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Independent Pricing and Regulatory Tribunal (IPART)

By email: ipart@ipart.nsw.gov.au

Review of discount rate methodology for local government infrastructure contributions

Local Government NSW (LGNSW) welcomes the opportunity to provide feedback to IPART's review of the discount rate methodology for local government infrastructure contributions. This submission follows initial discussions at our consultation meeting with IPART on 2 October 2025.

As highlighted during the meeting, the review of this issue is a highly complex and technical matter. As LGNSW is the peak body for councils in NSW, this is a principles-based submission and LGNSW encourages IPART to consider the detail in individual submissions from councils directly impacted by this review.

Current practice

Under current IPART guidelines, councils may choose to apply a Net Present Value (NPV) approach when preparing and administering a Section 7.11 contributions plan. This approach uses a discounted cash flow model, where contribution rates are calculated so that the present value of anticipated revenue from future development is equal to the present value of anticipated costs of the infrastructure needed to service future development. It allows councils to account for timing differences between when the infrastructure is delivered and when developer contributions are received. The discount rate under this model is currently based on the cost of debt.

LGNSW understands that The Hills Shire Council is the only council in NSW using the NPV model in its contributions plans. Per our consultation with the council, this method is highly complex and resource-intensive, requiring substantial input from council finance staff.

This complexity likely explains the limited uptake of the NPV model, with most councils instead preferring simpler and more traditional approaches such as indexation using appropriate indices (e.g. CPI or building cost indices) in their contribution plans.

Local government borrowings

According to the ABS, in 2023-24 NSW councils held $3.47 billion in loans against $246.73 billion in assets, which reflects a very low gearing ratio. Councils maintain a very low uptake of debt due to financial and political reasons. Financially, exposure to fluctuating interest rates and potential changes to government grant funding can impact on councils' ability to service debt and may deter councils from seeking loans. In addition, the depreciation expense for assets funded by debt is also a deterrent. Politically, there remains a strong perception that debt equates to poor financial management, a view perpetuated and reinforced by the emphasis of State and Federal Governments, the Reserve Bank and the media on debt reduction and maintaining AAA credit ratings.

While debt aversion can contribute to infrastructure backlogs and affect intergenerational equity, attitudes are gradually changing. Many councils recognise the need for prudent use of borrowings through financial institutions such as T-Corp to equitably fund long-term infrastructure.

It is also noted that a common misunderstanding of intergenerational equity also acts as a deterrent to borrowings. Communities may interpret intergenerational equity as meaning you should not incur any debt that will be passed on to future generations. This view is incomplete as it fails to recognise that it is totally appropriate to incur debt to fund long-term infrastructure. This debt should be paid off over the lifespan of the asset, which may well extend into future generations with current and future beneficiaries contributing to the cost.

Review of discount rate methodology

In April 2025, the Western Parkland Councils wrote to IPART requesting a review of the discount rate methodology. In theory, a higher discount rate (**cost of equity**) would result in higher developer charges and support higher overall contribution levels for councils. The councils engaged with the Centre of International Economics (CIE) in support of their request. The CIE report argues that councils' infrastructure is largely funded through equity (ratepayer revenue), rather than debt, and that a cost of equity rate as opposed to cost of debt, would better reflect the real cost of capital under the NPV model.

As acknowledged in the Issues Paper, IPART has historically taken the view that councils are not corporations able to raise equity externally, and therefore their cost of capital should be based on debt.

LGNSW understands the rationale of the two differing views of the discount rate and recognises that the interactions between discount rates, contribution levels and development feasibility are highly complex. We recommend IPART consult with other technical stakeholders to fully understand the potential financial impacts.

Given that only one council currently uses the NPV methodology based on cost of debt, it is questionable whether there would be much of an increase in uptake of a NPV model based on the cost of equity. It would not appear that the cost of debt vs the cost of equity is the decisive factor in itself.

LGNSW recommends IPART further examine barriers to uptake. To support broader adoption, IPART should provide clear guidance, standardised tools and templates and the necessary training to help councils consider using the NPV model in administering their contributions plans.

Separately, LGNSW continues to advocate for the removal of the current caps on developer contributions and strongly opposes the deferral of contribution payments by developers. In the past, councils have faced issues recovering money owed for infrastructure contributions. The time and administrative costs in pursuing these outstanding payments can be substantial. Where payments are deferred, councils can also be exposed to greater risk of default by developers and costly, protracted debt recovery proceedings. Delayed payment also exposes councils and ratepayers to cost escalation as the price of purchasing land and delivering infrastructure increases over time.

LGNSW would like to emphasise that the review of the discount rate methodology for local government infrastructure contributions should ensure it is fit for purpose and consistent with the aim of timely provision of local infrastructure. More importantly, any reform should not disadvantage councils and more importantly reflect the financial sustainability of the local government sector. Given that the differences between the cost of equity and cost of debt models are only likely to be marginal, LGNSW recommends that councils have the choice of either option alongside existing cost index-based options.

We look forward to continued engagement on this issue.

For further information, you are welcome to contact LGNSW Chief Economist Shaun McBride on [redacted].

Yours sincerely

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