Review of Fees for Development Control Services

Issues Paper

INDEPENDENT PRICING AND REGULATORY TRIBUNAL
OF NEW SOUTH WALES

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DP 23 December 1997

Submissions

Public involvement is an important element of the Tribunal's processes. The Tribunal therefore invites submissions from interested parties to all of its investigations.

Submissions should have regard to the specific issues that have been raised. There is no standard format for preparation of submissions but reference should be made to relevant issues papers and interim reports. Submissions should be made in writing and, if they exceed 15 pages in length, should also be provided on computer disk in word processor, PDF or spreadsheet format.

Confidentiality

Special reference must be made to any issues in submissions for which confidential treatment is sought and all confidential parts of submissions must be clearly marked. *However, it is important to note that confidentiality cannot be guaranteed as the Freedom of Information Act and section 22A of the Independent Pricing and Regulatory Tribunal Act provide measures for possible public access to certain documents.*

Public access to submissions

All submissions that are not subject to confidentiality will be made available for public inspection at the Tribunal's offices immediately after registration by the Tribunal and also via the Tribunal's website. Transcriptions of public hearings will also be available.

Public information about the Tribunal's activities

A range of information about the role and current activities of the Tribunal, including copies of latest reports and submissions can be found on the Tribunal's website at www.ipart.nsw.gov.au.

Submissions on the issues raised in this paper should be received no later than 23 February 1998.
Comments or inquiries regarding this report should be directed to:
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1 INTRODUCTION

This issues paper is the first stage in the process of reviewing fees charged by councils and other consent authorities for development control services.

Currently, the approval and certification system is governed by two main pieces of legislation: the *Environmental Planning and Assessment Act 1979* (EP&A Act) and the *Local Government Act 1993*. Issues relating to subdivision are covered by the *Local Government Act 1919*. Legislation concerning conservation, land use and other issues also influences the control of development.

New legislation streamlining the development control system will come into effect on 1 July 1998.

Ahead of the introduction of the new legislation, and pursuant to section 12A of the *Independent Pricing and Regulatory Act 1992*, the Premier has requested the Independent Pricing and Regulatory Tribunal (IPART) to review pricing principles for development assessment fees. The terms of reference for the review are set out in Attachment 1.

For the review, IPART is required to:

a) determine pricing principles for development fees

b) establish guidelines for competitive neutrality.

1.1 Changes to development control and fees

The *Environmental Planning and Assessment Amendment Act 1997* will:

- introduce a single, integrated system of providing consent to development
- provide for a proposed development to be assessed by a process which reflects the significance of that development
- involve the private sector in the assessment process and in issuing certificates.

The Department of Urban Affairs and Planning has produced a brochure outlining the forthcoming legislative amendments and providing contacts for further information. A copy of the brochure is enclosed with this issues paper.

IPART's review will establish pricing principles and an indicative fee schedule for fees charged for development assessment services, and provide guidance for fees for the 2 areas which will be opened up to competition - complying development and post-approval processes.

IPART welcomes submissions in response to this issues paper. **Submissions must reach IPART's office by Monday, 23 February 1998**.

Public hearings in relation to this review will be held in Sydney during the first quarter of 1998. Following the hearings, an interim report will be published. Further submissions will be sought prior to the release of the final report in June 1998.

2 CURRENT AND PROPOSED FEES ARRANGEMENTS

2.1 Introduction

This chapter:

- outlines the current legislative basis for development applications
- comments on aspects of the new Amendment Act
- identifies the fees that are covered by this review.

2.2 Current legislation

Section 68 of the *Local Government Act 1993* (LG Act) outlines the building activities for which prior approval from council is required. These activities include the demolition and erection of buildings. Division 3 of Chapter 7 of the LG Act prescribes the processes for applications, and states that applications must be accompanied by a fee.

Subsection 77(3) of the *Environmental Planning and Assessment Act 1979* (EP&A Act) outlines the development application process. Maximum fees are prescribed by the regulations.

Subdivision development is controlled under Part XII of the Local Government Act 1919. It is also covered in many cases under the EP&A Act, through local environmental plans. The legislation permits councils to charge fees for subdivision, development and building applications, subject to maximum fee levels specified in the EP&A Act's regulations. Councils determine their own fee schedules for a range of matters including, for example, the checking of design drawings for roads, on-site inspections, and inspections for final certification and release of plans.[1]

Under the present system there are many pieces of legislation and a multiplicity of arrangements for development processes and for the setting and charging of fees.

2.3 New legislative process

The *Environmental Planning and Assessment Amendment Act 1997* brings building, development and subdivision approval processes together under the one piece of legislation.

Development can be classified as:

- state significant or local – local development requires consent by councils or other consent authorities, state development requires the consent of the Minister.
- complying – requiring consent by councils or accredited certifiers.
- exempt – not requiring consent.
- prohibited – development that is not permitted.

State significant development includes major industrial developments, for example a coal mine, which are of state or regional significance. Under the new Act the Minister for Urban

[1] *Review of Subdivision and Outdoor Advertising Fees*, N.A.T. Consulting Pty Limited, April 1995.

Affairs and Planning assesses the application and either approves or refuses the proposed development.

Local development may include shopping centres or town house developments. In most cases, local councils will be the decision makers for local development.

Complying development is routine development, the environmental impact of which can reasonably be assessed in terms of predetermined criteria such as height, set back and the Building Code of Australia (criteria covering, eg, structural soundness, design, amenity and access, and water management). Complying development may include alterations and additions to single-storey residential dwellings. The private sector will be empowered to compete with councils in issuing complying development certificates.

Exempt development does not require any form of consent. It may, in certain circumstances, include garages, garden sheds and internal renovations.

The Act includes areas where complying and exempt development can not apply.

Under the new legislation, the Minister for Urban Affairs and Planning will authorise professional associations to act as accreditation bodies that will assess whether individuals should be granted accreditation.

2.4 Reforms of fee structures

The EP&A Act's regulations establish maximum fee levels for development charges. In the past 17 years that the regulations governing fees have been in force, there have been no significant changes in the fees or fee structure. Although some fees were increased as part of the changes to the regulation in 1994, fees have not been indexed, nor have fee structures undergone any major reforms. In developing principles for fee structures, and in developing indicative fees, there are many issues to be considered.

The provisions regarding the charging of fees in the Local Government Act 1993 are general (Section 608). Section 609 of the Act lists the factors which must be taken into account by councils in determining fees:

- "the cost to the council of providing the service
- the price suggested for that service by any relevant industry body or in any schedule of charges published, from time to time, by the Department (of Local Government)
- the importance of the service to the community
- any factors specified in the regulations."

There is also a provision for higher or additional fees to be charged for a higher standard of service.

Other issues to be considered in developing pricing principles and new fee levels are discussed in Chapters 3 and 4.

2.4.1 How will fees be charged under the new system?

Fees are currently charged separately for a development application, building application and subdivision application. Under the new system, these separate applications will not

exist and only one fee will be charged at the initial development application stage. Councils and State Government will be able to charge additional fees for services open to competition, including post approval certificates.

2.5 Scope of this review

IPART's review will (a) establish pricing principles and indicative levels for monopoly fees in the development control process, and (b) provide guidance to help local government in setting fees for other services, which will be open to competition.

Table 2.1 lists the fees which are to be addressed by this review.

Table 2.1 Development fees

Fees for which IPART is to recommend pricing principles and establish indicative fees	Fees for which IPART is to consider competitive neutrality issues	Fees and charges not covered by the review
Development Applications	Complying Development Certificates	Developer Contributions S94
• Advertisements	Construction Certificate	All Bonds, eg. Footpath Deposits
• Subdivisions	Compliance Certificate	
• Hospital, School or Police Station erected by a Public Authority	Occupation Certificate	Administration Fees not currently regulated, e.g. Monthly Building Statistics
Modification of a Consent	Subdivision Certificate	
Certified Copy of a Document held by a Consent Authority		
Council Registration of Certificates		
Planning Certificate		
Building Certificate		
Review of a Council Decision (New fee – s82A of the Act)		
Issue of Strata Subdivisions (NB this may become open to competition as a result of further legislative amendments)		

The specific fees for which principles and indicative pricing levels are to be established by this review are the Development Application fees associated with state significant and local development as defined by the EP&A Act, (ie development fees where the consent authority is either a council or the Minister). Part 9 of the EP&A Amendment Regulation[2] provides a description of the fees that are the subject of this review. A new fee will be charged for reviewing a council decision, as per Section 82A of the EP&A Amendment Act[3]. Principles and indicative fee levels are also to be established for the registration of documentation from accredited certifiers.

[2] Copies of the Regulation and Acts are available from the NSW Government Information Service, Ph: 9743 7200.

[3] A power which exists under the LG Act at Section 100, and which is to be reproduced in the EP&A Act.

The Tribunal will not recommend pricing principles for fees for complying development certificates as the issuing of these certificates will be competitive. The other areas which will be open to competition are the issuing of post approval certificates - construction, compliance, occupation and subdivision. As part of its review IPART will consider competitive neutrality issues to ensure that there is a level playing field once competition is introduced (see chapter 4).

3 PRICING PRINCIPLES

3.1 Introduction

This chapter raises issues associated with:

- which costs should be recovered by development fees
- what are efficient costs
- what pricing structures should be adopted

3.2 Which costs?

Development assessment fees should be set to recover the efficient costs associated with assessment of developments. Relevant costs may include labour, materials and a share of common or overhead costs such as head office costs and capital costs. In reviewing which costs are relevant to recover, IPART will consider:

- fully distributed costs
- marginal costs
- avoidable costs.

Fully distributed costs involves calculating the direct costs of providing the development assessment service plus a share of the council's common or joint costs. An example of joint costs is the costs of lighting and office space. Joint costs tend to be allocated to the various development assessment services on an arbitrary basis, eg according to the proportion of revenue earned. This approach is commonly used because it is relatively simply to apply and the information tends to be available from councils' accounting systems.

Marginal costs refers to the change in total costs of providing one more unit of service, in this case the additional cost of assessing one more development application. Marginal costs are usually lower than fully distributed costs, because the latter includes joint costs.

Avoidable costs are the changes in costs which occur when an activity expands or contracts, eg the change in costs when development assessments increase by say 20 percent, or the reduction in costs which occurs when the activity is reduced by say 20 percent. Thus avoidable costs are the marginal costs of varying output over a range rather than by a single unit.

3.2.1 What is a cross subsidy?

Technically, a cross subsidy occurs where some customers pay less than the marginal (or avoidable) cost and others pay more than the stand alone costs of supply[4]. In reality there may be a substantial gap between the two cost points, and prices based on either set of costs may not represent a cross subsidy. The term, cross subsidy, is often used to describe a situation where customers meet varying proportions of the joint costs of providing the development assessment service.

[4] Stand-alone costs refer to those costs that would be incurred if that customer alone was being provided a service without the advantage of being able to share joint costs with other customers.

Measuring the extent of cross subsidies between activities can be complicated when there is a high ratio of common or joint costs to attributable costs[5].

Cross subsidies can lead to a dead weight or efficiency loss. This happens when the subsidy encourages an increase in consumption to the point where the value that the consumer places on the service is less than the cost of producing it. In the past social policies such as providing equal access to services were implemented through pricing policies. These days, community service obligations are replacing cross subsidies as a way of implementing government social policies and objectives.

A study undertaken by consultants engaged by the (then) Department of Planning in April 1994 concludes that:

> "In fifteen years of the EPA Act, the major set of fees has been amended once, and that only being to change the minimum fee;
> There is an apparent shortfall between development and subdivision application fees and processing costs;
> That the extent of the shortfall due to the level of council efficiency and what should remain unrecouped because of public good, is difficult to determine"[6].

Councils have advised that in general, the fees currently charged do not cover the costs of the services provided. This is also a concern of ratepayers, who perceive that they may be subsidising developers. At the same time, developers and the building industry are concerned about the possible impact of higher fees on the costs of development and housing.

3.2.2 Who benefits and how should Councils' common costs be dealt with?

A cost recovery policy raises a number of issues. Is it only the developer or owner who is the beneficiary and must therefore bear the costs, or does the wider community receive a benefit from the development assessment function? The important issue here is the extent to which community need, economic development or heritage issues should affect charging policy - or whether these issues are better addressed by other policy instruments.

The treatment of common or joint costs requires consideration. For example, should joint costs such as policy formulation and head office be included in development assessment fees? Should variations in costs for different council areas be reflected in fee levels?

IPART will be making recommendations on pricing principles for development fees. To help IPART determine which costs should be recovered, comments are invited on:

- ***whether development fees should be based on fully distributed costs, marginal costs, or some other method of calculating costs***
- ***how to identify and allocate overhead or joint costs of councils to development fees***
- ***whether, and if so, to what extent, 'public good' benefits should affect fee structures or levels or whether such benefits are better addressed through other mechanisms***
- ***whether councils' accounting systems and procedures provide adequate costing information.***

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[5] If a cost can be allocated directly to a specific customer or activity, it is attributable. If not, it is termed a 'common' or joint cost.

[6] A Base Costs Study of NSW Local Government Planning and Development control fees, BIS Shrapnel Pty Ltd and NAT Consulting Pty Ltd, April 1994, p143.

3.3 Efficient costs

The aim of regulation is to ensure that Councils are not rewarded for inefficiencies in their work practices. Efficient and effective price regulation should provide for:

- Economic efficiency – giving current and future users the correct price signals for use of the service.
- Revenue sufficiency – for a commercial organisation this objective is paramount – revenues must be commercially sustainable. This includes a return on and of capital where relevant.
- Efficient regulation – encouraging minimum cost operations.

Efficient costs are important to ensure economic efficiency. Price regulation should encourage councils to achieve a high level of efficiency relatively quickly.

The only publicly available information on the relative performance of councils is contained within the Department of Local Government's Comparative Performance Indicators. IPART notes in its interim report on Benchmarking Local Government Performance in NSW:

> "…a number of areas of concern exist. These will need to be rectified to increase the usefulness and effectiveness of the publication. The major worries about the publication are: comparability of data, scope of indicators, presentation, and timeliness."[7]

In considering recommendations for pricing principles, IPART will need to consider:

- the current performance of councils relative to best practice
- the extent to which efficiency improvements are realistically possible, given the current industry structure.

To assist IPART determine the extent of costs to be recovered, comments are invited on:

- ***what is the scope for efficiency improvements in the processing of development assessments by councils***
- ***how to ensure that cost recovery does not also recover the costs of inefficient and unnecessary work practices and procedures***
- ***whether size, location or other differences between councils affect processing costs. If there are economies of scale, how can these be assessed.***

3.4 Pricing structure

Generally, the current pricing structure for development applications is based on the value of the proposed development cost as depicted in Table 3.1.

[7] *Benchmarking Local Government Performance in NSW, Interim Report*, IPART, December 1997, p22.

Table 3.1 Current development application fees

Estimated cost of development	*Maximum amount of fee*
Not exceeding $100,000	$100 plus $3 for each $1,000
Exceeding $100,000 but not exceeding $500,000	$400 plus $1.50 for each $1,000 above $100,000
Exceeding $500,000 but not exceeding $1,000,000	$1,000 plus $1 for each $1,000 above $500,000
Exceeding $1,000,000 but not exceeding $10,000,000	$1,500 plus 75 cents for each $1,000 above $1,000,000
Exceeding $10,000,000 but not exceeding $100,000,000	$8,250 plus 50 cents for each $1,000 above $10,000,000
Exceeding $100,000,000	$55,000

Some councils have argued that the fee structure should take into consideration the complexity of applications, and should reflect the number of hours spent assessing applications.

Section 612 of the LG Act requires councils to publish the amount of proposed fees, and to consider any submissions made. Proposed fees must be published in the draft management plan for the year in which the fee is to be paid. If fees are established after the commencement of the management plan, council must give public notice of at least 28 days of the proposed fees.

This review is developing a formula or structure and indicative fee ranges for development control fees. Councils will base their own set of fees on these principles and advertise them through management plans. The review of benchmarking in local government, currently being undertaken by IPART, raises concerns about the effectiveness of the management plans as a consultative mechanism. Many councils use additional methods of reaching their communities, including forums, newsletters and the media.

IPART seeks comments on:

- ***whether fees should be based on the value of the proposed development, taking processing time into consideration or should reflect some other pricing structure***
- ***what kind of communication or networking mechanisms could be used to help councils to develop and implement new fee structures***
- ***what kind of communication mechanisms could be used to advise the public of the new fees set by councils and state government.***

Under the new legislation, accredited certifiers are required to forward a copy of certificates to councils for registration. This creates a new cost for councils. Whilst it is the accredited certifier who receives the certification fee, the council bears the costs of maintaining a registry.

IPART seeks comments on whether councils should recover registration costs through an explicit charge payable by the accredited certifier, through general rates, or some other means.

It could be argued that customers should have a greater say regarding the quality of the services they are paying for. A number of councils are either examining or have implemented guaranteed standards for the services they provide. For the development assessment function these service agreements might address timeliness for specific aspects of processing applications or for undertaking site inspections, list contact officers at council, or provide mechanisms for public consultation on developments.

IPART seeks comments on whether service agreements should be part of the development control system, what consultative mechanisms are appropriate for the development of such agreements, and what dispute resolution avenues should be available for such agreements.

4 PRICING OF COMPETITIVE SERVICES

4.1 Introduction

This chapter examines:

- which services will be subject to competition under the reforms
- when these reforms will be introduced
- what councils must do to comply with competitive neutrality principles.

4.2 Competitive neutrality

Competition between the private sector and the public sector in any business activity raises the issue of competitive neutrality, which is often referred to as "the level playing field". In this context, competitive neutrality means operating in an environment which ensures that a public sector business does not enjoy a net competitive advantage (or suffer a disadvantage) in comparison to a private sector business solely as a result of its public sector ownership. Competitive neutrality does not require governments to discount other competitive advantages that they might enjoy through size, buying power or specialist expertise.

The requirement to apply competitive neutrality principles is a key feature of Australia's National Competition Policy. It applies to local governments as well as to federal and state governments.

The Environment Planning and Assessment Amendment Act 1997 contains provisions that will open up a significant portion of the development approval process to competition. The Act will enable developers to obtain development certificates from accredited certifiers in the private sector. These certifiers will compete for this business with local government and state organisations.

4.3 Services which may be subject to competition

The Environmental Planning and Assessment Amendment Act lists five types of development activity which may be assessed by accredited certifiers:

- *complying development*
  Under the new legislation, councils and state government will be able to specify that certain development activities may be undertaken as complying development, subject to the issue of a complying development certificate. A complying development certificate will state that a planned development fits within this category and meets all specified requirements. This certificate must be issued by an accredited certifier or the local council, prior to the commencement of development work. The exact type of development activity that will be classified as complying will vary between council areas, depending on the requirements of each council.

- *construction*
  A construction certificate is an endorsement of building and subdivision engineering plans and specifications stating that work carried out in accordance with those plans and specifications will comply with certain requirements prescribed by regulations. It allows work to commence on site.

- *compliance*
  These are a range of certificates that must be issued at various stages of development to indicate that:

  a) specific building work or subdivision work has been completed and complies with relevant plans and specifications
  b) a condition of the specified building work or subdivision work has been fulfilled
  c) specified requirements of the regulations have been fulfilled.

  A series of compliance certificates may be issued during the course of one project. Examples include mechanical ventilation system or certification of structural engineering plans.

- *occupation*
  The occupation certificate authorises that a development is suitable for occupation and use. It is generally issued at the end of the project. An interim occupation certificate can be issued for part of the building while under construction.

- *subdivision*
  Local council planning instruments may, in the case of complying developments, allow minor subdivision plans to be registered at the Land Title Office without further council approval. A subdivision certificate is an endorsement of these plans stating that they comply with local planning requirements and the requirements of the Act. In the case of local or state significant development environment planning instruments may allow subdivision certificates to be issued for particular types of subdivision.

IPART understands that under the proposed reforms, local and state government will have considerable discretion as to the type of development activities for which the above certificates may be issued. Councils and state government have until December 1999 to implement the reforms under the EP&A Act. The potential anti-competitive effect of exercising this right to delay implementation is discussed in section 4.5.

It should be noted that the issue of whether any *additional* council businesses should be subject to competition is beyond the scope of this inquiry.

4.4 Current requirements for councils to comply with competitive neutrality principles

The National Competition Principles Agreement (NCP) states the key requirements of competitive neutrality. In summary these are:

1. All "significant Government enterprises" (as defined in Government financial statistics) must:

   (a) where appropriate; adopt a corporatisation model
   (b) impose:
   - full Commonwealth, State and Territory taxes
   - debt guarantee fees
   - regulations to which private sector businesses are normally subject.

2. Agencies which do not fit into the above category but nevertheless undertake some significant business activities, must:

- where appropriate, implement the above principles; or
- ensure prices charged for goods take account of debt guarantee fees, tax equivalent regimes and regulatory compliance, and reflect full cost attribution for these activities.

Clause 7 of the NCP states that these principles are to apply to local government.

The NSW Government has issued a policy statement on the application of National Competition Policy to local government to help councils implement competitive neutrality principles and other requirements.

The Department of Local Government (DoLG) has issued detailed guidelines to help councils apply competitive neutrality principles.

The NSW Government has rejected a prescriptive approach to the introduction of these principles. However, if a council business receives an annual sales turnover/gross operating income of $2m or more, the council is expected to adopt competitive neutrality principles in full. If a council believes the application of competitive neutrality principles to its business will be detrimental overall, it must conduct a public and independent benefit/cost analysis which shows the net cost. Less strict requirements are proposed for smaller council businesses.

The DoLG guidelines require each council to introduce a complaints mechanism for handling competitive neutrality complaints. This complaints mechanism should be incorporated within existing mechanisms for handling complaints about council behaviour. Complaints which cannot be resolved by a council, may be dealt with by DoLG.

In considering policies for pricing contestable services (ie services open to competition), IPART will have regard to the competitive neutrality principles discussed in the National Competition Principles Agreement and the above policy documents.

In respect of competitive neutrality, the key issue will be the allocation of costs. In particular allocation of:

- administrative and overhead costs
- costs between staff who undertake both monopoly fee development work and contestable work.

IPART is interested in hearing the views of councils and other parties on issues relevant to the application of the current guidelines and complaints handling mechanisms.

IPART is also interested in learning stakeholders' views on:

- ***whether councils' current costing systems and institutional structures can price contestable work***
- ***how councils will ring fence (ie separate the accounting of) contestable and non-contestable activities***
- ***whether councils have adopted tax equivalent regimes***
- ***whether councils should have the right to price in a non-competitively neutral way in order to pursue legitimate policy goals (eg to ensure the broader community benefits from the extensive development approval process).***

4.5 The introduction of competitive reforms

Councils and state government may decide when and to what extent, they will allow the certification of specified development activities to be open to competition with the private sector. This discretion could be used to delay competition in the contestable services.

A related issue is whether the complaints mechanism should operate to consider instances where competitive services have not been introduced, or be limited to complaints about the failure of councils to apply competitively neutral prices correctly to businesses for which competition has been introduced.

IPART is interested in hearing the views of stakeholders on the best way to introduce competitive services and pricing required under the new legislation.

ATTACHMENT 1 TERMS OF REFERENCE

I, Bob Carr, Premier of New South Wales, refer under Section 12A of the *Independent Pricing and Regulatory Tribunal Act 1992* the following matter to the Independent Pricing and Regulatory Tribunal:

> *the review and development of a pricing policy and recommended indicative fees charged by Local Government and other consent authorities for development control services under the Environmental Planning and Assessment Amendment Bill 1997, recently passed by the NSW Parliament.*

The purpose of the review is to:

1. develop principles and indicative fees for the development assessment system (excluding complying development); and

2. provide guidelines to assist in the setting of fees for complying development and post-approval processes, which are to be opened up to competition.

In particular, the Tribunal shall:

a) review the overall current pricing policies and fee structures of consent authorities as they relate to the development, building and subdivision functions under the Environmental Planning and Assessment Act 1979, Local Government Act 1919 and Local Government Act 1993;

b) identify those fees that may warrant continuing government regulation having regard to the guiding principles for legislation review specified in clause 5(1) of the Competition Principles Agreement;

c) examine through case studies, current practice with respect to the charging of fees and the principles established in this respect;

d) review the extent and type of research that has been undertaken in respect to the development of these pricing policies and fee structures;

e) report on the level and structures for the charging of fees by Local Government and other consent authorities for development control services as proposed under the Environmental Planning and Assessment Amendment Bill 1997;

f) make recommendations covering monopoly development assessment functions in respect to a transparent pricing policy, with indicative fees for a range of Councils having regard to consumer satisfaction and community participation and the balance of efficiency, effectiveness, quality delivery of service and equity considerations; and

g) develop principles which will provide guidance for the setting of fees for complying development certificates and for post-approval processes, having regard to competition policies.