Submission No 77

INQUIRY INTO ABILITY OF LOCAL GOVERNMENTS TO FUND INFRASTRUCTURE AND SERVICES

Organisation: Bega Valley Shire Council

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The Hon. Emily Suvaal, MLC

Parliament House
Macquarie Street
Sydney NSW 2000

Dear Ms Suvaal,

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

Council welcomes the opportunity to provide feedback on the Standing Committee on State Development's inquiry into the ability of local governments to fund infrastructure and services. Council had provided a submission to IPART on the terms of reference for the financial sustainability review they were poised to undertake (Attachment 1). We bring forward similar comments for your inquiry and encourage the committee to consider what IPART were initially asked to review as some of the IPART terms of reference were valuable. Whichever mechanism of government review is used I implore the committee leading this inquiry to proactively listen to the challenges our sector is facing and provide courageous and realistic recommendations to the government on how we can move forward to ensure that Councils across the state are able to deliver much needed services for their communities.

We appreciate that the inquiry has commenced and acknowledges that "*Councils are experiencing significant financial challenges which are threatening the long-term sustainability of the sector*" as stated in the media release to launch the inquiry. There is a risk this review will look back and miss the opportunity to make material changes that can positively impact local government. No doubt you will find from the various submissions received that there is no magic fix. Correcting the course of Local Government will take time and likely successive governments to implement but laying the foundation and planning for the change now is imperative.

There is no one size fits all and regional Councils are far more vulnerable, particularly with our limited ability to generate revenue. The evidence is clear, without significant state and federal government support Councils do not have the ability to fund the infrastructure and services our communities have come to rely on. This is not simply a cash flow issue. The expectations of what Councils are required to deliver in our local communities has continued to increase. Financial sustainability in Local Government requires analysis beyond financial statements and ratios and focus on the cost pressures the sector continues to face, the dependence we have on unreliable revenue streams and the need for pragmatic leadership. We want the regions to be liveable yet Councils ability to generate the revenue needed to ensure the roads we drive on are not failing, the libraries are open and the sporting fields are match fit is limited.

Looking at only financial sustainability ratios is missing more than half the picture of what informs local government finances. If it was as simple as revenue vs expenditure then Councils would operate like the private sector and stop services that were not profitable. This is not a choice available for an organisation that is established to deliver services to the community with service costs socialised across the ratepayer base.

We recently made a very tough decision to increase rates by close to 50% in the middle of a cost-of-living crisis. This increase wasn't to increase services, it was to have the funds available to catch up on our infrastructure backlog and retain the services we currently provide. This is the cost of doing business and we know this increase is not enough to keep us financially sustainable. Undertaking the special rate variation process and the extensive community engagement to support this increased friction and division in our community. When service levels are not meeting expectations, it escalates dissatisfaction and impacts trust and confidence in government.

The sector is not perfect; mistakes have been made, untoward conduct and poor leadership have at times placed communities in vulnerable positions. However, in most instances Councils are working for positive outcomes for their communities and the continued financial strain that many of us are facing is untenable. Explaining a rate increase beyond rate peg and the complexities of Local Government funding to ratepayers is difficult. Seeking to engage and retain qualified staff is equally challenging when we can't compete for the skills and talent we need to deliver the services our community expect.

We provide the following input against each of the terms of reference.

That the Standing Committee on State Development inquire into and report on the ability of local governments to fund infrastructure and services, and in particular:

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

Regional Councils have limited ability to generate own source revenue, as has been evidenced through various studies of the sector. Prior to applying for the special rate variation (SRV) we rationalised our property portfolio and unlike metro Councils we don't have high-demand carparking to help inject revenue. Our rates income is constrained by rate peg and many of our fees and charges are also regulated by the State Government. The recent Local Government Audit Office report clearly shows the level of income for Councils is not adequate and there are risks associated with reliance on significant state and federal government grants. Across the sector, a review of finance ratios will show that councils are not meeting their obligations.

In the Bega Valley we manage assets valued over $1.9billion, our road network alone is 1,500kms. Our population is dispersed across various towns and villages across a shire that is over 6,200km^2. Almost 80% of the shire is National Park, State Forest or public reserve that provide no rateable income. We have been crippled by rising costs to maintain our assets, well above rate peg. If we don't spend the adequate amount on assets now, we risk further deterioration, costing us all much more in the long run. When we applied for our SRV, our asset and financial plans were modelling that our real need was a 90% increase in rates. The gap in what needs to be spent on our assets vs the income we can obtain continues to widen.

We are fortunate that we have been successful with grants to help deliver a range of projects, however as governments seek to manage their own deficits we are now seeing a constriction in available grant funding. It's important to consider in the fickle and ever-changing grants economy that we are often diverting our focus from servicing, maintaining and renewing existing infrastructure, to expend effort on applying for grants made available to support new or upgraded assets, then diverting resources to deliver the funded projects within electoral cycles. These new or upgraded assets, often highly valued by the community, only add to the maintenance and depreciation costs we are required to absorb.

In responding to the multiple disasters that have impacted our community, Council is grateful for the NSW Disaster Assistance Arrangements which has supported the repair of numerous assets. However, the guidelines for this funding program are complex and don't include Council water and sewer assets, community halls or public amenities as essential public assets therefore they are outside of the provisions of the disaster recovery funding arrangements. There are also no betterment provisions in the guidelines. These restrictions are limiting and removes the opportunity for Councils to take a resilience focussed approach to asset repair in the design and rebuilding process. Like-for-like repair is not optimising DRFA funding to consider and reduce the physical and financial impact of future disasters.

We exist in an operating environment where our income is constrained by legislation, grant funding is declining and service expectations from both the state government and community are increasing. Local government is particularly vulnerable for all these reasons. Collectively we must face some uncomfortable truths and make some hard choices.

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

I trust that other submissions have provided the detailed financial analysis of the gap that exists between rate peg and costs borne by local government so we have not duplicated this information in our submission. The misalignment between rate peg and cost increases was addressed in the IPART review of rate peg methodology final report which I encourage all inquiry members to review. https://www.ipart.nsw.gov.au/Home/Industries/Local-Government/Review-of-rate-peg-methodology

There is a risk this inquiry could end up focussing on rate peg alone, with three of the seven terms of reference explicitly referencing the rate peg. As the committee will know, the rate-peg methodology has recently been reviewed and amended with broad engagement in the sector. IPART's new Base Cost Change model does not account for obvious variables, however it is an improvement from the LCGI approach. Council welcomes IPART establishing a council reference group to advise on the implementation of the new rate peg methodology as the forum to work through issues and provide feedback on what the specific adjustment factors component of the rate peg should be.

Looking back at the implications of rate-peg can help us understand why we are where we are, but it won't fix the problem we have in front of us right now. We are eager to see this inquiry acknowledge the challenges rate pegging has created, but we would like to see the committee focus on solutions for the future that the government can enact.

(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

The inadequacy of funding for local government also needs to consider how the expectations of what Councils are required to deliver has increased. Let's take a recent example of the March 2024 announcement of the Internment Levy that has been imposed upon Councils who operate cemeteries. With little consultation the state government is now asking Councils to collect this levy. It's extra administration costs like this that in isolation appear small, however cumulatively make an impact on our bottom line.

We continue to provide services on behalf of other levels of government and wear the costs of rate exemptions, emergency services contributions, pensioner rebates, libraries funding and increased regulatory functions. LGNSW released a report in November 2023, showing that cost-shifting from the state government is equivalent of more than $460 per ratepayer. https://lgnsw.org.au/Public/Public/Advocacy/Cost-shifting.aspx

(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

Rate-pegging has been in place since the mid-1970's and in the last 20 years there have been many government led reviews to consider it's social and economic impact for ratepayers, Councils and council staff. This is not a new issue and successive governments' have availed themselves of the plethora of research, reports and recommendations. Knowledgeable academics have provided extensive guidance for the sector and I would recommend to the committee Professor Jospeh Drews 2022 booked titled *Saving Local Government- Financial Sustainability in a Challenging World.*

Rate peg is often pitched as protecting ratepayers; however this is false economy. Many Councils, like ours, are having to apply for significant rate increases to play catch up. If rates were increased in line with cost increases it would be far more sustainable for ratepayers and Councils. Ratepayers now and those in the future, will be hit with the indirect social and economic costs that come when infrastructure such as roads, bridges, playgrounds, and sporting facilities are not maintained to the levels required. Our communities become less liveable.

As the level of government closest to the community there is often a commitment not to reduce services, particularly in small regional areas that rely on the vital services provided by Councils to function. Childcare, aged care, disability services and community development are part of the service delivery mix of many regional Councils as we become the last place of resort when it's no longer viable for the private sector, or other levels of government to deliver those services.

As employers, regional Councils play a critical role in our local economy. At Bega Valley Shire Council we employ over 450 staff and the continued financial pressures we face impacts our service delivery and organisational culture. Going through service reviews and the SRV process was challenging for staff. They live and work here and are driven to deliver for their community and doing so in a financially constrained environment is difficult. We are struggling to compete with the private sector to obtain the skills and talent we need to deliver our services with salary structures tied to the Local Government Award.

(e) compare the rate peg as it currently exists to alternative approaches with regards to the outcomes for ratepayers, councils, and council staff

An alternative approach to the current rate peg model is no rate pegging. This would allow Councils in consultation with their communities to determine the appropriate rate increases needed to deliver services that meet local need. Self-determination would be far more efficient than the endless advocacy undertaken to make needed changes that have not been realised. The IPART rate peg methodology review, and other analysis on this approach have outlined the trust and confidence communities would develop in their Council to self-manage and not put rates too high – or above what was needed. The Integrated Planning and Reporting framework, done well, helps to support this process.

(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

From an internal and operational perspective, the SRV process is complex, resource intensive and time consuming. In the community it is divisive and difficult for leadership (elected officials). IPART are operating under outdated guidelines from 2021 and the whole process erodes trust in all levels of Government. There are also flaws in the process including no provisions for catch-up in multi-year SRV's should the assumed rate peg not align with the actual rate peg. We were instructed by IPART to assume a 2.5% rate peg when applying for the SRV. With the actual rate peg higher (4.9%) than the amount we were instructed to assume there is a shortfall in the funding we were anticipating the SRV increase would provide and now there is no capacity to catch up the shortfall. In effect our approved second year SRV of 19.6% is reduced to 17.2% well below the amount needed to meet the objectives Council outlined in the SRV application. This places more financial pressure on Council.

(g) any other related matters.

Grants

Councils are required to develop 10-year Long Term Financial Plans and make assumptions on our level of expected grant income but the forward visibility of what is going to be available from both the state and federal government is limited. We are supported by grant programs from various state government departments however these grants are ad hoc, increasingly competitive, and not always aligned with the priorities Council has set. If the state government pooled that grant funding into a model like the Federal Assistance Grants where the allocation is untied and Councils have ability to fund the priorities it outlines in its planning documents then Council's financial position would be improved through stability and visibility of income beyond the political whim of election cycles.

Audit Costs

Audit costs for Councils have continued to escalate since the NSW Audit Office (AO) took over all NSW Council audits. LG Solutions, a local government service provider, undertook analysis of the increases and determined there has been a cumulative $21.7m in extra audit costs (beyond the rate peg). This is general revenue that could have been spent on infrastructure replacement. *(Source: October 2023 LG Debits and Credits Newsletter)*. We have also experienced delays in the AO meeting reporting obligations which is influencing the compliance rates for submission. The AO has become a bottleneck and it is costing Councils. Last year we had to absorb a 29% increase in audit costs.

Financial Assistance Grants

Whilst this inquiry has no capacity to amend the Federal Financial Assistance Grants (FAG) we call on the State Government to support our sector's advocacy to see the FAG allocation returned to 1% of Federal Taxation revenue. The FAG allocation is simply not enough and the early payment in recent years only serves to distort the reality of the dire financial situation many Councils are facing. We are also advocating that the population factor in the general-purpose component of the FAG allocation be reduced from 30% to 10% providing improved outcomes for regional Councils who are far more reliant on FAG allocations than metropolitan Councils who have income generating capacity. If the committee was to look to other jurisdictions for guidance then we recommend your consideration of the recent changes by the Queensland government in their 2021 methodology review.
https://www.statedevelopment.qld.gov.au/lg-dev/for-councils/governance/queensland-local-government-grants-commission/2021-methodology-review

Rating of unrateable land

Across NSW there are large sections of government-owned unrateable land. Often the government-owned land is dependent on local government assets and services to support its function and use.

Examples of this include forestry trucks traveling on local and regional road networks and visitors to national parks accessing local road networks. In the Bega Valley Shire, over 80% of the land is non-rateable, contributing to our financial sustainability issues and directly linked to the infrastructure and services we are expected to provide.

Emergency Response
Under the *State Emergency Response Management (SERM) Act* Councils have been given two key un-resourced responsibilities. The first of those is to convene a Local Emergency Management Committee (LEMC) which has broad responsibilities relating to planning for and managing during emergencies. The second is to employ a Local Emergency Management Officer (LEMO) which has defined responsibilities under the *SERM Act*. How councils go about resourcing and supporting emergency management in reality is highly variable. In many cases in rural and regional areas the LEMO role is tacked on to the responsibilities of another employee of council, sometimes a lower-level officer role and other times to an already overstretched executive team member role. In reality the responsibility should sit much closer to an executive level role and the function should report directly to the General Manager/CEO who has legislative responsibility for chairing the LEMC.

As chair of this inquiry when finalising your report to Government we offer the following to assist in the development of recommendations to deliver much needed change.

- Remove rate pegging and allow Councils in consultation with their communities to determine the appropriate rate increases needed to deliver services.

- Remove the Rural Fire Service depreciation costs from NSW Councils and ensure all RFS assets are controlled, managed and accounted for by the RFS through the State Government.

- Reinstate the ESL subsidy and develop a fairer, more transparent and financially sustainable method of funding critically important emergency services in consultation with local government.

- Fully fund pensioner rebates.

- Review and update the NSW Disaster Assistance Arrangements and NSW Natural Disaster Essential Public Asset Restoration Guidelines to include water and sewer assets, community halls and public toilets and allow for betterment when Council are required to rebuild assets.

- Review and update the 2021 Office of Local Government SRV guidelines. Simplify the SRV process and shift the burden of proof to IPART to justify why an increase should not be permitted for a Council that can demonstrate the need for an increase.

- Remove the requirement for Councils to have their annual financial audits undertaken by the NSW Audit Office and cover the costs of the audit process.

- Develop a structured funding methodology for State Government funding to support Councils. A state equivalent of the un-tied Financial Assistance Grant.

- Provide increased visibility of grant funding program announcements, reduce delays in issuing deeds and reduce the onerous grant acquittal reporting.

- Allow greater flexibility in grant funding programs including provision for:

- existing Council employees to be redirected to grant funded projects- many state government programs do not permit this which means Councils have to outsource to contractors impacting our ability to deliver grant funded projects.
- Councils to build in adequate overheads and administration costs which are often limited in grant programs.
- Councils to apply for program level funding for asset categories not just individual projects such that funding allocations can be managed simply and easily across programs of work without administrative burden.
- Increase thresholds for contingency in project budgets acknowledging that from the time a project is scoped and costed to for an application to when notification of a grant outcome is successful, the deed execution process to procurement of services there is often a cost escalation beyond the value of the grant and co-contribution.
- Provide grant funding programs that support strategic planning and strategy development.

- Where cost shifting clearly exists reimburse Councils for service provision.

- Change legislation to allow the rating of forestry and other currently unrateable government land.

- Use funds allocated to the NSW Reconstruction Authority to fund executive level Local Emergency Management Officers (LEMOs) to ensure that our communities are better prepared for and protected during emergencies.

- review legislative fees and charges and include indexation aligned with rate peg - not a fixed fee that is not updated annually.

- simplify the complex planning system and further invest in the planning portal to ensure it is fit for purpose and optimised.

- cap the cost of Local Government elections (follow precedent in Queensland who passed legislation in May 2023 to set caps on electoral expenditure) and instruct the NSW Electoral Commission to introduce electronic voting systems.

I am certain the committee with receive a range of submissions from across the LG sector, echoing similar sentiments to those outlined above. We support the collective advocacy submissions from LGNSW, the Canberra Region Joint Organisation, the United Services Union and Country Mayors Association (CMA) NSW. We trust that we have demonstrated that it is more important to focus on the future and what the State Government can do now to help Local Government.

Over the years there have been numerous Local Government sector inquiries and reviews, we look forward to this inquiry and positive changes that will result in responsible, realistic and sustainable financing of councils to deliver local infrastructure and services that will serve our community needs now and into the future. Should the committee members require any further context or evidence on the matters raised above I am more than happy to be contacted.

Regards,
Iliada Bolton
Director of Business and Governance