

Mr Andrew Nicholls PSM
Chief Executive Officer
Independent Pricing and Regulatory Tribunal
PO Box K35
Haymarket Post Shop NSW 1240

Via email: [REDACTED]

Dear Mr Nicholls,

Discount Rate for Local Infrastructure Contributions

On behalf of The Parks, Sydney's Western Parkland Councils, I am writing to request that the IPART review the methodology for calculating the local government discount rate used by local councils when using the net present value method for updating Section.7.11 plans when setting infrastructure charges.

A land and acquisition study done on behalf of the Western Sydney Planning Partnership (WSPP) in 2022 identified a \$1.1 billion structural gap between local contribution plan income and actual land acquisition costs for the growth areas of Western Sydney. One of the recommendations in the study was the use of a net present value (NPV) calculation methodology to calculate rates (including for land) in local contributions plans, particularly where these contributions plans contain significant land acquisition-related costs.

This study identified also that when setting infrastructure charges, councils are exposed to three key risks that can result in a shortfall in the funding required to deliver planned infrastructure. These risks relate to development timing – which is a result of the mismatch between infrastructure outlays and the anticipated contribution revenues; market take-up – whether the forecast development will materialise in the life of the plan; and cost escalation arising from two separate sources – inflationary forces and increases in infrastructure quality standards or performance specifications over time.

In September 2024, we wrote to Ms Kiersten Fishburn, Secretary of the Department of Planning, Housing and Infrastructure (DPHI) requesting DPHI provide a determination on the use of measures to mitigate the risks associated with setting infrastructure charges, when councils utilise the NPV method for updating Section.7.11 plans. In her response, we were encouraged to contact IPART for consideration of this matter.

The WSPP has obtained expert advice from The Centre for International Economics (CIE) as a basis to request a review of the methodology for calculating the recommended discount rate used in the NPV methodology to set contribution charges. In summary the key points in the CIE paper are:

- IPART currently sets a discount rate for developer contributions that is based on debt finance. This provides a very low discount rate (currently 1 per cent real).
- CIE recommends that IPART moves to a benchmark entity approach, consistent with how IPART thinks about cost of capital for other areas of regulation. This approach

would mean applying a cost of capital consistent with the level of systematic risk of the activities that are being undertaken by councils as part of their local infrastructure contribution plans.

- CIE also recommend that the risk level for these activities be above the risk level for the economy in general. Based on evidence from public companies that undertake similar activities, they recommend a risk level that equates to an equity beta of 1.47 with a debt share of funding of 40 per cent.
- It is not clear if the discount rate used for council contributions should be a pre-tax or a post-tax discount rate. Under the above recommendations, the post-tax real discount rate (using February 2025 IPART data) would be 6.5 per cent and the pre-tax real discount rate would be 8.5 per cent.

At its March meeting, The Park's General Managers Group resolved in part to:

- b) ENDORSE the Chair of The Parks General Managers Group writing to the Chief Executive Officer of IPART requesting that IPART review their methodology for calculating the local government discount rate used by councils when using the NPV method for updating Section.7.11 plans when setting infrastructure charges.**

The CIE report is attached. I understand there was an informal discussion between CIE and IPART officers during the preparation of the report.

I would like to now request your support to review the methodology for calculating the local government discount rate used by councils when using the NPV method for updating Section.7.11 plans when setting infrastructure charges.

Please feel free to contact WSPP Director Luke Nicholls at [REDACTED] or on [REDACTED] or myself on [REDACTED] should you have any questions.

The WSPP office will contact your office to seek to arrange a time to provide you with an overview of the matters raised in the report.

Yours sincerely,

[REDACTED]

Ben Taylor
Chair, The Parks, Sydney's Parkland Councils
Chief Executive Officer, Wollondilly Shire Council

Attachment:

"Discount Rate for Developer Contributions", The Centre for International Economics (18 March 2025)