Submission
No 55

INQUIRY INTO ABILITY OF LOCAL GOVERNMENTS TO FUND INFRASTRUCTURE AND SERVICES

Organisation: Tamworth Regional Council

Date Received: 26 April 2024

All correspondence should be addressed to the General Manager

The Director
Standing Committee on State Development
Parliament House, Macquarie Street,
Sydney, NSW 2000

Dear Sir/Madam

ABILITY OF LOCAL GOVERNMENT TO FUND INFRASTRUCTURE AND SERVICES

On behalf of Tamworth Regional Council thank you for the opportunity to make a submission to the inquiry into the ability of local government to fund infrastructure and services.

Council's submission follows.

Please contact the undersigned should you wish to discuss this matter further.

Yours faithfully

Rami Abu-Shaqra
Chief Financial Officer

26 April 2024

Tamworth REGIONAL COUNCIL

All correspondence should be addressed to the General Manager

Tamworth Regional Council

Submission to the NSW Legislative Council's Standing Committee on State Development

Ability of local government to fund infrastructure and services.

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1 Council Background

Tamworth Regional Council (Council) is located in the New England Region of New South Wales. The local government area (LGA) is bounded by Gwydir Shire in the north, Uralla Shire and the Walcha Council areas in the east, Upper Hunter Shire in the south, and Liverpool Plains, Gunnedah and Narrabri Shires in the west.

The Council LGA incorporates an area of 9,893 km², including the surrounding towns and villages of Nundle, Manilla, Barraba, Bendemeer and Kootingal. The current population of the LGA is approximately 65,000 and projected population growth is around 1.2% pa. The Tamworth region Gross Regional Product is estimated at more than $3.7 billion, which represents approximately 0.55% of the state's Gross State Product.

Council financial affairs are managed through the Consolidated Fund (CF). However, and for the purposes of this submission, we will focus our analysis and responses on the General Fund (GF). The General Fund refers to all Council activities within the CF other than water and sewer funds. Water and sewer were excluded as they are run on a commercial basis and their revenue streams are not as heavily regulated as the General Fund which supports most of Council's community related services. Our key challenge is to ensure that the General Fund is financially sustainable and generates enough revenues to address all operational and growth agenda of Council and community.

The financial performance of Council's General Fund for the last few years was as follows:

Table 1 Tamworth Regional Council's select indicators of GF financial performance[1]

	2018/19	2019/20	2020/21	2021/22	2022/23
Rates & Annual Charges	44,619	44,451	47,329	49,436	52,435
User Charges & Fees	28,427	22,769	22,514	23,919	32,993
Other Revenues	3,345	1,690	2,136	2,636	3,270
Grants & Contributions - Operating	19,081	21,965	24,729	29,714	38,243
Grants & Contributions - Capital	31,420	31,137	30,831	43,235	39,542
Interest & Investment Revenue	2,347	890	625	754	3,117
Other Income	0	2,834	2,462	2,138	1,742
Total Income from Continuing Operations	**129,239**	**125,736**	**130,626**	**151,832**	**171,342**
Employee Benefits & On-costs	43,710	44,088	44,713	47,419	52,135
Materials & Services	23,971	17,068	25,386	33,554	46,124
Borrowing Costs	2,070	1,610	1,951	1,625	1,840
Depreciation & Amortisation	22,388	24,798	25,997	26,968	32,377
Other Expenses	11,109	11,270	9,077	1,114	12,174
Total Expenses from Continuing Operations	**103,248**	**98,834**	**107,124**	**110,680**	**144,650**
Net Operating Result	25,991	26,902	23,502	41,152	26,692
Net Operating Result before Capital Income	**(5,429)**	**(4,235)**	**(7,329)**	**(2,083)**	**(12,850)**

	2018/19	2019/20	2020/21	2021/22	2022/23
Total Assets	**1,140,106**	**1,393,683**	**1,463,266**	**1,610,741**	**1,818,875**
Operating Performance Ratio	0.66%	-1.87%	2.79%	-1.33%	-1.38%
Own source operating ratio	60.25%	57.67%	57.01%	51.33%	55.07%

[1] *Financial Reporting | Tamworth Regional Council (nsw.gov.au)*

As Table 1 shows, Council's financial situation in recent years was one of relatively persistent deficits. This is a result of modest increases in revenue due to regulated charges and recent economic climate whilst cost of doing business witnessed exponential increases due to labour shortages, supply chain disruptions, climate change extreme events and double-digit increases in cost of material and contractors.

In the following sections, we will be addressing, albeit briefly, all of the terms of reference of the Inquiry. We will highlight our key issues and proposed solutions. We will not however be in a position to give evidence at a hearing.

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

A financially sustainable Council is one that has the ability to fund ongoing service delivery and the renewal and replacement of assets, while ensuring sustainable funding sources. A key indicator for this is a **positive** net operating result before capital grants and contributions. A focus on achieving a positive or surplus result will enable Council to adopt capital programs and asset management plans, sustainable organisational structures and annual budgets within a prudent long-term financial framework. Longer term economic modelling is critical to the success of meeting the needs of the community it serves. Council has established the following financial objectives and strategies to ensure its continuing sustainability:

- maintain service levels where possible and fund other recurrent obligations such as loan repayments, plant replacement and employee leave entitlements;
- pursue strategic management objectives identified in the Community Strategic Plan;
- preserve the investment of the community in the many assets to which Council is custodian; and
- protect itself against financial setbacks, and where possible, unknown contingencies.

Tamworth Regional Council's approach to improved financial sustainability includes a continuous review of its efficiency and effectiveness and catering for what Council "can do" in keeping with the overall aim of fiscal responsibility. However, the constraints on Council's ability to raise general fund income and limited recurrent government funding, combined with inflationary pressures on the costs of labour, plant and materials, are so significant that they are potentially leading to:

- a widening gap between the amount of funding needed and the amount of funding available for the maintenance and renewal of assets; and
- a lack of capacity to provide new facilities or increase current service levels without a consideration for offsets or funding options.

Council needs to balance these financial responsibilities with the various desires of the community to ensure the maximum benefit is returned from resource allocation. Unfortunately, many factors impacting Council's ability to adequately address the needs and aspiration of its community are not within Council's control. This is prevalent in Council's ability (or inability for that matter) to raise enough funds for regulated and community services (i.e. Community Service Obligations). This is where government grants are expected to come and bridge the gap.

For us, the grants (both capital and operational) represent 40 – 45% of our total revenue. The issues we face in this type of revenue source are as follows:

- Capital grants are hard to project and plan for. Sourcing them requires extensive work for engagements and studies where the outcome is not guaranteed. They usually require co-funding and always come with no life-cycle costing support. The latter is critical to support the assets management program of community assets (like libraries or community halls) or any other assets that are not commercial in nature. In other words, more often than not we create more liabilities, not assets, by utilising those grants.

- Operational grants, while predictable, is not keeping pace with real inflation and growth. In our case, we have received a Federal Assistance Grant (FAG) of circa $10m in 2011/12, being 11.7% of our total revenue at that year, when our total assets were $966m and our expenses were $87m. In 2022/23, we received circa $12m, being 7% of our total revenue of the same year when our total assets were $1.8b and our expenses were $145m. In other words, FAG's Compound Annual Growth Rate (CAGR) during the period from 2011/12 to 2022/23 was 1.65% YoY when our assets grew by 5.9% YoY and our expenses grew by 4.7% YoY during the same period. Interesting to know that over the ten years from 2009 to 2019, our FAG has increased by 14.6%. During the same period, the overall inflation rate, measured by the CPI, has increased by 23.4% (Australia's cost of living over the last decade – Parliament of Australia (aph.gov.au).

- Contributions made by developers are heavily regulated and their use is restricted. Often Council faces the inevitable of spending on infrastructure projects years after the collection of those funds when the cost originally estimated to complete the work is no longer valid and prices have moved up significantly; placing increasing pressure on council's other reserves to bridge the gap.

Other sources of income are highly dependent on economic activities (i.e. User charges and fees) or the economic climate (i.e. interest and investment revenue). During COVID, our Council took a big hit on those sources of revenue and was required at the same time to step up its support to rate payers facing financial hardship in paying their dues to Council and address the extreme weather conditions that took its toll on our infrastructure and our economic recovery. Some welcomed emergency grants came as a relief but that was a temporarily measure and is not expected to have a long and lasting impact.

3 Examine if past rate pegs have matched increases in costs borne by local governments:

During the decade up to the COVID year of 2020/21, our analysis shows that the rate peg was aligned with the inflation which was modest and to a large extent, within the RBA's range of 2 – 3%. The only issue there was that we were not been able to build enough reserves for assets renewal program as rate peg was barely allowing us to recover the increases of cost of doing business. From that year onwards however, the financial gap between what we were able to raise and the rise of cost started to widen as follows:

Table 2 Tamworth Regional Council's cost increases compared to rate peg and CPI

	2019/20	2020/21	2021/22	2022/23
Rate Peg[1]	2.70%	2.60%	2.00%	3.70%
CPI - 12 months to June[2]	-0.30%	3.80%	6.10%	6.00%
Tamworth Regional Council – % increase in GF Employee cost[3]	0.86%	1.42%	6.05%	9.95%
Tamworth Regional Council – % increase in GF Materials & Services[3]	-28.80%	48.73%	32.18%	37.46%

[1] *The rate peg | IPART (nsw.gov.au)*
[2] *Consumer Price Index, Australia, December Quarter 2023 | Australian Bureau of Statistics (abs.gov.au)*
[3] *extracted and calculated from Financial Reporting | Tamworth Regional Council (nsw.gov.au)*

- Some of the increases in the employee cost and materials are due to the increase of volume of work which required hiring extra staff and procuring more material and contractors. However, a big part of it is due to rate or price increases. In 2023/24. we have applied the NSW Award increases of payroll of 4.5% in 2023/24. Contractors and services providers have increased their prices way above the average CPI. For example, bitumen resealing (for road maintenance) contract rates have increased by 50% during the above period. The cost of bridge replacement contracts has increased from $6,000/m² in 2019 to $18,000/m² for most recent contracts.

- Clearly past rate pegs were no near the true increases in cost of providing critical services to community.

- On the other hand, disperse communities in regional and rural areas should not be expected to have the capacity to sustain huge rate increases to fund the ever-increasing cost of managing and maintaining a vast regional area without support from other tiers of government. This is another reason why we believe rate peg alone will not fix the financial sustainability question of regional and rural councils.

4 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

In year 2021/22, Council has made the following payments, net of any government subsidies:
(*Note: assumptions were made to arrive at some of those numbers*)

- Public library operations: $2.5m (subsidies represent 8% of gross amount)

- Emergency Services Levy: $757K (subsidies represent 35% of gross amount)

- Mandatory pensioner rate rebate: $824K (subsidies represent 55% of gross amount)

- Government and non-government owned property rate exemptions: $1.9m

- Other services (e.g. companion animals, Development applications, noxious weeds, crime prevention, RFS, protection of environment ..etc.): $1.8m (being cost of service less any related revenue, e.g. fees, state government grants or subsidies)

The above totals to approximately $7.8m, which was fully funded from our General Fund. This is 16% of our Rate and Annual Charges for the General Fund in 2021/22. Our General Fund's Net Operating Result before Capital grants and contributions for the same year was a deficit of $2m. Some years are better than this and some other years are worse, that is another problem of not being able to plan our service delivery program in the constantly changing government policies and budget allocations to local government.

Notwithstanding the varying government support year on year, there seem to be a trend where cost shifting is getting worse. For example, for the Water Fund, the NSW Government introduced pensioner rebates and initially paid the full cost of the rebates. Whilst the NSW Government still requires Councils like us to pay pensioner rebates, the level of subsidy provided by the government has fallen significantly.

From the above we conclude that the impact on cost shifting on the financial sustainability of our Council cannot be underestimated.

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

In August 2023, Independent Pricing and Regulatory Tribunal (IPART) has issued the final report on the "*Review of the rate peg methodology*". Having consulted with ratepayers, councillors, council staff and other stakeholders across NSW about council rates, IPART came back with recommendations to develop, among other things, a new methodology to allow councils vary their general income annually to reflect changes in the cost of providing local government services. The rate peg of 2024/25 of 4.9% is a welcomed step in applying this new methodology.

Tamworth Regional Council has detailed its position during the consultation phase of this review. In summary, we are in favour of a rate peg that is forward looking and considers population decreases (not just increases). We also believe that reducing the rate peg by a % of productivity disincentivises innovation and penalises councils for efficiency gains and should be removed. Finally, we believe that NSW councils, under the strict IP&R frameworks that require extensive community consultation that allows for intervention by the community and mandates numerous consultation steps, should be granted flexibility in deviating from the announced rate peg to address their unique situation and locality.

It is early for us to judge whether or not the new approach will mark the beginning of a "fit for purpose" rate peg but for many councils, including ours, this will not fix past mismatches. Therefore, we have applied for a Special Rate Variation (SRV) for the coming two years.

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

On 5 February 2024, Council has submitted an application before IPART for a cumulative permanent Special Rate Variation (SRV) increase of 36.3 per cent over two years commencing in the 2024/2025 financial year. This application was resolved by Council in its meeting on 28 November 2023 following an extensive community consultation from 13 September to 31 October 2023.

Throughout the consultation period, Councillors and Council staff explained to the community the need for this SRV to support the long-term financial sustainability of Council in delivering its current level of community services. Please refer to our application here.

Council also explained to the community the alternative options to SRV. Finding savings and implementing cost containment measures are now running out of steam and short of SRV, Council will be in a position to consider reduced levels of services to balance its budget.

The whole process was demanding and took its toll on Councillors and Council staff. Council has to procure the services of a specialised consultant to assist in addressing the stringent and complex criteria of IPART before applying. This is an unavoidable extra cost just to ensure that Council complies with IPART's requirements. Staff was also heavily involved with Councillors and rate payers in many workshops, pop ups, online and in-person meetings which was often proven emotionally challenging in these times when members of community are doing it tough with increases in cost of living and now faced with the potential of a “jump’ in their rate payment.

The above could have been avoided if councils were allowed to increase rates in tandem with increases of cost of doing business and in yearly consultation with their communities. Council has little issues with its other “business” services, namely waste, water and sewer as rates increases on those services are not subject to a rate cap or peg like the general rate but they are nonetheless, closely regulated to ensure that Council, as service provider, is not charging excessive rates and is considering users’ ability to pay before adopting.

7 Recommendations

- NSW Government to consider sponsoring and promoting the use of Public Private Partnership (PPP) to complement its capital grants to ensure that councils’ key capital programs are adequately funded, properly managed and delivered and assets created are responsibly maintained throughout their useful life. Unlike federal or state government PPPs, local government PPP will not succeed without Federal or State Government sponsorship due to the smaller scale of projects at the local level and the lack of relevant expertise within councils to handle the rather complex nature of PPP documentation and management.

- NSW Government provide to councils, particularly the regional and rural ones, untied operational grants similar to the Federal Assistance Grant.

- NSW to advocate to the Federal Government to have the FAG increased in value, considering the real increase of cost of doing business and be redistributed more equitably according to need (i.e. reduce the amounts going to metro councils to increase the amounts allocated to regional and rural ones)

- Allow councils to raise special levies for items that have community support (e.g. a CBD levy on businesses to maintain the main street) without the onerous, timely and costly process required by IPART.