Author name: G. Kennett

Date of submission: Friday, 30 July 2021

Your submission for this review:
The submission is detailed in the attached correspondence. In conclusion, the proposed population growth factor is supported if; The factor is applied evenly to all councils in NSW based on state growth figures Any charges, levies, or contributions paid by councils to the NSW Government are added to the permissible income over and above rate pegging amounts The ESL and EPA Waste Levy now account for 10% of total general rates revenue for Kyogle Council, which is then handed to the NSW Government. If the state wishes to recover these costs from the local community, then at the very least, this must be accounted for outside the rate pegging system. If there is going to be a population growth factor applied over and above the rate peg, then it should be applied on the basis of the state-wide growth figure, and apply to every council equally. This will encourage those who have the capacity to raise additional revenue through available sources to do so, while ensuring that those not presently experiencing growth, have an opportunity to provide their community with a standard of services that might encourage growth in their areas. If the population growth factor were to be applied in this manner, it would be simple to administer, and the worst that could happen is a series of thriving and vibrant communities right across the whole state, which would benefit of all of NSW.

Reference: IPART Rate Peg
Contact: Graham Kennett

July 30, 2021

Independent Pricing and Regulatory Tribunal
PO Box K35, Haymarket Post Shop
Sydney NSW 1240

Re: Review of the rate peg to include population growth

The current proposal being considered by the IPART is deeply flawed in its scope and focus. The premise that the Rate Peg should be varied for those areas that are experiencing growth, whilst remaining in place to restrict those areas that are experiencing population decline, is almost akin to planning for the destruction of regional communities, and will only serve to expand the gap between those that have and those that have not. This flies in the face of the principles of Horizontal Fiscal Equalisation, and is seen as deeply insulting to struggling regional and rural communities.

Limiting the ability of a council to generate revenue undermines its ability to deliver services to attracts new and retains existing residents. The current oppressive arrangements stack the odds against rural and regional councils to grow.

What we are seeing in rural and regional NSW, is that the revenue available to councils has diminished to such an extent, that it has led to a decline in services and a major factor leading to net migration away from these areas. At almost every turn, there is another government regulation, restriction or redirection of funding that reduces revenue available to these councils. The minimum per capita payment in Australian Government Financial Assistance Grants (FAGs), rate pegging, matching funding requirements for external grants, competitive grants focused on areas of growth, are all examples of this cumulative impact of revenue pressures that is perpetuating declining population trends. For clarity, the rate peg does not allow for the general revenue of councils to increase with price increases each year. The rate peg is specifically designed to reduce the real level of income generated by councils to below the cost of delivering services, through the application of an arbitrary "*productivity factor*" over many years, which has left councils in NSW on the brink of financial failure.

There is a pronounced vertical fiscal imbalance that exists in the Australian federation, and a dramatic horizontal fiscal imbalance between councils in NSW that threatens the long-term sustainability of local government in NSW. There have been severe revenue constraints and cost shifting liabilities imposed on local government by the NSW state government, as well as grant funding reductions in real terms from both the NSW and commonwealth governments. This situation has led to a crisis in the financial sustainability of local government in NSW and the services it delivers to the local communities. There has been an awareness of this crisis for well over a decade now, and despite multiple reviews and inquires providing recommendations and solutions, the situation remains essentially unchanged today.

Horizontal fiscal imbalance occurs if different governments at the same level in a federation (eg different councils) possess unequal capacity to provide public services. This horizontal fiscal imbalance is obvious when comparing local government areas across NSW, with the services delivered in many regional, rural and remote communities a far cry from those afforded to their metropolitan counterparts.

The principles for the distribution of FAGs were designed to help address this in some way. However, they have also been criticised for the limitation that the minimum per capita amount of the FAGs distribution places on this objective. Councils on the minimum grant generally:

- Have greater revenue raising capacity
- Are not relatively disadvantaged
- Have economies of scale
- Are geographically smaller
- Experience year on year growth

The minimum per capita amount severely restricts the state's ability to allocate an additional share of FAGs to those that need it to deliver a minimum service level to communities that lack access to economies of scale or scope, have low socio-economic status, or are remote. The per capita minimum grant amount is increasingly diverting income away from those who need it the most, and adding to the horizontal fiscal inequity that exists between metropolitan and regional communities.

In essence, the very councils that are now being considered to be able to generate additional general rates revenue by altering the peg, are already receiving a disproportionate share of the funding available through the FAGs. This is funding that should be going to those councils that need it most, which are generally those lacking growth. Now IPART is being asked to consider a proposal to allow these same councils to generate even more income, and as if to rub salt into wounds, councils that genuinely need more revenue are excluded from even being considered in the process.

The financial relationship between state and local government in NSW is cause for much angst. The NSW Government does provide special purpose grants to local government, but for the most part these have historically been essentially compensation for the transfer of assets and/or service responsibility such as Regional Road grants, the Country Towns Water Supply and Sewerage Program, library subsidises and pensioner rebates. Not only is the revenue transfer from the NSW government to local government relatively small, there is the control over general rates revenue, as well as the impact of cost shifting associated with a variety of services imposed onto local government by the state.

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Cost shifting occurs when the responsibility for, or merely the cost of, providing a certain service, concession, asset or regulatory function is shifted from one sphere of government to another, without corresponding funding or revenue raising ability required to deliver that new responsibility. Cost shifting forces councils to divert ratepayers' funds away from much-needed local infrastructure projects, to meet additional demands placed on them by state and federal governments.

The most recent cost shifting report from (Local Government NSW, 2018) outlined the extent of cost shifting on local government in NSW and concluded that cost shifting continues to place a significant burden on councils' financial situation. The key points from this report are summarised below;

- cost shifting was estimated at $820 million in 2015/16 (or around 7.5% per cent of councils' total income)
- cost shifting is up $150 million from 2013/14, and totals $6.3 billion over the last 10 years
- cost shifting exceeds the estimated annual infrastructure renewal gap
- The NSW government is responsible for 98% of the cost shifting with the federal government responsible for the remaining 2%
- The main contributors are;
    - EPA Waste Levy - $305 million
    - Emergency services contributions - $127 million
    - Public libraries shortfall - $130 million
    - Pensioner rebate reimbursement gap - $61 million
    - The rest are various regulatory and compliance burdens

In relation to the impact of rate pegging on Councils (Allan, Darlison, & Gibbs, 2006) shows that the overall rate increases in NSW were lower than in any other state between 1995/96 and 2003/2004. The increases over this period were; NSW (29.2%), ACT (35.2%), Tas (36.3%), SA (55.1%), QLD (55.6%), WA (64.8%), Vic (66.1%)

The increase in Gross Domestic Product (GDP) for this same period was 61.8%. If NSW rates revenue was allowed to increase in line with GDP over the period, this would have provided for an extra $600 million in rates revenue annually. This would have more than likely allowed local government in NSW to avoid the annual funding shortfall and financial burden it faces today.

In order to ameliorate the financial sustainability crisis facing local government in NSW, and provide ongoing clarity and stability around the level of funding for local government, there is a need to focus on;

1. Providing certainty for local government revenue by removing or significantly altering the rate peg system
2. Reducing cost shifting from state to local government by;
    - Reducing the regulatory and compliance burden on local government
    - The NSW Government taking back responsibility for Regional Roads
    - Increased library funding

- Fully funding pensioner rebates
- Removing the EPA waste levy from councils outside the metropolitan and coastal growth areas
- Placing all NSW Government Levies and taxes such as the Emergency Services Levy (ESL), outside the general revenue affected by rate pegging

There are two main sources of revenue available for councils in addition to the rate pegged general rates revenue. These are from Supplementary Valuations and Infrastructure Developer Contributions. Supplementary Valuations primarily result from new land releases, and are generally closely aligned with growth. Income from infrastructure contributions is also linked to new development and land releases, and essentially only available to Councils that are experiencing growth. When growth is planned for and managed well, these charges should allow for the additional costs associated with growth to be funded by developers, rather than general rate players. The recent NSW Government policies that push to limit these charges, essentially led to the focus on using general rates to make up the difference. This is just shifting the cost away from the property developers that profit from new development, and shifting it on to the existing population. If this policy was not in place, then the need to find an alternate source of revenue to fund growth would not exist.

The other area for growth mentioned in the issues paper was infill or increased residential density, which the Issues Paper notes does not attract the Supplementary Valuation process. However, a well-constructed Developer Contributions Plan can recover some of the additional costs from developers. The increased density of population also brings increased opportunities for economies of scale.

Where an area has population decline and/or a static population, this lack of growth also reduces access to economies of scale. When this is combined with ongoing increased government compliance requirements, additional cost shifting to local government, and increased community expectations, the cost of delivering services increases on a per capita basis for these communities. Where this whole review of the rate peg to include population growth process falls down is that it fails to recognise this, and offers no opportunity for additional income generation for these councils.

Where the biggest flaw lies with the current logic around treating councils with growing populations differently, is that the current rate peg methodology groups all councils into a single Local Government Cost Index (LGCI) model. This model fails to account for differences in the cost of service delivery, and access to economies of scale, that exist across the many councils in NSW. The model is heavily skewed towards metropolitan and large regional councils, and significantly disadvantages rural and remote councils by comparison.

A recent example is the increases in Emergency Services Levy, which was accounted for in the LGCI as a 0.02% increase in general rates revenue in 2021-22, but for Kyogle Council the actual increase in the ESL that year was 1.6% of the total general rates. So, of the 2.6% rate peg, 60% of the additional income generated went straight back to the NSW Government in ESL increases alone. The cumulative impact of the increases in ESL since 2018-19 has been equivalent to 2.94% of general rates, with the LGCI providing for a cumulative increase in general rates of 0.2% over the same time.

This is just one example of many where the LGCI model fails to account for what are significant discrepancies between rural, remote, regional, and metropolitan councils.

The ESL and EPA Waste Levy now account for 10% of total general rates revenue for Kyogle Council, which is then handed to the NSW Government. If the state wishes to recover these costs from the local community, then at the very least, this must be accounted for outside the rate pegging system.

If there is going to be a population growth factor applied over and above the rate peg, then it should be applied on the basis of the state-wide growth figure, and apply to every council equally. This will encourage those who have the capacity to raise additional revenue through available sources to do so, while ensuring that those not presently experiencing growth, have an opportunity to provide their community with a standard of services that might encourage growth in their areas.

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In conclusion, the proposed population growth factor is supported if;

- The factor is applied evenly to all councils in NSW based on state growth figures
- Any charges, levies, or contributions paid by councils to the NSW Government are added to the permissible income over and above rate pegging amounts

Should you have any further enquiries please do not hesitate to contact me during business hours on [redacted]

Yours faithfully

[redacted]

General Manager

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References

Allan, P., Darlison, L., & Gibbs, D. (2006). *Are Councils Sustainable? Final Report: Findings and Recommendations of the Independant Inquiry Into the Financial Sustainability od NSW Local Government.*

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