North Sydney Council Submission

Assessing Local Government Revenue Raising Capacity

In this submission from North Sydney Council, answers or comments have been provided wherever possible to the questions raised in the Issues Paper. Not all questions have been answered because they apply to interstate comparisons.

1. Revenue

1.1. Trends in Local Government revenue

What are the principal factors explaining the trends in revenue from councils' various sources? Why has 'other income' been growing at a faster rate than council rate revenues and sales of goods and services?

In NSW, because of the rate-capping regime, Councils have been obliged to turn to other sources of income to keep up with the rising costs of delivering services. With the rate cap generally being pegged to CPI, revenue for NSW councils has generally not been keeping up with expenditure for the same level of service delivery. This is because the costs of staff and materials, as well as levies imposed by the State Government have risen by approximately 2% more than CPI. This is certainly the case for North Sydney Council.

Development levies are an important source of capital funds for providing new facilities. When NSW experienced rapid rates of development, at least along the coast and within Sydney metropolitan area, the amount of funds received from development levies was high. But as development plateaued in the last four years, development levies amounts have diminished, and this is a significant problem for Councils, which rely on these as a means of capital funding for new and improved infrastructure for the increased population that comes into the council area as the result of development. Reliance on such levies, which will inevitably vary in accordance with development trends, is a major risk for Councils in NSW.

For metropolitan Councils, such as North Sydney, commercial property and parking facilities (both parking stations and parking meters) have become important sources of revenue to fund ongoing maintenance and service delivery. Parking Enforcement is a significant issue for inner metropolitan councils where demand for parking is high. This raises important revenue, however quotas or targets are not set, and the aim is to achieve parking compliance not additional funds. There should not be reliance on fines as a form of revenue, because they can fluctuate depending on whether people break the law or not.

Do these trends differ between States and Territories, and between urban, rural, remote, and indigenous local governments? If so, what are the primary factors explaining such differences?

There are differences between urban and rural councils because the potential for revenue-raising differs. North Sydney Council has a relatively low proportion of revenue from rates and charges at 39% in comparison with many other councils, and particularly rural councils. North Sydney Council also receives a lower percentage of revenue from Government grants than rural councils. However North Sydney Council has some capacity to raise revenue from property and investments because of its location.

1.2 Capacity to raise own-source revenues

What are the principal factors that determine the magnitude of the various revenue raising bases available to local governments? How and why might they differ between local governments within and between States and Territories (for example, by council type or location and functions required of them), and over time?

Clearly in NSW the existence of rate-pegging for the last 30 years has been a major factor in limiting the ability of councils to raise rates commensurate with the need to meet infrastructure maintenance requirements and the demands of residents and rate-payers for services.
If rate-pegging did not exist then Councils rate revenue would be dependent on the amount of revenue necessary to provide services desired by the community. If a rating structure were similar to land tax then the revenue would increase equivalent to the increases in ratable valuations. In this situation, the valuation type used for rating would largely be irrelevant eg land value or capital improved value.

Other factors are:

- Population size of the council area
- The degree of urbanization of the council area which will impact on the ability to raise revenue from property, parking and other urban services
- The willingness and ability of the council to provide user-pays services
- Whether the area is a visitor attractor and funds can be raised from people paying for tourism, recreation or other services provided by councils. The problem with being an area, which attracts visitors as is the case for North Sydney with its Sydney Harbour frontage, is that there are not always opportunities for raising revenue from visitors and so the local community has to pay for the ‘wear and tear’ of large visitor numbers on parks and other infrastructure eg. New Years Eve and Australia Day events.

What are the key determinants of the capacity and willingness of resident households, organisations and businesses to pay for services provided by their local governments?

The key determinants of capacity and willingness to pay are:

- The socio-economic level of the area and the level of household and business incomes
- The number of resident property owners in comparison with investment property owners: In North Sydney, approximately 50% of residents are tenants. Investment property owners are generally less inclined to pay for services provided by councils.
- Business property owners, who operate their own businesses in the area, are more inclined to pay for services where they see a direct benefit to their business. In North Sydney, businesses have agreed to pay special levies for commercial areas, where they see the funds going to streetscape improvements and the like.

What scope is there for local governments to augment their revenues with fees and charges collected from non-residents? How and why might the scope to do so differ between local governments?

There are some opportunities but these are limited because many council services are not able to discriminate between residents and non-residents.

Council parks and reserves are open to anyone regardless of where you live. Library services are free for example, whether you are a resident or not. Entry fees for recreation facilities are the same for residents and non-residents.

Opportunities exist where it is possible to differentiate between residents and non-residents because there is an entry point to the service, and/or vouchers or identification stickers can be provided. These include, for example:

- Providing free or discounted parking for residents, whilst charging visitors
- Providing free or discounted access to waste management services, whilst charging non residents full fees (does not apply to North Sydney because we don't have a waste management facility)

Do local governments have policies, which in effect, limit their own-source revenue raising? If so, what are these policies and what might be factors holding back councils from increasing their own-source revenue? What might stand in the way of changing the policies to expand the ways, and extent to which local governments raise revenues?

There are some limitations on Councils being able to operate commercial services on an equal footing with the private sector. Councils are public bodies, accountable to their communities and are not always in the position of being able to operate services purely for the profit that can be achieved. There may be legislative impediments (eg. statutory fee limitations) and community service obligations and requirements, which limit revenue-raising capacity. In 2002, Council undertook a study on the total cost of providing the Development Application Process and found that only 23% of this cost was recovered by way of statutory fees.

Councils also have local policies with the aim of improving the quality of life and visual amenity of the area, which may impact on revenue-raising capacity. North Sydney Council has, for example, a policy of limiting advertising in public areas, and does not sell advertising space on Council property, including bus shelters.

2. State and Territory government regulatory constraints

2.1 Land rating and valuation methods

To what extent do limits on land categories that local governments can adopt for rating purposes restrict their capacity to raise rate revenues? What are the principal reasons why some local governments do not pursue differential rate setting even where they are free to categorise their own land?

North Sydney Council does have differential rating, distinguishing between residential and business rates.

Do restrictions on land valuation methods affect the capacity of local governments to raise revenue? If so, how and to what extent?

The system of valuation in NSW, and the application of rates to land value leads to distortions and inequities in the rating system. This is particularly the case in inner urban areas where land values are high and there is considerable development of medium and high density housing. The system of Capital Improved Value would take into account development of land, and could provide for greater equity in rating between low density and high density developed land. Whilst a different valuation system may smooth out the distortions in rating, however, it would not lead to an overall increase in rating revenue in a rate-capping environment and would result in a re-distribution of the existing rating burden.

2.2 Rate pegging

What are, or might be, the reasons for rate pegging?

The reason for rate-pegging in NSW is a long-standing lack of confidence by successive State Governments in the ability of Councils to manage their own financial affairs. The fact is that rate-pegging is politically popular at the State level. This has not stopped State Governments from raising their own taxes and charges at far higher levels than CPI over many years. The difference between increases in land tax revenues (State responsibility) and Council rate revenue over the same periods of time provide a stark example of the different standards applied.

To what extent does rate pegging limit the ability of local governments to raise council rate revenues?

Rate-pegging limits the ability of Councils in NSW to raise rates over the percentage determined by the Minister for Local Government. The annual maximum rate increase allowed is generally around CPI. There is no relationship between the capped rate increase amount and the reality of increased costs of providing local government services.

Councils in NSW are able to make application to the Minister for a special variation to the increase of rates. Many Councils have used this option to apply for special levies, such as Environment Levies or Infrastructure Levies, as well as Levies in commercial areas for streetscape improvements. These Levies are always time-limited, for example for five years. They provide much needed revenue for identified infrastructure management and improvement, such as storm water drainage. However they do not address the underlying problem of rating income not keeping up with rising costs. While the Minister has approved many special rate variations, not all applications are successful.

Are local governments able to raise revenues from other sources to compensate for the potential revenue raising limits imposed by rate pegging? How, and with what consequences?

Councils are able to raise revenue from fees and charges for Council services, where there is not a statutory fee set (for example development assessment) or a requirement that the service be free (for example, borrowing books from libraries). However fees and charges must still be at a level of people’s willingness to pay. Revenue-raising from fees and charges therefore only goes part way towards compensating for the limits imposed by rate-pegging.

2.3 Concessions and exemptions

To what extent do mandated exemptions and concessions limit the ability of local governments to raise council rate revenue?

Government buildings, government agencies and private schools attract large numbers of workers and students from outside the North Sydney Council’s boundaries who utilize the local facilities without making any financial contribution. If these organisations were ratable then Council could expect to receive a significant increase in rate revenue.

What are the existing arrangements in each State and Territory regarding the payment of council rates and rate-equivalents by Australian, State and Territory landholders?

On land which is leased for private purposes, rates are payable by the lessee.

What are the existing arrangements in each State and Territory regarding the provision of concessions, and the compensation by State and Territory governments for the loss of revenue by local governments from these concessions?

Mandatory pensioner rebates are reimbursed at the rate of 55%.

To what extent do exemptions and concessions limit the ability of local governments to raise revenues?

Exemptions do limit the amount of revenue raised however exemptions, rebates and concessions are forms of hidden subsidization.

Are local governments exempt from taxes and charges by other tiers of government? If so, what are they? Does any lack of reciprocity favour or disadvantage local governments?

No. This is a clear disadvantage to local government.

2.4 Setting fees and charges

What are the regulatory requirements and guidelines applied to local governments for setting fees and charges?

Councils are required by law to set fees and charges on an annual basis as part of the management plan and budget process. The proposed Fees and Charges have to be advertised, and are open to submissions from the public. They must then be formally adopted by Council.

To what extent are local governments constrained in setting fees and charges? To what extent are the requirements and guidelines followed by local governments?

Some fees and charges are set by State regulation, for example fees in the planning and development area. The level of fees (statutory fees) does not cover the true cost of processing and assessing development applications.

Other charges, such as the Domestic Waste Charge, are set by Councils, but the activities on which these funds can be spent are limited by legislation (Local Government Act). These charges are limited to “reasonable cost benefit” and do not permit the payment of dividends.

The guidelines (or regulations) are followed because failure to do so would lead to sanctions from the State Government.

To what extent do local governments under or over-recover the costs of supplying goods and services?

Generally councils under-recover the costs of supplying goods and services, because of the need to provide value for money to the rate-payers, willingness of residents to pay and community service obligations.

What scope would there be to raise additional revenue if the limits were removed?

There would be significant scope to increase revenues either by way of recovering the true costs of providing some services or permitting the payment of dividends.

3. Impacts on individuals, organisations and businesses

3.1 Council rates

What would be the effects on individuals, organisations and businesses of local governments increasing council rates?

Rates are a cost of owning property and pay for services provided by councils. Without the ability to charge rates, councils would not be able to provide services to the ratepayers, residents and businesses in the local government area. If rates are increased to cover the costs of service delivery, the services should be what the community wants and needs and provide value for money. In North Sydney, our rates are seen as being low on average in comparison to similar councils, therefore any moderate increase would not place a significant burden on the ratepayers.

What effects might rate pegging and the choice of land valuation methods have upon individuals, organisations and businesses?

The choice of land valuation method and rate-pegging in North Sydney has led to the vast majority of residential rate-payers paying very low rates. Approximately 80% of households in North Sydney pay the minimum rate, which is currently $371 per annum. This goes nowhere near covering the costs of services provided to these households. Most ratepayers in medium and high density housing pay the minimum rate, which means that, for example, a multi-million dollar penthouse apartment with views of Sydney Harbour will attract the minimum rate.

To what extent are council rate revenues used to subsidise the delivery of goods and services for which fees and charges are collected? What are the consequences?

The Development Application Process as mentioned earlier, is heavily subsidised to the tune of 77% from general revenue. Other examples are Library, Childcare & Community Services, Sporting Facilities and Community Centres (halls).

To what extent do efficiency and equity considerations contribute to the attractiveness of council rates as a source of local government income?

It is an efficient method of ensuring that most property owners contribute to the cost of providing local services.

3.2 Sales of goods and services

To what extent do councils cross subsidise the prices of goods and services?

Councils do cross subsidise the prices of goods and services. Some examples in North Sydney are:

- Pool entry fees are set for an adult at $5.50, which entitles the person to a swim. This is a competitive entry fee compared to other council swimming pools. However there are discounts for pensioners, seniors and students. The total revenue from fees and charges at the Pool does not fully cover all costs of operating the Pool. However there would be community protest if Pool fees were increased significantly or if the discounts were reduced or ceased. So the Pool operations is subsidized by other Council revenue, such as commercial rental of space at the Pool for restaurant businesses.
- Fees for development assessment are set by the State Government. They do not cover the cost of providing the development assessment service, which has to be subsidised by other revenue sources.
- Vacation care services are provided by Council with fees that are competitive with other councils, but on the low side. Fees are kept within a certain range to ensure their affordability, however this has meant a shortfall between revenue received and the cost of providing the service. Council has recently decided to outsource the provision of vacation care to an external provider in order to cut the cost of providing the service, through economies of scale.
- Sporting Facilities and Community Centres (halls) are all significantly subsidized to ensure accessibility is available to the community.

If services are subsidised, are the subsidies funded by higher rates or other fees and charges? Could full cost-recovery fees and charges be collected? What would be the consequences? Are any other revenue sources used to subsidise services?

Subsidies come from Council's total revenue including rates.

Do councils use the return on their long-lived assets (profit and depreciation) to cross subsidise services? If so, what are the consequences for the sustainable provision of infrastructure services?

Yes. Generally, expenditure on infrastructure is negatively impacted.

What would be the principal implication for individuals, organisations and businesses of applying or removing cross subsidies?

Assuming that Council's revenue base is significantly less than it should be in an ideal situation, then people and organizations would pay more or would choose to vary their use of the services.

3.3 Developer charges and contributions

To what extent do local governments employ developer contributions and charges to finance investments in new and upgraded assets?

Many Councils in NSW, including North Sydney Council, depend on development contributions to fund new and upgraded assets. In North Sydney significant improvements to the pool, library, community centres and parks have been funded not totally but to a large degree from development contributions. North Sydney Council was able to collect quite large sums from development when the property boom was at its peak. However with the decline in development in Sydney, the funds from development contributions have also declined. This means that some new and upgraded facilities have had to be deferred.

Are there legislated limits to contributions that can be required or charges that can be collected?

Council are required by legislation to prepare a Development Contributions Plan, outlining what funds will be collected and how the funds will be expended. This has to be placed on public exhibition, and is open to challenge from developers. Development levies only apply to commercial, medium and high density residential development in North Sydney and are all limited to the increase in population as the result of new development.

Are there legislated constraints on the use of revenue raised from developer charges?

There has to be a nexus between the additional demand created by the development and the facilities to be provided by the funds raised. The funds can only be used for capital projects and not to cover recurrent costs, including maintenance of facilities.

What are the effects on individuals, organisations and businesses of the use of developer charges and contributions?

Development contributions add to the cost of development in NSW, and these costs are passed on to the end purchaser. Development contributions are generally less than 2% of the end value of most developments.

What is the most appropriate way to recover the costs of new and upgraded assets?

There is an argument that the costs of new and upgraded assets should be recovered from higher rates, because all ratepayers will benefit from the improved assets, not just those who have recently developed or purchased property in a new development (on which development contributions were levied).

3.4 Fines and other pecuniary penalties

What are the effects on individuals, businesses and organisations of fines and other pecuniary penalties and increases in them? What measures are there in place to protect against the possibility that local governments might view fines as a revenue raising instrument more than as an appropriate deterrent?

There are fines applicable in NSW (and therefore in North Sydney) to:

- parking infringements
- dog control infringements
- development and building compliance breaches
- food premises compliance breaches

Penalty infringements (fines) are only given when there has been a breach of the relevant law. Authorised officers are not able to issue fines where the law has not been broken. If fines were given inappropriately, there would be many more successful appeals to the courts. The legal system provides the framework for ensuring that policing of compliance with relevant laws is undertaken appropriately by authorized council officers.

The amount of fine for a particular breach is set by State law, not by councils.

3.5 Interest income

To what extent are local government cash reserves the result of State government imposed borrowing limits?

It is the rate-pegging legislation that has a far greater impact on the need to maintain cash reserves than are imposed borrowing limits.

What are some of the implications of these limits and how do they affect capacity of local governments to raise revenues?

If rate-pegging did not exist, then revenues could be more efficiently allocated (matched) over the long-term to the expenditure.

4. Factors influencing expenditure and revenue raising

To what extent is there scope for local governments to reduce the unit costs of their operations? If so, how might they most effectively reduce their costs? What effect would such cost reductions have upon their revenue raising requirements?

Councils need to be efficient in the delivery of services. In NSW, the rate-pegging regime and the limitations on revenue-raising capacity have meant that generally Councils have been forced to be efficient in their operations. Councils could reduce costs by cutting out the “value-added” components of service delivery, such as the customer service interface, the community-building and cultural services. However these components are generally well appreciated by residents and ratepayers, and their loss would not be seen as an improvement of council service delivery.

How and to what extent have structural reforms, such as boundary changes of local governments and service sharing arrangements, affected operational efficiency?

Structural reforms may achieve some improvements in operational efficiency by reducing administration. However such changes do not reduce the community’s demand for service delivery nor reduce infrastructure management and maintenance requirements. Where structural reform has taken place, the evidence is that the demand for services remains the same and any administrative savings are short-lived.

4.2 Service levels and pricing

What guidelines and requirements are available to assist local governments to determine the appropriate range and standard of services, to measure and allocate their costs, to determine their revenue requirements, and to set rates, and fees and charges, accordingly?

The Councils Charter in the *NSW Local Government Act 1993* sets out the expectations of local government. The Charter is quite broad-ranging leaving open to NSW councils to a large extent the choice of services that they provide. There are some services that councils are required to provide, and this includes waste management services, and the maintenance of local infrastructure, in particular roads, and environmental control. Other services councils can choose to provide, such as the range of community services. The provision of services is in response to demand by the community.

There are no guidelines in NSW to assist local government to determine the range and standard of services. This is the responsibility of each elected Council.

4.3 Financial and asset management skills

What effect might the lack of financial and asset management skills of managers and lack of appreciation of the relevant issues by councillors have on the revenue raising capacity and effort of local governments?

Good financial and asset management skills are needed in local government to assess the infrastructure funding needs, to develop long-term financial plans and to advise Councillors on the ability of councils to fund service delivery and infrastructure management and maintenance in the long-term. Without such skills, councils are left making decisions on the basis on inadequate information and planning. Revenue raising opportunities could be missed and future income streams lost.

To what extent do local governments find difficulty in attracting and retaining suitably qualified experts in financial and asset management? What types of local governments experience the greatest difficulties?

There is a lot of competition in local government to attract suitable expertise in asset and financial management. This is an area of skill shortage. Councils in metropolitan areas generally are able to find suitable expertise so long as they pay the right price. However rural and regional councils have far more difficulty in attracting suitable and qualified people in an environment of skill shortage. The reality is that people with financial and assert management skills are attracted to the private sector, where remuneration is higher.

4.4 Incentive effects of grants and subsidies

What grants and subsidies are provided to local government by State and Territory governments? What is the value for each category of grant? Are there any terms and conditions attached to these grants? Do these terms and conditions distort the incentives of local governments to raise their own revenue? If so, how and why?

Grants from the State Government only represent a small proportion of the overall revenue of North Sydney Council. Any grants received do not cover the full cost of undertaking the works or projects. The level of grant funding from State Government for some service areas is declining, eg. Library grants, road safety grants. This is an area of significant cost-shifting, with programs initially funded by the State Government, and then over time, when the community expectation is that the service will continue to be provided, the State grant funds decrease or cease altogether. Grants are received for, for example:

Annually

- library services (represents 5% of cost of providing service, and decreasing)
- road safety (represents about 50% of cost, with the State grant percentage decreasing)
- regional roads maintenance (State grant is 30% of cost to maintain these classified roads)

Upon successful submission

- environmental projects (energy efficiency; water savings)
- green space (green space and access to Sydney Harbour)

Given that the grants from the State Government represent such a small proportion of Council's revenue and do not cover the full cost of delivering projects, or undertaking ongoing maintenance, they in no way provide a disincentive to councils to raise their own revenue.

What grants and subsidies are provided by the Australian Government? What is the value of each category of grant? Are there any terms and conditions attached to these grants? Do these terms and conditions distort the incentives of local governments to raise their own revenue? If so, how and why?

North Sydney Council receives the minimum annual Financial Assistance Grant and Roads Grant from the Commonwealth, which constitutes about 1.6% of Council revenue. The Roads portion of the FAG grant is about 16% of local road expenditure. These grants do not provide any disincentive to raising other revenue.