

Council Reference: 75639E (D24/105732)

14 March 2024

Independent Pricing and Regulatory Tribunal (IPART)

Attention: Jessica Clough

Email: [Jessica.clough@ipart.nsw.gov.au](mailto:Jessica.clough@ipart.nsw.gov.au)

**Dear Ms Clough**

**Feedback – IPART review of financial model for Council’s in NSW  
Terms of Reference (ToR)**

Shoalhaven City Council thanks IPART for the opportunity to provide feedback on the NSW Governments draft Terms of Reference (ToR) regarding IPART’s review of the financial sustainability model for Council’s in NSW.

Council reviewed the draft ToR and relevant issues at their Ordinary Meeting of 11 March 2024, resolving to lodge this submission (MIN24.118):

*That Council:*

1. *Receive and note this report; and,*
2. *Note the amendments approved at the ordinary meeting of the 11 March 2024 and make a formal submission to IPART with the following amendments to the submission at attachment 1:*
  - a. *Consider the financial impost of tourism related activities on Councils assets and services that are not directly recoverable via rates and fees & charges.*
  - b. *The suitability, and advisability, of rate pegging methodology given its deficiencies, and long-term impacts on local government sustainability and infrastructure backlogs.*
  - c. *Impacts of disasters, disaster funding management and infrastructure impacts on local government financial performance outside of standard IP&R scheduled works.*
  - d. *The mechanisms and suitability of Financial Assistance Grant funding, and the diminishing revenue yielded by the current model versus originally proposed model in the context of operating sustainability.*
  - e. *The significant and ongoing impacts of State and Federal government cost shifting on Council’s operating and asset performance, as well as the inability to recoup costs from the NSW Government across a range of areas.*
  - f. *Barriers to use of Developer Contributions in addressing existing infrastructure provision and maintenance requirements.*

- g. Review of full cost recovery mechanisms for statutory and legislated services, such as development applications, where statutory set fees do not achieve full cost recovery.*
- h. Ongoing and additional requirements in standard service delivery to meet the needs of evolving practices, technology and governance risks (such as cyber security and digitisation for example), impacting operating costs and performance.*

Council appreciates that the draft ToR has been constructed to include issues relevant to transparency and accountability and aim to align with the review of rate peg methodology undertaken by IPART last calendar year.

Council cannot understate the importance of this review. Councils are the level of government closest to our communities and perform a critical role in service and infrastructure delivery. The ongoing financial sustainability and long-term funding models for Councils is paramount to ensuring that communities continue to achieve and enjoy local priorities and core service delivery.

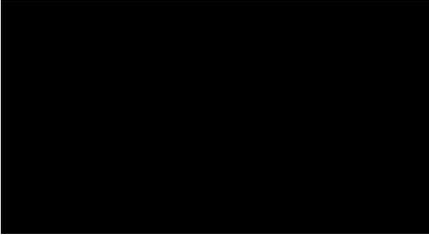
The draft ToR does not include a number of relevant areas that significantly impact local government financial position for all Councils in NSW. This includes reasonable revenue sources, cost shifting, funding mechanisms and the rating system as a whole. To this end, Council requests that, to achieve a holistic and fulsome review of the financial sustainability of Councils in NSW, the following must be included in the ToR for investigation and in devising a final report:

- The suitability, and advisability, of rate pegging methodology given its deficiencies, and long-term impacts on local government sustainability and infrastructure backlogs.
- Impacts of disasters, disaster funding management and infrastructure impacts on local government financial performance outside of standard IP&R scheduled works.
- The mechanisms and suitability of Financial Assistance Grant funding, and the diminishing revenue yielded by the current model versus originally proposed model in the context of operating sustainability.
- The significant and ongoing impacts of State and Federal government cost shifting on Council's operating and asset performance, as well as the inability to recoup costs from the NSW Government across a range of areas.
- Barriers to use of Developer Contributions in addressing existing infrastructure maintenance requirements.
- Review of full cost recovery mechanisms for statutory and legislated services, such as development applications, where statutory set fees do not achieve full cost recovery.
- Ongoing and additional requirements in standard service delivery to meet the needs of evolving practices, technology and governance risks (such as cyber security and digitisation for example), impacting operating costs and performance.
- Consider the financial impost of tourist related activities on Councils assets and services that are not directly recoverable via rates and fees & charges.

The report attached, tabled at the Ordinary Meeting of 11 March 2024 for Councils consideration, outlines rationale for Councils requested inclusion of these points in the Terms of Reference.

Shoalhaven City Council would welcome any opportunity to further discuss these matters and the review of financial sustainability for Local Government in NSW. Please do not hesitate to contact [REDACTED] at any time or should IPART require any further information on this submission.

**Yours sincerely**

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## CL24.64 IPART Submission - Draft Terms of Reference for NSW Council's Financial Model Review.

**HPERM Ref:** D24/66567

**Department:** Finance

**Approver:** [REDACTED]

**Attachments:**

1. Shoalhaven City Council - Letter to IPART - Feedback - Terms of Reference - Council's Financial Model Review for Council's
2. Draft - Terms of Reference for NSW Council's Financial Model Review.

### Reason for Report

The purpose of this report is to inform Council of the current draft Terms of Reference (ToR) related to the NSW Governments tasking of IPART to review the financial sustainability models of Councils in NSW. Furthermore, Council's support in lodging a formal submission to IPART on the draft Terms of Reference is sought, outlining requested inclusions in the current ToR to effectively assess and address better long-term financial sustainability.

### Recommendation

That Council:

1. Note and receive this report; and,
2. Make a formal submission to IPART on the NSW Government's "Draft Terms of Reference for NSW Councils Financial Model Review" at attachment 1.

### Options

1. Council resolve to lodge a submission as recommended.  
Implications: No further resource, policy or risk issues are apparent.
2. Council resolve to not lodge a submission on the draft Terms of Reference.  
Implications: No further resource issues are apparent. Risks identified with respect to ToR deficiencies will not be expressed to IPART.
3. Council resolve an alternate course of action.  
Implications: Implications are unknown and will depend upon the resolved position.

### Background

In 2023 IPART, as part of their review of the rate peg methodology for Councils in NSW, recommended to the NSW Government that an independent review of the financial model for Councils be undertaken. As a result, the NSW Government has now tasked IPART to undertake such review, examining key issues impacting the financial sustainability of Councils and Local Governments overall financial models. In IPART's 'Review of the Rate Peg Methodology Final Report' provided to the NSW Government in August 2023 was noted:

- Longstanding financial sustainability issues
- Some councils are experiencing financial sustainability problems, which they suggest are related to the current financial model for councils.

- This is requiring strong financial management and council action to either increase rates or cut services, at a time when many people are less able to afford higher rates or to do without essential council services.
- Ratepayers are concerned about cost of living pressures and affordability of rates while they also depend on and value council services.
- Councils are very diverse, and IPART heard that a 'one size fits all' financial model does not respond to the specific and individual needs of councils and their community priorities.

On 11 January 2024 IPART received a draft Terms of Reference (ToR) from the NSW Government to guide their investigation and reporting accordingly, in line with section 12A of the *Independent Pricing and Regulatory Tribunal Act 1992*. IPART are now seeking feedback on the NSW Government's draft Terms of Reference. A review of the ToR has been undertaken by relevant staff, including finance and Councils Chief Financial Officer. The draft ToR appears at attachment 2. Submissions on the draft ToR must be made by the 15 March 2024.

The draft ToR proposes IPART review and recommend improvements on the following matters:

1. Whether the current funding model will sustainably support the needs of communities.
2. The visibility of councillors and the community over the financial and operational performance of their councils.
3. Whether the current budget and financial processes used by councils are delivering value-for-money for ratepayers and residents.
4. Whether councils (both councillors and staff) have the financial capacity and capability to meet current and future needs of communities.
5. How can better planning and reporting systems improve long term budget performance, transparency and accountability to the community?
6. Any other matters IPART considers relevant.

While the inclusions are all relevant and needed, the ToR fails to pick up on a range of specific matters that such a review would benefit from investigating, identifying and making recommendations on.

### **ISSUES FOR CONSIDERATION**

IPART is aware of the significant variations to average residential rates across Councils in NSW, and as a result Councils are struggling to meet minimum benchmarks (namely infrastructure backlog ratios and operating performance ratios) leading to the inability to meet minimum required community service obligations and unable to fund ongoing activities, which cannot be addressed via the current rate peg methodology.

### **EXTERNAL FACTORS:**

Many NSW Councils have dealt with the impacts of multiple (as many as 14) declared natural disasters in recent years including devastating bushfires, multiple floods, landslide events and impacts of east-coast low pressure systems that have caused substantial damage to our coastal and hinterland areas. Where Councils are lucky enough to secure grant funding for the betterment of affected assets, the forward funding of grant opportunities impacts both Councils cash position (operational surplus) and ongoing infrastructure backlog targets. During 2023, Shoalhaven City Council had forward funded over \$30 million in grant funding awaiting acquittals, which needed to be drawn from the general fund and liquid cash. Furthermore, since 2020, the cost of dealing with COVID-19 impacts (including supporting ratepayers), interest rates and inflation have impacted debt position and caused a decline in

the cash position of Councils across the state, hindering their ability to deal with unexpected circumstances (such as disasters) or forward fund grant opportunities moving forward.

#### RATE PEG CHALLENGES:

Current rate methodology and application does not account for the variable nature of different local government areas (LGA's), including those where non-primary residences are utilised for commercial/tourism purposes. There are several mechanisms that could be used to assess the maximum applicable rate for a property, including whether the premises is being utilised for Short-Term Rental Accommodation (such as AirBnB), and taking the improved capital value for rating purposes (as opposed to land valuation). Alternate mechanisms such as these would ensure that increases were not compromising the most disadvantaged individuals in our communities but were recovering income from those that are more likely to be able to afford it – akin to the method applied to scalable personal taxable income brackets.

The population factor fails to address the additional operational and capital costs of a growth council and is not achieving its intended purpose to enable Council to maintain per capita genera income over time. Council's per capita income will decrease as our population grows and we will be unable to maintain existing service levels.

Regional areas, particularly those in coastal locations which are subject to the breadth of different weather events and asset impacts, are faced with increased usage of critical infrastructure through peak visitation periods (predominately roads, beaches, parklands, footpaths, amongst other asset categories). However, the current rating methodology does not include mechanisms to collect the additional maintenance requirements from tourism related developments, but rather defaults to collection of revenue across the entirety of the rate base. Allowance to collect additional revenue from industries that benefit from tourism influx during peak periods would allow a contribution to the impacts and added wear & tear on critical public infrastructure.

It is in the community's best interests that Council is able to fund the level of services, infrastructure and assets at a level of reasonable expectation and which ratepayers can realistically afford. The number of Councils in NSW reporting operating deficits has increased since 2016, and more than half of NSW Councils do not meet the Office of Local Governments *Infrastructure Backlog Ratio*.

The application for Special Rates Variations (SRV) can be problematic, as they create contention and division in communities unnecessarily, where ratepayers have already been struggling with cost-of-living issues post COVID-19. Special Variations are typically applied for at a point of criticality for Councils where years of rate peg application have not been sufficient and left ongoing deficits across core services delivery areas. They have become a process for Council to follow when a sharp and large increase in rates is required, due to the shortfalls created over a long time period and loss of associated compounding that would have been achieved through lesser overall rates increases.

In short, had the rate pegging methodology been sufficient for the past decades, and allowed Council's in NSW to apply reasonable but conservative rateable measures over time to address infrastructure backlogs and true operating costs, as well as the ability to implement levy amounts (such as environmental levy for coastal protection), Shoalhaven City Council would not have been presented with the prospect of a 44% special rate variation this financial year.

#### FINANCIAL ASSISTANCE GRANT DECLINE:

There is a significant and immediate need for the Federal Government to confirm payment schedules of the Financial Assistance Grants (FAG) directly to Local Government, and further, increase the amount to a minimum of 1% of total taxation revenue. This is not a new issue for Councils, and while originally introduced on a platform of 1.2% of personal income

tax revenue (to be increased to 2% over time), the current levels are closer to 0.5%. This increase alone, with certainty over the financial year in which the grant is paid to Council, will substantially and positively increase operating sustainability and Councils ability to meet growing infrastructure needs. In Shoalhaven City Council's present situation, an increase of FAG to 1% would address 70% of our total operating deficit.

Statewide, 54 of 128 (42%) Councils failed to meet the operating performance benchmark in 2022. Had the Financial Assistance Grant (Councils share of personal taxable income revenue) been double its current rate, 36 of those would have been in surplus, bringing the total not meeting the benchmark to 18 (or only 14% of all Councils in NSW).

#### GOVERNMENT COST SHIFTING:

The shifting of financial burdens from the NSW Government to Councils is consuming rateable income at a local level at an unsustainable rate. In 2023, data compiled by independent experts *Morrison Low* showed that in the 2021/22 year a total of \$1.32 billion in costs were shifted onto Council in NSW by the State Government, totalling on average an additional \$460 per ratepayer annually. An increase of 78% from the 2015/16 financial year.

The top 5 cost shifting categories for which Councils do not have a mechanism to recoup costs are:

1. Waste levy = \$288.2 million.
2. Rate exemptions = \$273.1 million.
3. DA and Regulatory functions = \$208 million.
4. Emergency Services Contributions = \$165.4 million.
5. Funding of Libraries = \$156.7 million.

The NSW Waste Levy is a prime example where revenue collected by Council on rates notices is gathered by the State Government, and not wholly redistributed back to Local Governments who undertake end-to-end waste management functions (from kerbside collection, to landfill activities and end-of-life remediated landfill maintenance).

#### DEVELOPER CONTRIBUTIONS:

Councils are able, through adopted and approved 7.11 and 7.12 infrastructure contribution plans, to charge developers for new infrastructure where there is a nexus to the development in question. These plans have typically incorporated larger project delivery focussed on social infrastructure and transport infrastructure respectively. Ongoing, many projects are never realised as the total cost (particularly when coupled with inflation and other economic factors) is not recouped via the infrastructure charges.

Where developments impact existing assets and cause increased degradation of assets, there is limited ability to utilise developer contributions for the purposes of addressing asset maintenance backlogs. The ability for Councils to allocate even a percentage of 7.11 or 7.12 internally restricted funds towards maintenance would assist in addressing asset maintenance backlog targets, and upkeep of existing community assets in perpetuity.

#### ONGOING OBLIGATION FOR SERVICE DELIVERY:

Councils carry a statutory and legal obligation to perform and deliver crucial services to our communities, including road maintenance, public open space maintenance, local planning, development assessment, and libraries (amongst an array of others). The delivery of these services and infrastructure at an acceptable level is critical to ensuring public faith in government as well as being crucial to the economic, environmental and social fabric of NSW across its unique communities. Adding to these base services is an ever-increasing cost of emerging issues and risks. For example, in maintaining large volumes of personal information for our residents, ratepayers and customer base, cybersecurity has become both

a needed and legislated matter for Councils to address, without any additional funding from other levels of Government to do so. Added to this are statutory limits on fees and charges for required functions that no longer reflect the true cost of delivering the service (for example end to end development assessment and court appeal matters), and which Councils must now fund shortfalls in delivery through other means. In effect, additional required operational matters and statutory set fees continue to impact Councils financial position, without the ability to recoup costs via any mechanisms other than our applied rates base.

### **IPART's NEXT STEPS**

IPART will be required to undertake further public consultation as part of the review, including publishing a draft report prior to finalisation, and undertaking a formal public hearing. The final report will be presented to the Minister for Local Government within 12 months of the receipt of the draft ToR, and thus is expected to be finalised with recommendations by 11 January 2025. The final report will be tabled in Parliament.

### **RECOMMENDED SUBMISSION FROM SHOALHAVEN CITY COUNCIL**

The report and recommendations that arise from IPART's review have the potential to impact all Councils in NSW for decades to come. The draft ToR provided by the NSW Government contains much needed and broad inclusions on the transparency and governance for the review of Councils financial sustainability and elected representative and community input into these systems. They do fail to identify and make the subject of review specific matters we know have, and will continue to, impact Councils financial position and stability into the future.

For the reasons outlined in this report, and arising from a substantial review by key internal staff members, it is recommended that Shoalhaven City Council (by way of resolution) make a submission on the draft ToR that requests inclusion of specific issues impacting Councils financial sustainability as follows:

- The suitability of rate pegging methodology, its deficiencies and long-term impacts on local government sustainability and infrastructure backlogs.
- Impacts of disasters, disaster funding and infrastructure impacts on local government outside of standard IP&R scheduled works.
- The mechanisms and suitability of Financial Assistance Grant funding, and the current model versus originally proposed model in the context of operating sustainability.
- The marked impacts of government cost shifting, including operating and asset performance, as well as the inability to recoup costs from the NSW Government.
- Barriers to use of Developer Contributions in addressing existing infrastructure maintenance requirements.
- Ongoing and additional requirements in standard service delivery to meet the needs of evolving practices, technology and governance risks (such as cyber security and digitisation for example).

### **Internal Consultations**

The following internal consultation has occurred regarding the content of this paper and the proposed submission:

1. Chief Financial Officer.
2. Executive Management Team.

### External Consultations

Several Councils in NSW have been consulted on this matter in the review of the draft Terms of Reference.

### Community Consultations

No community consultation has occurred given the timeframe and nature of the submission. However, Council has recently consulted with our community on the prospect of a Special Rates Variation, and feedback has noted that the proposed increase was not supported.

### Policy Implications

Shoalhaven 2032 Community Strategic Plan priorities relate to this report and its recommendations:-

4.1 – Deliver reliable, high quality services.

4.2 – Provide transparent leadership through effective government administration.

And further, the following progress measures:

- Community satisfaction with basic council services.
- Council's financial benchmarks (number of financial ratios that meet the 6 target ratios).

Holistically, the IP&R Framework links Councils' financial position to our ability to deliver services. Implications on the following associated Council plans (our *Resourcing Strategy*) result from base revenue and rates scenarios: *Workforce Plan*; *Long Term Financial Plan*; and *Asset Management Policy/Strategy/Plan*.

### Financial Implications

Should the draft Terms of Reference not contain the right criteria for specific review of issues impacting Councils financial sustainability, the ongoing impact and deficiencies of rate pegging, revenue models and Special Variations will affect Local Governments in NSW, and the communities we serve, into the future.

### Risk Implications

Should a submission not be made, there is a risk that IPART will not incorporate the relevant criteria into the final Terms of Reference.