Submission
No 86

INQUIRY INTO ABILITY OF LOCAL GOVERNMENTS TO FUND INFRASTRUCTURE AND SERVICES

Organisation: Ku-ring-gai Council

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

Submission by Ku-ring-gai Council

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KU-RING-GAI COUNCIL

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Introduction

Ku-ring-gai Council welcomes the opportunity to provide comments on the ability of local governments to fund infrastructure and services in line with the Terms of Reference released by the NSW Parliament's Standing Committee:

- the level of income councils require to adequately meet the needs of their communities
- examine if past rate pegs have matched increases in costs borne by local governments.
- 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.
- 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.
- compare the rate peg as it currently exists to alternative approaches with regards to the outcomes for ratepayers, councils, and council staff
- 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.
- any other related matters.

Ku-ring-gai Council is currently in a satisfactory financial position; however, the economic environment has changed and Council's financial capacity in future years will decline without additional funding or adjusting current operations and services. All Councils across NSW face a range of significant challenges relating to the provision of services and infrastructure to local communities, delivery of statutory requirements, while maintaining financial sustainability and minimising the costs to ratepayers.

Council's submission advocates for a comprehensive review of local government funding, and that this is necessary to ensure the long-term sustainability of local government and the essential services they provide.

> s7.11 and s7.12 Developer Contributions will not be enough to provide for the infrastructure needs of a growing population.

This submission is made against the backdrop of the new NSW housing policies that will increase housing density and population growth in Ku-ring-gai and the Greater Sydney area. While it is expected that this growth will generate additional revenue from rates and development contributions, it will place immense pressure on existing infrastructure and the additional services required to sustain a growing population.

We recommend that any review of the rate peg and local government funding model be informed by projections of population growth and the additional demand for essential services and infrastructure delivered by local government resulting from the Transport Oriented Development and Low and Mid-rise Housing SEPPs.

Any changes to the methodology should better support councils to invest in roads, open space, community facilities and other infrastructure required to accommodate expected growth.

This submission is consistent with the themes and principles outlined in Ku-ring-gai Council's draft Resourcing Strategy (on public exhibition until 16 May 2024 and available here: Ku-ring-gai Council plans Ku-ring-gai)

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

The current levels of income that councils receive is insufficient for long-term financial sustainability and meeting the needs and expectations of local communities. There are a number of reasons for this.

> In the last 10 years Council experienced a 40% increase in operation expenditure while rates increased by only 28%.

Like other NSW councils, Ku-ring-gai Council relies heavily on income from rates. Rates comprise approximately 60% of Council's revenue. While the rate peg offers some protection to ratepayers from sudden and steep increases, it also restricts councils' ability to keep pace with rising costs. Over the past 10 years Ku-ring-gai Council's costs for providing services have gone up 40% while rates have only gone up by 28%. This means that Council is finding it difficult to keep pace with rising costs of infrastructure and services, especially for growing communities.

<u>User fees & charges</u> are also an important source of revenue, contributing around 14% of Council's income. However, statutory limits on many fees and charges prevent councils from making decisions about the appropriate level of subsidisation or adjusting fees in line with the actual costs of service delivery. Without adjustments for rising costs, Councils struggle to cover service expenses and are expected to absorb these costs. This means that some services, like development applications, are being subsidised by other ratepayers. Councils have limited influence over statutory fees, which often do not align with CPI increases or accurately reflect service delivery costs.

> **Recommendation 1:** Introduce regular reviews on the process of indexation of statutory fees and charges to ensure they cover cost of service delivery while considering social equity.

<u>Grant funding</u> is an importance source of additional revenue for NSW councils and make up around 12% of Ku-ring-gai Council's annual income. However, much of this grant funding is short-term, unpredictable, and tied to specific projects or issues. This makes long-term planning more difficult. Financial Assistance Grant levels are more reliable, but only make up a fraction of council revenue (around 2.9% for Ku-ring-gai Council).

<u>Development contributions</u> assist in funding new capital projects and new infrastructure. However, ongoing maintenance and operational expenses on newly built assets, as well as asset depreciation, are left unfunded leaving councils to make up the difference. This puts additional pressure on service levels and contributes to financial instability for NSW councils.

> Long-established Councils face challenges whereby rates are not sufficient to upgrade or replace ageing infrastructure

Many buildings, drains and other key assets in Ku-ring-gai and other LGAs were built decades ago. Over time, these assets have not received adequate upgrades or replacements as Councils are forced to prioritise limited resources. This has created a significant backlog in infrastructure maintenance and renewal, placing a financial burden on current and future generations. With limited sources of recurring funding and the quantum of funds required for infrastructure backlogs Councils must explore Special Rate Variations and other options of funding.

<u>Other income sources.</u> Councils also derive revenue from other sources like rental income from commercial and community properties. However, community property rentals are often heavily subsidised, and investment revenue streams cannot be relied upon as a major source of revenue due to the risks associated with investment of public money.

We believe that improved data management, efficient oversight, targeted support and a data driven approach across the sector is also important to a more effective and sustainable local government system in NSW.

Recommendation 2: The committee should consider appropriate resourcing to the Office of Local Government (OLG) and deliver on the NSW Audit Office recommendations from May 2023 to develop and maintain a data management framework, sector support and compliance activities.

If past rate pegs have matched increases in costs borne by local governments

Past rate pegs in NSW have not kept pace with the increasing costs borne by local governments. This has resulted in a significant funding gap, hindering councils' ability to invest in critical infrastructure and maintain service levels.

It is important to note that recent IPART reviews to the rate peg methodology have improved the way that changes to costs and population growth are considered. Nonetheless, staff costs are a major council expense, wages have grown steadily over the past decade (by 2.64%) but the annual average rate peg (2.3%) has not consistently matched this growth. The cost of building and maintaining infrastructure has also risen significantly. Cost shifting is also a driver of increasing costs that is not incorporated into the rate peg methodology or local government funding model.

The long-term impact of this has been increasing pressure on service levels and Councils' infrastructure backlog. The lack of insufficient funds for maintenance and upgrades of ageing infrastructure has resulted in a growing infrastructure backlog across NSW. At Ku-ring-gai Council, we maintain an asset portfolio of around $2.2bn, and the current reported backlog costs to renew all assets that are not in a satisfactory condition is $323m.

The lack of insufficient funds for maintenance and upgrades of ageing infrastructure has resulted in a growing infrastructure backlog across NSW.

As a specific example of cost shifting, Councils have been directed to recognise the "red fleet" items of NSW Rural Fire Service plant as assets in Council's Annual Financial Statements and fund the depreciation of all of these assets. For Ku-ring Council these assets are valued at $2m and depreciated in Councils Assets Register. Cost shifting is further discussed below.

Other significant costs that are not considered in the rate peg are cost of natural disasters and climate change. The increasing intensity and frequency of natural disasters and extreme weather events highlight the impact of climate change on financial sustainability. This includes assessing infrastructure adequacy, cleanup expenses, and the necessity of funding mitigation and adaptation measures. Exploring available funding mechanisms to address these additional costs is crucial.

In some cases, councils are forced to reduce or limit service levels to stay within their budgets, impacting on the delivery of essential services.

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.

Addressing cost shifting is an urgent priority for all councils. A review of the regulatory and compliance burden imposed on NSW local governments and streamlining of high-cost, low-value regulations and reporting requirements would free up resources currently dedicated to administrative tasks and allow councils to focus on service delivery.

Ku-ring-gai Council estimates that it incurs approximately $13 million annually on cost-shifted responsibilities, representing a significant portion (8.6%) of its operating income. These costs include contributions to the Emergency Services Levy, waste levy, public library operation, pensioner rebates, and various regulatory functions mandated by the state government.

Recommendation 3: The committee should investigate the legitimacy of cost shifting from other levels of government and its impact on financial sustainability. This investigation should explore funding mechanisms to account for these cost transfers, combining regulatory reforms, budgetary provisions, and appropriate funding to ensure Councils can meet their obligations effectively.

One important step towards achieving this goal is strengthening Better Regulation Statement (BRS) and Regulatory Impact Statements (RIS) for new and amended regulatory proposals. Consultation and formal agreements between the NSW Government and local councils to share the full cost of regulatory functions would help to minimise unnecessary financial burden on local government.

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, and

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

As detailed elsewhere in this submission, the rate peg has had complex social and economic impacts on ratepayers, councils and council staff. It successfully keeps rates low for residents, but this comes at the expense of service quality and infrastructure investment.

NSW and Victoria are the only states with a cap on rates revenue growth, and data published by IPART show that NSW has had the lowest per capita rates income (except the Northern Territory) since around 2003[1].

While the rate peg slows rate increases for residents and ratepayers, this effectively requires councils to cap service levels and funding for services and programs. Insufficient funding for infrastructure maintenance can impact on the quality, accessibility and safety of community infrastructure as costs of maintaining ageing infrastructure continues to increase over time. Even with the most prudent financial management, it is increasingly difficult for councils to keep pace with rising wages, construction and other costs. This limits investment in new and upgraded infrastructure, services and other programs that communities say they need. It also makes it difficult to maintain competitive salaries for key positions and to attract and retain talent.

Recommendation 4: The inquiry should consider the suitability of rate pegging methodology, its deficiencies and long-term impacts on financial sustainability and infrastructure backlogs. It should also consider ways to provide for a clearer and more transparent process, greater predictability in setting rates, account for cost-of-service adjustments, alternative valuation methods and a review of rate exemptions and subsidies.

[1] IPART (2021) The impact of population growth on council costs and revenue (https://www.ipart.nsw.gov.au/sites/default/files/cm9_documents/Information-Paper-1-The-impact-of-population-growth-on-councilcosts-and-revenue-June-2021.PDF)

The current rating system based on unimproved land value presents challenges for councils dealing with changing demographics and development patterns. For example, the build-to-rent model disadvantages councils and increases inequality in applying rates. Large-scale rental developments pay minimum rates despite creating a higher demand for services. This creates an inequitable situation for existing ratepayers who are subsidising these developments.

Recommendation 5: The inquiry should consider adopting "capital improved value" for a fairer and more equitable rating system, especially in urban areas experiencing growing medium and high-rise development due to NSW Government policy reforms.

Under the Local Government Act and regulation, rate exemptions and subsidies are provided for Crown land, land owned by public transport and water corporations, religious bodies, schools, public hospitals and other landowners and occupiers. While delivering community benefits, many of these institutions benefit from services provided by local government and/or are undertaking commercial activities.

Recommendation 6: The inquiry should conduct a review of rate exemptions and subsidies for non-profit and government landowners and occupiers to achieve a better balance between community benefit, fairness, and revenue generation.

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.

The current Special Rate Variation (SRV) process allows councils to apply to raise rates above the peg in exceptional circumstances. However, the SRV process is administratively burdensome. It can be a lengthy and resource-intensive exercise for councils, requiring them to gather and submit a significant amount of data to justify their request. This can divert valuable time and staff resources away from core service delivery functions.

Recommendation 7: The inquiry should consider a system where councils demonstrating a strong track record of performance are provided with more autonomy to set rates to meet their local needs. This performance could be measured using a set of standardised KPIs of efficiency, including service delivery, infrastructure, and resource allocation, as well as community engagement and overall organisational performance.

A clear definition and standardised methods for measuring performance and efficiency in local government would also enable councils to identify areas for improvement, optimise resource allocation for service delivery, provide transparency for ratepayers and support IPART in evaluating the merit of applications for special rate variations. Where an SRV process is required, we feel there is opportunity to streamline and simplify the current systems to make the process less time-consuming and resource-intensive for councils.

Collaboration between tiers of government is crucial for delivering essential infrastructure projects that deliver both state and local objectives.

A special rate was proposed under the Local Government Amendment (Rates) Bill 2021 to allow for special rates to be levied for intergovernmental projects that benefit the community. Ku-ring-gai Council has one joint project with the Department of Education, St Ives Multi-Purpose Complex project that is assumed to be funded from an Intergovernmental special rate. Unfortunately, the Office of Local Government has not yet provided guidance on the timing for its implementation. Consequently, the Council is currently awaiting further clarification on this matter.

Recommendation 8: The inquiry should consider enacting section 495 of the Local Government Amendment (Rates) Bill 2021 to allow for special rates to be levied for intergovernmental projects would support the delivery of critical infrastructure required to support population growth.