LOCAL
GOVERNMENT
NSW

LGNSW Submission
IPART Review of the Rate Peg to Include Population Growth

Issues Paper

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LOCAL GOVERNMENT NSW

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Introduction

Local Government NSW (LGNSW) is the peak body for local government in NSW, representing NSW general purpose councils and related entities. LGNSW facilitates the development of an effective community-based system of local government in the State.

LGNSW welcomes the opportunity to present local government views on the review of the *Rate Peg to Include Population Growth*. The proposal to allow rates to grow beyond the peg based on population growth represents a major reform to the rating system. The proposal offers the potential to provide real benefits to councils, communities and the State. However, LGNSW recognises that developing a model that provides equity and efficiency is a complex task and will be made harder if it has to deal with competing objectives or mixed agendas. For example, the proposed linkage with infrastructure contributions. LGNSW objects to this linkage.

General Comments

LGNSW is pleased that the Government, in accepting and supporting the findings and recommendations of the Productivity Commission, has finally acknowledged that rate pegging has been having a negative impact on NSW since its introduction in 1996-97. The NSW Productivity Commission (PC) has confirmed the long held views of local government and the findings of numerous Inquiries over past decades.

In recognising the damaging consequences of rate pegging it is now incumbent on the NSW Government to reform or remove rate pegging.

LGNSW welcomes the Government's commitment to align rates with population growth. Population growth is clearly a major driver of infrastructure and service costs for councils. LGNSW agrees with the PC finding that:

Local government is constrained in its ability to service growing communities due to the long-standing practice of rate pegging. Currently, the formula does not allow councils to increase their rates revenue with population. This has resulted in declining per capita revenue for high growth councils and is a disincentive for councils to accept development.[1]

LGNSW supports the recommendation that:

Subject to review by the Independent Pricing and Regulatory Tribunal, reform the local government rate peg to allow councils' general income to increase with population[2].

This would be a major reform and a significant improvement to the current system. However, LGNSW is concerned that this will not fully address the problems resulting from rate pegging. There are other cost drivers and revenue constraints that would not be accounted for by this change. These factors are independent of population growth and include costs driven by the expanding roles and responsibilities of local government, rising community expectations, rising project costs, cost shifting and the ongoing decline in Commonwealth Financial Assistance Grants in real terms. These factors impact on all councils, not just 'growth' councils. It is disappointing that the terms of reference do not extend to changes beyond those related to population growth.

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[1] Productivity Commission -Review of Infrastructure Contributions in New South Wales- 2020 p.39
[2] Ibid

LGNSW maintains the view that the best solution to the problems of rate pegging is to unconditionally remove rate pegging. States that do not impose rate pegging have avoided the problems identified by the PC.

Councils are also expressing serious concerns about the Governments apparent intention to tie reform of the rate peg to reductions in infrastructure (developer) contributions. While this is not specified in the terms of reference, this was implicit in the Governments unqualified acceptance of the PC recommendations[3], formed part of the basis of modelling by the Centre for International Economics (CIE) that supported the PC report and it was the clear message in the joint media release by Ministers Stokes and Hancock, announcing the IPART review[4]. It was disconcerting that the media release pre-empted the independent review process.

LGNSW is of the view that the findings of the PC on the negative effects of rate pegging are independent of the infrastructure contributions process and the matters should be addressed separately. Many councils see this as a cost shift from developers onto ratepayers and councils. While it is acknowledged that there may be ways to design the policy to help ensure there is a net gain to councils, the linkage detracts from the primary objective of reducing the negative impacts of rate pegging.

It has been indicated, although it is not entirely clear, that the increased rates resulting from inclusion of population growth will only apply to new development/residents. LGNSW supports this objective. It would be inequitable to spread the additional increase in rate revenue across all ratepayers in the local government area (LGA). Particularly so, if that also involves cross subsidising reductions in infrastructure contributions. Further, doing so would be counterproductive to the PC's objective of removing the *disincentive for councils* (and communities) *to accept development.* It would be rational for existing communities to strongly oppose all new development if that development will result in increased rates. At this stage it is unclear how this can be achieved.

LGNSW is also of the view that the growth factor should apply to all growth, not just growth above the state average or some other growth threshold. If we accept the PC finding that the rate peg does not adequately account for population growth it follows that all growth should be included so that it is not only 'above average' councils that benefit from this reform.

Response to IPART Questions

1. What council costs increase as a result of population growth? How much do these costs increase with additional population growth?

Population growth increases council costs associated with the provision of infrastructure and services to support the increased population. This includes the cost of new community infrastructure that is not funded by infrastructure contributions, the augmentation of existing infrastructure to deal with greater numbers, the ongoing maintenance costs and operational costs in the daily running of the infrastructure and the costs of expanding service delivery to support the increased population.

The caps on infrastructure contributions and the highly restricted essential works list have dramatically increased the infrastructure costs to councils by all but excluding the recovery of capital costs for community buildings. The list excludes core infrastructure expected by communities such as libraries, community halls, aquatic centres and sporting facilities.

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[3] Ibid
[4] Stokes/Hancock Ministerial Media Release 24 March 2021

The costs impacts also vary with the type of development. Greenfields developments typically have higher land acquisition and new infrastructure construction costs. Areas of infill development face higher infrastructure augmentation and improvement costs. This may include very high cost and disruptive works like realigning roads and footpaths or replacing old and inadequate drainage systems.

LGNSW agrees with the comment made by Penrith City Council that the growth in costs associated with the new population commence before the development as demand commences for planning and infrastructure delivery. This places a burden on the existing population to forward fund the infrastructure delivery and associated land acquisition costs for the incoming population. This is further disadvantageous given Council's inability to levy for the full cost of delivering the infrastructure for new communities.

LGNSW also concurs with the Revenue Professionals in noting the growth in secondary dwellings is negatively impacting on council costs. These self-contained dwellings house population growth, increasing demand on infrastructure and services, but are not captured by the rating system. LGNSW considers that this in itself should be addressed by rating reform, particularly where the properties are rented out.

2. How do council costs change with different types of population growth?

The type of population growth can have significant influences over council costs, varies across the state and has many different overlays. As noted above, greenfield and infill developments may face different cost structures.

Demographics is a major factor. For example, if the growth is driven by young families, there is increased demand for sporting facilities, bike ways, pre-schools, youth services and activities. If population growth is being driven by retirees, councils face the additional costs associated with accessible infrastructure and related services. In the latter case, councils are also impacted by lower revenue as a larger proportion of the population will receive the pensioner rate rebate. The NSW Government continues to fund 55% of the rebate but remaining 45% is a cost to councils and communities.

Councils costs are also impacted by an influx of social and community housing and the transfer in status of existing social housing. Community housing and aged care are increasingly being run by not-for-profit Public Benevolent Institutions which are exempt from land rates. Councils with this type of residential development continue to provide services to the occupiers of these premises such as libraries, footpaths, open space and leisure facilities however, there is no contribution made towards supporting the network of services. This also needs to be addressed through rate reform.

3. What costs of population growth are not currently funded through the rate peg or developer contributions? How are they currently recovered?

As noted above, infrastructure contributions do not fund:

- the construction and fitting out of social and community infrastructure such as libraries, sporting facilities. aquatic centres, or community centres or other recreational facilities. They only fund the land for such facilities

- asset renewal, depreciation and maintenance for new infrastructure, including infrastructure funded by infrastructure contributions such as roads, bridges, footpaths and drainage works funded by contributions
- operational costs
- increased demand for services (e.g. community services, childcare, development applications, regulatory services, sanitation etc).

Councils attempt to recover these costs through:
- rates, particularly special rate variations (SRVs)
- grants and subsidies when and where available
- fees and charges
- investment and entrepreneurial revenue (limited)
- reducing costs.

This usually proves to be inadequate and results in the delayed or non-delivery of infrastructure and services to the detriment of existing residents as well as the new residents. Existing residents are particularly disadvantaged by SRVs to forward fund infrastructure for new development.

4. Do you have any views on the use of the supplementary valuation process to increase income for growth, and whether this needs to be accounted for when incorporating population growth in the rate peg?

The supplementary valuation process is important to the proper functioning of the rating system. It is the only existing mechanism that allows the rate base to expand with population growth. However, as the PC has found, it does not provide adequate revenue to support the growth, particular the provision of infrastructure.

The supplementary valuation process also fails to capture secondary dwellings, as previously noted.

In the absence of alternative models, LGNSW can see no reason to change the current practice.

5. Are there sources of population data we should consider, other than the ABS historical growth and DPIE projected growth data?

Of the options presented by IPART, LGNSW considers the most appropriate methodology to be projected growth (as provided by DPIE) with adjustment for actual historical growth based on ABS data.

Projected growth is relevant as this will be the population that infrastructure planning and delivery is based on. However, many councils lack confidence in the DPIE data and seek the assurance provided by census based ABS data. Many councils report underestimation of growth or over estimation of decline, particularly in rural and regional areas.

6. Is population data the best way to measure the population growth councils are experiencing, or are there better alternatives (number of rateable properties or development applications, or other)?

To the extent that the costs of infrastructure and service delivery are based on the number of users, population data will provide the best indicator. It also provides the benefit of capturing the number of people housed in secondary dwellings. However, consideration could be given to referencing other data such as Occupation Certificates, DAs or supplementary valuations. However, it is unclear whether this will make a material difference in the long run.

7. Do you think the population growth factor should be set for each council, or for groups of councils with similar characteristics? How should these groups be defined?

Ideally a population growth factor would be determined for each council so that the growth factor reflects the individual characteristics of each area and the specific nature of that growth. LGNSW acknowledges that this would be administratively complex but as a minimum the growth factor should be determined for cohorts of councils with similar characteristics.

8. Should we set a minimum threshold for including population growth in the rate peg?

No, if population growth is considered a cost driver that is not adequately captured in the rate peg, it follows that all population growth should be included in the rate peg.

9. What is your view on the calculation of the growth factor – should we consider historical, projected, projected with true-up, a blended factor or another option?

As noted under question 5, of the options presented by IPART, LGNSW considers the most appropriate methodology to be projected growth (as provided by DPIE) with adjustment (true-up) for actual historical growth based on ABS data.

10. How should the population growth factor account for council costs?

In the interests of administrative simplicity 100% of the population growth factor should be applied. It would be difficult to determine adjustments for individual councils based on growth in revenues outside the peg.

11. Do you have any other comments on how population growth could be accounted for?

As noted in our introductory comments, LGNSW believes that the best solution is to simply abolish rate pegging. This would help support the financial sustainability of all councils not just growth councils, however defined.

Another alternative would be to revisit IPART's original recommendation in the final report of the Review of the NSW Local Government Rating System that involved growth outside of the peg based on Capital Improved Valuations (CIV). The model currently proposed model differs from the CIV based model seeks to incorporate population growth within the peg.

12. Do you have any comments on our proposed review process and timeline?

LGNSW recommends that the review process be extended.

The issues involved in developing a methodology to insert a growth factor into the rate peg are highly complex. The process has been further complicated by the Government's linking of reform of the rate peg to reductions in infrastructure contributions. As noted at the outset, the review paper is best described as a preliminary step in the review process. It presents a high level overview and appropriately seeks comments from councils and other stakeholders on basic foundational elements of a new model. Councils appreciate this, but they will need the opportunity to provide detailed comment on more developed models and options. LGNSW acknowledges that IPART will be conducting workshops with councils as well as targeted individual interviews as part of the next stage of the consultation process. However, LGNSW further recommends that a second issues paper be released for consultation before IPART advances to the Draft Report stage.

Questions to IPART

The Issues Paper raises a number of questions that need to be addressed in the next rounds of consultation to help councils make definitive comments. These include:

- Will the growth factor apply to all ratepayers across the local government area or only to new development?
- Will the growth factor be restricted to residential rates or will it apply to other rating categories (e.g. business)?
- Will there effectively be two pegs – one for designated growth areas and the standard peg for other councils?
- Will the additional rate be in the form of a Special Rate?
- Application of a growth factor based Special Rate would be relatively straight forward for greenfield development, but how would it be applied for infill development?
- How will the introduction of a population growth factor affect Special Rate Variations (SRVs)? Would existing variations be retained? Modified? Will councils subject to the population growth factor be able to apply for future SRVs? or, How will SRV applications be affected by the population growth factor?
- Will there be multiple growth factors applied in local government areas that experience both greenfield and infill development?
- Will the higher growth factor inclusive rate apply permanently, or will it apply for a fixed period?
- Depending on the definition of growth thresholds for eligibility (e.g. setting the threshold at the NSW average population growth rate) many councils that experience new growth and development will not benefit from the growth factor. Will the proposed reduction in infrastructure contributions (e.g. through further restriction of the essential infrastructure list) apply to all councils or only those councils who would have the benefit of a growth factor? If it will apply to all councils, how is it proposed to compensate councils below threshold councils for the loss in contributions?

Conclusion

The list above is not exhaustive and LGNSW will be pleased to continue working with IPART and other stakeholders in developing a methodology that will help address the problems associated with rate pegging and provide a more equitable outcome for councils and communities. We look forward to reviewing more detailed models of how a population growth factor can be incorporated into the rate pegging process. This will enable us to offer more definitive feedback. LGNSW appreciates that this is a complex task.

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