QPRC

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Review of Rate Peg
IPART
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Sydney NSW 1240

Dear Chair

Rate Peg and Population Growth

Thank you for the opportunity to provide comment to the IPART Review of the Rate Peg. This submission is a collaboration by Queanbeyan-Palerang Regional Council (QPRC), with Regional Cities NSW (RCNSW) and the Canberra Region Joint Organisation (CRJO). We appreciate the Minister's intention to form a rate peg methodology that allows the general income of councils to be varied annually in a way that accounts for population growth. It is acknowledged the methodology will take into account changes to the infrastructure contribution system recommended by a recent review by the Productivity Commission.

We note the current rate peg and infrastructure contribution system do not provide for the operating and maintenance costs of infrastructure or increases in the volume of services demanded by a growing population. However we are concerned both reviews should account for the differential rates of growth and costs between metro, coastal, regional city, regional and rural councils in NSW.

This submission is arranged into Issues and Opportunities, then responds to specific questions requested by the Consultation Paper. The focus of course should be on the financial sustainability of local councils – we refer to recent media on merged councils and a report by Local Government Solution (LGS) on the deteriorating financial position of councils generally.

Issues:

IPART noted there are limitations of the system which result in most councils receiving less income from rates for each new resident compared to existing residents. IPART also acknowledges the patchy population and development growth between metro and regional areas.

Fundamentally though, we urge IPART to incorporate a mechanism to recognise either population growth (or asset growth as a proxy) as margin above the rate peg for all councils, regardless of whether the individual LGA rate of population growth is at or above the NSW rate of growth.

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This section of the submission records our views on the issues related to the rate peg review, and opportunities to reframe the structure of rating and financial sustainability of regional councils.

Infrastructure Growth

i. many councils have been the (grateful) recipients of grants for new or upgraded community assets, noting much has been introduced through infrastructure stimulus by Governments, and most of which were not contemplated in the respective asset management plans (AMP) or financial plans. As a result, the life-cycle maintenance and depreciation expense related to those assets have negatively impacted the operating result and balance sheet of the local councils
ii. newly constructed and gifted assets subsequent to new developments (particularly linked to an LPA), create a similar legacy in terms of AMPs and financial statements
iii. some councils under-collect infrastructure contributions as they strive to generate economic activity; are subject to the contribution cap (< $20k in regional NSW); and must capital fund the balance of works contemplated in s7.11 plans
iv. regional cities tend to construct infrastructure to a higher scale and provide services for the broader regional population – with it bringing higher loads and costs to service. Indeed, regional city LGAs therefore support the populations and infrastructure expectations of nearby smaller settlements
v. the accumulation of s7.11 contributions to the point they are sufficient to undertake the works outlined in contributions plans, are often eroded by cost escalations greater than the indices (CPI) afforded by those plans
vi. with deteriorating operating results, some councils may then be unable to borrow to renew or replace other assets; or borrow to raise capital to match grants or co-fund developments
vii. as a consequence, the value and collection of infrastructure contributions lag growth, are subject to cost escalation, and prompt decisions by councils to defer works; then ultimately, population demand outstrips infrastructure capacity

Property Growth

i. the general rates yield from new developments (ie through supplementary valuations) may not cover scheduled maintenance, repair and renewal (MRR) costs of new assets, nor adequately contribute to the maintenance of existing infrastructure assets
    a. for example, a new masterplanned suburb in Queanbeyan expects over 18,000 new residents by 2031, in 6,500 new subdivided lots
    b. it constructs and dedicates to QPRC around $20m new assets each year
    c. averaging 400 lots per year, and yielding around $500k in supplementary rates, that growth covers annual depreciation expense (ie the annualised renewal costs/year) of those new assets, but falls short of higher operational/servicing costs (eg cleaning amenities, mowing parks and grounds etc), and makes little contribution to existing assets or services
ii. it is problematic to increase the general rates of new development areas only to compensate for the above, without substantially increasing the notional yield and redistributing the rate burden though the subcategories

Population Growth:

i. government (DPIE) forecasting uses lag indicators, primarily used to flatten planning horizons for new or expanded public infrastructure and services such as health, education, police and the like
ii. population forecasting captures capital city and nett interstate migration, but seems unable to capture intrastate or metro to region movements
iii. forecasting is not nimble enough to capture out-of-sequence population surges such as intrastate relocation from metro to regional areas, due to COVID for example – particularly into regional cities
iv. councils staffing FTE should rise proportionately with increase in assets to be maintained, and services delivered through those assets to provide for population growth. For example
    a. QPRC maintains a 7.5FTE/1000 resident staffing ratio
    b. Infrastructure asset growth forecast is ~5%; population growth forecast is ~10% in 5 years
    c. staffing should rise 35FTE at ~$3.5m/yr, and new asset depreciation will rise $2m, yet new property rates yield $2.5m over that 5 year period
v. government harbours ambitions to increase density in metro and regional cities, often through secondary dwellings and granny flats. Similarly, government aims to increase social housing in regional areas
    a. therefore, while the population increases, there is no associated increase in rates yield

In line with the findings of the Productivity Commission and other reports, we suggest:

Ideal Growth:

i. infrastructure planned and delivered in line with population growth
    a. shaped by (refreshed) DPIE regional strategies
    b. led by local residential and economic strategies, with land released in orderly stages, supported by infrastructure expansion plans
    c. values for land to be acquired or dedicated should be staked at pre-zone or development uplift levels
    d. infrastructure estimates and contribution rates refreshed at contemporary construction costs by region, per each council term – and not rely on CPI
ii. population mapped to infrastructure expansion, and monitored using lead indicators
iii. subcategory rates yield for growth localities designed to cover MRR costs identified in AMP and in turn, meet the asset ratio benchmarks
iv. flexible rates structures to differentiate infrastructure MRR and servicing yields

Opportunity:

IPART seeks a rate peg methodology that allows the general income of councils to be varied annually in a way that accounts for population growth, so that councils to be able to continue to provide quality infrastructure and services to their communities, including in those local government areas experiencing population growth. We appreciate IPART has identified impacts on council costs.

Again, we urge IPART to incorporate a mechanism to recognise either population growth (or asset growth as a proxy) as margin above the rate peg for all councils, regardless of

whether the individual LGA rate of population growth is at or above the NSW rate of growth.

We note population forecasts are proposed to pre-empt rate peg and infrastructure levy determinations, with IPART suggesting the following options:

Table 2 Population growth factor – options

Method	Historic growth	Projected growth	Projected growth, with adjustment for actual growth	Blend historic and projected growth
Source	ABS historic (2 year lag)	DPIE projected	DPIE projected, with retrospective adjustment for historic growth based on actual growth reported by the ABS	Blending of ABS historic and DPIE projected, using x[a]% historic and (1-x%) projected for LGAs
Pros	Simple to administer; consistent with LGCI	Simple to administer; revenue can rise in line with future growth	Removes risk of under or over recovery of income; councils can increase revenue in expectation of future growth	Relatively simple to administer; mitigates the risk of significant over and/or under recovery of revenue by allowing for a mix of both
Cons	Time lag - councils can increase revenue only 2 years after growth has occurred	Projections may result in under or over recovery of income (e.g. impacts of COVID-19)	Administrative burden; if growth is lower than projected, future revenue may be lower; if growth is higher, rates may increase in future	Some risk of under or over recovery of income remains

However we dispute the notion that coastal and regional cities and many regional councils are either not experiencing steady growth, and in the context of post-COVID intrastate migration, certainly dispute the growth of those areas would not be equivalent or greater than the NSW growth. Accordingly, we suggest the following mechanisms to manage and fund growth.

We urge IPART consider a reframe of the structure of rating and financial sustainability of regional councils, with suggestions outlined below.

Population Growth:

i. utilise *lead* rather than *lag* indicators for annual population growth forecasts
    a. most councils utilise ID Profiler, which includes population forecasting and economic modelling
    b. example https://forecast.id.com.au/queanbeyan-palerang
    c. local data available to councils may include
        i. lag time between issue of 10.7 planning certificate and s603 financial certificate indicating property turnover (and capture former postcode of purchaser)
        ii. occupation certificates (OC)
        iii. change in sewage effluent
        iv. change in kerbside waste collections
        v. change in AADT at key arterials
ii. new residential OC's multiplied by respective household structure (eg 2.75) as an early indicator of population growth
iii. differentiate regional city growth from the broader region, as often one offsets the other in state population growth estimates
iv. consider an annual population numerical floor (ie > 500), rather than % increase as an impactor on infrastructure and services
v. establish intrastate migration metrics, including metro to regions, not rely just on nett interstate migration
vi. consider *zones/bands of growth* based on like cohorts (metro, coastal, regional city, region, rural, far west); or geography (perhaps DPIE planning regions, FER or joint organisations)
vii. recalibrate the annual LGA population forecasts with 5 yearly ABS census statistics

Financial Growth:

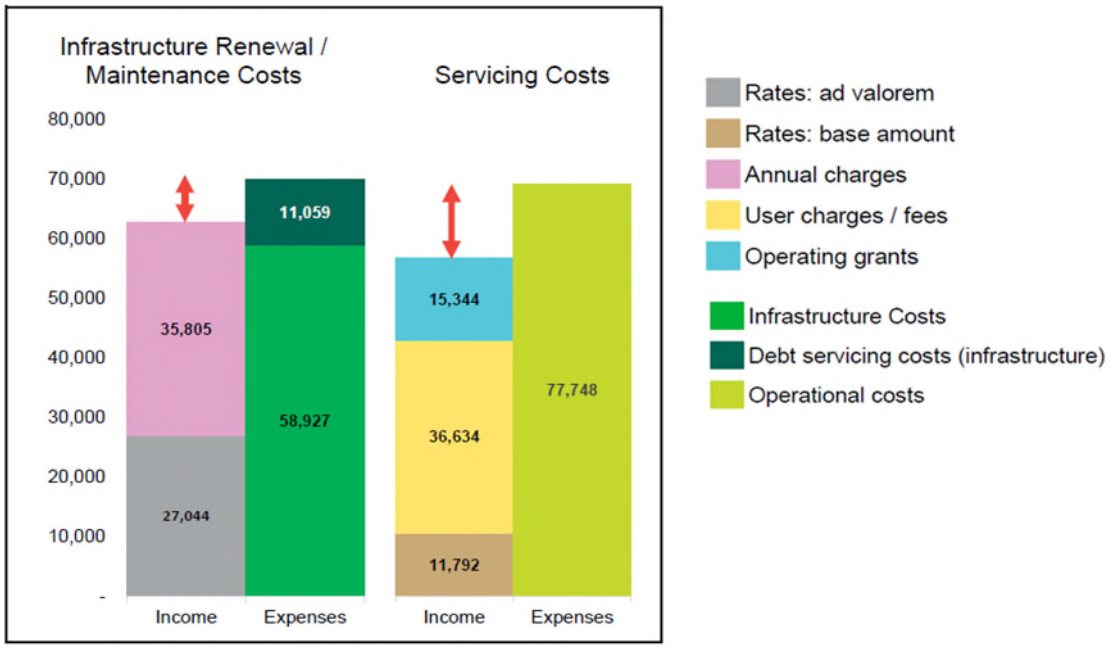
- retain rate peg as minimum for councils with zero or negative growth
- add population growth or asset growth indices as margin above rate peg to all LGAs
- utilise annual population growth indices per *zone* as margin above rate peg, or
    a. consider growth in depreciation (as % general rates yield) as consequence of *new* infrastructure as a proxy for growth, and
    b. consider 5-yearly % change in asset values due to revaluations (which reflect uplift in unit costs of replacement of *existing* assets), as a recalibration of costs growth for local government, rather than CPI
- adjust rate peg at Year 6, should ABS census result not reflect annual forecasts
- pool s7.11 and s7.12 contributions held in plans for greater than 5 years or the subject of complete/inactive developments, and allow their expenditure in similar catchments on renewal of *existing* infrastructure, drawn from existing AMPs and Delivery Program

- enable a (non-SRV) infrastructure levy to be established by councils to
    a. co-fund capex and debt with grants *and*/*or* contributions
    b. service debt by the infrastructure levy
    c. facilitate intergenerational equity and smoothing of capex
- encourage councils to establish an environment and infrastructure SRV, published and ring-fenced to support planned catchment, climate and infrastructure programs and projects impacted by population growth
- consider option for regional levy/ies for seed or co-funding
    a. may be Joint Organisation based
    b. planning, collaboration and joint funding with NSW Local Land Services, Transport for NSW, or Water NSW
- establish ULV-based emergency service tax as part of NSW property tax reform
    a. issue annual tax notice by Revenue NSW, including land tax, duty tax
    b. discontinue annual contribution from local councils (currently a hidden tax)
        i. provides around 4% one-off uplift to many council's general rate yield, and removes risk of contribution exceeding rate peg
    c. transfer emergency service assets from councils to Government
        i. removes MRR and depreciation expense from operating results

In addition, it is suggested a reframing of rating structures be contemplated. For example, QPRC has established the 'Narrow the Gap' principle in its financial strategy which aims to progressively map and match asset and service expenses to related revenue sources such that:

- progressive property taxes (based on land valuation), including ad valorem rates, utility annual charges, development contributions and asset specific grants cover the cost of maintenance, renewal, upgrade and debt servicing costs of infrastructure
- community service obligations (CSO) are funded through the fixed component of the general rate (base amount) and general purpose grants (FAG)
- additional services to community and business (above the CSO) are funded through fees, charges and specific purpose grants
- water, sewer and waste services (including attributed corporate costs) are funded by user charges and fees
- governance and corporate overhead costs are attributed across the asset and service areas

The ‘Narrow the Gap’ principle is illustrated in the chart below:



In this way, transparency improves with:

- infrastructure MRR and relevant debt progressively matched to ad valorem rates, annual charges and related grants (including proposed infrastructure special rate aligned to growth) - or asset standards and levels of service modified accordingly
    - SRV may be applied to ad valorem component to reflect funding required for MRR of infrastructure, or servicing of debt for infrastructure
- base rates, grants (incl FAG) and fees progressively matched to CSO and services - or levels of service and seed-funding grant programs modified accordingly
    - SRV may be applied to base rate component to reflect funding required to meet or improve levels of service or facility operating nett costs
    - may be set at rating sub-category to differentiate levels of service between localities
- ring-fenced SRVs introduced to plan, fund and report on contemporary issues (eg growth, climate, environment, different asset standards or levels of service)

It is also suggested an alternative policy setting for rate pegging may include:

- annualised asset growth % to guide the rate peg
- annualised new asset growth or population growth % to guide the above-rate peg margin

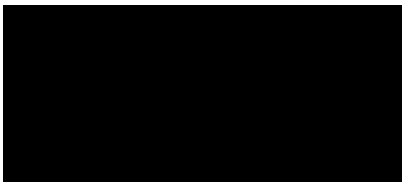
It is suggested IPART utilise lead rather than lag indicators for annual population growth forecasts. Most councils utilise ID Profiler, which includes population forecasting and economic modelling, as well as local data available to councils may include occupation certificates (OC), change in sewage effluent, change in kerbside waste collections, change in AADT at key arterials. For example new residential OC's multiplied by respective household structure (eg 2.75) as an early indicator of population growth.

DPIE forecasts QPRC population growth at 0.5% pa (2016-2041), while ID Profiler sets growth at 1.53%pa (equivalent to 390 new dwellings). Yet annual dwellings growth is currently averaging around 500pa. With NSW growth at 1.1%, QPRC would not qualify for the proposed population rate peg using DPIE forecasts.

Similarly it is suggested Government establish intrastate migration metrics, including metro to regions, not rely just on nett interstate migration; and consider zones/bands of growth based on like cohorts (metro, coastal, regional city, region, rural, far west); or geography (perhaps DPIE planning regions, FERS or joint organisations). The annual estimates may then be recalibrated to the annual LGA population statistics with 5 yearly ABS census.

We would be pleased to discuss elements of this submission further with the IPART team.

Yours sincerely,



Peter Tegart
CEO
Queanbeyan-Palerang Regional Council

Feedback on IPART Questions

1. What council costs increase as a result of population growth? How much do these costs increase with additional population growth?

Increased population and visitor growth bring several cost increases:

- *new urban estates with expanded green space require additional mowing, weeding, spraying etc*
- *additional pedestrian and road traffic increases street litter/cleaning frequency*
- *higher utilisation of existing playing fields, community facilities and the like, increases frequency of servicing (eg cleaning toilets, linemarking) and pressure on access to limited facilities leading to community demands for new or expanded facilities*

The caps on infrastructure contributions and the highly restricted essential works list have increased the infrastructure costs to councils by excluding the recovery of capital costs for community buildings for example. The list excludes core infrastructure expected by communities such as libraries, community halls, aquatic centres and sporting facilities.

Council costs begin with the strategy, options and concept stages in planning for growth, not just the construction and maintenance of new or upgraded infrastructure to accommodate growth.

2. How do council costs change with different types of population growth?

Mostly with frequency of servicing and deterioration of assets (eg road surfaces due to increased loads).

Demographics is a major factor. For example, if the growth is driven by young families, there will be increased demand and for sporting facilities, bike ways, youth services and activities. If population growth is being driven by retirees, councils will face the additional costs associated with accessible infrastructure and related services. In the latter case, councils will also be impacted by lower revenue as a larger proportion of the population will receive the pensioner rate rebate. The NSW Government continues to fund 55% of the rebate but remaining 45% is a cost to councils and communities.

3. What costs of population growth are not currently funded through the rate peg or developer contributions? How are they currently recovered?

QPRC costs are differentiated into:

i. infrastructure MRR of the asset (eg potholes, painting, reseals)
ii. asset servicing (eg cleaning toilets, mowing, street cleaning)
iii. service operations (eg library, pools, sports centres)
iv. services (youth, environment, development etc)

As outlined in the submission, in QPRC (i) is aimed to be funded by rates and annual charges, while (ii-iv) are funded through grants, service fees, base rate and FAG

While a portion of FAG is attributed to population growth, it is the maintenance-repair-renewal (MRR) on expanded infrastructure networks, with increased loads (as a consequence of development and population/visitor growth) that is not compensated by FAG, development contributions or supplementary valuations

The growth in secondary dwellings is negatively impacting on council costs. These self-contained dwellings house population growth, increasing demand on infrastructure and services, but are not captured by the rating system.

4. Do you have any views on the use of the supplementary valuation process to increase income for growth, and whether this needs to be accounted for when incorporating population growth in the rate peg?

As outlined in the submission, the general rates yield from new developments in QPRC (ie through supplementary valuations) may not cover scheduled maintenance, repair and renewal (MRR) costs of new assets, nor adequately contribute to the maintenance of existing infrastructure assets

a. *for example, a new masterplanned suburb in Queanbeyan expects over 18,000 new residents by 2031, in 6,500 new subdivided lots*
b. *it constructs and dedicates to QPRC around $20m new assets each year*
c. *averaging 400 lots per year, and yielding around $500k in supplementary rates, that growth covers annual depreciation expense (ie the annualised renewal costs/year) of those new assets, but falls short of higher operational/servicing costs (eg cleaning amenities, mowing parks and grounds etc), and makes little contribution to existing assets or services*

It is problematic to increase the general rates of new development areas only to compensate for the above, without substantially increasing the notional yield and redistributing the rate burden though the subcategories.

The supplementary valuation process also fails to capture secondary dwellings, as previously noted.

5. Are there sources of population data we should consider, other than the ABS historical growth and DPIE projected growth data?

i. *utilise 'lead' rather than 'lag' indicators for annual population growth forecasts*
    a. *most councils utilise ID Profiler, which includes population forecasting and economic modelling*
    b. *those forecast metrics may be complemented with council data*
    c. *example https://forecast.id.com.au/queanbeyan-palerang*
    d. *local data available to councils may include*
        i. *lag time between issue of 10.7 planning certificate and s603 financial certificate indicating property turnover (and capture former postcode of purchaser)*
        ii. *occupation certificates (OC)*
        iii. *change in sewage effluent*
        iv. *change in kerbside waste collections*
        v. *change in AADT at key arterials*
ii. *visitor data may also be utilised to gauge the impact on services and infrastructure on a cohort that does not directly contribute to rates*

6. Is population data the best way to measure the population growth councils are experiencing, or are there better alternatives (number of rateable properties or development applications, or other)?

As outlined in the submission,

i. consider growth in depreciation (as % general rates yield) as consequence of new infrastructure as a proxy for growth, and

iii. consider 5-yearly % change in asset values due to revaluations (which reflect uplift in unit costs of replacement of existing assets), as a recalibration of costs growth for local government, rather than CPI

7. Do you think the population growth factor should be set for each council, or for groups of councils with similar characteristics? How should these groups be defined?

As outlined in the submission,

i. differentiate regional city growth from the broader region, as often one offsets the other in state population growth estimates

ii. establish intrastate migration metrics, including metro to regions, not rely just on nett interstate migration

iii. consider zones/bands of growth based on like cohorts (metro, coastal, regional city, region, rural, far west); or geography (perhaps DPIE planning regions, FER or joint organisations)

iv. recalibrate the annual LGA population forecasts with 5 yearly ABS census statistics

8. Should we set a minimum threshold for including population growth in the rate peg?

No, the growth factor above rate peg should apply to all LGAs, not just those at or above NSW growth threshold. As an alternative:

i. consider an annual population numerical floor (ie > 500), rather than % increase as an impactor on infrastructure and services

9. What is your view on the calculation of the growth factor – should we consider historical, projected, projected with true-up, a blended factor or another option?

Refer Q5

10. How should the population growth factor account for council costs?

Refer Q4-6

11. Do you have any other comments on how population growth could be accounted for?

As outlined in the submission, consider a reframing of rating structures. For example, QPRC has established the 'Narrow the Gap' principle in its financial strategy which aims to progressively map and match asset and service expenses to related revenue sources such that:

- *progressive property taxes (based on land valuation), including ad valorem rates, utility annual charges, development contributions and asset specific grants cover the cost of maintenance, renewal, upgrade and debt servicing costs of infrastructure*
- *community service obligations (CSO) are funded through the fixed component of the general rate (base amount) and general purpose grants (FAG)*
- *additional services to community and business (above the CSO) are funded through fees, charges and specific purpose grants*
- *water, sewer and waste services (including attributed corporate costs) are funded by user charges and fees*
- *governance and corporate overhead costs are attributed across the asset and service areas*

Enable a (non-SRV) infrastructure levy to be established by councils to
- *co-fund capex and debt with grants and/or contributions*
- *service debt by the infrastructure levy*

12. Do you have any comments on our proposed review process and timeline?

Please refer to the section on 'Financial Growth' in the submission.

We are happy to progress these views and concepts through further discussion with IPART.

For further information on this submission, please contact Peter Tegart (CEO) on [redacted]