

**Submission
No 110**

INQUIRY INTO ABILITY OF LOCAL GOVERNMENTS TO FUND INFRASTRUCTURE AND SERVICES

Organisation: Lismore City Council

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Standing Committee on State Development

***New South Wales Inquiry into the Ability of
Local Governments to Fund Infrastructure
and Services***

Lismore City Council Submission

1. Background/ Terms of Reference

On 21 March 2024 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
- (b) examine if past rate pegs have matched increases in costs borne by local governments
- (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
- (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
- (e) compare the rate peg as it currently exists to alternative approaches with regards to the outcomes for ratepayers, councils, and council staff
- (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
- (g) any other related matters.

2. Response to the Terms of Reference

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

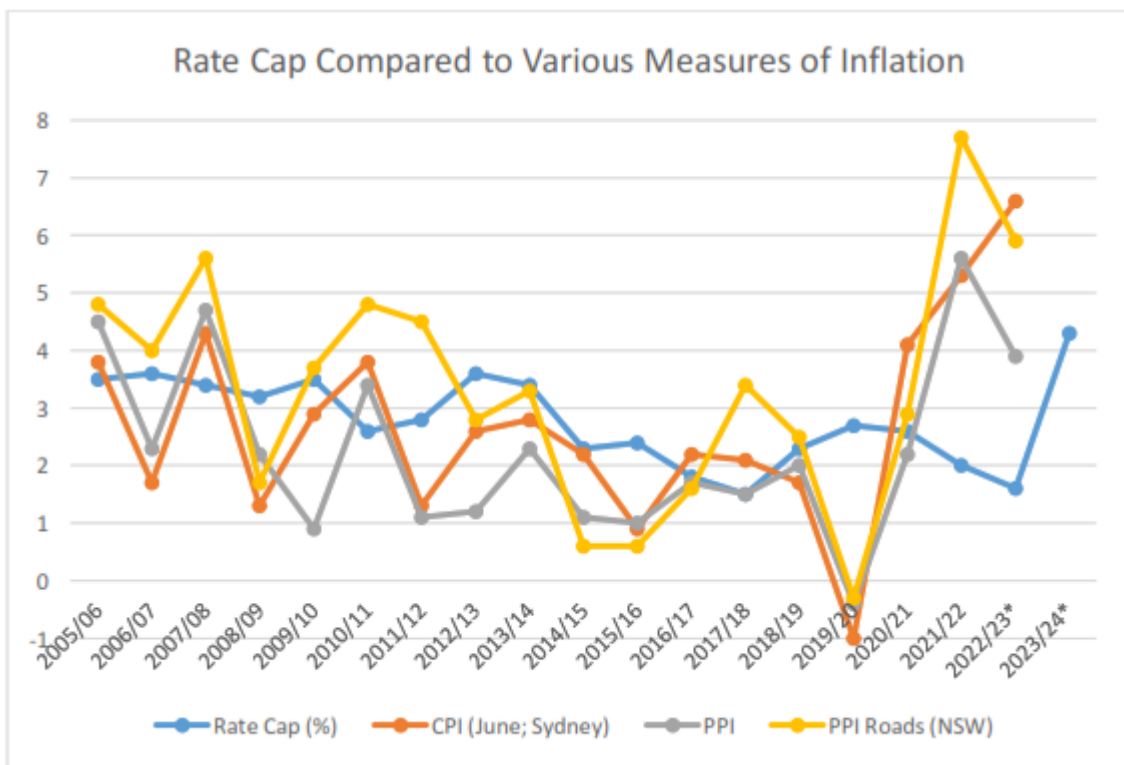
It is difficult to generalise the level of income required by councils to deliver services as each council has a unique profile in terms of discretionary services, geographical spread, rating base, other revenue raising capacity (for example, some councils are able to levy rates from the mining industry), and socio-economic issues. Many remote councils are faced with the prospect of managing very large LGAs with relatively low rating income, whilst this may not be the case for many urban and large regional councils. Financial sustainability is defined as a council's ability to cover their service provision requirements and other financial obligations without compromising their capacity to meet future commitments. Over time, community expectations in terms of the services that councils deliver has increased significantly beyond the traditional "roads, rates and rubbish". For example, there is an increasing focus on issues such as climate change, social services and affordable housing. Historically, most councils in NSW are faced with the challenge of deteriorating infrastructure due to their inability to adequately fund asset maintenance and renewal works. Local government's capacity to maintain existing services and infrastructure is compromised. In many instances councils are already forced to cut services and defer crucial infrastructure expenditure, which has seen a significant growth in the infrastructure backlog many councils (include Lismore City) are facing. A broader financial base is required for councils to effectively meet new statutory obligations, deliver new services demanded by the community or to build new infrastructure required to support development. Lismore City Council's draft 2024/25 budget indicates a net consolidated operating loss (before Grants and Contributions provided for Capital) of some \$13.6m (this includes \$36.4m in depreciation) and indicates that Council is unable to renew its assets at an appropriate level. This is

in keeping with most large regional councils. This situation does, however, improve over the life of Council's Long-Term Financial plan.

Levels of service in relation to assets include accessibility, quality, responsiveness, affordability, customer satisfaction, sustainability, health and safety, and financial performance regarding the delivery of assets to the community, any combination of which can be impeded if assets are in an unsatisfactory condition.

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

Rate pegging in NSW commenced in 1977 and has over time significantly eroded the NSW local government sector's capacity to implement rate increases commensurate with cost increases. Some recent examples include the rate peg determination of 0.7% for 2022-23, (later adjusted to 2.5% for most councils after introduction of a one off Additional Special Variation), which fell significantly short of the inflation rate of 8% in 2022-23, resulting in a material reduction in real rate income. (Lismore Council opted for a nil increase in 2022/23 due to the hardship caused by the recent flood). Some previous rate pegs have included an "efficient factor" that resulted in rate pegging below the (already conservative) local government cost index, causing further hardship for many councils struggling to deliver balanced budgets.



The above graph illustrates plots the NSW rate-cap against various indices including the Consumer Price Index, the Producer Price Index (PPI) and the PPI (roads component). Of note in the significant increase in the road cost index, which is a major issue for most councils, Lismore included. Other costs that have gone up significantly are insurances and the Emergency Services Levy contribution.

The local government cost index factors in changes in costs on a basket of goods for an "average council", however costs move differently for differing categories of council such as metropolitan, regional and rural. Council's typically have a different mix of services, for example a large rural or regional council will typically have a large road network in comparison to its rating base when

compared to a smaller urban council. Rural and remote councils typically bear higher costs due to a less competitive supply market and goods transportation costs.

Whilst the changes to the rate-peg methodology for 2023/24 was a positive step forward, IPART have concluded that *“Our new rate peg methodology is designed to respond to many of the issues raised in consultation. But it cannot address all the issues people have highlighted during the consultation. The rate peg cannot adequately address the efficiency or sustainability of the cost base of councils”*. Councils should be able to determine their annual rate increases (subject to a reasonable maximum) based on the cost increases that are unique to their individual circumstances.

(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

In terms of expanded service delivery, the Commonwealth Hawker Report (2003) put in succinctly: *“there had not only been increasing diversity across Australian local government service provision, but also an expansion of the roles beyond those traditionally delivered by the local sector”*. This shift includes assuming responsibilities for more social issues such as community safety, affordable housing and an increase in activity around regulatory monitoring. This pressure has resulted in a “leakage” of funds away from essential asset maintenance and renewal for many councils.

Financial sustainability remains the major challenge facing local government as evidenced by the crippling infrastructure maintenance and renewal backlog (NSW) of approximately \$3.8 billion (according to Office of Local Government figures). For Lismore City, the backlog figure is approximately \$201m (2022/23). This is a significant increase on the 2012/13 figure of \$23.2m and is evidence that Council’s capacity to invest in its assets has eroded over time.

Table 3: Asset backlog summary

Estimated cost to satisfactory	Backlog \$ (000's)	Backlog ratio % (Backlog / WDV)
Buildings	23,527	35.5%
Other Structures	281	1.5%
Roads	50,499	12.0%
Bridges	7,028	8.3%
Footpaths	299	1.1%
Bulk Earthworks	0	0.0%
Stormwater	1,758	2.2%
Water Assets	25,687	15.3%
Wastewater Assets	88,849	27.5%
Open Space and Recreation (inc. Land Improvements)	96	15.0%
Swimming Pools	2,856	57.2%
Total	200,880	12.4%

Cost shifting by the NSW Government onto local government is currently estimated to be approaching \$1 billion per annum (representing around 7% of total local government operating revenue). Lismore City Council is still analysing the impact of cost shifting in relation to our 2024/25

draft budget, however this is likely to be more than \$10 million. This represents funds forfeited over time that could have been directed to delivering works and services.

(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

As mentioned earlier, the compound effect of rate pegging has caused a growth in the infrastructure backlog in NSW. This can have a negative social and economic effect, for example due to poor roads, recreational, and other community facilities. Councils with low levels of discretionary income have less capacity to provide community and social services such as youth and seniors programs. Areas with poor infrastructure are less likely to attract new businesses and tourism opportunities. To meet financial sustainability targets, many councils have undertaken cost cutting measures that have involved reducing staff numbers and services. Often staff numbers are reduced, and service levels maintained, which can impact already-stretched employees. Rate pegging can affect rural councils more than their urban counterparts because rural councils generally rely more on rates than other sources of revenue. This would not be as prevalent in states that are not constrained by rate pegging.

(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 review of the rate peg methodology resulted in a new methodology that came into effect in 2023/24. This involved replacing the previous “one size fits all” Local Government Cost Index with a “Base Cost Change” model with 3 components - employee costs, asset costs and other operating costs. In addition, and a separate Base Cost Change model for the three council groups (metropolitan councils, regional councils and rural councils). Whilst this was seen as a positive step forward it still does not consider cost pressures applicable to individual local government areas. Independent studies showed that when compared to other states that have uncapped systems, NSW has suffered from several main problems. Firstly, NSW local government had reduced inter-municipal equity due to disparate council rating structures. Secondly NSW councils had much higher levels of debt and infrastructure backlogs due to the restrictions of rate pegging on revenue generation. The abolition of rate pegging would allow rates to be set at a level that provides the appropriate levels of works and services to the community. There may be impacts on staff – rather than working backwards and making the budget “fit” within the constraints of the rate peg, more work would need to be done in costing agreed-to and sustainable service levels. Service level discussions with the community would be an essential part of the rate setting process. The unwinding of some of the imposts of cost shifting would provide additional funds and take the pressure of rate increases, thereby helping the ratepayer.

A review of the Federal Assistance Grants methodology is well overdue. This would greatly assist both councils and ratepayers in that more funds would be provided to councils whilst minimising the impact to ratepayers. The percentage of the Federal Assistance Grants (FAGs) as a share of federal taxation revenue to local government is now a little over half a percent. (FAGs have declined from one per cent of federal taxation revenue in 1996 to just 0.5 per cent in 2024.) Lismore City Council’s FAG for 23/24 is \$7.7 million. If this was raised to the historical 1% allocation, the extra income would be a further \$7.7m for Council, which would have a significant impact on Council’s budgetary position.

(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

As any council who has been through it will attest, the process of making a Special Rate Variation is usually arduous and time consuming. Having said that, it does provide a layer of rigour and can provide a reality check to councillors and senior management in relation to a council's financial position. The process can be improved by ensuring assessment panels have members who have real-world local government experience. The turnaround time for SRV assessments needs to be reduced to allow councils to take remedial action in a timelier manner. Whilst SRVs provide an important mechanism for councils to raise additional income (usually to fund infrastructure improvements), the very fact that they exist and that most councils in NSW have made some sort of SRV application attest to the fact that rate pegging has not kept pace with councils need to operate sustainably. It should be noted that seventeen councils had SRV approvals in 2023/24.

(g) any other related matters