26 April 2024

Hon Emily Suvaal MLC
Chair
Standing Committee on State Development
Legislative Council
NSW Parliament

Online submission at: www.parliament.nsw.gov.au

Dear Ms Suvaal

Inquiry into the ability of local governments to fund infrastructure and services

Southern Sydney Regional Organisation of Councils Inc (SSROC) welcomes the NSW Legislative Council Standing Committee inquiry into the financial sustainability of councils. We would like to express our disappointment that the IPART review did not proceed and would recommend that it does proceed after this review.

SSROC is an association of twelve local councils in the area south of Sydney harbour. SSROC provides a forum for the exchange of ideas between our member councils, and an interface between governments, other councils and key bodies on issues of common interest. The SSROC area covers central, inner west, eastern and southern Sydney, an area with a population of almost 1.9 million, that contributes much of Sydney's gross domestic product.

The Inquiry is timely, with councils facing increasing local infrastructure and services responsibilities. At the same time, their finances are increasingly heavily stressed; local government revenue sources are rising at a slower rate than costs are increasing, costs are being shifted from state to local government, and community expectations are ever increasing.

This submission is presented to align with the Terms of Reference of the Inquiry.

1 The level of income councils require to adequately meet the needs of their communities

1.1 Declining Rates Revenue

While there has been significant broadening of the role of local government and services delivery, there has been an increasing decline in rates as a proportion of total council revenue. The overall percentage of local government revenue generated from council rates declined from 54 per cent in mid-1970s to 38.6 per cent in 2005-06 and this trend has significantly continued to date. It is notable that the proportion of revenue raised by user charges grew from 13.3 per cent to 30.3 per cent over the same period. Though Federal and NSW Governments provide substantial grants to councils, they constitute less than 10 per cent of total revenue[1].

SSROC supports the recent changes to the NSW Rate Peg calculation, in that the methodology is now forward-focused, using more realistic reflection of current costs rather than historical ones. But it does not address the financial situation of those councils that have a base level that is insufficient.

[1] Department of Transport and Regional Services submission to the Productivity Commission – Assessing Local Government Revenue Raising Capacity.

This theme was also supported in a review undertaken by the NSW Productivity Commission in 2020, in which the per capita rating income was lower than the required levels. The Commission's Review said that rate pegging forced councils to reduce the quality and quantity of infrastructure to service their communities or recover the cost from infrastructure contributions.

1.2 Changing Complexity and Scope of Services

Local governments in Australia are increasingly required to provide more and more services, and those services are increasingly sophisticated and complex. Selected examples of council functions and services today include[2]:

- Engineering (public works, construction and maintenance of roads, bridges, footpaths, drainage, cleaning)
- Resource recovery services (recycling, garden organics, bulky and residual waste collection, processing and disposal; community recycling centres, drop-off events, and chemical clean-up events)
- recreation (swimming pools, sports courts, recreation centres, playgrounds, halls, kiosks)
- health (water and food sampling, noise control, meat inspection and animal control)
- community services (childcare, elderly care and accommodation, refuge facilities, meals on wheels, counselling and welfare)
- building (inspection, licensing, certification and enforcement)
- planning and development approval, place-making
- administration and compliance (quarries, cemeteries, parking, animals)
- cultural/educational (libraries, art galleries and museums)
- environmental services (trees, storm water, water sensitive urban infrastructure, weed control)
- other (abattoirs, sale yards, markets, lifeguard services).

The services councils provide are increasing due to community needs and pressures and these services vary between metropolitan, regional and rural councils. Consistency across the sector in terms of funding would be recommended. Those that have to fund statutory fees and charges require review annually in line with cost increases.

1.3 Developer Contributions

Apart from rates and grants, other key sources of income do not have reliable timing and impact long-term cash flow planning for councils. Developer contributions for example, a source of local infrastructure funding, are highly variable and unpredictable[3].

Faced with increasing expectations of local amenity and infrastructure services, population growth and funding constraints such as rate pegs, local governments find it difficult to keep pace with public infrastructure and the service needs of community.

Developer contributions are to fund embellishment and new infrastructure for growing populations associated with development. The contributions do not cover the increase in maintenance or depreciation associated with the works, and this can only be covered by a special rate variation, which seems neither appropriate nor logical.

Many SSROC member councils face significant redevelopment pressure, and rely heavily on development contributions to help fund new infrastructure to support population growth and new development. These include delivering and maintaining local road networks, pedestrian and cycle ways, stormwater and water management, town centre public realm upgrades, parks, recreation and community facilities and a range of other infrastructure vital to supporting and creating liveable communities, business growth, job creation, connectivity and quality of life. The development

[2] Department of Transport and Regional Services submission to the Productivity Commission – Assessing Local Government Revenue Raising Capacity.

[3] National Housing Finance and Investment Corporations. Developer Contributions: How should we pay for new local infrastructure? Media Release, 31 August 2021

contributions system, principally the s.7.12 plan and planning agreements, are integral to ensuring that necessary infrastructure can be provided to support growing communities in our local areas.

Restrictions on the use of the funds and maximum caps on development contributions have effectively limited councils' ability to fund to community infrastructure attributed to growth of development and populations.

Given the rising cost of labour and materials required to deliver local infrastructure and replacing/upgrading aging assets, councils are relying more and more on general revenue as a source of capital funding. Developer contributions are far from sufficient for councils to match rising costs.

1.4 Councils are not all the same

Communities typically have far greater demands for infrastructure and services than Councils will ever be able to afford to meet. Councils are required to consider the needs of their diverse communities, and do so with extensive consultation under Integrated Planning & Reporting (IP&R) requirements. Each Council also serves a different community, depending upon factors such as rural or metropolitan, coastal or inland, predominant industry and mix of ethnicities.

SSROC recommends that the industry is supported to develop a prioritisation framework to consider services, service levels and budget-setting for staff, councillors and community based on the IPR framework, in accordance with identified priorities and risks. Examining services in this way would facilitate the allocation of costs as closely as possible to the beneficiaries of the activities and functions.

Opportunities for councils to raise own-source revenue also vary greatly depending on the nature of the local government area, that is large metropolitan, small metropolitan, regional or rural. These different situations will need to be taken into account and the fact acknowledged that any measures identified may be of little value in some councils' circumstances.

1.5 Infrastructure Delivery and Assets

Assets support the provision of services to the community, and therefore are a key part of the overall provision or services to the communities and must be balanced with the other priorities that councils must manage. Each council's approach to the management of assets will vary slightly, as will the portfolio of assets that they manage. For example, not all councils have water or sewage assets, and some have extensive rural road networks or are impacted by coastal issues.

In the metropolitan area of Sydney, the issue is further exacerbated by the uncertainties relating to the current planning reforms aiming to dramatically increase the availability of housing. The reforms are progressing quickly without any clear plan for the necessary supporting physical and social infrastructure, and in the absence of any reliable overarching city-wide strategic plan - updated Six Cities Plan and City Plans. These plans are critical inputs to councils planning their future infrastructure needs.

Given this substantial uplift resulting from the recent NSW Government's housing reforms, which aim to meet the federal government's Housing Accord target of 377,000 new homes by 2029, it is concerning that this announcement has not included details on infrastructure planning and funding and how communities will be supported as demand for services, facilities and assets increases. Existing s7.12 contributions will not be adequate to support expected growth. An appropriate alternative funding mechanism is needed.

The NSW Government's reforms on housing are likely to create something like 180,000 new dwellings over the next 17 years within the SSROC area. It is generally expected that substantial infrastructure upgrades and services will be required to address increased community needs. This is particularly the case for the light rail, bus services, open space, community facilities and other infrastructure. Transport studies commissioned by Randwick City Council for example have indicated that peak hour services are already at capacity and augmentation will be required to meet the demand. Whilst the NSW Government's Housing Productivity Contribution package is intended to address regional infrastructure, there is no current commitment to improved transport services such as those in the Randwick LGA.

Councils often seek to balance their budgets by re-allocating funds from capital purposes to maintain recurrent service levels, impacting the quality and condition of vital community infrastructure assets.

1.6 Regulated and Statutory Fees

Other examples placing a strain on financial sustainability, include the gap between regulated service costs and the corresponding regulated fee and/or charge. These often do not fully cover the costs of various regulatory functions imposed on councils, leading to additional financial burdens passed onto ratepayers who do not utilise the service and must then subsidise.

The NSW Independent Pricing and Regulatory Tribunal's (IPART) final report on the *'Review of the rate peg methodology, August 2023',* found that ratepayers expressed concerns about affordability and considered that councils could improve how they communicate with their communities. Improving the transparency and management of costs and funding model plays a critical element in addressing this finding.

A material example is the stormwater charge, which has remained unchanged for over 10 years. Further the mandatory pensioner rebate also has not increased in line with CPI, which results in many councils providing a voluntary rebate on top of the mandatory, which is then subsidised by other ratepayers.

2 Past rate pegs have not matched increases in costs borne by local governments

2.1 Rate-pegging

The rate base was originally set around 40 years ago, and the rate peg applied each year has not matched inflation over that time, and so the level of rates of revenue has consistently fallen relative to costs.

Furthermore, a correction is needed to re-base the years of deficient pegged increases, which have contributed significantly to councils' current financial situation. Base rates have never been reassessed to check the appropriateness of the value today, or in line with current costs. Without such adjustment, councils will continue to struggle to cover rising operational and capital expenditures with increasingly inadequate revenue from rates.

Adequate funding for infrastructure and assets is a multifaceted issue. There is a growing infrastructure backlog across NSW, largely due to the limited funds available to maintain existing assets as required. Grant funding by other levels of government is often for capital investment only, leaving councils to fund the maintenance of the new asset from the existing rate base.

The number of Special Rate Variations (SRV) approved in recent years signals that the fundaments of the local government financial and funding model are not working. According to Local Government Professionals[4], of 178 SRV applications were made in the decade 2012 and 2022, of which 165 were approved in full or in part. The necessity for so many legitimate, justifiable applications signals a very flawed funding model. The vast majority (142) of the SRV cited one of more of three reasons: financial sustainability, infrastructure backlogs and future infrastructure spending obligations. All three justifications would reasonably be expected not to be issues if the funding model were right.

2.2 Consider ***all*** costs and revenue flows

This review should examine the entire local government financial model holistically, including income and expenditure pressures. The review needs to cover matters such as rates, domestic waste charges, emergency services levy, the environmental levy and increased requirements such

[4] Local Government Professionals Australia, submission to the Review of the Rate Peg Methodology Issues Paper, 4 November 2022.

as cyber security and the NSW government's mandatory new organic waste collection and processing services.

New costs of emerging responsibilities on the sector are realities for councils. These include the capacity to be able to build resiliency into our infrastructure networks, so that it is not only designed to withstand current risks, hazards and threats, but for the life of the asset and to be able to withstand future hazards such as those arising from climate change.

The capacity for the local government sector to develop its own capabilities to deal with external impacts that cause it shocks and stresses is important. For example, economic factors which drive up the cost of delivering services, and the increasing frequency of severe weather events jeopardise not only short terms service obligations but also longer-term strategic goals.

SSROC recommends that the reporting framework is reviewed to ensure this is transparent for decision makers and the community. Budget and financial statements are the two documents used, and evaluating their effectiveness would assist in this matter.

2.3 Streamline processes

NSW councils are very tightly and heavily regulated, and there is scope for some processes associated with this regulatory framework to be streamlined.

For example, the process for making a very effective Environmental Levy permanent is complex and difficult. IPART requires detailed financial modelling, community engagement and supporting documentation. Furthermore, the timing of the process must carefully consider budget cycles, future project specifications and internal resource implications. As more and more councils seek SRVs, consideration should therefore be given to streamlining the process, improving on line lodgements and providing support to councils who decide to go down this pathway in order to deliver improved services and protection of the environment.

2.4 Legislative Framework

The Inquiry should have regard to ensuring that the suite of legislation, regulations and standards that currently control the way a council operates are updated and modernised to reflect the broad range of responsibilities beyond roads, rates and rubbish. Some elements of these controls are close to 40 years old and do not necessarily reflect or support the needs of an efficient and effective local government sector today.

The following list notes relevant matters that SSROC recommends should be considered within the terms of reference in order for the Inquiry to be comprehensive (no relative priorities should be inferred from the sequence):

- Introduction of Capital Improved Value (CIV)
- Value capture from land development (including the ability to use some of these funds for operational purposes)
- Cost-shifting
- Pensioner rebates funding aligned to rate peg and increase annually
- Rates exemptions
- Fee waivers
- Regulated charges and cost recover: mimic the Domestic Waste Charge, which recovers actual costs, rather than there being a gap
- State and Federal grant funding and the impacts of this on Councils
- Funding of environmental sustainability initiatives
- Funding for increasing cyber-related matters
- Funding for resilience in infrastructure
- Funding for additional obligations imposed on councils by State and Federal governments, such as: the NSW food organics mandate and regulatory responsibility for commercial and industrial organics waste and Safety by Design (Hostile Vehicle Mitigation and Public Domain CCTV) requirements
- Funding for impacts of tourism and increased visitation

- Funding of infrastructure, where, for example, changes are made to the State planning regime demanding intensification of development, however no funding is provided to Councils to invest in the necessary additional infrastructure
- Allocation of Developer Contributions for maintenance for new assets for a set period based on an agreed formulae
- A model that distinguishes between metropolitan, regional and rural councils and addresses the diversity of base cost patterns
- Reduce the levels of compliance reporting as referred to in the 2014 IPART Local Government Compliance and Enforcement Final Report[5].

3 Current levels of service delivery and financial sustainability in local government, including the impact of cost shifting on service delivery and financial sustainability

3.1 Defining Financial Sustainability

Resilience and sustainability are important to local government. SSROC member councils, through their local government finance working group defined Financial Sustainability as follows:

"A financially sustainable council is one that:

- Effectively manages its financial resources to achieve the long-term viability of essential services and infrastructure, while maintaining fiscal responsibility. This includes the ability to generate and manage revenues (through a balanced mix of sources such as rates, fees and charges and grants) and to efficiently manage operational costs and capital investments.
- Maintains a prudent level of financial reserves and adequate working capital to safeguard against unforeseen economic challenges and emergencies.
- Ensures that appropriate budgeting, responsible debt management and strategic long term financial planning are in place.
- Seeks to meet the community's needs (via the Integrated Planning & Reporting framework), without compromising the ability of future generations to enjoy similar or improved services and infrastructure."

SSROC recommends that any proposals regarding financial sustainability such as rate pegging, cost shifting and grant funding needs to consider the above definition.

This is a very important consideration for the scope of this review. There is currently no accountability for a council to implement corrective action if it adopts a budget deficit or if its Long Term Financial Plan has deficits in short to medium term. Greater regulation on financial governance and sustainability is required.

3.2 Cost-shifting

The cost-shifting survey recently completed by Local Government NSW (published in November 2023) found a total cost-shift to Councils of $1.36 billion in 2021-22. This is an increase of $540 million since the last report from the 2017/18 financial year and represents lost services, lost opportunity and lost amenity for all our residents and businesses. It is equivalent to over $460 annually per ratepayer. Councils are close to their communities, and must face residents directly to answer for rate increases, reduced services or degraded infrastructure.

Cost-shifting is increasingly eroding financially sustainability in the local government sector and risking the capacity of councils to deliver tailored, grassroots services to their communities and properly deliver and maintain vital local infrastructure.

[5] https://www.ipart.nsw.gov.au/Home/Industries/Special-Reviews/Reviews/Local-Government/Local-Government-Compliance-and-Enforcement

The cost-shifting examples in NSW, along with their associated financial impacts, include:

- Waste Levies
- Rate Exemptions
- Development Applications
- Emergency Service contributions
- Library Funding Shortfalls
- Companion Animals
- Contaminated Land Management
- Protection of Environment Operations
- Noxious Weeds.

In 2021/22 the waste levy was the largest of the shifts, accounting for $288 million paid by councils, and largely diverted to NSW consolidated revenue instead for being fully reinvested in the waste sector. The emergency services levy and related contributions was the largest direct cost-shift ($165.4 million), while the NSW Government's failure to fully reimburse councils for mandatory pensioner rate rebates cost councils $55.2 million. NSW Government originally committed to 50 per cent of the costs of library operations, but has not done so, at a cost to councils of $156.7 million.

As Local Government NSW emphasised, NSW Government should consider reinvesting $750 million revenue (2020) from the NSW Waste Levy back into the growth and transformation of waste services. Funding is needed for priority infrastructure outlined in the Waste and Sustainable Materials Strategy and to provide financial support to encourage investment and innovation in circular economy[6]. This would put councils in a better position as the challenge of waste services delivery by councils increases.

IPART's final report on the *'Review of the rate peg methodology, August 2023',* found that Ratepayers expressed concerns about affordability and considered that councils could improve how they communicate with their communities. Improving the transparency and management of cost shifting plays a critical element in addressing this finding.

Un-funded and unreasonable cost-shifting is not a sustainable practice for local government and cannot continue. SSROC strongly recommends that this aspect of local government finance to be examined as part of this Inquiry.

3.3 Grant funding

Grant funding is often problematic for councils. Grants are often allocated for specific projects, which councils must first fund and then claim reimbursement at specified milestones and/or at the time of acquittal. This process is often complex and time-consuming to administer, requiring the provision of data and reports, sometimes to a level that is well in excess of the need for prudent management of public funds. Making funds available to meet the costs initially often presents a cash flow problem, particularly if the project is large, and can distort financial statements.

Sometimes funding programs require councils to match state government funding. This can also present challenges for councils, especially if the funding process means that budgets for the required time period have already been set. This funding mechanism can also be beyond the reach of councils with smaller budgets, or whose priorities, driven by the Community Strategy Plan and Long Term Financial Plan, simply lie elsewhere.

Grant funding is usually contestable, an approach that it touted as best practice. In reality, it often results in grants being allocated with councils with strong grant application capability. Without

[6] Local Government NSW, 2022-2023 State Budget NSW Local Government Priorities, January 2022

reasonable assurance of success, the mechanism does not deliver a reliable funding source. It can be counter-productive too, forcing councils to devote resources to application processes without any guarantee of funding, no matter how good their business case might be.

Grants for capital projects are also generally for the capital investment only, with no funding made available to Councils for the ongoing asset management, operation and maintenance liabilities that new works come with. Councils have difficulty raising enough funds to maintain or replace assets, and backlogs develop over time.

There is little liaison between local government and the State (or Federal) governments on priorities for local government, development of funding programs and targeting and timing of grants. More engagement with local government as programs are developed would be beneficial to all concerned.

While grants are certainly a useful funding mechanism, the way in which they work should be tailored to the specific outcomes sought. A funding arrangement that is more partnership-based, focused on achieving those outcomes, would generally be more appropriate than the current inflexible and inefficient approaches, which do not always align with the priorities of a council's local community.

3.4 Planning services and compliance

Local governments must comply with many legal and regulatory requirements, which can be intricate, time-consuming and resource intensive. For example, councils face an ongoing financial burden in defending DA decisions and ensuring compliance with planning controls. Funding and training is needed to support streamlining of processes across local government, implementing AI tools to improve the quality of applications lodged, to cut down processing times and efficiently deal with simple development applications. Councils also need support to digitise a range of local approval processes, to make them faster, more efficient and more transparent. This includes digitising planning applications, building permits, and other regulatory approvals. It also necessitates the implementation of ever-evolving cyber-security measures.

Robust land use planning must include be supported by evidence-based research and analysis. Councils face increasing costs associated with undertaking specialist technical studies, assessments and research such as heritage reviews, transport investigations, economic impacts analysis and feasibility studies.

4 Social and economic impacts of the rate peg in New South Wales for ratepayers, councils, and council

4.1 Rate peg and community

The rate peg has enormous impact for unmet infrastructure and community services in our communities. Faced with infrastructure and services backlogs as well as a backlog for maintaining and replacement of depreciating community service assets, councils are in tight positions, even as community needs and demands from these local government increase.

4.1.1 Community infrastructure and services

Councils identify key community infrastructure, community and cultural service needs through community and social planning processes, the IP&R and prioritising. Many of these needs cannot be met because of councils' constrained financial position, which is often substantially linked to rate peg. Childcare, community playgrounds, local and district libraries and services to improve access for the elderly, people with disability and culturally diverse communities in our council areas are not viewed as a luxury, but rather as a necessity. Unfortunately, these services are either not in place or severely constrained.

Inadequate local library services and poor provision of accessible computers leads to digital disadvantage in low socio-economic suburbs, perpetuating low education attainment, poor school outcomes and unemployment.

4.1.2 Non-residents

Some councils in Sydney have large influx of people into an area, such as to beaches over the summer period. The local ratepayers bear the cost for street cleaning and other services to support tourism, a key income-generating sector for the state. Constrained incomes will have corresponding impact on ability to provide the services. SSROC urges that these be also considered in a complex and diverse financial modelling process for councils.

4.1.3 Affordable housing

Affordable housing is increasingly a key issue not only in metropolitan councils, but also in regional areas. In metropolitan Sydney for example, affordable rental housing for key workers for our communities such as teachers, nurses, police officers, drivers, age care and disability workers, shop keepers, and many other workers, is a very important matter that local governments cannot ignore as rents in the private sector soar. Housing unaffordability for these essential workers has direct implications for the social and economic life of our communities. Councils are in a better position to partner with community housing providers on affordable housing if they are not constrained by backlog of community infrastructure and community services resulting cumulative rate peg resource constraints.

4.1.4 Community engagement

Effective and meaningful engagement is a core role of local government and informs the vision and direction of council. The community expects a high degree of engagement and opportunity to be heard and be considered in key changes and decision-making. In accordance with regulatory requirements, (including the Community Engagement Strategy) councils actively seek to engage broadly with the community which entails adopting creative and often more expensive techniques to share information and to obtain feedback that represents the views of the community. Given the volume of community engagement activities, councils face financial and resource challenges as the community expects timely and effective consultation on projects, programs and policy changes.

4.2 Rate peg and councils

The practice of rate-pegging has had cumulative negative impacts on councils, eroding their financial sustainability and contributing to their difficulties with funding operational services, infrastructure and asset maintenance. Rates have clearly, deliberately, not kept pace with inflation, severely affecting councils whose costs rise with inflation the same any other organisation.

Combined with other financial constraints, many of which are touched on in this submission, the rate peg has been an unhelpful mechanism for councils' financial sustainability, effectively restricting revenue without regard to costs.

4.3 Rate peg and council staff

The range of skills, attitudes and commitment of staff varies in the same way as any other organisation. With working conditions governed by the Local Government Award, staff are largely protected from the negative impacts of the financial situation of the council.

Many staff are deeply committed to serving their communities. These people can find the negative effects of financial challenges, such as cuts to services, stressful and challenging. Those directly customer-facing can face verbal, sometimes even physical, abuse as a result. Some staff find their workloads increasing to unmanageable levels and are forced to provide a lower, or slower service then they are satisfied with. These circumstances can be stressful and potentially linked to ill health and high rates of sick leave.

Attraction and retention of skilled staff into the local government workforce is an essential element to providing efficient services and a sustainable model. Local government positions, including planners, engineers and heritage specialists, play a critical role in local government in addressing and responding to a range of urban challenges, balancing competing demands and managing sustainable long term growth. Given the state-wide skill shortages in a number of key local government areas, councils rely more heavily on consultancies and agency staff to undertake DA, strategic work and obtain other specialist advice. This has financial implications for councils.

The representative body for the strategic planning profession, the Planning Institute of Australia, has advocated for the Federal government to invest in the profession by addressing university undergraduate places and promoting it as a career path. SSROC supports this proposal is supported, and furthermore, HECS fees for planning related courses should be reduced to incentivise students to enter the profession.

5 Alternative approaches to rate peg with regards to the outcomes for ratepayers, councils, and council staff

SSROC is of strong view that the system of rate pegging is not a suitable mechanism for achieving the aims of controlling unreasonable rate increases while maintaining the financial sustainability of councils in NSW, and welcomes consideration of alternative control mechanisms. The IP&R framework includes extensive consultation and engagement with the community. It represents an opportunity to challenge the rates and charges and to understand the financial drivers, which addresses the problem that the rate peg system was established to solve.

In its 2023 final report on the rate peg methodology, IPART identified measures to improve the rating system, including:

- Allowing councils to use the Capital Improved Value land valuation method to set the variable component of rates to ensure they can set equitable and efficient rates for all residential and business ratepayers, regardless of their property type;
- Better targeting eligibility criteria for rates exemptions;
- Ensuring that statutory charges reflect the efficient costs incurred by councils in providing statutory services, so councils do not need to use rates income to cover the costs of providing these services; and
- Developing a mechanism to enable councils found to have insufficient base rates income to achieve financial sustainability.

5.1 Considerations for alternatives: ratepayers

Eliminating, or at least reducing, some of the costs shifted onto councils from NSW government would enable councils to either better service their communities by using the rates income directly instead of directing a proportion to the NSW government. The current state of local government finance is such that it is unlikely that rates could be reduced or increased less than otherwise would have been the case, because of existing backlogs and ever-increasing costs. However, ratepayers would benefit from improved service levels, and/or better asset maintenance.

To achieve this opportunity for recovery, councils could be relieved from paying an Emergency Services Levy (ESL). This is a reasonable proposition since councils do not provide or have any influence over the cost or efficiency of the services that the levy funds. The ESL puts upward pressure on rates, and perpetuates the current complexity resulting from the difference between council budgetary cycles and notification of actual cost. However, if the NSW Government insists on councils paying this levy, councils should be able to recover the actual cost impost.

The Inquiry should catalogue and review all Government levies/taxes and consider whether costs paid by councils (and therefore by ratepayers) can be justified and if not, can be removed. The Local Government NSW's Cost-Shifting Survey would inform this alternative model on Government-related costs absorbed by councils.

5.2 Considerations for alternatives: councils and council staff

An alternative approach to rate-pegging should recognise the differences between urban, regional and rural councils, recognise the cost of managing assets, and include reasonable and robust financial modelling.

The alternative model for rate peg review should incorporate an approach to further work with councils to determine new and emerging costs to council. These costs are increasingly significant for councils and include cyber security measures, environmental impacts, and coastal works. IPART has proposed adjustments to the rate peg on an as-needs basis for new external costs, recognising that climate change, cyber security and servicing of new community facilities are important cost items. The proposal has some merit and should be considered, noting that each individual council is likely to have its own set of unique costs.

One alternative model could have a particular provision for external costs emanating from "cost shifts" from different levels of government that affect financial sustainability and capacity to service their communities. If a cost must be shifted to local governments, then the opportunity should exist for it to be recovered: councils cannot continually absorb additional costs.

Another alternative could involve a simple up-front consultation process by IPART across all councils, possibly as part of preparing for an annual review of rate peg. This would gather useful insights on the demands by councils and allow for possible adjustments. The consultation should include seeking information from councils on specific abnormal and extraordinary costs. Joint Organisations (JOs) and Regional Organisations of Councils (ROCs) are in a good position to coordinate and consolidate member councils' input.

6 The special rate variation process and its effectiveness in providing the level of income councils require to adequately meet the needs of their communities

6.1 Special Rate Variation (SRV) and rates base

NSW Government and IPART need to work with local government to agree principles for financial modelling to inform special rate variation. While the SRV process can be effective for addressing financial challenges in the short-term, if the underlying base is inadequate, the effectiveness will be eroded over time. Combined with the continuing application of the rate-peg, the process of erosion will accelerate.

Fundamentally, the basis for calculation of rates needs to be reviewed since this has not changed in the 40 years of rate-pegging, and council needs have changed substantially in that time, creating the increasing need for SRVs.

The Final Report from IPART into the Review of the Rate Peg, August 2023, noted:

> *"As a result, we consider that councils with longstanding financial sustainability issues driven by an insufficient base level of rates income could benefit from a mechanism to reset their base"*

SSROC support this IPART recommendation and therefore recommends that councils should be able to reset their rates base through a one-off process.

6.2 SRV principles

In its Review of the Rate Peg Methodology IPART observed:

1. that full cost recovery be an important element of any review, to prevent accumulated costs becoming an inequitable drain on councils' funding,
2. the need to commission an independent review of the financial model for councils in NSW, including broader issues than just the system of rate pegging, with sufficiently holistic scope.

These considerations equally apply to special variations, and in their application would result in a much better model. The scope should include rate rebates and exemptions, use of the capital improved valuation method, exceptional costs, rates base adjustment and government taxes and levies.

The perception of an SRV in the community is that Councils are doing something out of the ordinary by asking for an SRV, where in fact it has become a mechanism to fund population growth, developer contributions infrastructure, community services and other services expected by a well governed organisation and diverse local community.

SSROC supports the IPART's observations, and therefore recommends these considerations to the Inquiry.

6.3 SRV process and effectiveness

The SRV process is intensive and should be necessary only rarely. The relative frequency of SRV applications and approvals shows that the funding model is flawed. Furthermore, while SRV can deliver an effective one-off adjustment, in the current model the same deterioration of finances is inevitable over time.

SRVs are generally perceived as bad and unnecessary, whereas they are becoming a fundamental tool to secure financial sustainability. Although they have become a critical tool, the political and costly nature of an SRV can act as a deterrent for councils, which is not ideal. The timeframes and criteria appear to be created for a tribunal or financial professionals. Whereas the community engagement could be more robust on exploring service funding and community expectations.

6.4 Cost-shifting

SRV processes need to cover cost-shifting. Cost-shifting in this context refers to other tiers of government through various channels shifting the cost of services or facilities to councils, and ultimately to ratepayers. Councils should not be required to seek a SRV for items that are from cost shifting or are a regulated service: these costs needs to be compensated for in some way.

The Emergency Services Levy in particular is a major issue for councils. It is symptomatic of the increasing trend of cost-shifting from the State government to local government. Councils have no control over the cost-effectiveness or efficiency of emergency services, and yet are required to fund them. This particular cost is the largest direct shifting of cost from state to local government in NSW.

If councils must pay the ESL, then they require the ability to create a charge, similar to the Domestic Waste charge, to cover that cost. This would assist cost recovery and improve transparency with ratepayers.

Most recently the NSW government has announced that the Beachwatch program, which tests water quality at Sydney beaches, is in future to be funded by Sydney councils. Given that Sydney councils have no control over sewage outfalls (the major source of bacterial contaminants at beaches, controlled by Sydney Water), there appears to be no justification for imposing this cost on metropolitan councils.

6.5 Balancing costs and expectations

Expenditure guidelines or similar outlining how to prioritise council services for internal funding would be helpful. Although the precise definitions would vary between councils, it would be a useful guide to what should be funded by the different types of income available to councils, and could be a useful prompt to council to consider an SRV request when appropriate. There are currently no revenue guidelines or revenue policies linked to how council functions should be funded, and community perceptions of what is the responsibility of councils, inevitably vary.

Councils need to determine what functions and activities are core according to the priorities of their communities. Other services require a transparent funding strategy and associated transparent reporting. Clarity is also needed where subsidising across services occurs.

7 Other related matters

7.1 Procurement

Local governments can achieve cost savings and better efficiency by pooling resources more often for the procurement of good and services that all need. SSROC questions why the NSW Government keeps the local government tendering threshold so low, with the result that the majority of purchasing, particularly when procuring jointly, requires a full open tender process.

This necessitates significant effort on the part of potential suppliers, and is a barrier to tendering for smaller businesses who do not have large sales teams to complete the full documentation required, or simply do not understand the need to comply in full with the conditions of tender.

For councils (and regional organisations with procurement functions), these procurements often result in resource-intensive activities including responding to supplier questions, compliance checks, probity review, evaluation and reporting. While these checks and balances are undoubtedly required for large, complex and high value procurements, they can be excessively onerous for simpler, lower value procurements.

SSROC recommends the review of local government procurement guidelines and threshold, potentially to align with procurement practices and thresholds by State agencies of similar size.

7.2 Resource-sharing opportunities

Local governments could potentially benefit in efficiency from sharing more resources with the State government, such as some common IT systems, which are at present only available to the State. We could be working more closely with Treasury or Service NSW, for example, on common matters such as banking contracts and matters around leasing and licensing.

Joint insurance pooling is also potentially an opportunity that local and State governments could consider, noting that insurance may be harder and harder for Councils to get into the future, at a competitive rate.

NSW Government entities could also enable access to their data in the same way that agencies can allow access across NSW Government, but councils cannot access the same data even though we share the same community wellbeing outcomes and are obliged to do so.

7.3 IPART Review of the council financial model in NSW

SSROC would like to express our disappointment that the IPART review did not proceed and would recommend that it does proceed after this Inquiry.

The planned review of the council financial model in NSW was an extension of years of work into the rate peg methodology and domestic waste charge, and could have covered the entirety of the way in which councils' finances operate in NSW. This was a logical extension into an ongoing discussion and stakeholder engagement process.

This Inquiry, while informative, is focused on the specific issues of income adequacy, rate pegs, cost-shifting and SRVs. It does not necessarily take an objective view of the whole financial system (except potentially as "other related matters"). There SSROC recommends that the IPART Review proceed in due course, informed by the findings of this Inquiry.

7.4 Financial Reporting and Financial Governance Framework

The Inquiry could include in its scope an assessment of whether separating financial statements by services would improve financial management.

There is a common perception that Councils have plenty of cash, though this is predominantly restricted. The Inquiry could consider expanding the reporting and transparency of operating cash flow, and expanding any restricted revenue, i.e. interest on restricted reserves, regulatory charges, operating grants that are for capital purposes.

Conclusion

Thank you for the opportunity to provide this submission to the Inquiry into the ability of local governments to fund infrastructure and services. The Inquiry is hugely important and has the potential to move NSW to a holistic approach to review of councils' financing model in NSW, improving financial resilience, efficiency and sustainability. A summary of SSROC's recommendations is attached.

SSROC and its member councils will welcome opportunities for collaboration and integration in the development and implementation of better climate-sensitive planning system outcomes for councils, community and the environment.

This submission has been prepared in consultation with councils' senior financial staff. However, in order for it to be made within the timeframe for receiving comments, it has not been possible for it to be formally endorsed at a meeting of the SSROC Delegates. I will contact you further if any issues arise as a result.

If you have any queries, please do not hesitate to contact me or Vincent Ogu, SSROC Program Manager on 02 8396 3800.

Yours sincerely

HSloan.

Helen Sloan
Chief Executive Officer
Southern Sydney Regional Organisation of Councils

Attachment: Summary of SSROC Submission Recommendations

Numbers in the left-hand column refer to the relevant section in the main body of the submission.

Section	***Summary of Recommendation***
1.	***The level of income councils require to adequately meet the needs of their communities***
	Recommendations:
1.1.	Address the decline in rates revenue relative to total revenue. Permit councils to review and increase their rates-base where appropriate.
1.2.	Recognise the increasing complexity and scope of council services, which drive up and bring new costs. Recognise the differences between metropolitan, regional and rural councils, which influence both needs and costs.
1.3.	Establish a developer contributions policy that reflects the realistic costs of community infrastructure, including ongoing maintenance and renewal.
1.4.	Support the sector to develop a framework for prioritising budgets in accordance with Community Strategic Plans developed under the IP&R system. Recognise that opportunities for own-source revenue vary greatly between councils, which limits their overall capacity to be independently financially sustainable.
1.5.	Update and publish the Six Cities Plan and City Plans for metropolitan Sydney. Publish details of how transport and community infrastructure to support the current housing reforms will be planned and funded.
1.6.	Annually review statutory fees and charges in line with cost increases and improve the transparency of this model.
2.	***Past rate pegs have not matched increases in costs borne by local governments***
2.1.	Reset rates and base rates to better reflect the actual costs to and value of councils. Review grant funding programs to accommodate the cost of ongoing asset maintenance and renewal as well as initial capital investment.
2.2.	Include in the scope of the Inquiry: • the whole local government financial model • emerging new costs • effectiveness of reporting frameworks in achieving transparency for decision-makers and the community.
2.3.	Review and streamline the regulatory processes whereby councils implement or adjust charges.
2.4.	Review relevant legislation, regulations and standards to ensure that they reflect and support the needs on efficient and effective local government today.

3. Current levels of service delivery and financial sustainability in local government, including the impact of cost-shifting on service delivery and financial sustainability

3.1. Define "financial sustainability" for NSW local government.

Require a council that adopts a budget deficit or long term financial plan with deficits to simultaneously adopt a corrective action plan.

3.2. Limit council payments to NSW Government to those costs that councils actually incur and have control over.

Reinvest waste levy revenue into the waste sector.

3.3. Review grant funding programs to take into account council cash flow and budgetary cycles.

Review the extent of reporting on grant expenditure to make it commensurate with the level of funding in question.

Review the appropriateness of the approach to funding for the nature of the program e.g. contestability, matched funding, milestone reimbursement.

Facilitate engagement by NSW government priorities and related funding programs with councils, to streamline targeting and timing of grants.

3.4. Fund councils to appropriately resource their planning functions and related costs.

4. Social and economic impacts of the rate peg in New South Wales for ratepayers, councils, and council

4.1. Recognise the impact of the rate-pegging approach on councils' ability to maintain infrastructure and community services.

Recognise the need for councils to serve all their community, including vulnerable groups, and and which choose to provide services to those who may not be able to afford them.

Restore local library funding to its original level of 50 per cent of operational cost.

Consider how costs should be allocated when incurred as a result of non-residents visiting a local government area, particular places popular with tourists such as Bondi beach.

Consider how councils can support the provision of affordable housing e.g. by funding a partnership between a council and a community housing provider.

Recognise councils engage with the community on services, demands and budgets through IP&R processes, yet are thwarted by the rate page in meeting those expectations.

4.2. Address the decline council revenue resulting from the rate peg.

4.3. Consider the impact of declining revenue on council staff.

Support the Planning Institute of Australia's advocacy for Commonwealth investment in the planning education to encourage students into this career path.

5. Alternative approaches to rate-pegging with regards to the outcomes for ratepayers, councils, and council staff

5.1. Catalogue and review all Government levies/taxes and consider whether costs paid by councils (and therefore by ratepayers) can be justified.

Remove from councils the liability for unjustified levies/taxes.

5.2. Consider:

- Requiring robust, published financial modelling.
- Include new and emerging costs such as cyber security and climate change adaptation.
- Recovery of costs imposed by other levels of government.
- A consultation by IPART with councils as part of the annual rate-peg review.

6. The special rate variation process and its effectiveness in providing the level of income councils require to adequately meet the needs of their communities

6.1. Permit councils to reset their rates base where appropriate.

6.2. Review SRV principles in the light of full cost recovery and the results of any review of the local government financial model.

6.3. Establish a more financially viable rating system that ensure that SRV applications are exceptional and not the standard approach to adjusting for continually declining rates revenue.

6.4. Permit councils to recover any costs shifted from state government, especially where councils do not incur or have any control over those costs.

6.5. Develop guidelines to assist councils to prioritise costs relative to their basic functions and local priorities.

7. Other related matters

7.1. Support councils and joint procurement of goods and services by lowering the tendering threshold.

Review local government procurement guidelines and threshold, potentially to align with procurement practices and thresholds by State agencies of similar size

7.2. Permit councils to access NSW government systems and data where they have common functions and interests.

Consider pooling NSW and council insurance.

7.3. Resume the proposed IPART review of local government financial model on conclusion of the Inquiry.

7.4. Consider whether separating financial statements by services would improve council financial management.