Submission No 69

INQUIRY INTO ABILITY OF LOCAL GOVERNMENTS TO FUND INFRASTRUCTURE AND SERVICES

Organisation: Federation Council

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FEDERATION COUNCIL

Inquiry into the Ability of councils to fund services and infrastructure - NSW Parliament's Standing Committee on State Development 26/04/24

Introduction

Federation Council is pleased to make a submission to this inquiry and thanks the NSW Government for instigating this. Council states however from the onset that there remains in the past, numerous finalised reviews and inquiries, of whom the recommendations, some adopted by Governments of the day and some not, should all be closely reviewed as part of this.

In other words, this is not a new situation. The financial sustainability challenges of Local Government are well known by people in Local Government and many within the State Governments over time, exist for a variety of reasons and the causative factors go back decades. Some relate to mindsets, for example –

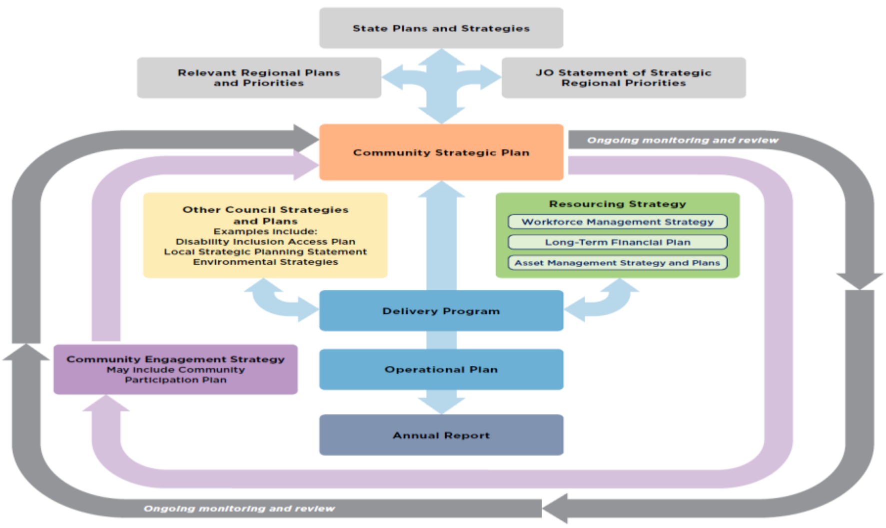
- Ignoring depreciation losses and aiming for balanced budgets or minor surpluses excluding depreciation, un-willingness to raise rates in the past,
- Lack of resources directed to strategic planning – asset management/financial sustainability),
- Some relate to legislation (cost shifting, rate pegging),

and all have resulted, for most rural and regional Councils, of years of underfunding assets. The situation then arises where most rural and regional Councils have had to already or will in the near future, apply for large special rate variations (SRVs) impacting on community in terms of capacity to pay, when coupled with the current cost of living challenges such as electricity and grocery prices.

Terms of reference and responses

(a) The level of income councils require to adequately meet the needs of their communities.

The Integrated Planning and Reporting (I P & R) framework that Councils are required to implement, as mandated by the NSW Government via the NSW Local Government Act 1993, **is designed to** ensure Councils have a sufficient level of income to adequately meet the needs of their communities. One of the main factors as to why Councils do not have the adequate funding is due to an ineffective (not full implementation/utilisation) of the I P & R framework. See pictorial below of the framework.



source https://www.olg.nsw.gov.au/wp-content/uploads/2021/09/IPR-Graphic.png

The primary area where most Councils fail in their obligations is in the Resourcing Strategy (the plans/strategies outlined in the green box on the right).

In simple terms Councils must consult with the community and be the custodian but not the owner, of the ten year (minimum) horizon Community Strategic Plan (CSP). This aspirational plan sets out the community aspirations and vision for the future by way of strategic objectives. after consultation (not only with community but with State and Federal agencies - who typically don't engage), the community aspirations and vision for the future. Councils split across usually 5 key themes, in this Councils case, Built, Natural, Economic, Social and Well Governed Federation.

Council then takes its key deliverables that it considers it can deliver, in continuing consultation through the community primarily by way of annual adopted 1 year Operational Plans, 4 yearly rolling Delivery programs, aligned with Councils terms, and all aligned to the CSP. Each Council term the new Council has to before the next financial year, reconnect with the community to update the CSP. Each six months as a minimum, Council must report on its progress, along with Quarterly Budget Reviews, annual reports including audited financial statements, and end of Council term reports.

Councils tend to underutilise the intent of the Resourcing Strategy in the green box. That is they undertake to do all this work, whilst not fully costing this and ensuring they have a Workforce Plan, Asset Management Plans that focus on core maintenance and renewal of core assets before anything else, and a plausible Long Term Financial Plan that will deliver on this. In a true I P & R implementation, any Special Rate increases would be considered as part of this process, and if IPART considered this effectively, it should be approved. That is broadly the community would give their consent to the increases if fully engaged and in the main supportive, from the I P & R processes.

It is acknowledged that IPART have provided considerable support to Councils in preparing and considering special rate variations in recent times, as one of the earlier criticisms of Councils was they did not apply for SRVs as the process was too onerous. This may have been the case but possibly as big a factor was the unwillingness of Councils to have the hard conversations with the community.

Federation Council since establishment has been working on financial sustainability, and the Strategic Asset Management Plan and State of our Council Infrastructure reports, highlight the significant backlogs Council faces in being financially sustainable.

In order to assist Councils to ‘catch-up’, the State and or through the State lobbying to the Federal Government for an increase to the Financial Assistance Grants, should enact a mechanism for a significant funding program over 4 to 5 years for example where Councils were funded for addressing this backlog.

(b) Examine if past rate pegs have matched increases in costs borne by local governments.

This should not take the committee too long to arrive at an answer here, its no. Put simply, when IPART base a maximum allowable rate peg increase amount each year on a CPI basis, that is on a 'basket of goods', it does not go anywhere near reflecting Councils cost structures.

Councils do not shop for baskets of goods. It is understood that capacity to pay is a real factor, and hence the CPI increases to ratepayers for their baskets of goods, is real, however it should not then be used to align that to what cost pressures Councils face. Rising bitumen costs (aggregate/stone and emulsion) are all affected by world events such as conflicts, causing the price of oil to rise. Oil whilst being the main ingredient for fuels, is also used for emulsion (tar) for bitumen roads. Council's also face rising electricity costs that are not part of the basket of goods.

Rural and Regional Councils including the former Corowa and Urana, typically tended to historically hold rates low, with some including the former Corowa Shire on at least one occasion not even adopting the maximum allowable rate peg, and its understood no increase was applied. This obviously has a compounding effect in that the total rate income is a cumulative total, meaning effectively in applying the rate peg the following year, it is on the previous year's original rate base. Therefore, the foregone opportunity to raise the rates, will never be regained in $ terms.

Whilst not applying for special rate variations or not applying the maximum recommended amount of increases set by IPART, can ensure Councils continue to work to do more with less, helps to reduce inefficiency, encourages services to be reviewed and in some cases reduced, where the community accepts it, (or in some cases are not even aware of a reduction), the longer term adverse effects (asset deterioration and financial sustainability challenges) are what Federation Council and many other Council' are facing now.

Also as unquestionably now proven by the Independent Review, merged Councils on top of other growing cost pressures, and the above discussed low rating practices, are on average 11% more expensive to operate due primarily to dis-economies of scale. The exact opposite of what the Government intended to create by merging Councils, scale and capacity.

A sustained systemic underfunding of basis asset maintenance principles (renewals such as resealing bitumen roads and re-sheeting gravel roads for example), means eventually in the worst case, total asset failure and costly backlogs of repairs. In some cases, total asset replacement (full road reconstructions) are needed at around ten times the cost of ongoing maintenance.

So, it's inevitable that Councils without ever or rarely implementing special rate variation increases, and still attempting to in the main, keep the same and in most cases grow services, the situation is where it is now. The former Urana Shire never applied for any special variations and whilst the former Corowa Shire did, they were of relatively minor amounts, around 7 to 8% each year etc. over 4 years, including the rate peg, that clearly were not informed by any robust asset data or the increases would have been far higher.

For example, the conditions of the roads, drainage, and buildings and facilities assets have not improved or even held condition over this time since the increases were received, and at the time of applying, a robust assessment would have arrived at required increases far higher than what was applied for and received.

The financial issues facing Federation Council are all clearly not as a result of merger, nor have they occurred over the time since merger, they are as a result of sustained underfunding and a lack of strategic management. This is not a criticism, in fact all Councils including Corowa and the former Urana did the best with what they had, the issue was, they never had enough. The mindset was always to cut cut cut and not increase staff, and hope for a miracle from the State or Federal Governments that didn't come.

With a hesitancy to increase rates, either by not applying the full rate peg, or by not applying for special rate variations, or if applied, not to any robust, yet still affordable and defendable level to allow for responsible financial (including asset) management, the need is now for Federation and many other Councils to apply for rate increases above 50%, because their current rates in total are so low to begin with, when compared to cost structure factors such as road lengths.

(c) 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.
Cost shifting has long been a lobbying point for Local Government, and for the most recent proof, refer to the report recently commissioned by LGNSW.

https://lgnsw.org.au/common/Uploaded%20files/Cost_Shifting/ML_Report-LGNSW-Annual_Cost_Shifting.pdf

Councils' services have gradually increased over time, in the main due to growing expectations of the Councils to do more in areas such as Tourism/Economic Development, Community Services, and in areas such as where the State and or Federal Government withdraw from, such as support for Doctors in rural towns. Federation Council continues to carefully review all of its services and has in recent years made reductions in non-mandated areas of Council where it thinks it is reasonable, in areas such as tourism and community services. It should be noted though that the Council has to consider the entire rate base when making such decisions and not favour one co-hort over another. Tourism/events and community services can be very important pieces of the social and economic fabric of communities.

The Independent Review into Federation Council by the University of Newcastle Institute for Regional Futures, led by Professor Joseph Drew - refer

https://www.federationcouncil.nsw.gov.au/Council/Our-Organisation/About-Federation-Council/Independent-Peer-Reviewed-Business-Case-Study-of-Federation-Council-University-of-Newcastle

highlighted the issue of Councils moving from being more an enable to a provider across many years, in areas such as where in the past volunteers would have carried out work. This can include areas such as recreation ovals and the like. The issue facing Councils though is the ever increasing liability (risk management) of managing volunteers means there are often good reasons why Councils have had to step into areas where in many years gone by, it was carried out by volunteers. This increased risk management coupled with ageing and in some cases declining population in communities (volunteer burnout) has meant there are less and less people to do this work also.

Other financial challenges include there have been no real increases (some hardly changed and some haven't met with cost increases), in concurrent funding road programs such as the State Government Road grants and Roads to Recovery (Federal). Whilst programs such as Fixing Local Roads and Bridges were welcomed, they are competitive grants so some Councils win and some lose, and also they are not aligned often with any similar Federal Programs.

(d) 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.

The review should look at all other states rate pegging/systems and noting that the Victorian Government were for years without the NSW based rate peg system, but now have a similar system. The introduction of rate pegging in NSW in the late 1970's and early 1980's has now meant for over 40 years, costs facing Local Government have not matched revenue coming in. This has no doubt led to social and economic impacts, as roads for example are an area which can be validly argued are determinants of social and economic well-being. The safety situations from underfunded roads, including the state transfer in the 1980s of regional roads to Councils, are well documented. Refer to this for one such report - https://www.audit.nsw.gov.au/our-work/reports/regional-road-safety

Also Federation Council has one of the most productive grain growing regions in the state, and in some years has around 15% of the states total grain intake to silos, entering silo facilities in the Council area. Council has also been extremely generous in its allowance for all roads to be accessed predominately by all size vehicles, subject to NHVMs requirements. But generally, road trains and b doubles/triples are allowed across most roads, to allow farms to have a greater chance of being as productive (efficient) as they can. The downside of this is farms are now in terms of freight out and freight in, a 365 day a year freight task, as they move grain off at all times of the year, as opposed to many years gone by where on farm storage was not as prolific. Moving grain in wet winters for example does significant damage to both sealed and unsealed roads, especially those made in the 1960s or 1970's that were not designed for this load.

(e) compare the rate peg as it currently exists to alternative approaches with regards to the outcomes for ratepayers, councils, and council staff.
The IPART rating review report highlights this.

https://www.ipart.nsw.gov.au/Home/Industries/Local-Government/Reviews/Local-Government-Rating-System/Local-Government-Rating-System

Whist there have been some improvements to the SRV process, there needs to be a far greater link and process to Councils I P & R framework, so increases above any 'standard rate peg' are 1) not as extreme in % and $, and 2) not seen as such an alarmist thing as they are now. The standard rate peg needs to be totally re-evaluated each year and have industry experts and Councils on a panel, that allows for far more cost drivers then what is currently used, to ensure the increase is more reflective of materials Councils use, and not just other factors for example population growth. Council with population decline face more pressure then those with growth, as it is not as simple as closing down a Hall, Football ground etc, when the population reaches a certain level.

(f) 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.
With respect a lot of these points are the same, refer to earlier comments. It is clear the SRV process whilst improving, is still not the answer, and if the rate peg were more reflective, this could help, however the SRV process needs a complete re-write in order to ensure it is more flexible for elected Councils through the I P & R framework to determine and set their own increases each year.

(g) any other related matters.
Of particular importance is the recommendations of the NSW Independent Local Government Review Panel across 2013-2015 that provided, excepting the failed amalgamations that were aimed primarily to create more efficient Councils and they have been independently proven to cost more to run. Refer to the earlier reference to the Independent Review.

The State needs to assist Councils in lobbying for the Financial Assistance Grants, to be brought back to 1% of total taxation revenue. The State needs to get to a position of being a positive partner with Local Government, and the NSW Audit Office can play a big role, as could a properly resourced Office of Local Government. At the moment it is left to individual Councils, and industry experts like Professor Drew, and his many relevant reports, and insightful videos, on the problems facing the sustainability of Local Government.

Further, the State Government need to assist those Joint Organisations who have proven they have Councils willing to make them successful, such as Ramjo, with recurrent funding. It was the State Government who put forward JO's as a possible solution to Councils facing lack of capacity, and whilst the State use the JO's when it suits them, to engage with many Councils at once for example, the State also needs to recognise that Councils foot the bill for this, and to come forward with a decent funding partnership.

Finally the lack of security in funding programs for critical infrastructure such as Water and Sewer replacements is very concerning. The State Government need to turn back the clock to the days of the Town and Country Water schemes, and allow a more known and structured process, (and not a competitive process), for the State to then provide their share of funding towards major treatment plant upgrades and renewals.

Council would be pleased to attend a hearing on this critical inquiry and give evidence if invited.

Thanks again for the opportunity to provide this submission.