under the Local Government Act 1993, that is to align general revenue and expenses.

Further evidence that the rate peg has not kept pace with increased costs borne by local governments based on the number of applications for a special variation. Since the current Local Government Act commenced in 1993 there have been 876 applications approved for a special variation out of nearly 1,200 applications made, these numbers indicate that the statutory peg is not fit for purpose and has not matched increases in costs.

Recently there have been two reviews undertaken by the IPART and the impact of these has not yet been fully realised:

- Review of the rate peg to include population growth – October 2021
- Review of the rate peg methodology – August 2023

3. Current levels of service delivery and financial sustainability in local government, including the impact of cost shifting on service delivery and financial sustainability, and whether this has changed over time.

Even now that this inquiry has commenced the NSW Government is set to impose a tax on every burial and cremation carried out. Councils will have no choice other than to pass the additional expense onto grieving families, increasing the costs of burials and cremations at what is an already very challenging time and for no benefit.

An annual cost shifting survey conducted by Local Government NSW (LGNSW) has identified that '*cost shifting onto local government remains one of the most significant challenges facing NSW councils today. The unrelenting growth of cost shifting to councils is increasingly eroding any possibility*

6 IPART Review of rate peg methodology, September 2022 page 13

of financially sustainable local government and risking the capacity of councils to both deliver tailored, grassroots services to their communities and properly maintain vital local infrastructure.

Alarmingly, the latest research commissioned by LGNSW shows that the increase in cost shifting has been accelerated by various NSW Government policies.'[7]

In the latest cost shifting survey which based on 2021-22 data '*LGNSW Cost Shifting Report – How State Costs Eat Council Rates*' has identified the most significant examples of cost shifting as:

1. The waste levy - $288.2 million.
2. The cost of rate exemptions, that are redistributed and passed onto other ratepayers - $273.1 million.
3. State and Federal levels of government implementation or increases in regulatory requirements through legislation that is then administered by local government - $208 million.
4. The Emergency Services Levy - $165.4 million.
5. Local Libraries, the original commitment from State Government was to fund 50 per cent of libraries cost, it now covers approximately 8 per cent of the total costs - $156.7 million
6. The NSW Government's, mandatory pensioner rebates - $55.2 million.

The report goes on to say that '*The 2021–22 Cost Shifting Survey has revealed that cost shifting totalled $1.36 billion in 2021–22' 'far exceeding historical records and representing an increase of $540 million since the Cost Shifting Survey was last carried out in 2017–18.'*[8]

The survey has identified the additional cost to each ratepayer in the council classifications as between $420.90 and $590.80 per annum:

Fig 1 LGNSW Cost Shifting 2023: How State Costs Eat Council Rates Report Summary and Highlights – November 2023

Accordingly cost shifting is reducing the ability of councils to provide services to their communities and to be sustainable in their approach.

4. Assess the social and economic impacts of the rate peg in New South Wales for ratepayers, councils, and council staff over the last 20 years and compare with other jurisdictions.

We do not have access to data to respond to the social impacts of the rate peg.

7 Local Government NSW Cost Shifting 2023: How State Costs Eat Council Rates Report Summary and Highlights November 2023
8 Local Government NSW Cost Shifting 2023: How State Costs Eat Council Rates Report Summary and Highlights November 2023

Previous inquiries have noted the heavy demands placed on local councils to fund infrastructure and financial sustainability. The NSW Treasury Corporation (TCorp) report *Financial Sustainability of the New South Wales Local Government Sector*[9] reported a number of key findings from the 152 of the councils surveyed, these included the following.

- Operating deficits are unsustainable – only one third of councils in 2012 reported an operating surplus. Over the period 2009 to 2012, the cumulative operating deficit of NSW councils totalled $1 billion.
- The total infrastructure backlog of NSW councils had reached $7.2 billion by 2012.
- Financial sustainability is deteriorating with nearly 50% of councils' financial outlook likely to be rated 'weak' or lower by 2016-17.
- A large asset maintenance gap exists within the sector with a $389 million deficit in 2012 alone.
- Councils need to start consulting their communities about ways to either increase revenue, lower existing service levels and or standards, and pursue efficiency savings.

Based on the findings from its review into the financial assessment and sustainability of the local government, one of TCorp's recommendations was for rate increases that meet underlying costs of delivering services. TCorp went on to say '*Where a decision by Council is made to increases rates and charges at a lower than required factor, the impacts of such actions must be clear in the context of each Council's sustainability*'.

We do not believe in the philosophy of unnecessary rate increases. Political pressure to keep land rates low achieves only one result, poor outcomes for the community. Local councils strive to provide the best possible works, services, facilities and infrastructure to their communities and political decisions at both the local and state level to keep land rates low and running with a vernacular of protection is fictitious at best.

NSW councils adhere to strict IP&R frameworks that require extensive community consultation that allows for intervention by the community and mandates numerous consultation steps. It is important to note that the IP&R framework was not in place when rate pegging/capping was introduced in 1977 yet the NSW Government has made no concessions to allow the ratepayers of NSW more choices in how the community can be better funded.

5. Compare the rate peg as it currently exists to alternative approaches with regards to the outcomes for ratepayers, councils, and council staff.

Recently there have been two reviews undertaken by the IPART and the impact of these has not yet been fully realised:

- Review of the rate peg to include population growth – October 2021
- Review of the rate peg methodology – August 2023

[9] NSW Treasury Corporation (TCorp) report Financial Sustainability of the New South Wales Local Government Sector April 2013

The rate peg has included a population growth factor since 2022-23 made on a council by council basis. The population factor is calculated as the change in residential population less any increase in general revenue from supplementary valuations. Not all councils receive a population growth factor, in 2022-23 there were 81 of the 128 NSW councils that received a population growth factor of 0%, in 2023-24 there were 87 and for 2024-25 there are 79.

We maintain our position in regards to population growth aligning with the original IPART recommendation in the Review of the Local Government Rating System for a transition to Capital Improved Values (CIV) as a mechanism to allow councils revenue to grow as the communities they serve grow.

We believe that this should be revisited for the reasons outlined below.

CIV is efficient:

- Easily understood, landowners are more likely to know the value of their 'property' than the value of the land that their house sits on.
- The Premier requested IPART review the rating system to be 'easily understood'. The IPART delivered on this in the 2016 Review.
- High values contribute more, low land values contribute less.

CIV enables immediate effect due to population growth:

- Councils receive supplementary rate income and grow as they do now due to subdivisions;
  - Growth in vacant land (same as now) = uplift in rates
  - Growth in value once building complete = uplift in rates
- Minimal lag between subdivision (new plan) and rate income
- Rates are paid as growth occurs.
- Minor growth due to increased capacity (e.g. secondary dwellings) is identified.

The review of the rate peg methodology undertaken by the IPART has resulted in further changes that affect the peg from 2024-25. According to the IPART "*The new methodology we have applied will better account for the diversity among NSW councils and help ensure ratepayers contribute only to costs relevant to their local government area.*" "*These rate pegs are based on employee cost increases, forecast inflation and council-specific changes in Emergency Services Levy contributions and population growth*."[10] The new peg is forward facing and now accounts for any changes in contributions for the Emergency Services Levy (ESL) from one year to the next.

6. Review the operation of the special rate variation process and its effectiveness in providing the level of income Councils require to adequately meet the needs of their communities.

Historically it is dependent on the rate base the council had when rate pegging was introduced and what that council has implemented since. Following on from the NSW Governments 'Fit for the Future' investigation many councils found it necessary to apply for significant rate increases to

[10] IPART Media Release Rate peg set for 2024-25 - 21 November 2023

remain sustainable. This situation leads to injustices in intergenerational equity as the current and future ratepayers are paying for mistakes by preceding councils by not raising the appropriate fair and equitable land rates.

Smaller and more frequent rate increases that align with the need to fund essential services and infrastructure should be permitted outside of the onerous and often politically sensitive Special Variation process. The Revitalising Local Government review said '*The Panel can find no evidence from experience in other states, or from the pattern and content of submissions for Special Rate Variations, to suggest that councils would subject their ratepayers to grossly excessive or unreasonable imposts if rate-pegging were relaxed.*'[11] The panel went on to recommend that rate pegging transition to a streamlined approach by quoting advice from the IPART for, '*increased flexibility for councils to set rates within a margin of 3% above the rate-pegging limit.*'[12] However, '*the Panel considers that a margin of up to 5% would be more realistic where councils need to make significant short-medium term inroads into infrastructure backlogs and correct operating deficits.*'[13]

Essentially, instances of kicking the can down the road for future generations to deal with should be discontinued and council infrastructure backlogs greater than 2% should be encouraged to increase their rate base to bring the ratio back to <2% in a period determined by the IPART. The IPART would need to consider the impact and capacity of the community and any other efficiency savings that might be available to the council.

To put this in perspective the amount of any shortfall in rates levied in a particular year has a compounding effect on future years, this occurs due to the way in which the Permissible Income calculation is determined. By way of an example, if the amount that a council needs to fund its expenditure from rates is short by say $1million the starting point for their permissible income in year 2 will be short $1million plus any amount of the peg for that year. Therefore, if the peg was 5% the council would be $1,050,000 behind in the first year and over a period of ten years this number (assuming 5%pa peg) will exceed $11.5million and give rise to the absolute need for a special variation.

7. Any other related matters.

- Capital Improved Values. We maintain our position in regard to population growth aligning with the original IPART recommendation in the Review of the Local Government Rating System. Capital Improved Values (CIV) provide a pathway for growth due to the uplift from vacant land to occupied land facilitating the population growth outcomes without the need for the IPART factor each year. The IPART proposed mechanism allows each councils revenue to grow as the communities they serve grow through the uplift in land value from vacant to built land.

  CIV is better understood by the community.

[11] Revitalising Local Government - Final Report of the NSW Independent Local Government Review Panel October 2013 page 42
[12] Revitalising Local Government - Final Report of the NSW Independent Local Government Review Panel October 2013 page 44
[13] Revitalising Local Government - Final Report of the NSW Independent Local Government Review Panel October 2013 page 44

- Exemptions
    - Community Housing Providers – should not be exempt from land rates, the residents are users of council provided works, services, facilities and activities.
    - Aged Care and retirement villages run by Public Benevolent Institutions - should not be exempt from land rates, the residents are users of council provided works, services, facilities and activities.
    - All land used for Residential or Commercial purposes should not be exempt. This concept had been raised in numerous inquiries and reports.
    - Affect on funding and budgeting – large exemptions. The legislation allows an exemption to apply pro-rata as a proportion to the period of eligibility. In some cases land valued many millions of dollars could be purchased and become exempt during the current year, without any advanced notice. If exempt the council will need to abandon the rates levied having a direct impact on the current budget.
    - State Forestry – should not be exempt from land rates.
- Pension Rebate Concessions – social welfare is the responsibility of state and federal governments and full funding of the rebate scheme should not be a responsibility of local governments. The amount written off by councils should be discontinued and fully funded by the NSW government.
- Emergency Services Levy – The NSW Government is currently in the process of considering reforms to the ESL. A consultation paper 'Reforming the emergency services funding system' was released on 10 April 2024 with submissions closing 22 May 2024. Local councils are required to contribute 11.7% of the costs to run Fire and Rescue NSW, Rural Fire Services and State Emergency Services each year, collectively contributing $220 million. It is recommended that the state government remove the council contributions and instead manage collections through Revenue NSW as recommended by the *Portfolio Committee No. 4 – Legal Affairs Fire and Emergency Services Levy November 2018*.

Thank you for the opportunity to make this submission, if you have any questions regarding our submission please do not hesitate to be in touch.

Yours faithfully

Andrew Butcher
President NSW Revenue Professionals