REPORT ON PROCEEDINGS BEFORE

STANDING COMMITTEE ON STATE DEVELOPMENT

INQUIRY INTO THE ABILITY OF LOCAL GOVERNMENTS TO FUND INFRASTRUCTURE AND SERVICES

CORRECTED

At Jubilee Room, Parliament House, Sydney on Friday 17 May 2024

The Committee met at 9:15 am

PRESENT

The Hon. Emily Suvaal (Chair)

The Hon. Mark Buttigieg
Dr Amanda Cohn
The Hon. Wes Fang
The Hon. Stephen Lawrence

PRESENT VIA VIDEOCONFERENCE

The Hon. Scott Farlow
The Hon. Emma Hurst

The CHAIR: Welcome to the first hearing of the Committee's inquiry into the ability of local governments to fund infrastructure and services. I acknowledge the Gadigal people of the Eora nation, the traditional custodians of the lands on which we are meeting today. I pay my respects to Elders, past and present, and celebrate the diversity of Aboriginal peoples and their ongoing cultures and connections to the lands and waters of New South Wales. I also acknowledge and pay my respects to any Aboriginal and Torres Strait Islander people joining us today.

My name is Emily Suvaal, and I am the Chair of this Committee. I ask everyone in the room to turn their mobile phones to silent. Parliamentary privilege applies to witnesses in relation to the evidence they give today. However, it does not apply to what witnesses say outside of the hearing. I urge witnesses to be careful about making comments to the media or to others after completing their evidence. In addition, the Legislative Council has adopted rules to provide procedural fairness for inquiry participants. I encourage Committee members and witnesses to be mindful of these procedures.

Ms CARMEL DONNELLY, PSM, Chair, Independent Pricing and Regulatory Tribunal, affirmed and examined

Mr BEN STRATE, Acting Chief Executive Officer, Independent Pricing and Regulatory Tribunal, affirmed and examined

Ms FIONA TOWERS, Executive Director, Pricing and Policy, Independent Pricing and Regulatory Tribunal, affirmed and examined

The CHAIR: Would you like to start by making a short opening statement?

CARMEL DONNELLY: Thank you, Chair. I will just make a few opening remarks and also begin by acknowledging the traditional custodians of the lands we now call New South Wales. We pay our respects to Elders, past and present, and to all Aboriginal colleagues and stakeholders. Thank you very much for the opportunity to appear at this important inquiry. My opening remarks are going to be about some tribunal observations that have been made in recent work relevant to the terms of reference. Last year IPART recommended that the Government commission an independent review of council financial models, and that arose from consultation and analysis we did with some of our reviews last year.

We have a standing set of functions delegated from Executive Government about setting the rate peg, assessing special variations and making decisions on those when councils seek an increase in their rates revenue above the rate peg, and also in assessing contributions plans. But last year we also reviewed the methodology for the rate peg. Through all of that work, we had around 2,000 submissions. We also commissioned some independent research and surveys with ratepayers, and a range of broader issues were raised. The tribunal was convinced that any improvements to the rate peg or to the special variation process were not going to be enough to address those broader issues, and that is why we suggested a broader review was needed. I will quickly give you a summary of some of the other observations, but I am happy to take questions shortly.

Some of the feedback, very clearly, from councils was about problems with financial sustainability. There were also very strong views from a number of councils about not supporting the existence of the rate peg and the need for improvement for the special variation process. We acknowledge that, but that was outside of our terms of reference and we were not doing a broader review at that time. Ratepayers very much stressed their concerns about affordability and service quality, roads came up a lot, and also council financial management. It does seem that people have an awareness of local issues, going back through some time, that they have been concerned about.

We have published that consultation, and there is quite a lot of information I can point you to. Financial sustainability was raised so frequently that we undertook some high-level analysis from available information and identified that, certainly, it appears some councils—not all, but some councils—are facing financial sustainability challenges, and I am happy to talk more about that. We noted the diversity in councils and the particular challenges for rural and regional councils, and I am happy to talk a little bit more about that. While we have implemented some improvements to the rate peg methodology—and we still have work to do in that space—we, at the end of the review, felt it wasn't enough to address the broader issues. We did make some specific suggestions in our report for things that could be considered in the review, which I am happy to talk about as well. I think I will probably leave it there. I'm happy to elaborate further and take questions.

The CHAIR: The Committee has adopted to allow free-flowing questions today. Does anyone have any questions?

Dr AMANDA COHN: I have plenty.

The Hon. WES FANG: So do I. I just do not want to hog all of the time. I am sure Mr Farlow will have some as well, online.

Dr AMANDA COHN: I wanted to start off by asking a clarifying question. You have listed, on average, the breakdown of income for councils across the State. In that it was listed that, on average, 31 per cent of income was from grants and contributions. Have you done any work to break that down further so we can get an understanding of what proportion of those grants is tied to specific projects or KPIs for specific departments versus how much of that, for example, is Federal, untied Financial Assistance Grants?

CARMEL DONNELLY: I think that's certainly a very good question, and it would be extremely pertinent to this review. Yes, we provided some information about that. I'm not sure if we have a further breakdown. Ms Towers might know.

FIONA TOWERS: I don't think we have any further breakdown. We can give it to you by metropolitan, rural and regional, but I don't think we have that breakdown—

CARMEL DONNELLY: Of the source of revenue.

FIONA TOWERS: —of the source and what it's tied to.

Dr AMANDA COHN: I will try to find that out from some of our other witnesses during this inquiry. My second question was about developer contributions, which you have mentioned in detail in your written submission. We are obviously in a paradigm at the moment where we have a housing crisis and massive increases in land value. Do you think that the local government sector is adequately capturing developer contributions to fund infrastructure?

CARMEL DONNELLY: Certainly we've had some issues raised with us over the same period of time about contributions plans that are allowed under section 7.11, which are the ones that we will assess. The issues range from the fact that it does seem that the scope of the numbers that we have to assess, which is an oversight over the councils, is increasing because of the scope creep. There are also some concerns that are being raised about the fact that some types of infrastructure are not able to be funded out of developer contributions—so, community facilities.

We've recently raised an issue with the Government about the fact that we've had a recent council that—this is no particular criticism of them, because they've reviewed their plans. But in an environment where costs have increased rapidly or circumstances have changed, it's possible for contributions plans to be in place for some years with regular review, but there is a forecasting risk and there is a financing risk inherent in that. If costs increase, we've pointed out there is a lack of clarity about who needs to pay for that increase in costs. If it's councils, then they need to have clarity that that's them. If it's ratepayers, that's an extra cost at a time of cost-of-living. If it's developers, there can be unintended consequences potentially for developer contributions increasing at a time when you want to see new housing being built. We have raised that issue. We were requesting that there be some clarification to the guidelines for contributions plans in that space.

Dr AMANDA COHN: Some councils have raised—I think you mentioned—scope creep. I know you have to assess contributions plans—I think it's \$20,000 and \$30,000, off the top of my head. I understand there is an issue with that benchmark perhaps not being the right number anymore but, beyond that, is there also an issue with the quantum of the contributions caused by the same scope creep?

CARMEL DONNELLY: I think those thresholds that you mentioned have been in place since 2010, albeit there has been a revised ministerial direction that there are some exceptions to that. It's a little bit complicated and it's probably a question for the Department of Planning, Housing and Infrastructure in terms of the detail. I gave some thought about this and I'm not sure that we know how many councils are impacted by those thresholds. But it does seem possible that more plans are either coming into needing our assessment process than was intended—and I will say something about that—or that, where councils decide that they don't wish to go through the assessment of contribution plans and through that process, then effectively that cap is giving them less developer contribution than they might otherwise have had.

We are in the process now—we have consulted with councils and we are very grateful for their input about how we can improve our process because it can be quite lengthy, and we go into a lot of detail. When I first took up the role of chair, there were on the table some reforms that were being proposed that would mean that IPART's role would be more focused on dispute resolution and the more complex and perhaps the more costly developer contributions, and so our method probably suits that. Now that we seem to be facing some increased volume of them coming in, we are looking to have a new approach, which we will be consulting on soon, which would have a more streamlined approach.

Dr AMANDA COHN: In your written submission, you listed a number of issues that we might consider. One of them was better targeting the eligibility criteria for rate exemptions so that ratepayers aren't subsidising the cost of providing council services where that's not justified on efficiency and equity grounds. Those of us that have been councillors probably know some of these examples from our own areas. Could you elaborate further for the Committee on some examples of those issues or what those categories are?

CARMEL DONNELLY: We actually did a report in 2016 where we looked at local government rating. One of the things that we recommended then was that there be a better focusing and a better targeting of exemptions. The suggestion that the tribunal made at that time was to target it on the use of the land rather than the type of owner. I'm not here to defend the past. I acknowledge that time has gone by and circumstances have changed, but that is on the table. The interesting thing is that it has come up during our more recent consultation as still an issue. It has come up from both councils who experience having quite a bit of territory that might be rates exempt. They may have a lot of forests et cetera, but they still need to maintain roads and so on around that. Also, ratepayers who I have read in submissions will say, "I'm a pensioner but I'm living in this circumstance and yet the people across the road in a different kind of residential environment have some exemptions." At least people believe that. There is a fairness right down to the individual issue. We don't necessarily have the answers. We certainly think, though, that it is an important issue that could be due for some evaluation.

Dr AMANDA COHN: I am still going through this list. The next one was using capital improved value to set the variable component of rates. I know we've got the Valuer General later today so we're probably going to discuss this in depth, but could you outline some of the work that you've already done on that?

CARMEL DONNELLY: Yes. In that same review in 2016, we suggested that the legislation—so it would be the Parliament and the Government considering whether the ad valorem component of rates should be based on the capital improved value and not the unimproved value. Some of the things that have been raised and continue to be raised with this issue are that, in areas where perhaps there is a lot of high-rise development, the unimproved value of the land that is used to calculate rates is really divided amongst many apartment owners. You can have an expansion population and a number of people paying relatively low rates but, to some extent, you're accessing the same services. I know that there are other arguments and that this is not an area where there's total agreement, but it is one that has continued to come up. We originally had thought that it would be appropriate for metro but perhaps rural and regional councils could have a choice as to which basis they would use and give them more flexibility. Once again, I'm not here to bring out all of the things that IPART has ever said and go through them, but the things that we've mentioned in our submission are things that are still being raised with us.

Dr AMANDA COHN: I was interested in the differences in rate peg methodology, which I think will come up substantially during this inquiry. I'm interested in your LGCI metric, noting that other jurisdictions either don't have a rate peg or are using different ways of calculating it. I read in the submission that you use the "metro", "rural" and "regional" categories to account for differences in spending between councils. Do you think that just having those three regional categories adequately captures the diversity of councils? I'm thinking off the top of my head of places like Uralla, which runs an aged-care facility. There might be substantial differences within those categories in terms of the service offering that would impact the costs.

CARMEL DONNELLY: That's a very important question. There are probably quite a few comments that I will make about that, if you don't mind me going back in history a little bit. I know it's relevant to the terms of reference. Before IPART was delegated the authority to set the rate peg, the methodology wasn't terribly clear. That's my assessment based on what I've been able to see. It did, however, track Consumer Price Index—CPI—reasonably. In the years before we took the role on, it became clear that CPI is not necessarily appropriate for councils. I would say that it's not appropriate because it's a basket of goods for a household. If you look at it, about half of that are things like what you pay for a home, food and beverage for a household, and household furnishings and those sorts of things, whereas councils are spending money on roads and bridges.

The Local Government Cost Index was something that IPART developed as part of taking over setting the rate peg, and it is a different basket of goods that's meant to reflect the costs that councils need to meet and track changes in inflation there. There were some weaknesses in that. It was one size fits all, with one rate peg number. Until 2021 that's what the legislation required. We have now moved away from the Local Government Cost Index because we based it on Australian Bureau of Statistics data, which was very accurate in terms of being factual actuals and not a forecast, but there was a time lag. When we came to that year where, coming out of COVID, inflation increased, this time lag, we acknowledge, created problems for councils because the volatility wasn't catered for in the rate peg.

We have now moved to more forward looking, with some more forecasts. One element of the formula is a forecast based on the primary producer index for roads and construction, so we're getting more and more focused. Our methodology now does allow for the three groups that you mentioned of metro, rural and regional but, more than that, we now have more factors that are down to the individual council. We absolutely recognise the diversity. I think you made a very important point as part of your question that there are rural councils that very clearly face different challenges to metropolitan. One of the things that we've observed—and there are probably a couple here you will be interested in, but one definitely is that there can be market failure and there can be withdrawal of services from other levels of government.

There can be a situation where council is the safety net and provides services that councils in metropolitan areas would not need to because the services are available and the private sector has stepped in. We did a couple of reviews of child care over the last year. We found certainly that when you come to communities that are more vulnerable and that are more isolated, the private sector is not providing early childhood education and care services; it's not-for-profits and councils. So that is a good example. I might leave it there. I think there was another point, but I've probably gone on for a bit long.

The Hon. WES FANG: In your submission I noted that there were some interesting aspects around the survey of ratepayers that you undertook. I thought I would drill down a little bit more on that. Ultimately, councils deliver services to ratepayers, and it's often said that they're the closest level of government to the people, so the detailed work you have done in relation to surveying those ratepayers is crucial to understanding what they expect from their councils as part of this inquiry. I note that you indicated in your opening statement that there were concerns around some of the services that are provided, and you focused on roads in particular in that opening statement. The other term that's come up today is "mission creep". Can you provide a little bit more clarity around those concerns that ratepayers had in relation to the delivery of services from council?

CARMEL DONNELLY: Yes. There's quite a bit in that. In our review of the rate peg in our report, we have a special appendix on the feedback that we got from stakeholders. So that's an interesting resource. We've published the work that ORIMA did in undertaking this survey. We also have another appendix on financial sustainability. We heard from ratepayers that many appreciate council services—and, in fact, really rely on them—and they don't want services cut. But there were questions that people will raise in our consultation about the expenditure on services they don't use. There's certainly a desire for very good consultation on what the priorities are.

I'm going to come in a minute to your question about the issue about what should the money be spent on and what ratepayers think, but there are two points I want to make first. It's clear to us that there are some people who do not have the capacity to pay increased rates. In fact, at a community level there are communities that have limited capacity to pay increased rates and yet they rely on these services. When we do our work, there's a very difficult balance. If the services that are needed can only be funded by rates, does that mean that if there is low capacity to pay in a community, the council is inevitably going to be very challenged financially, or is there another solution there?

The other thing that's found in our research—and I won't go into it in great detail—was ORIMA's report. We didn't edit it at all; they did the work. On page 29 of their integrated report, they've summarised what ratepayers think about rates increases. There are diverse views, but there are majorities of people who say, "Look, we'd prefer that each council has its own ability to set its rates and it's not one size fits all. We would prefer that they're approved to have some smaller rate increases, and then the bigger ones require some scrutiny and consultation." So they're some of the things the community has said to us. The other thing is that ratepayers are often concerned that the special variations undermine the protections of the rate peg as they see it. But even the rate peg, which is really a cap on the total revenue that can be collected from rates and similar sources, which is about a third of council's income on average, doesn't translate into what the increase is for a person's individual rates. One of the things that's been raised with us is: Is the rate peg really working for individuals?

In terms of the final part of your question about what people expect the services for, there's quite an interesting discussion that has gone on over the many years of reviews into financial sustainability and local government of how do you tackle the fact that they're diverse? They are elected councillors, they've got diverse communities and they've got to meet their needs, and the services vary from place to place. So comparisons are difficult, as well as assessing what is the reasonable level of funding for, if you like, the core role? Some ratepayers clearly have a more minimalist view where they think, "You're looking after the property and the roads. Do that well. Why are you spending money on a museum when the roads are no good?" There's that sense that comes through qualitatively. This is from submissions.

There are other councils that have communities with higher socio-economic status and more capacity to pay who can go for a more enhanced level, and they may be much more advocating for the growth of their economy and providing additional facilities. You assume that's with the agreement of their community. But, as I mentioned, the rural and regional councils often have a kind of safety net role. It comes through the consultation that we don't quite yet have a common language about what's the core role that councils must have reasonable level of funding for. If they choose with their community to enhance, they can fund that in a range of ways, including, potentially, special variations and added rates, but other fees and charges. If they have a gap in terms of the safety nets for the additional services—the sorts of things that Dr Cohn mentioned—or, in fact, there's a low capacity to pay, then where do other sources of funding come in to assist?

The Hon. WES FANG: Normally what I would do when I'm approaching a topic like this is I would tease out a number of theories by way of questions and then come to where I think the evidence points to. I'm going to do it in reverse now, because I know we're limited on time with you. I could talk to you all day about these issues, because I think it's fascinating. In my travels across the State I've been to some of the really rural areas, where there's a sparse population and a very low ratepayer base in very low-income areas, and engaged with those ratepayers and councils. Then you look at somewhere like the City of Sydney, where they've got a very dense population with high income and probably a much more wealthy ratepayer base.

If you look at the operation of those two councils, ultimately what we're talking about is the funding of infrastructure and services here. How do the two different groups believe their councils operate? You touched on it briefly by saying that rural and regional councils have a much more safety net role. Has that come through in the feedback, that in effect they typically do the roads, rates and rubbish components very well and that the services that they provide, like libraries and parks et cetera, they manage to do it generally within their pot? They're not doing the advocacy and political aspects as much as, say, some of the more wealthy councils. Was the happiness reference of the ratepayers in rural and regional indicating to you higher than somewhere like the City of Sydney, where the ratepayers may look to have their councils be politically and socially active in their services?

CARMEL DONNELLY: There are a few observations I can make from our work. Although, I have to say, this has been incidental to other work. For instance, I went to Broken Hill as we were starting to think about this sort of work to review water pricing. I met with the mayor and a number of the councillors there. From time to time I will go out and visit councils. It makes sense to me—with the challenges of somewhere like Broken Hill, with the isolation, attracting skills, the issues that are quite unique to Broken Hill—that there would be many parts of New South Wales in the more rural and regional areas that have very different challenges to the metropolitan. When we met with the metropolitan councils, yes, they may well have population pockets with higher socio-economic status, but also diversity within and people who have significant needs for support in terms of their community services and so on. They often have growth and the challenges that come with growth in population.

The regional councils are more likely to have those difficulties with attracting capability and workforce, and not just the councils but the businesses in town. They have extensive road networks to maintain and that has come through very clearly, and particularly with all of the fires, floods et cetera, the damage. I live in a small town—I don't live in Sydney—and I know this from my own experience, and certainly, the challenge is enormous there. They often will have a high proportion of people who are pensioners, and we have before recommended that the pensioner discounts be evaluated. We've recommended that several times. Some of them have a decreasing population and a loss of industries, and lower capacity to raise revenue from other sources.

And then, back to one of the earlier points I think that you made, these councils may have had, historically, very low rates and they are very aware of the challenges of their community and loath to apply for increases. The special variations process, we know, can be challenging and so they might put that off until they really have to. One of the problems that we've observed with the rate peg is that, it having been put in place in the 70s, increasing by a percentage that for most of its life has been one size fits all, those that have started from a higher point have had increases on that higher base and those that have had a historically low rate base, it's like, are they moving further and further apart?

The Hon. WES FANG: It's exacerbating the problem.

CARMEL DONNELLY: It's exacerbating the problem. So what we have suggested is that part of what needs to be considered is a way to have a reset. It's not the only space where we've said there needs to be a reset. Cost shifting has come up quite a lot, and one element of what we think about as cost shifting is where councils could raise other revenue from statutory fees and charges but they haven't been indexed. Now, it wouldn't be enough, in my view, to just index them to start from now, from the low base. There needs to be a consideration of what's the efficient cost, what's the service that the local government is providing that should be not funded and subsidised by ratepayers but should be funded from fees—a reset of that as well.

The Hon. WES FANG: I guess the crux of all that is how do you do that in a way that doesn't create a price shock for, in particular, those ratepayers who are the most vulnerable, who rely on the base services—the roads, rates and rubbish—that these councils deliver? And how do you create an equity model that's going to apply across the whole State? Is it possible at all or is this going to be work that's not done in a financial year, as in, it can't be imposed over a financial year? Is it something that needs to be imposed over a forward period of, say, five, 10, 20 years, so that you haven't got this massive price shock for people as they move into the adjusted period?

CARMEL DONNELLY: Look, at one level, I think—I don't have the answer to that, and we haven't done this work. But I think it is a very good question to be saying, "Does there need to be a price shock?" If you've got more clarity about what are the core services that need to be funded, and there are communities that don't have the capacity to pay, what are the other alternatives? I use the example of if you're in a village where 90 houses burn down and no-one has anything, you don't expect those people to pay through their rates for the recovery, because you know they've already been hit hard.

The Hon. WES FANG: Some councils might though.

CARMEL DONNELLY: They might, and that's where we look at special variations and we'll look at is the impact reasonable? But is there a need for another source of funding to top-up some councils so that they are able to deliver services with a low rate base or a low capacity to pay? That's a question I don't have the answer to. The other thing, your question about longer price paths—we regulate and have roles in energy, transport, water, in a range of other areas, and we look at pricing. Where you don't want to encourage short-term thinking, then a longer price path, thinking about the longer term outcomes that can't be achieved year by year by year, is another model. I have turned my mind to this and we did, in 2009, recommend that there might be some pathways for some councils to get onto a longer term path, perhaps even not have the rate peg if they met some performance and financial management criteria. I think it would need legislative change. That's my opinion. I'm not a constitutional lawyer by any means, but I think it's framed at the moment to be an annual amount. So it's a policy question, ultimately.

The CHAIR: I might start with a few questions about the issue of financial sustainability. What differentiates a council that has to seek a special rate variation from a council that doesn't, in your view?

CARMEL DONNELLY: Look, they are diverse. There will be, usually, in each year, a council that is looking for something for a special purpose that they have generally good support from their community for—it's quite focused; it's quite small. They're not facing fundamental financial sustainability issues necessarily, and there aren't questions about financial management. It's about a choice. So there have been councils that have applied for an increase, knowing that it's an increase in the total income that they can raise but it's going to translate into higher rates to cover a particular purpose from a particular industry. Or, as for one of the ones this year, Randwick council has had an environmental levy in place through special rate variations over 20 years, and they were seeking to just hold it in place permanently to continue to fund environmental action. So that's one case. At the other extreme we will see councils where it is clear to us that there are financial sustainability issues, and that's probably the majority.

The CHAIR: So the majority of councils? I suppose—

CARMEL DONNELLY: Not to say that—no. They're required to show us that there is a financial need, and we can look at a number of measures that would show that they're not meeting benchmarks or they don't have enough unrestricted cash that they can use for the services they need to pay for—something like that.

The CHAIR: Are there any other insights that process gives you into the finances of a council? You talked a bit about—

CARMEL DONNELLY: We've certainly heard from councils. I'm really grateful that some of them came to workshops and gave us some very straightforward feedback that it's a costly, burdensome process for them, that it is quite complex and, more than that, there is a high degree of contentiousness and that can be, obviously, within the elected councillors. They've got a difficult decision to make and there are diverse views in the community as well. We've heard that there are councils that would be very reluctant to apply for a special rates variation, and they may not end up doing that until they do have quite critical financial need.

The CHAIR: What more is needed, would you say?

CARMEL DONNELLY: We did suggest that there be a look at what could be improved about the special rates variation process. Sometimes ratepayers think that we're really doing a very forensic audit and going over all the books. We're not. It's a high-level assessment against criteria set by the Office of Local Government. We used to require councils to notify us in November, but we no longer mandate that. We get their applications in February and we give their decisions in May, usually. We think that we could look at the timing and if we can improve that. We could look at if we can simplify to go to the complexity to reduce the burden on councils.

One of the suggestions we've canvassed is could we allow joint applications if there are a number of councils that are facing similar issues? They may be members of a group or they may be neighbouring councils and perhaps they could work together to put a case up jointly. Another suggestion that has been canvassed is, for those councils that have got the historically low rate base and need a reset, are there particular measures that could trigger that they need to come and apply for a special variation to look at sustainability, rather than having the councillors themselves face that contentious situation?

The CHAIR: I just wondered if I could ask a few questions about the rate peg generally now. Is it fair to say that the rate peg methodology is designed to keep rates per capita, effectively, constant, in real terms?

CARMEL DONNELLY: I think that it's fair to say that it is doing that better now since 2022 when we introduced a population factor. The aim was to allow the total amount of revenue that a council can collect from rates to increase as the population increased, which would hold it steady per capita. But we would acknowledge that there were many years where the rate peg did not do that before that population factor was introduced. In fact, we now have a core rate peg that we deliver—it's still individual for each council—and then there's an allowance on top for population growth. We would not have been able to do that before the legislation changed in 2021.

The CHAIR: How much growth in council revenue per capita has the rate peg methodology allowed for over the last 10 years, would you say?

CARMEL DONNELLY: I am sure we have the answer to that. It might be one that I take on notice and give you some data.

The CHAIR: Do you have a view also about how much council costs per capita have grown over the same time period?

CARMEL DONNELLY: I think that's a very important question. I wouldn't say that we know, as a tribunal, because we haven't had to do this kind of broader review. What I would say, though, is that there is evidence that the cost shifting exists. Some of the things that have been raised with us—as you are aware, there are new services that local government needs to deliver and then there's no additional funding. We now have a special adjustment factor in the rate peg that we're going to work with the reference group and see whether or not we can take that into account. There's still a question about whether it should be paid for by rates—whatever that service is—or something else.

Some of the other sorts of areas where the funding has decreased is another part of the cost shifting. But I think the big one is: Has the role of local government expanded? Sometimes that has happened in consultation with the community and that's what the community wants. Sometimes it would probably have come under the umbrella of cost shifting, additional revenue-collecting functions, or through government policy or commercial decisions or, as we talked about before, other service providers leaving a rural or regional area or town and council needing to step in.

The CHAIR: In your view, are the special rate variations necessary to keep councils functioning?

CARMEL DONNELLY: I can answer that in two ways. On one level, if we've got a rate peg, then I can understand the intention that there needs to be another avenue for councils to come and seek additional revenue when there has been a change that hasn't been addressed in the rate peg. I would support that avenue being there. That's an answer of yes, but in context.

The CHAIR: I might shift now to ask some questions about what the alternatives may be to address the financial sustainability issues facing councils. In your view, do councils spend the money they receive wisely?

CARMEL DONNELLY: It's not something that we've actually examined. As I said to you before, when we consult on special rates variations, we often get quite a bit of local information which would show that ratepayers question that.

The Hon. WES FANG: I deliberately didn't ask that question because I thought it was too subjective.

CARMEL DONNELLY: It is subjective. It hasn't been our role. We don't audit and we don't go in and examine that. We don't have that sort of information. We have very defined functions and the Office of Local Government obviously has other functions. I'm sure the Office of Local Government would be able to give you some examples of some excellent work and we do hear from people that they appreciate the services. But it's probably a question for others.

The CHAIR: Should the rate peg change, what assurances or schemes could be put in place to make sure that councils charge rates that are reasonable?

CARMEL DONNELLY: Alternatives to the rate peg?

The CHAIR: Yes.

CARMEL DONNELLY: Again, I need to say that the tribunal doesn't have views on this because we haven't done this work; you're doing this work. One thing I would say is that we certainly hear from ratepayers that they don't want bill shock. Something that is a pact with ratepayers about more manageable increases could be something to be considered. Ultimately, the councillors are elected councillors and they have a job to do and they're accountable to their population. It's possible that good transparency of information would help their community to hold them accountable.

We haven't looked at the alternatives. We've really got to the point of calling out that the problem is bigger than the rate peg and it's bigger than special variations. I would go back to that 2009 report, where we suggested that there might be different pathways for different councils, but mindful of the fact that the councils that might be best able to demonstrate very healthy financial management might be the councils that aren't facing the disadvantages of rural and regional communities and have the historically low rate base, and floods and droughts and all of that. It's a bigger picture.

The CHAIR: Talking about the special rate variation process again, given that you have insights into councils' finances through this process, it would seem that some councils inevitably turn to the SRV process to fund recurrent expenditure, given enough time. How do you balance the high rates of SRV uptake—because there is a high rate of SRV uptake—to cover current expenditure, with the idea that the rate peg methodology is supposed to accurately capture costs?

CARMEL DONNELLY: It captures costs from the base where you are now. It doesn't tackle that historic low rate base. I believe it was contemplated in the legislation and the provisions that allow for the rate peg—and also allow for the special variation—that, of course, there would be circumstances that occur and changes in the community that would mean that there needed to be a step change. I have heard the view that if the rate peg was much larger, that would give councils more flexibility for that step change. But I've also heard concerns from ratepayers about that situation. The ORIMA findings that I pointed to a few minutes ago do point to they prefer to say, "Yes, you can have a manageable increase but, if there's a need for something big, there needs to be some more community consultation and scrutiny." Does that answer your question?

The CHAIR: In a way, yes. I will pass to the Hon. Emma Hurst now.

The Hon. EMMA HURST: Thank you to the witnesses for joining us today. You have covered a lot around this question, but I just wanted to refer to a specific example because I'm in another inquiry where we're looking at the issue of pounds. It's certainly been raised in that inquiry by one council that the rate peg is part of the problem as to why they can't provide sufficient pound facilities. I just wanted to get a bit of an understanding about how the process of setting that rate peg actually accounts for things like pounds, where we've seen a sudden increase in the number of people who've got companion animals and we have seen a significant number of animals dumped into pounds. If the councils are saying in another inquiry that that rate peg stops them from being able to provide proper pound services because of the rate peg, I just wanted to get the other side of that.

CARMEL DONNELLY: Okay. Certainly, I think many people are not really aware of all of the services that councils provide and how important they are. Services around food safety, water, human health and also animal health and wellbeing are clearly part of those core services. The rate peg methodology, and I might see if Ms Towers wants to talk a little bit about this, is quite high level in looking at the labour costs which are an important part of the services—so what is the cost for the work force? What is the cost for assets and then what are the other costs? And we don't go into a huge amount of detail with that. But what we do have that's new is a strengthening of other adjustment factors that could come up. So if there was an increase in council services that are needed in any area—including, for instance, in animal welfare—then that could be something that the reference group that we're consulting on at the moment could raise with us.

We could say, instead of needing to have a special rates variation, we know this is something that's being seen by a number of councils. We might look ourselves at IPART, at what's the data showing us about this increase in costs, and which councils there may be a case for an adjustment that lifts it. So we are looking at something that's, in a way, halfway between the rate peg and special rates variations. It's new. We're really only just moving to implement that. But to enable knowledge about these sorts of things—and others that have been raised are cybersecurity, climate change resilience and so on.

FIONA TOWERS: That's right. I mean, I would exactly agree with what our chair said. And if it was a material cost, the new process would allow councils to put that forward and we would consider that as an adjustment mechanism. The labour costs are in the labour component and the operating costs should be in the operating component so, on average, those things are captured.

The Hon. MARK BUTTIGIEG: This is an interesting topic. If you are looking at this purely from a logical perspective, it's really just a function of the sophistication of the model, isn't it? If the model is good enough to pick up all those inputs that you've been outlining—the labour costs, recurrent costs, shocks to the particular council area, cross-subsidies because of inequities and all that sort of thing—in theory, if the model is sophisticated enough, and we've got computers and very clever people these days, isn't it just a case of, if enough investment is put into the model, then it's a fair system and councils should be allowed to increase rates in accordance with what the model spits out? Is it that too simplistic or—

CARMEL DONNELLY: I am going to give you a yes and no. I alluded before to the fact that, before 2021, we were bound that it was one number across the whole State. You can see from what we've talked about today that we're making it more forward looking. We're improving the measures. Through looking at more special adjustment factors, we could be building out a more fine-tuned model that would provide a better reflection of the increase in costs that councils need to continue to deliver those services. But it doesn't undo the historical problems of councils having started from a historic low rate base, or for that long period of time where councils were not given an increase in their revenue when their population increased. Some councils have tackled that through special rates variations, but not all, probably. We're committed to continuing to review and consult with the model. We think there'll be healthy—

The Hon. MARK BUTTIGIEG: Basically what you're saying is there's a structural adjustment that picks up the historical rate base issue and then you get the model right.

CARMEL DONNELLY: That's right, but there have been those gaps in the past that I've talked about and then, on top that, the natural disasters, the drought, the pandemic, the disruptions, economic volatility. It would be a good time to have a reset. I still think that councils will work with their communities and decide that they want to deliver a new service or do something different. If the communities are agreeing with that and the plans are all out there and there's consultation, they may want to come and say, "We need a special step increase." But some of those issues are the historical issues of it not being as fine-tuned as it could be, and we can keep working on fine-tuning it.

The Hon. EMMA HURST: I've just got one final question about the special variations. I note in your submission that the majority of those special variations were processed. However, 10 were declined. I'm not asking for any specific details about those specific 10, but I am just wondering what aspects, or what problems, would there be in that application to refuse a special variation?

CARMEL DONNELLY: We look at each one case by case. We get the applications. We publish them. We call for submissions—obviously it's expected that the council will have done its own consultation as well and we take that into account—and then we assess them against criteria that are set by the Office of Local Government. We're looking for evidence of a financial need—which doesn't mean there's financial mismanagement or sustainability, but is there a case for financial need that we can look at?

Is the impact of the rate increase reasonable on ratepayers? So we will look at affordability, we will look at—compared to similar councils, neighbouring councils—the income levels, how many people are pensioners, how many people own their own homes, a number of those factors, and the community feedback. We'll look at what productivity cost containment the council has already done and how well they consulted because we're not required to show that the community supports, but they must have been informed about the need. They must have been accurately informed about the extent—like how large those rate increases that are proposed are.

The short answer is that some councils will not meet those criteria. We'll have gone through a thorough assessment and then we will say, "No, you don't meet the criteria." We may come to the view, as the tribunal, that they might have asked for an increase that's going to go on for five years of continued increases, but they've only shown that the need is there for two. And after that their numbers will be improving, and so we may say, "We'll give it to you partially." We'd be happy to take it on notice if you would like to get a bit more information about the sorts of factors without going into detail about particular councils.

The Hon. EMMA HURST: That would be great.

The CHAIR: Thank you for your evidence today. That is all we have time for. The secretariat will contact you in relation to questions taken on notice and any supplementary questions.

(The witnesses withdrew.)

Ms SALLY DALE, Valuer General of New South Wales, affirmed and examined

Mr STEWART MCLACHLAN, Chief Executive Officer, Valuation NSW, sworn and examined

The CHAIR: Thank you to our next witnesses for joining us today. Would either of you like to start by making a short opening statement?

SALLY DALE: Yes, that would be great. Thank you, Chair and the Committee, for the opportunity to attend today. After discussion with Mr Mclachlan, we'd like to make a joint statement about our appearance today and some of the insights we may be able to provide or expand upon about the New South Wales valuation system and potential considerations should changes to how that system applies to local government be considered. As the Valuer General, my core responsibility is to oversee the New South Wales valuation system, including the valuation of almost 2.7 million parcels of land annually to a combined value of almost $2.8 trillion. With a mission of ever improving the system to ensure public trust and confidence, this is no mean feat, and I thank both Valuation NSW and former Valuer Generals for their respective operation and stewardship to date.

Relevant to today's inquiry, this system is a core pillar which underpins the rating and taxing system for local councils and the New South Wales Government. Before passing to Mr Mclachlan, it is important to note that, as an independent statutory officer, my role is clearly defined by law and as such I do not have a preference of valuation systems, and any comments that may be provided today are on the basis of informing the Committee of how the system or the changes as outlined in my letter to the Committee may work.

STEWART MCLACHLAN: With circa 200 value adders, Valuation NSW is the agency established in the Department of Planning, Housing and Infrastructure to support the Valuer General's functions and operate the New South Wales valuation system on a day-to-day basis. In addition to those core functions, Valuation NSW, importantly, undertakes market research to ensure the latest technology and emerging trends in the valuation industry or across other jurisdictions are known and analysed. This includes how local government contribution plans may be underpinned or the different types of valuation systems utilised in other jurisdictions, and I note former Valuer General and/or agency submissions to previous IPART reviews on the types of systems across Australia.

Collectively, Ms Dale and I look forward to answering any questions you may have about the New South Wales valuation system and its application to the inquiry's topic as well as insights into how other systems may work, ensuring that any potential changes are underpinned by known and quantifiable advantages and disadvantages. Lastly, it would be remiss of me not to highlight that the New South Wales valuation system is ranked equal first in the world by the International Property Tax Institute and has been routinely recognised by other State jurisdictions as a leader in Australia, most notably by Queensland in a cross-jurisdictional valuation system review, circa 2012.

The CHAIR: Thank you. We might start with questions from the Hon. Wes Fang.

The Hon. WES FANG: Just noting that, obviously, we use unimproved values at the moment, and there was talk about moving to capital improved values. I am interested in the work that is required to maintain databases for one or the other. I imagine unimproved values are easier to maintain a value for because it does not require any survey work and it does not require any information in a database as to what has occurred on the land. Would that be a baseline to start the questioning?

SALLY DALE: Both systems require a database of property attributes and, obviously, surveyors are involved in surveying the land and registering deposited plans. That information as well as aerial mapping is used by Valuation NSW and our valuers. It is a good question, because capital improved values obviously include the improvements on the land, so a requirement would be to have a centralised database of what those improvements on the land would be. To my knowledge, now, we don't have a centralised database with that data. That being said, there are private operations that have data available and aerial mapping, but it is very varied—the quality of that information—especially when you're looking at regional and rural properties versus metropolitan where there's been a lot of sales and advertisements that valuers and alike can use, like floor plans and photographs of internals.

The Hon. WES FANG: In relation to the Government of the day seeking to move, through legislation, a requirement that capital improved values be used, what would you think would be a reasonable timeframe for you to create such a database that councils could then use to set rates. The other part of that is: How much would it cost for you to establish that secondary database and survey—I think you said 2.7 million plots of land that you are responsible for?

SALLY DALE: That's correct.

The Hon. WES FANG: I imagine that you have your unimproved value and your database of that, and you then have to work out 2.7 million improvements that have or have not occurred on those plots?

SALLY DALE: That's right. The timeframe—whether it would come to Valuation NSW or the Valuer General to set up that database. It may be in conjunction with another government department. But we did a review back in 2016 in relation to capital improved values, and we've recently done a further update of that review. We're thinking that it could take five years to not just get the database in place but, obviously, it would be a big change to work processes. We would have to increase our workforce, and there's also the consideration that there could potentially be a lot more objections in the first instance if we did move from land value to capital improved value.

The Hon. WES FANG: I was not even going to get to the point where they challenge.

SALLY DALE: Yes. In regard to the costs, our update of the review also looked at costings. At the midpoint range, we were looking at $282 million up to $500 million at the high end. And if you just look at the private sector and you take that as an example, in the banking and finance sector they will often get desktop valuations for cost-efficiency purposes, and a valuer will carry out a desktop. For a standard residential property, a desktop will cost between $100 and $120, and that's with a valuer sitting at a desk and looking at aerial imagery and photographs. Obviously, then, you've got to take into account that information won't be available for every single property, and there are also very complex properties when you look at commercial and industrial. In those instances, you would have to send out a valuer in the field to go and carry out an inspection. With that in mind, I think $500 million could be conservative.

STEWART MCLACHLAN: The other thing I would add to Ms Dale's answer is it's 2.7 million land values. If we move to capital improved, it's 3.6 million roughly, circa, so the job is obviously bigger.

The Hon. WES FANG: But more rateable properties so the councils might do that with glee. My last question in relation to this is have you done any modelling around the differences between, say, metropolitan areas and rural and regional? Because I imagine there would be a more detailed model that could be built around, say, the Sydney CBD area and the outer Sydney area because of databases and the like. It's going to get a lot harder as you go out to regional areas where property sizes can become quite large. Have you done any work in relation to how that would impact the difference between rateable prices in metropolitan areas versus rural/regional and whether there's a cost benefit in doing that in relation to the work that you do outside of what councils do?

SALLY DALE: We've done a model, a very broad model, that has looked at the system as a whole. Stewart might be able—

STEWART MCLACHLAN: The shorter answer is I think it's logical—some of the points you're making. But, no, we haven't taken the initial or updated piece that we've done to that level of detail on the basis that it's just to ensure that we are across what a high-level broadbrush view would be to move to the system. But obviously our role is delegated by Sally and very defined in law of what we need to do on a daily basis.

The Hon. WES FANG: The Government hasn't asked you to do any modelling work on any of this at the moment?

STEWART MCLACHLAN: At a detailed level, no, we haven't been asked to do any of those things.

The CHAIR: You talked about the cost of implementing a move to capital improved value. What are the proposed benefits of moving to such a scheme?

SALLY DALE: As I said in the opening, I've got no preference one way or the other, and there are actually pros and cons for both. I think for capital improved values, it's probably easier for people to understand because it's based on sales evidence of the whole property; and land values, there are instances, and we do get objections where people don't understand how we've gone back to a land value. That being said, we are running an education program to try and assist and help people understand that. Apart from that, both systems, as Stew mentioned in his opening statement, have been reviewed and there are benefits to both.

STEWART MCLACHLAN: I think that's fair. I would say there's a really good summary in the submission that the former Valuer General made to IPART in 2016 about advantages and disadvantages of the systems. As Sally said, understanding is the main advantage of capital improved values that we see but obviously there are significant disadvantages both from a cost perspective to stand that system up but also to maintain it. As Sal mentioned, objections, but the other part is that with capital improved values there's an ongoing maintenance cost that would need to be understood, particularly around supplementary valuations. Every time someone does a capital improvement to their property, that would trigger a new valuation, arguably, and that would obviously be quite labour intensive.

The CHAIR: Are there technological advancements that could streamline the implementation and ongoing management of a capital improved value system?

SALLY DALE: There has been a lot of talk in the market, and they have been in the market for a number of years, around AVMs, which is an automated valuation model, which is a simple linear regression—and I'm not going to go into the detail of that here—or a multiple regression.

The Hon. WES FANG: Butters will be happy. It's computer modelling. It just spits out the answer, right?

The Hon. MARK BUTTIGIEG: Otherwise known as progress.

SALLY DALE: We have run pilots internally over the last couple of years looking at automated valuation models. There are limitations with those models though. They work reasonably well in areas where properties are homogenous, so similar land and similar improvements. But where they don't work well is in areas where there are different styles of property—so take an inner city area, for example, where you may have terrace homes or properties on wide frontages. Also in areas where there may be views or varying topographies, their accuracy there is definitely not at a level that would promote public confidence. Also the same goes in regional areas where there's a lack of sales evidence. Those models aren't accurate and I would say they're unable to be used in most instances. There is talk now of using AVMs with AI but it is very much in its infancy and at this stage we're keeping a close eye on technology advances and are in touch with people in the international valuation community. But at this stage there is no system I'm aware of that would be provide the accuracy required.

The CHAIR: You mentioned being in touch with the other communities. How have other States or countries that use capital improved value systems managed that transition and ongoing costs?

SALLY DALE: I can't talk if they've transitioned from land value to capital improved value because, as I said, there are pros and cons to both. In Australia, for example, Queensland and New South Wales both use land values. The other States will use land values along with capital improved values and annual values, which is rental values. So every State in Australia, except Queensland and New South Wales, which are quite similar—but everyone's using a different system, and the same goes for overseas. I know over in the UK they actually retrospectively value the improvements back to a date in the 1990s. So everywhere around the world they're using a different system. As Stew mentioned, in 2019 New South Wales's system was ranked equal first in the world along with Hong Kong for their valuation system, which is land values.

The CHAIR: Do you see opportunities for councils to leverage more sustainable income from the property they hold?

SALLY DALE: I couldn't comment on that. Stew?

STEWART MCLACHLAN: I'd say that's not something we could comment on.

Dr AMANDA COHN: Most of my questions have already been asked by the other members of the Committee, but the review that you've done looking at the feasibility of potential implications of implementing capital improved value—I know there are a lot of stakeholders we are going to hear from who are very keen for that change to be made. Are there any other findings of that review that you haven't already been able to speak to in response to questions?

SALLY DALE: Probably strata units. The reviews that I've read, there have been comments around strata units, and I think the implication there is we value land value. When you're looking at, say, a large residential apartment building, the way it works is we actually will value the plot of land that relates to that apartment building and then that land value is apportioned to each unit as per their unit entitlement, which is on the strata plan. On a proportionate dwelling basis, I can see the argument that, yes, the proportion is low in regards to land value per dwelling. That being said, there may be the potential to look at a different rating category for strata units.

The CHAIR: Are you aware of any other States where they do that differently, for example, say, apply a volumetric method and rate into the sky, if you like?

SALLY DALE: I'd have to take that on notice. As I said, the States that use capital improved value, they would actually look at that individual unit value. But I would have to take that on notice in regard to the States that just use land value.

The Hon. WES FANG: The bit that I'm trying to get my head around in relation to if we were to move to this method would be that you've got—and I'm simplifying it down to base level—your unimproved database that you're currently using for land values. It has the annual price changes, and you can see that when you get your land value certificate. You can see the up and down, although mostly it's up, depending on which way you've got your valuation and where you live. So you can see the percentage changes per year. When you've got, say, an empty plot of land and then you build the house on it, you would see that percentage change. Do you get a percentage change for the land in that year change, and then you've got the house, which would have a separate value? Then do they change so that you've got the land value increasing and the property increasing, or does it then become one package? There are a number of ways around this model that I'm trying to get my head around to work out how much workload that creates for you, Mr Mclachlan, because ultimately it would be borne by you to ensure that the figure is—

STEWART MCLACHLAN: There are a few others with me in Valuation NSW.

The Hon. WES FANG: No. They've sent you here. Let's be honest, you're the front face of this.

STEWART MCLACHLAN: Yes.

The Hon. WES FANG: Is this really a feasible change? If it is, what time frame is going to be needed to move to that?

The CHAIR: Can I follow up with how would you implement it as well? How would you implement the shift?

SALLY DALE: Firstly I will answer your question in regard to the way land value moves with house prices. Interestingly, we provide on our website data in regard to that. We will actually track the land value against the capital improved value, and in the vast majority of cases those two lines are proportionately moving at the same level.

The Hon. WES FANG: That's interesting. I imagine that some suburbs would have your three-bedroom, cookie-cutter house and then the next suburb over might have larger plots with much bigger houses. Sometimes the capital growth in those areas tends to be—

SALLY DALE: Generally, though, when you look at the area as a whole, they will move very similarly.

The Hon. WES FANG: And implementation time frame if you were to—

The CHAIR: And how would you implement a change to capital improved value?

SALLY DALE: I'd probably pass to Stew there, because he's the one that's—

The Hon. WES FANG: He's the front face. He's the one they sent here.

STEWART MCLACHLAN: The good news is both Sal and I have discussed this, and we've also discussed it with former Valuers General of New South Wales that happen to now work within Valuation NSW. So we're very fortunate to have the expertise. It is implementable. The three key steps that we would need to take are, A, have the adequate time, and we think five years is that time period; and, B, set up the appropriate system. That's going to be the first and foremost system that we would do. We are currently building a new valuation system known as Val IQ for the Valuer General, so it would be about modifying how that is being built to ensure we can capture the appropriate data fields that we need to. C is to make sure that we have the adequate capacity in terms of our total workforce. At the moment, obviously, land values have been used for many, many years. We have a very tried and tested method that is easy to grapple with—well, not easy, but it is relatively known how it is to be grappled with year by year. It would be more about improving our overall capability but more so our capacity internally, so we would need a lot more valuers. That workforce would be needed both initially and then, ongoing, it would still be lifted on the basis that there are a lot more supplementary valuations to do.

The CHAIR: Is there a potential role councils could play in supporting the Valuer General in moving to a capital improved scheme in a more timely and efficient way?

STEWART MCLACHLAN: I think there's a role that—

SALLY DALE: If we move to capital improved values, we need a centralised database of improvements. That is potentially where councils would be able to assist us in providing that data up-front, but then ongoing providing that regular data. Then we would need to have communication when someone made improvements to a property, whether it was additions or a pool.

The CHAIR: That all goes through council anyway, doesn't it?

SALLY DALE: That's right. We would need to be notified and then we'd need to send a valuer out in the field.

The Hon. WES FANG: But they're also conflicted because they'll receive the benefit of the increase in the improved value.

The CHAIR: Could there be maybe a simplified or hybrid model that may help councils to have more categories of rateable land that they can charge for?

SALLY DALE: Again, I'm independent. If the Government decides that they want to go to a hybrid model, we are capable of providing that. They do that in other States. They've got land value, capital improved value and rental value. So, yes, it would be possible. Again, though, it's weighing up the cost benefit of moving to capital improved values: What are the advantages and what are the benefits versus the cost?

The Hon. MARK BUTTIGIEG: This is a key question. Is there someone who's given an opinion in the bureaucracy that—

The Hon. WES FANG: IPART, 2016.

The Hon. MARK BUTTIGIEG: —in the long run, if you invest up-front, obviously it's got a tail for return on the investment. But, in an ideal world, if we got that capital add value base going, with all the money that that requires to invest in that modelling, is it in the long run a better system in terms of all the issues we've raised of equity, rate base and all the rest of it?

SALLY DALE: We haven't done the modelling. You'd probably have to ask councils or the parties that are asking for capital improved value.

STEWART MCLACHLAN: The only thing I'd say is that question has been covered by Henry in 2008 or 2009 about equity and whether or not it would be a better system. In that review he does say that, from an equity standpoint, it may not be better than land values. That is my understanding.

The Hon. MARK BUTTIGIEG: This is Ken Henry?

STEWART MCLACHLAN: Henry in 2010, I think.

SALLY DALE: It was 2010 or 2009, I think.

STEWART MCLACHLAN: Somewhere between 2008 and 2010. It's Friday.

The Hon. WES FANG: It's bracketing.

SALLY DALE: I think it's page 258.

The Hon. MARK BUTTIGIEG: Thanks. I'll go straight to it.

STEWART MCLACHLAN: Okay, it's 258.

The Hon. MARK BUTTIGIEG: That's a very important answer, because there's no point going down this path if you're not sure if it's going to be the best.

STEWART MCLACHLAN: That would be a key consideration of anyone considering it. The other thing I'd say is, in terms of payback periods, we did do some modelling on how much it costs up-front and then what we think it would cost to administer year by year versus what we currently expend to administer the land value system, and there is no payback period in our calculations.

The Hon. WES FANG: This next question might send some shocks through a number of accountants. Would a move to capital improved values perhaps suggest a change in the way we calculate land tax?

SALLY DALE: That would be a decision to be made by Treasury or Revenue or another area of government.

The Hon. WES FANG: But it would make it easier for them to tax on capital improved value as opposed to—

STEWART MCLACHLAN: I don't understand, sorry.

The Hon. WES FANG: Land tax is based on the unimproved value of the land.

STEWART MCLACHLAN: Yes.

SALLY DALE: Yes.

The Hon. WES FANG: So if there was a database of capital improved value—

SALLY DALE: Obviously, the values would go up, but it would be how you would determine the tax base based on that increased value.

The Hon. WES FANG: Which is why there might be some nervous people if that happened.

The CHAIR: That is all we have time for today. Thank you so much for coming in and giving evidence. The secretariat will contact you in relation to any questions on notice.

(The witnesses withdrew.)

(Short adjournment)

Mr WILL BARTON, Vice President, Institute of Public Works Engineering Australasia, NSW and ACT, affirmed and examined

Mr JOSH DEVITT, Chief Engineer, Institute of Public Works Engineering Australasia, NSW and ACT, sworn and examined

The CHAIR: I welcome our next witnesses. Would you like to start by making a short opening statement?

WILL BARTON: Yes, I would, thank you. Before I come to my substantive opening remarks, I would like to thank the Committee for the opportunity to appear before you today. IPWEA NSW and ACT, which I'll refer to as the institute, has enjoyed many years of friendship with all parties and continues to stand by as a trusted source of advice, information and assistance in all things public works and infrastructure. The institute has now been operating in one form or another for over 100 years. We are a registered charity and our purpose is simple: to enhance the quality of life of New South Wales and ACT communities through excellence in public works and services. We represent individual engineers, technical officers, road safety officers and paraprofessionals from across the State and who primarily work within local government. We lead, inform, connect and represent the profession in the ongoing pursuit of our purpose.

We contest that the current funding framework—that is, rate pegging—has ultimately cost the community far more than it has ever saved and it is no longer fit for purpose, if indeed it ever was. Rate pegging seeks to peg revenue generated by rates—and thus costs on businesses and households within an LGA—by a percentage determined by the Independent Pricing and Regulatory Tribunal. Generally, a council's budget is driven primarily by infrastructure assets: up to 70 per cent of a regional or rural council's budget is usually dedicated to infrastructure asset spending, with that portion reducing to about 50 per cent for councils in the metropolitan area. The thing about infrastructure assets is that they're expensive. They're expensive when they're funded appropriately, but they are wildly expensive when they aren't.

It is very simply the case that rate pegging has led to decades of deferred asset expenditure, which only results in an ever-growing backlog. For roads and bridges last year, that amounted to an annual underspend of $680 million—an increase from $380 million, or thereabouts, just three years prior. But unlike many other services, asset renewal in particular becomes ever more expensive as it is deferred. What I mean by this, and by way of an example, can be illustrated by looking at the life cycle of a road, which is pertinent, given councils in New South Wales are responsible for over 80 per cent of the road network within the State. Once built, a road generally only requires minor, ongoing maintenance—clearing of drains that are designed to keep water away from the road structure, that is, the pavement; management of vegetation for the same purpose; and the added purpose of road safety et cetera.

Anywhere between eight and 15 years post-construction, the seal of the road, or the upmost layer which protects the road structure from water, will require renewal—think of this as repainting the weatherboards or the roof of your house—and this maintains the protection of the pavement sub-structure. While this varies considerably in cost across the State, it is safe to say that most treatments cost between $5 a square metre and $20 a square metre. Delay this work and allow moisture to penetrate the pavement or the underlying sub-grades and those costs rapidly escalate to anything between $50 and $250 a square metre—a tenfold increase. That is just the cost of the repairs. It does not consider the increased costs of maintenance to fill the growing number of potholes, the cost to the economy of productivity losses, the cost to the individual of increased vehicle maintenance and damage, nor the increased risk of crashes.

The pothole crisis of 2022-23 had its roots in rate pegging. Certainly, it was the wet weather which was the ultimate stressor that resulted in the large-scale failure of the transport network that is our road network, but that stressor would not have had anywhere near the impact had we in place a sound road network. Considering the whole of life, the most cost-effective way of delivering infrastructure assets is to fund renewals in particular when they are required and when they fall due. Ultimately, we see these higher costs funded. Every year we see special rate variations approved, leading to significant increases in rate income across a short number of years. But the costs I've already mentioned, those largely avoidable costs, have already been incurred. We also see—and, I will add, we are very grateful for—grant programs being rolled out to plug the gaps created by rate pegging. Fixing Country Roads, Fixing Country Bridges and the $500 million pothole fund last year are but some examples.

These are very real acknowledgements that the current funding model, that rate peg, is failing our communities and supplementary funding is required to maintain our assets. As grateful as we are for these, there is no denying that they simply serve as a sugar hit and, just as it is in the human body, a sugar hit in these circumstances leads to inefficiencies, waste and decay. It prevents us from planning long term for our workforce. It sends us into a scurry, competing with each other for skilled staff and contractors; it often inflates the market, allowing those contractors who have been able to hold on during the tight times to command a premium when demand outstrips supply; and it does nothing for those that have seen the work dry up between these sugar hits and have had to close their doors. Such grant programs are also geared toward the new, the upgraded, the sexier projects ripe for the ribbon cutting—noting the three that I've already mentioned are the exceptions.

These grants fail to allow for the ongoing, recurrent costs which come with such projects. Once the politicians and media depart, rate pegging means that our members must cut even further into already insufficient budgets to try and stretch an impossibly small balloon over an impossibly large elephant. I could go on—sustainability, skills pipeline, resilience and betterment, high-capacity networks to support the growing freight task—but in the interests of time, I won't. In closing this opening remark, our first priority is to seek a funding model for local government which provides for greater certainty and continuity of funding, which will allow our members to undertake the long-term planning needed for assets that typically last between 20 and 100 years and upon which every individual in this State is reliant on to lead a safe and quality life. We are here today, standing by, ready and willing to assist with that task.

Dr AMANDA COHN: Thank you so much for being here. I first wanted to pick up on your example of the life cycle of a road, which is a fantastic illustration. You were describing the unintended consequence of the rate peg. I'm wondering whether it goes further than that and it's not just an unintended consequence: it's, fundamentally, the rate peg not fulfilling its purpose. I'm going to quote from a witness submission earlier today. The IPART submission says:

> We consider the function of the rate peg is twofold … This helps ensure that they can maintain the scope, quantity and quality of these services over time without undermining their financial sustainability.

Is it your view that the rate peg is actually fundamentally not meeting that function?

WILL BARTON: It is. I might defer to Josh in a moment on this. We have, historically, seen the roads construction cost index, which is one index that measures the annual change in the cost of delivering road networks, outstrip by some margin the rate peg. We have some other indexes—wages, electricity and so forth—continually outstrip the rate peg. Within New South Wales we operate in the Integrated Planning and Reporting framework. That, I think, is intended to deliver a level of autonomy to communities, but that autonomy does not extend then to the question of funding.

Rate peg is imposed on us. We are the only level of government which has its wings clipped in that regard. It is a legislative requirement that we prepare asset management plans, that we prepare asset management strategies that these respond to and reflect the wishes and the desires of the community. But when it comes to funding these in their fullness, councils are forced to go down the path of special rates variations, which are costly and time consuming—politically, they can be problematic—and they simply do not support the efficient funding of local government.

JOSH DEVITT: Just to add to that, and I note that in our submission we did call this out as well, that councils are now getting forced into the position of having to make some tough decisions about the service levels that they offer to communities. I was speaking to one of our members in a regional council the other day about potentially divesting themselves of certain asset classes because they just can't afford to sustain them at all. That is a ripple effect from the rate pegging that we're starting to see manifest for certain communities.

Dr AMANDA COHN: You also went into quite a lot of detail in your written submission about the nature of grants, and you particularly commented that constantly having small single-project grants isn't good for long-term staff development. What do you see as the impact on the broader community of that lack of development in the workforce?

WILL BARTON: I think, first and foremost, it amplifies the impact of the skills shortage we're already in. It's quite well known that there's a shortage of skilled engineers and technicians that are related to the management of assets within New South Wales—and, indeed, across Australia. What tends to happen, in my own experience in my own council, is that we see a rapid increase from time to time in grant funding. For our own situation, in the three to four years up to about 2020-2021, we had an average capital spend of about $20 million. With natural disasters, with other grants and so forth, that's now exceeding $100 million. We've had to try to ramp up our workforce to meet that challenge in 12 months. The impact on the community is often one of delays—of having to suffer through the damaged infrastructure or infrastructure which is no longer in a suitable condition or fit for purpose. That brings with it a whole range of costs that I've already mentioned—costs on time, costs on vehicle maintenance, costs on damage and, sadly, from time to time, cost of lives as well.

Dr AMANDA COHN: In your submission, you also commented on the administrative burden of having to perpetually apply for grants rather than having a greater amount of untied funds. In particular, you commented that funding provided by Federal sources is typically much less onerous from a governance perspective. I'm certainly not aware of any community pushback that people feel like Federal funding to councils is poorly regulated or requires more reporting. I'm interested if you could go into more detail on that, and perhaps what lessons from Federal funding could be applied to State funding.

JOSH DEVITT: Yes, I'm happy to field that one. We've certainly seen—there are some comparative programs out there, and one that stands out is in regard to bridge renewals. There are certain funding streams at the Federal level and the State level to that. This was highlighted, I think it was two years ago, at our Local Roads Congress, where the touchpoints for a Federal program were four but the touchpoints for a State program were 12. That clearly highlights the extra governance and the extra reporting requirements that are put over the top of a State-level program, as opposed to a Federal-level program.

The other thing I would mention is that we see inconsistencies as to how grants are administered, and the reporting requirements vary from program to program as well. One of our members in the far north of the State, who's been through some natural disasters over the last few years, was relaying to me the other day that as a part of their post-disaster recovery I think they had 65 separate funding sources with 250-odd touchpoints from a reporting perspective. When we talk about the burden, that's a very clear example of the need for additional officers within the council to manage that side of it, and it's just not sustainable in the longer term.

Dr AMANDA COHN: Thank you, that's a really great example of that inefficiency.

The Hon. EMMA HURST: I've just got a couple of questions. I know you've already talked a little bit about funding grants that are coming from State government, and your submission talked about the fact that they're more focused on new builds rather than asset maintenance and refurbishments. I wanted to get a bit more information about that. Is that something that historically is continuing to happen, where we're seeing an infrastructure backlog in certain assets that the councils already have? Is that related to the fact that the grants are still going to those new, shiny things, rather than making sure that the things that are there are getting the money that needs to go into them?

WILL BARTON: Sorry, I'm struggling to follow along with the nature of the question. If you could perhaps just repeat the key question that you have.

The Hon. EMMA HURST: Sure. In your submission, you talk about the funding grants from State governments. You argue that they should be focused more on asset maintenance and refurbishments rather than new builds. I just wanted to get a bit more information about that—whether the grants are currently all going into these new establishments and, meanwhile, we've got this whole issue with the actual maintenance and refurbishment of things that council already has.

WILL BARTON: Yes, that's quite correct. In essence, councils across the State can't afford what they've already got, and yet these grants often result in adding to that problem and adding to the burden. In my own experience, we have a backlog of several tens of millions. That has come about for a number of reasons and is certainly exacerbated by the disasters that we've experienced up in the north-west of the Sydney Basin. There is certainly a case and a need for new infrastructure; we don't contest that. What we would seek, though, is that these grants reflect that there is an ongoing cost to this infrastructure and that that is considered within a new infrastructure funding model.

The classic example is the requirement to provide a new pool, for instance, when a council already has an ageing pool that requires renewal, or it might be one that's a little more complex, which is our natural disaster funding. We welcome, of course, the ability to introduce betterment and resilience. That often comes with an increase in value, which leads to increased depreciation costs and also maintenance costs. We again see that tail that lingers for the next decades as an ongoing cost. Ideally, what we would seek is not necessarily an increase—although we would always welcome that—but a redistribution so that the grant funding actually meets the need.

Coming back to the point I made earlier, councils are required to develop asset management plans which reflect the community's desires, the community's wants and what that community wants to achieve, in a self-determining kind of way. The grant programs which come out, particularly from the State but also from the Feds, often don't reflect that, and so councils are forced to step outside of their asset planning to avail themselves of these opportunities.

The Hon. EMMA HURST: Absolutely. An example I spoke about this morning as well, and one that my office often hears about, is the power systems within councils. We often hear from councils that they're in disrepair or built out of tip sites. I assume that fits a little bit into that example, as well, where it's about maintenance and making sure that the structures that are in place now are fit for purpose, in a similar way to the pool example that you gave. Do you think that just restructuring those grants as they currently stand to ensure that that's factored in there for the long term—how do you see that playing out? Is it still sort of like a one-off grant, or is it something that kind of—I'm just trying to picture how, structurally, that changes within government.

WILL BARTON: I think the Roads to Recovery grant which my colleague Mr Devitt mentioned is a really good example. It's probably the most secure grant funding that we have in terms of tenure and longevity, where we know, often years in advance, what the allocations are going to be and we can plan accordingly. That also allows for and, in fact, is predominantly used for renewals—that is, to repair what we've already got, as opposed to new assets. But whatever the ultimate funding model looks like, it has to be reflective of the fact that there are these long-lived costs associated with infrastructure which have to be recognised through that process.

The Hon. EMMA HURST: From your organisation's position, what sort of recommendations would you like to see come out of this inquiry? Ideally, would you like to see the rate peg system removed altogether, or do you want to see specific improvements? What, ultimately, would you like to see as recommendations?

JOSH DEVITT: I think we're supportive of, I suppose, as Will alluded to, a redistribution of the funds that are going into those grant programs, whether that's in the form of a more sustainable grant funding model or even an increase in base load funding. Really, what we're seeking to see is funds that will support that sustainable investment in council workforces over the longer term and will meet the needs of those assets across their full maintenance cycle. And we certainly called that out in our submission. I suppose one other point I'd make in regard to that is that one of the challenges with the competitive grant process at the moment is that it tends to favour larger, better resourced councils, and we tend to find that the smaller regional and remote councils are the ones that miss out, which are typically the ones who need this funding more anyway. So again there's that imbalance between where the money is going to, and I think we would support a redistribution to try and create a more equitable distribution of funds.

The Hon. EMMA HURST: So you're more focused on those grant programs generally.

JOSH DEVITT: That but also, potentially, a revision to rate pegging, to allow councils the freedom to set the levels themselves to a large degree.

WILL BARTON: If I can add onto that, we do have infrastructure assets which are delivered by councils, which aren't impacted by rate pegging—water and sewer assets, for example. There is no cap on how or by how much these costs can increase, but there is a robust process in place to develop asset management plans and strategic business plans and so forth, to justify annual increases. We don't see there being any difference between the provision of a water treatment plant and a water treatment and distribution network versus a road network. They're infrastructure that serve a purpose, serve a community. They both are governed by or managed through asset management plans, which respond to a community's desired outcome. One is constrained by rate peg. The other is free, within reason, to increase the annual revenue to reflect the needs of that network and of that asset class.

The CHAIR: I might start with a question now about infrastructure costs. In your submission, you mentioned about the rate peg making infrastructure costs more expensive in New South Wales. I just wondered if you could explain that a bit more for us and also if you've got any data to support that.

WILL BARTON: Certainly. I might start and then throw the data question to Mr Devitt. I touched on it in my opening remarks, which is I have, within my own context, about 700 kilometres of sealed road that I'm responsible for. On average, that costs about $10 a square metre to reseal. Reseal is a vital practice to protect the pavement structure. It's the pavement structure which gives us the strength and that allows vehicles to safely travel along the road network. If that seal is not updated, that $10-a-square-metre cost becomes $100 to $200 to $250 a square metre. Some of those reseals are able to be programmed and undertaken when they're required. But ultimately, because of the funding constraints on us, not all of those reseals can be, and so what we see is a progression of that road deteriorating.

With every year that you do not do that reseal, the cost to repair becomes greater and greater. It begins with isolated pavement failures, moving to more wholesale failures across larger sections, and ultimately it leads to the failure of the structure itself—a little bit like a building or a house. If you don't maintain the roof, the walls start to deteriorate. Then the floors and then ultimately the foundations begin to deteriorate. It's far more expensive to address those latter problems than it is to do the initial work required to protect the structure. So, because of rate pegging and that constraint on our ability to fund those assets, essentially, we're turning a $5-a-square-metre problem into a $100- or $200-a-square-metre problem, which ultimately has to be fixed. It's those SRVs which we're seeing come through to do that cost but not before we see an increase in maintenance costs, because we have to try and maintain the network in a safe and serviceable standard throughout that deterioration, but also, instead of repairing a seal, we're repairing a full structure.

JOSH DEVITT: Just in regards to the data to support that, we've got a longitudinal study that we've been undertaking for about 20 years now, called the road Asset Benchmarking Survey. That's collecting data from all the councils across the State as to their infrastructure backlog and the condition of their assets. One of the metrics that we track is that backlog over time. We have seen it decrease up until about three years ago. As Will alluded to in his opening remarks, it's actually increased from about $380 million to $680 million. That's an annual backlog, as well. So, unless we're getting that increased funding, we're expecting the condition of the road network to deteriorate over time. I think that was probably highlighted most recently with the pothole failures that we saw across the entire State two or three years ago. In my mind, that's very much linked to this underspend in maintenance activities over that 20-year period. We're starting to see the ramifications of it now. That's what we're seeking to see funding increased to avoid, that happening again.

The CHAIR: It would strike me that that sealing of the road is just a common thing that you would you have to do or should or ought to do. In terms of the resourcing of councils, is there an argument to make, that a more well-resourced council system will lighten the State's burden in terms of project management?

JOSH DEVITT: Yes, absolutely. I'd certainly agree with that. We're very supportive of councils' building capacity within themselves. We think you get greater efficiency gains through having staff in house as opposed to relying on external contractors. So I think we'd certainly support that.

The CHAIR: How difficult is it for councils to attract high-quality engineers?

JOSH DEVITT: It's quite challenging in the current environment. We're in an acute skills shortage across lots of professions, but that certainly includes engineering. We tend to find that the competition—engineers will gravitate towards either the private sector or maybe State government and that councils struggle to be able to pay market rates to attract skilled staff.

The CHAIR: Councils aren't able to offer market rates. Is that what you're saying?

JOSH DEVITT: In many cases, no.

The CHAIR: Why do you think that is? What do you think the cause of that is?

JOSH DEVITT: It's partly linked to, I guess, the funding model within councils themselves. There's obviously some structural requirements there, around the local government award, that allows some wiggle room for people to offer more, but I think what we see is that it's largely limited by the funding that's available for those positions.

The Hon. MARK BUTTIGIEG: Is that problematic in the sense of not just having resident academic qualifications and expertise to do the nuts and bolts but not having people with the ability to oversight those contractual arrangements with professionals externally? Is that the main issue?

JOSH DEVITT: I think it's a bit of both. We're supportive of every council in the State having at least a couple of engineers within the organisation. But, in some cases, that may not be the case, and we can probably go off on a tangent here into our position on engineering registration. But, in short, there is a lack of technical capability within some organisations, and what we find is that that tends to defer to that more oversight model of project-managing external resources to deliver these works. But there is certainly a shortage, in some areas, of those project management capabilities as well.

The Hon. MARK BUTTIGIEG: Does that mean, as we stand today, there would be councils out there who just don't have anyone with the capacity to oversight those contracts in a way that's faithful to the ratepayers' integrity?

JOSH DEVITT: It's hard for me to generalise on that point.

The CHAIR: Do you think there's a need to create new opportunities for young engineers to get into council?

JOSH DEVITT: Absolutely. We're very supportive of that. One of our missions is to promote the profession of public works engineering. But I think certainly, from my experience—and Will may comment on this, as well. I've come through the ranks, as it were, through a council organisation. We certainly see the value that a career in that field can result in. So, yes, we're very supportive of that.

The CHAIR: Are you aware of any trends, in local government, of engineers being either attracted to or turned away from a career in local government?

JOSH DEVITT: I think what we tend to find is that obviously the market rates are a deterrent to people going into local government, but it's often couched in terms of there being a better work-life balance or flexibility of work in the local government sector as opposed to, say, the private sector. Coming out of COVID, the whole flexible work-life model has shifted a fair bit now. We haven't quite seen the full ramifications of that for our membership.

WILL BARTON: What I might add is that for many, many decades, State and local government were the proving ground of young engineers. We had the old Department of Main Roads or DMR, then RTA, then RMS, now Transport for NSW; similarly with Public Works. Councils, too, had strong cadetship programs. They had strong programs in place to bring, often, student engineers into their organisations, expose them for six months or 12 months to the workplace and to the field. Then they'd go off and finish their studies but, with that taste of public service, a lot would come back. We've seen over many years now that decline across both levels of government. We're certainly very keen to see that return not just to local government but to State, of course, so that we can foster that future generation. Like Josh, I'm a product of that. I started out as an intern down in the Riverina and progressively moved through organisations and councils almost exclusively.

The Hon. WES FANG: I knew I liked him!

The Hon. MARK BUTTIGIEG: That's an interesting point. What's been the catalyst for the gradual decline? You would have thought that a responsible general manager—and indeed a council—would at least recognise the requirement to have that resident expertise, if only as an oversight function. Where did it get to the point where, "We don't need that anymore. Let's just outsource everything"?

WILL BARTON: I don't think that you can point to one catalyst or event. I think what has probably occurred is that there's been a real struggle to attract engineers. From my time out in the Riverina, we saw that a lot. There were occasions where I would have to go two or three times to market to try to find a suitably experienced and qualified engineer. In that vacuum, consultants and contractors have filled that void. That is kind of then perpetuated, almost, as the standard way of doing business.

The Hon. MARK BUTTIGIEG: But wouldn't it have always been the case that the private sector paid over the odds, historically? I'm just failing to see the linear connection between—you know what I mean? Like 30, 40 years ago you would have got more as a private sector engineer than an engineer working for Ausgrid or council, so what has changed? There must have been a change in the philosophy somewhere along the line.

WILL BARTON: There was certainly the change to the Act in 1993 that removed—look, I won't expose what I was doing in 1993, but it was to do with school. My understanding is that prior to that, there was a requirement for a council to have a chief or municipal engineer, a shire engineer—

The Hon. MARK BUTTIGIEG: Right, okay.

WILL BARTON: —as well as the shire clerk and so forth. The introduction of the 1993 Act removed that requirement to have that position. There's a statutory, if you will, role within council. I can only imagine that that had some bearing and perhaps kicked off the trend.

The Hon. MARK BUTTIGIEG: We should note that, Chair, as a potential recommendation.

The Hon. WES FANG: Obviously this inquiry is looking at a number of issues—the ability of local government to fund infrastructure and services. I would think it's fairly clear that you're here advocating for the infrastructure component. But as well as a number of the structural issues that occur within the rating system for ratepayers, there also exists an increase in the services that councils are providing that are at best described as "non-core business". Have you had any chance to do any work in relation to the expenditure percentage in relation to councils on infrastructure over, say, the past number of years—whether it be a decade or so or a number of decades—to see whether the percentage of rates coming in and the percentage of that expenditure on infrastructure has been decreasing? Is that in response to councils doing more service or political-type work, which means they've got less to spend on infrastructure? It's really a Dixer; I've just tossed the ball in the air. Smack away, please!

WILL BARTON: I'm not aware of any research that our organisation has done. What I would say is that the—

The Hon. WES FANG: Anecdotal is fine.

WILL BARTON: We are certainly seeing—and I can cite, for example, the emergency services levy—but, generally, cost shift from other levels of government to local government increasing markedly. The number escapes me in the last report that LGNSW undertook, but I think it was something approaching $1 billion a year; it might have been $850 million or thereabouts. That has certainly eaten away at the budget available. I come back to the point that this is all within the context of a revenue-constrained environment. The emergency services levy is probably a classic, where in my own organisation we've seen it increase over the last six or seven years by about—I think it's at least 3 to 4 per cent over and above what's been allowed for through the rate peg, so that has outstripped. When a cost increases at a percentage greater than the rate peg, that has to come from somewhere. Infrastructure budgets are generally the largest line item a council will have in their budget.

The Hon. WES FANG: You'd hope so, anyway.

WILL BARTON: You would hope so. Generally that's where it comes from, because it's got the most capacity to absorb those kinds of cuts. But it is a case of death by a thousand cuts where, year on year, we're seeing these budgets. In all the organisations that I've worked for, until that point where they hit a trigger to require an SRV or some such, we see that continue to reduce.

The Hon. WES FANG: My final question is: Do you think that part of the issue is that councils have lost focus of their core business? Perhaps a redefining of the council role to the "roads, rates, rubbish", which is the traditional view of what councils were doing, would assist in the delivery of at least the infrastructure part for councils?

WILL BARTON: What I would say is that councils—and this is a saying that we have within our industry—are the level of government of last resort. Where the Federal or the State governments have either dropped the ball, made a deliberate withdrawal from an area or haven't yet identified an issue, it's often councils which are left to pick it up and provide the service—similarly with services provided by the private sector. When that becomes uneconomical—and child care is a classic, where out in the bush, until recent years, it hasn't been that economical to provide child care—communities look to their council to provide that. I am not in a position to say whether that's right or wrong.

I come back to the point about a community having that self-determination through the Integrated Planning and Reporting Framework. What I would contest is that something like infrastructure should be excluded from, we'll call it the rate peg, and what is then left is allowed for a community to say, "Okay, we value this service over this service" and start to make those trade-offs. Unfortunately, when you start trading off a service such as a library or an environmental health service or something like that against infrastructure, the impacts of funding cuts to infrastructure often aren't borne for many, many years. As Mr Devitt alluded to, the pothole crisis last year had its roots in decades of underspend. The seeds of that issue were sown before I went into uni.

The Hon. WES FANG: And the Riverina diplomacy is on display.

The CHAIR: In terms of councils and their current approach, can councils better share technology or best practice to be more efficient and get better value for spend? Is that an option?

JOSH DEVITT: Yes, certainly. A big part of what our organisation, what the institute works towards, is sharing best practice across organisations and looking for ways that councils can work more efficiently. A pertinent example that we're working with at the moment is a project called Asset AI, which we are working with Transport for NSW on. It is about passive data collection of road defects that are on the network through using vehicles that are already out there such as garbage trucks, school buses and things like that. The thought there is if you can get those efficiency gains—work smarter, not harder. But that also leads to a much more proactive approach to road maintenance activities. Councils have that full picture of where the defects are. They can intervene earlier and prevent that longer term deterioration and the need for a more expensive intervention. That's an example of where we think there is some work that councils can do.

The CHAIR: Would you say there's a huge gap between the best performing councils and others?

JOSH DEVITT: There are 128 councils in the State, so there's a range there. It's probably not as great as people sometimes make out—that would be my impression. I think there's probably work that can be done across the board to uplift capacity in local government. But there is obviously a range of context, given the funding and the size of all the councils across the State.

WILL BARTON: If I might add to that, from my own experience, having worked in both regional New South Wales and metropolitan New South Wales councils, there has been, I've observed, a distinct benefit from the close work that councils in regional New South Wales do with the organisations and agencies such as Transport for NSW. That has led to quite a marked—almost by osmosis—lift in capacity. It would probably be counterintuitive to think that a lot of regional councils in New South Wales, in terms of on-the-ground understanding of those basic, fundamental engineering principles of managing a road network, are often on par with, if not ahead of, some metropolitan councils. That's simply because they're exposed to State agencies such as Transport for NSW through arrangements such as the Road Maintenance Council Contracts, which is where councils perform maintenance and works on the State highway network on behalf of Transport for NSW. That close partnership, which is very, very common in regional New South Wales, is certainly a tangible example of where there is a significant benefit to communities and that uplift in capability because of those partnerships.

The CHAIR: I will finish with a final question, noting the time. We talked earlier about grants. How much of the council-owned infrastructure is funded by rates and how much is funded by grants, and is that effective and appropriate at the moment? Or maybe efficient and appropriate is a better word.

WILL BARTON: I don't think you would be able to easily quantify that. We have seen, particularly over the last three years with national disasters, the ratio of what's called own-source income—that is, income generated by rates, user fees, charges and so forth—in terms of the overall income of the council, often reduced markedly as we've seen significant grant funding come through for disaster reconstruction and so forth. I'm not aware of any council that identifies what infrastructure assets are funded by grants and what are funded by general revenue. It all comes into the mix and that proportion changes from year to year quite considerably.

The CHAIR: Thank you so much to you both for making the time to appear today and for giving evidence to our inquiry. The secretariat will be in touch if there are any questions on notice.

(The witnesses withdrew.)

Mr ERIN SELLERS, Principal Project Officer, Sydney Coastal Councils Group, affirmed and examined

The CHAIR: Thank you to our next witness for appearing today, and welcome. Would you like to start by making a short opening statement?

ERIN SELLERS: Sure, thank you. Firstly, I would like to thank you for the invitation for Sydney Coastal Councils Group to appear before the Committee today. We are a regional organisation of councils established in 1989. We represent the interests of nine member councils related to issues around the coast and estuaries. Our written submission was really directed towards non-rate sources of income, such as grants and levies, rather than rate pegging. We've initially noted in our submission that we believe that councils don't have a full understanding of the amount of what we call green infrastructure that's required to be installed to meet community expectations for clean and healthy waterways around Sydney. Initial evidence suggests that the life cycle costs for this type of infrastructure will be in the order of millions of dollars per year. We argue that funding for green infrastructure is, unfortunately, inadequate, partly because of rate pegging but also because of charges like the stormwater management service charge, which hasn't been increased since its introduction 18 years ago.

We also highlight some of the limitations of existing grant programs that councils have come to rely on for planning for coastal, stormwater and waste management. We believe the grant programs aren't as well designed as they could be for regional, multi-council approaches that the Sydney Coastal Councils Group promotes. We note that cost shifting is continuing to occur, with the New South Wales Beachwatch program being a recent example of that. Finally, we note the implications of climate change and coastal inundation. We believe that, in the absence of what we're calling a coastal adaptation planning framework, councils are probably not as prepared as they should be for the issues associated with coastal inundation. We are happy to answer any questions that the Committee might have.

Dr AMANDA COHN: Thanks so much for coming and for your written submission. My first question is about one of the comments you made about grants in the submission, particularly commenting that in many instances multi-council organisations aren't eligible for grants. That's to do with the way that organisations can be designated as ROCs or not. What do you see as the benefits for communities of self-identified groupings of councils being eligible to apply for funding together?

ERIN SELLERS: There are a lot of benefits for regional groupings of councils. It's very difficult for councils—particularly in Sydney—which are smaller than the regional councils, to do the type of projects that we do by themselves. We believe there are more benefits in coming together as a group to work on projects. The classic example that we've given in our letter is the coastal management programs, which are often done on a waterway and catchment basis: Sydney Harbour, Georges River and Cooks River. No one council can do that by themselves. It needs a group of councils. That makes the coastal management program project much more viable, and represents the interests of the communities within the catchment as well. Councils can also leverage a lot more from the grant funding when they come together.

Dr AMANDA COHN: Thank you. That's a great example. You mentioned cost shifting as well. I think every submission we've received talks about cost shifting. You've named the particular example of the Beachwatch program. Could you elaborate further on that, and what's happening to the community as a result of that cost shifting?

ERIN SELLERS: Yes, sure. It's a decision by the current Government to pass the cost of the Beachwatch program on to coastal councils. We believe that it was based on a report that was done by the previous Government, although councils weren't consulted at the time that that report was done. We have asked for a copy of that report. We've written a submission to the Minister and the Minister has kindly extended the consultation period for us. We're about to write back to the Minister and welcome that opportunity.

Dr AMANDA COHN: I also want to pick up from your written submission the comments you've made about the waste levy. I know that that's something that the Minister for the Environment is going to be reviewing as part of the circular economy strategy, and that's due by the end of next year. You've suggested that that could be changed to provide more flexibility for councils in the way they are managing waste. Could you provide a bit more detail or some examples of that?

ERIN SELLERS: Yes, sure. This is probably more the experience of one of my colleagues. But my understanding is that the waste levy can't be used for litter prevention activities. Groups like ourselves in coastal councils, we put a lot of effort into litter prevention rather than managing the litter once it has occurred. Unfortunately, it's our understanding that the waste levy and the domestic waste management charge can't be used for litter prevention activities, and we have requested that the Government, maybe, or IPART look at that. I think we also go on in the submission to say that under the NSW Litter Prevention Grants Program there's a big push for the EPA to get councils to look at other sources of funding rather than that program. We said in our submission it's kind of unclear where that money might come from. Hence, it would be great if the domestic waste management service charge or the waste levy could be looked at as a source of income.

Dr AMANDA COHN: You have already mentioned the importance of green infrastructure and the challenges that your councils are having to fund that. We heard earlier today from IPART. One of the comments that they made in their submission was about some councils introducing a local levy for environmental purposes. I think their example, from memory, was Randwick council. IPART has referred to that sort of spending as discretionary. I am interested in your view on the role of that sort of green infrastructure in those areas and whether that is actually essential infrastructure or discretionary infrastructure.

ERIN SELLERS: We would argue it's essential. We say green infrastructure is just as important as what we call grey infrastructure, which is our roads, our stormwater drainage network. The green infrastructure is essentially the life support system for the city. It's looking at your parks, your waterways, your green open spaces but also your built green infrastructure, which we have identified in the submission as, say, for example, stormwater quality improvement devices. We would say that that's essential infrastructure to meet the community expectations for a clean and healthy waterway, a clean and healthy environment. Yes, we would argue that that income—we wouldn't say that's discretionary. We would say that that would be essential for any council and its community.

The CHAIR: Could I ask you about rate pegging? How does rate pegging affect the management and preservation of our coastal and waterway infrastructure?

ERIN SELLERS: I would probably preface my answer by saying that in our submission we obviously haven't focused a lot on rate pegging, so it's probably a little bit outside of my expertise there. But, as a general statement, I would say that obviously council's financial situation is constrained, so it will obviously limit the amount that it needs to be able to spend on coastal and estuary management. I would also suggest that as council progresses through the coastal management program process, there will be a lot of actions that will be identified in those programs that will require funding. I think councils are going to be grappling with where that funding is going to come from—is it going to be rates, levies or grants?

The CHAIR: I will ask you about one of those levies now. Is the stormwater levy sufficient? What changes are necessary to it, if it isn't?

ERIN SELLERS: No, it's not sufficient. Based on a survey of our councils, we're finding that most of our councils are spending the money purely on addressing their existing stormwater infrastructure, their grey infrastructure—so looking at what's called renewals, or maintenance renewals, and upgrades of their existing infrastructure. There is less left over for spending on new green infrastructure, essentially. What we are arguing is for the State Government to look at increasing that stormwater levy at least in line with inflation, but we have also identified that it should achieve some measure of equity with Sydney Water service charge, for example.

The CHAIR: Tell me about why that infrastructure that you referred to is needed—that there's not enough money left over for those green upgrades.

ERIN SELLERS: Again, as I pointed out in the submission, community expectations have increased over many decades and they are rising steadily, and we have given the example of an increased community desire to swim in our waterways. To the Government's credit, through Sydney Water, they are definitely promoting that, which is a great thing. But to be able to do that and do that safely, we need to be retrofitting a lot more green infrastructure in our catchments to improve the water quality for swimmability.

The CHAIR: How is the current stormwater levy calculated? Is it indexed with inflation?

ERIN SELLERS: It's $25 per household, and that rate was set in 2006. It has not increased since that time, and there is no mechanism at the moment to be able to increase that. One of the things we have suggested, not in this submission but previously, is that maybe that's something that the New South Wales Government could put to IPART to look at that. If it were to be increased by inflation, it would be about $39 per household today. But I would also point out, too, that it represents only a few per cent of the rates income that council receives, so it's not a big impost on a community. It's about 50 cents a week.

The CHAIR: Interesting. It hasn't shifted in 18 years?

ERIN SELLERS: No, and we have made—or not just us but other organisations have made numerous representations to governments over the years saying that it really needs to be looked at.

The CHAIR: Yes, interesting. What innovative funding models could also support more sustainable coastal management in the face of these financial constraints that we talked about for councils?

ERIN SELLERS: There are different models out there. It's certainly not a position of Sydney Coastal Councils Group, but for myself personally I have done some work in what we call market-based instruments. They would be incentive schemes for private property owners to install green infrastructure on private properties. At the moment there are a few mechanisms that you can have to install green infrastructure. One is council or government pays for it in the public domain. You can also have it installed during the development process when a private property is undergoing redevelopment. But another way to do it—and this is one of the more innovative ways—is to encourage private property owners, incentivise them either through some financial incentive or planning incentive to install green infrastructure on their land.

The CHAIR: Can you tell us more about the specific challenges that coastal councils face when compared with their non-coastal council counterparts?

ERIN SELLERS: Probably some of the biggest challenges are just managing the coast as an asset. Obviously the coast is a dynamic space. It's subject to multiple hazards. Probably the big two would be erosion and also future inundation. Our open-coast councils, particularly Northern Beaches council, have got a lot of coastline, and they've got significant problems—which I assume the Committee is aware of at Collaroy-Narrabeen, for instance—but also our estuarine councils that are subject to coastal inundation, which is predicted to increase over the years. I point out that that hazard of coastal inundation will far surpass the risk from, say, floods and bushfires. That's pointed out in the recent New South Wales Government's State Disaster Mitigation Plan. So there are huge financial implications for those estuarine councils.

The Hon. WES FANG: I apologise that I had to duck out briefly; I am hoping that no-one has asked this question. In relation to the coastal council group versus a more inland, rural and regional setting type council group, do you believe that there is a difference in the cost burden between those councils? Do you believe that there's an impost because of the coastal location, having to deal with, often, the interaction with water, the issues around inundations and freak weather events where you might see erosion and the like? Does that create a cost that's not then ameliorated by other means, that you're then not able to claw back through things like grants and funds and the like from either State or Federal government?

ERIN SELLERS: I would say broadly coastal councils would have a greater cost burden than non-coastal councils but, unfortunately, I don't have the evidence to support that. I'd probably have to take that on notice and look to have that confirmed. But probably, to reiterate my last point, I would say that those councils—because of the coastal hazards they're facing, that is a huge cost burden. Again, yes, I think financially it's going to be difficult for councils. Again, taking Northern Beaches Council and the coastal protection infrastructure that they need to be building, that's many millions of dollars worth of infrastructure. A lot of that is falling to private property owners at the moment. I'm not sure if I can probably add any more to that.

The Hon. WES FANG: I was going to extrapolate that further and suggest that—and I don't know the answer. That's why I'm asking the question. If we surmise that coastal councils might have a larger cost burden because of their location, perhaps you could extrapolate that further and say that the regional coastal councils will then have a larger cost burden, because predominantly they might have a greater coastal frontage and less of a rateable base. I'm interested to see if there is any work done in relation to that and how they manage those differences.

ERIN SELLERS: Were you talking about councils outside of Sydney?

The Hon. WES FANG: Yes. Obviously Sydney coastal councils would have a very dense population and, I imagine, a very small exposure in relation to their sea frontage or the estuarine or river input into their land. Coastal regional councils would probably have a larger ocean frontage, larger costs in relation to those property protection issues, such as erosion and the like. I was curious to see if any work has been done in relation to that, particularly around the infrastructure component of costs to council.

ERIN SELLERS: It's an interesting question. I'm not aware of that work. Though, I would suggest that I would probably go to the Department of Climate Change, Energy, the Environment and Water.

The Hon. WES FANG: No, they're too busy shooting brumbies.

ERIN SELLERS: Okay. Because they've got a good overview of the coastal management programs that councils are doing and we've had presentations from DCCEEW staff previously where they've looked at the costs that are represented in those CMPs. Obviously, there's millions of dollars worth of actions. But I think it would be interesting to compare the CMPs done for regional councils to look at what they're up for compared to us here in Sydney.

The Hon. WES FANG: Yes, something we might have to look at.

Dr AMANDA COHN: Before we finish, is there anything that you were hoping to raise that the Committee hasn't asked you about?

ERIN SELLERS: Probably the take-home point I'd make would be around the stormwater levy. I'd really like to emphasise that. I know there's been at least one other submission from Stormwater NSW about the stormwater levy. That is long overdue, in our opinion, to be addressed. If the Committee is of a mind to make a recommendation to Government about that, we'd very much appreciate that.

The CHAIR: Have you done any work or do you have any appreciation for what the impact has been of not having indexed it at all?

ERIN SELLERS: That's a body of work that, as a collective, we're looking to do in the coming months. So there's going to be further work about that that we would like to present to the Government to look at the implications. Certainly, there's been work that the Government itself has commissioned, which we've referred to in the submission, about the financial implications of the stormwater levy.

The CHAIR: There being nothing further, we'll conclude. Thank you so much for making the time to give evidence. It's a really important perspective. The secretariat will contact you in relation to any questions on notice. We are now going to have a short lunch break.

(The witness withdrew.)

(Luncheon adjournment)

Mr GORDON MICHAEL BROCK, Director, Professionals Australia, Local Government Engineers Association, affirmed and examined

Ms ALYCIA VASILANGOS, Principal Industrial Officer, Professionals Australia, Local Government Engineers Association, affirmed and examined

The CHAIR: Welcome to our next witnesses. Would either of you like to start by making a short opening statement?

GORDON MICHAEL BROCK: I firstly thank the Committee for inviting us to appear today. I acknowledge that there was some confusion around our submission to this inquiry. I want to confirm that we commissioned some research, together with the United Services Union, by Professor Brian Dollery, and that was to respond to the Committee's terms of reference. I believe that's submission number 22 to the inquiry. We also provided a short supplementary submission focusing on some matters that we believe are relevant and consequential of the funding situation in local governments, which I think members of the Committee have a copy of. What I want to quickly do is outline two aspects to that.

There are two key aspects to our submission. We titled it "The Infrastructure Challenge" and we say that the two key issues facing local governments in New South Wales that hinder their ability to deliver and maintain infrastructure for their communities are a funding issue and also a capacity issue. We make the point through our submission that those two go hand in glove because, without resolving the capacity issue, even if you provide greater funds to the sector you will find that those funds aren't invested in an optimal way. If you fix the capacity side of things, then we say that that will bring efficiencies but without additional funding the infrastructure backlog will continue to grow. So that's the connection between the two.

With funding, we're content to rely upon the material contained in the Dollery report, except what we have done is grabbed some statistics from the Your Council website, a State Government-managed website, which talks to the asset base of local government. The asset base in local government we identify as $198 billion in New South Wales and the largest component of that, at $176.3 billion, is your infrastructure assets. So the infrastructure problem is actually a local government problem. You can't fix local government funding without dealing with that infrastructure issue.

What we then go on to do is talk about capacity—and I will hand over to Ms Vasilangos shortly to talk about that. We've titled that "Engineering and Technical Expertise". There are a couple of new pieces of research in that which we've provided the Committee that don't appear in the Dollery report. The first one is in relation to some statistics that we've gained from the Australian Local Government Association's 2022 Local Government Workforce Skills and Capability Survey. There's a breakdown of New South Wales data. Then there is some internal research that we've done where we've surveyed our members. I might, if the Committee is comfortable, hand over to Ms Vasilangos to explore that.

ALYCIA VASILANGOS: Our research indicates that the capacity problem is significant in terms of engineering expertise within the industry. Worryingly, it's growing and, arguably, it's potentially about to get a lot worse. The Australian Local Government Association's 2022 Local Government Workforce Skills and Capability Survey indicated that 60 per cent of councils responding to that survey indicated that they were experiencing acute skills shortages—attracting engineering, specifically. Even more concerning was the admission that 33 per cent of respondents to that survey had to resort to the hiring of lesser qualified employees to fill vacancies because of the difficulty to attract suitably qualified professionals. There are numerous pieces of research that indicate that if you've got not properly qualified engineers or not qualified engineers working on infrastructure projects, that is what leads to significant amounts of waste and cost blowouts.

We also undertake our own research of our membership and extended workforce every two years. It's a biannual survey that we've been doing since 2008 where we survey on employment conditions based on an employee's years of service and qualifications. When we conducted this survey in 2022, we asked employees how much longer they saw themselves working within the industry and, worryingly, almost half of our respondents indicated an intention to leave the industry within the next five years. So we have a situation currently where 60 per cent of the industry is saying we can't find engineers, 33 per cent of those are saying we're hiring people who aren't engineers just to fill the gaps and then we're hearing from our members that half of the existing workforce is intending to leave the industry within the next five years. Anecdotally, when we visit our members at councils we've heard stories of councils with up to 40 per cent vacancies in their engineering workforce, which is extraordinarily problematic when we're talking about an infrastructure backlog of $5 billion. If we don't have the engineers to do this work, we're not going to fix the funding issues and the financial sustainability of the industry.

GORDON MICHAEL BROCK: Finally for us, on the last page of our little supplementary submission there's an interesting chart which talks about the response of councils to this problem. You would imagine that if there's a skills shortage, you'd throw money at it. You'd come up to speed with the rates of pay that are required to attract these people and make sure that you've got those positions filled, but that's not what we're seeing. The reason we're not seeing that is because of the funding issue. There's not the capacity to resolve that problem in this way, given the funding constraints as evidenced and outlined in the Dollery report. For us there's a real connection—a real circle. You have to fix all of those issues if you're going to respond, we say effectively, to the problem. We might leave it there but happy, obviously, to take questions.

The CHAIR: Thank you so much. I'll hand over to my colleague Dr Amanda Cohn for questions.

Dr AMANDA COHN: I'm interested if you've had any conversations with your counterparts in other States, particularly acknowledging the cycle that you've described where not being able to recruit and retain staff means the financial problems are getting worse because of waste and cost blowouts, which means that they can't then offer the salary you need to recruit and retain staff. Are there any solutions that have worked in other jurisdictions that we should be looking to?

GORDON MICHAEL BROCK: We chart where members—if they're members of our organisation, Local Government Engineers Association, and they go and work in another industry, they can remain members of our organisation but they'd fall under the Professionals Australia membership category. We're able to see where members go once they leave local government, and they go often to State Government. They go to work with RMS. They work in, obviously, Public Works and those sorts of organisations. They might go to the State-owned corporations. They might go to Sydney Water or they might go to Hunter Water because, as Committee members would be aware, outside of the metropolitan areas water is maintained and managed by local councils, so there's a consistency in their skill sets. From there they might go to private enterprise.

I'll tell you what we don't see; we don't see anybody coming from those other areas to work in local government because we're just not competitive in that space. If you look at rates of pay that we survey and the results of our surveys more broadly in other industries, local councils, for our members with the same qualifications and experience—keeping all those things consistent—pay about 15 per cent less than the other industries where our members work. So there is a differential there. The other thing that we've noticed is, and it's described in Professor Dollery's report as a shifting in funding within the industry—and I will get this right because I thought it was a very useful way of describing it—from services to property to services to people. What that means is that the expenditure in the industry is moving away from expenditure on assets to an expenditure on other services that are provided by the councils, and there's a whole bunch of reasons as to why that might be—additional responsibilities within the sector—so there's just not the capacity to fix it within the sector as it currently stands.

Dr AMANDA COHN: Earlier today, we heard from your colleagues at the Institute of Public Works Engineering and they were talking about volatile funding, whether that's through one-off or short-term grants or special rate variations. They were talking about that volatility of funding actually being really counterproductive for asset maintenance. I was interested in your views on the same issue.

GORDON MICHAEL BROCK: Yes, that's right. We say in our supplementary submission, on the third page, that engineers are vital in developing those programs to maintain assets. But what happens is that they take the money where they can, with the funding, so they're shifting focus and the resources they have onto the infrastructure construction program, but then they're left with an additional asset that they've got to maintain. So it's an ongoing, perpetual cycle of cost. If you don't have the resources to manage and maintain, then the maintenance standards get dropped.

Dr AMANDA COHN: If you hypothetically had the same quantum of funding—and I know lots of councils want more funding—you could distribute it smoothly so that it was something that was predictable for councils in advance so they know exactly how much they would have to spend on infrastructure.

GORDON MICHAEL BROCK: Yes. The key is the long-term infrastructure plans, so you can dedicate enough to construction and you can dedicate enough to maintenance.

ALYCIA VASILANGOS: If I can add to that, predictable, known funding would also assist with the creation of positions because what we find is when you have grant funding and there are allocations for a particular project, it leads to short-term contracts, which are not particularly attractive, especially if they are on the local government salaries that they are on. It doesn't do anything to address the issues plaguing the industry with the attraction and retention of suitably qualified professionals.

The CHAIR: Thank you so much for appearing today and giving evidence. I just wanted to ask you about the infrastructure backlogs that you were talking about and what role you saw the rate peg as having in that in terms of making infrastructure more expensive or the backlog worse here in New South Wales?

GORDON MICHAEL BROCK: The best response to that is to refer to some of the material in the Dollery report. There were a number of points made that some of the factors that are included in the rate peg—we've got particular expertise and knowledge around the factors with the wage cost index, if you like, and the suitability of that. We certainly agree with the comments of Professor Dollery in relation to supplementing that or replacing that with something that we do know, which is the Local Government (State) Award wage changes. But also, there is evidence in the submission around the impacts of depopulation actually creating additional costs for councils, because it's not just the change in population; it's the density and it's the fact that whilst we might have a population that's growing, it's not growing uniformly, but the asset base in council areas isn't shrinking. The rate cap has a number of changes which are impacting negatively on funding for things like infrastructure because of the failings behind some of the criteria that go into the peg.

The CHAIR: If we can talk about specific grant funding now and the role that that's had with infrastructure projects. What impact has the grant program funding had in terms of the life-cycle cost of some of our infrastructure that we're looking at?

GORDON MICHAEL BROCK: I take the comments that we made to the Deputy Chair in relation to some of that. That volatility is an issue. We want to see the funding level increased, but it's the way in which it's paid, I think, and the consistency with which we'd like to see it paid, which allows that capacity for planning and resource allocation.

The CHAIR: Looking at ways to make it more efficient and appropriate, you would then say that having more consistency and reliability in the funding would be a much better option.

GORDON MICHAEL BROCK: Yes, that's right. We are the Local Government Engineers' Association, so you would expect us to have a view around the involvement of technical skills and the involvement of engineering people in that decision-making process because what we've found is that some councils just don't have that expertise in house, so they waste some money. They're not an informed purchaser of infrastructure services. They're not able to scope projects adequately and they're not able to recognise whether they're getting provided with what they have asked for and what they have paid for. So there is a waste, as Ms Vasilangos mentioned. There is a waste that arises and there are cost blowouts that arise.

The CHAIR: We heard evidence earlier this morning about the change in the Local Government Act in, I think, 1993 and the removal of the role of the principal engineer or chief engineer, it might have been.

GORDON MICHAEL BROCK: Yes, the chief engineer.

The CHAIR: What impact do you think that has had on the role of engineers in council?

GORDON MICHAEL BROCK: It's had a huge impact because at the moment in New South Wales, let alone local government, you don't have to be qualified to call yourself an engineer. There is no requirement to be registered, and that's another piece of work that we are keen to talk to you about and that we have spoken to a committee about previously. Once you remove the requirement to have people at the senior decision-making table with particular skills, then you remove an input that's necessary for things like decisions around infrastructure. Councils, as we said, by and large are infrastructure organisations. If they don't have the skills to manage the construction and maintenance of infrastructure, then they're letting their communities down and the ratepayers.

The CHAIR: When we are looking at engineers, how difficult is it for local government to attract and retain engineers at the moment?

GORDON MICHAEL BROCK: It's incredibly difficult and, as we pointed out, it's twofold: We're struggling to attract and there are vacancies. We were talking earlier and there are councils with vacancy rates in their engineering department of about 40 per cent at the moment. It's the worst that we've certainly seen for a long time. If you look at the material in our supplementary submission, of those that are actually attracted, half of them intend to leave. Some of them are retiring, of course, because it's an ageing workforce, but they're not all intending to leave engineering; they're just not going to work as an engineer in local government. That's the group of people we think are saveable, but not under the present arrangements.

The CHAIR: Is there a need, do you think, also to create new opportunities for young engineers to get into councils through apprenticeships or traineeships?

GORDON MICHAEL BROCK: Absolutely. We call them cadet engineers. We are working with Transport for NSW, for example, on a cadet and graduate program. Good work is happening elsewhere in this

State, regionally and in metro areas, to build cadetship programs and build—they're called "grow your own" programs—and develop those people. If local government doesn't have funding for those sorts of roles, then they are even going to be further behind because we've already given evidence that engineers working in the public sector earn more on average than engineers working in local government. It's an urgent problem that needs resolution.

The CHAIR: What would that look like? You talked about working with Transport for NSW. Would that look like working with OLG? How would that occur and what barriers are there to that currently happening? I'm just thinking, there are 128 councils, so you probably can't be working individual with each council. So we are looking at how—

GORDON MICHAEL BROCK: Ideally, there would be an injection of funds into the sector. What we've set up at Transport for NSW is what we call an Engineering Matters Reference Group. The Secretary of Transport for NSW sits on that, and the Minister attends the meetings from time to time as well. The idea there is to identify the skill needs and the capacity needs and then put in place programs, not just metro but regionally, to ensure that they're developing their own. I would think that a similar arrangement could be put in place with local government. I think it's well known—and the Parliament has certainly dealt with it this week, and we thank Parliament for approving amendments to the Local Government Act—that the industry parties are very close. We work collaboratively. We don't always agree, but we do work positively and collaboratively. We have an Employment Matters Reference Group that's with OLG, and we put in place these industry-building arrangements. I'm confident that we could do something like that for cadets.

The CHAIR: In terms of contracting out project management and delivery, are councils spending too much money on that currently, would you say?

GORDON MICHAEL BROCK: The simple answer is yes. What happens often—and this is anecdotal, but we talk to members about these matters—is that they are unable to provide or attract and retain sufficient numbers of engineers, so they're in a position where they have to contract out services. They tend to pay two or three times the hourly rate for those contractors that they've contracted out to. Often, with these bigger organisations, the level of the staff that they put on the projects is much less senior than what you would've had if you had additional resources in the council. Side by side, we've got design engineers or construction engineers working with people from the private sector on projects that could've been—not every project can be delivered in house by local government, we're not saying that, but some projects can be. Those people would be earning two or three times the amount of money that the in-house engineer is. It's that kind of "capex versus opex" bucket strategy, and if it comes out of the capital expenditure bucket, then it seems fair game, but it can't come out of the operational expenditure budget because it'd be seen as beyond budget. It's a nonsense, and it's been one of the real problems that we've seen emerge over the last 10 to 15 years.

The CHAIR: Do you think this is also related to what we said earlier about the market rates for engineers and local government not being as competitive? How much of that is an issue as well, in terms of attracting that talent and being able to do these projects in house?

ALYCIA VASILANGOS: It's significant. As my colleague identified, our research indicates that local government salaries are approximately 15 per cent lower than all comparable engineering salaries across Sydney, regional New South Wales and even Australia. In fact, even the Australian local government salary data that we have for engineers is significantly higher average salaries than those in New South Wales local government, so the industry really can't compete on pay. Perhaps years ago, they used to be able to compete on conditions, but because we are seeing such high vacancy rates, what we're seeing is workload intensification that we've never seen before.

If we look at the data in our research for the reasons where people are looking to leave, workload issues is a significant factor. Our research also indicates that concerns exist within our membership at a rate that we've not seen before, and we do these surveys every two years. The overwhelming evidence and feedback from our membership is that they feel that the councils are not filling vacancies in a timely manner, that there's not enough professionals employed in their area, and their workload issues are exponential. If we can't compete on salary and we can't compete on conditions, we're in a really big bind.

The CHAIR: Yes. That's really interesting because we heard earlier from the Institute of Public Works that one of the things that was more attractive in local government was the conditions. Whilst the salary might not have been as competitive, it was the conditions. What you're saying about workload implications adds another layer on top of that.

ALYCIA VASILANGOS: Yes, certainly, and in the conditions within the Local Government State Award we're very proud of, but the difficulty is that if we're completely under-resourced in our engineering departments, if work doesn't get done then people get performance managed and it's problematic.

The Hon. WES FANG: This morning we heard from IPART that there are some structural issues, potentially, in the way that rates are calculated and that in order to avoid bill shock, we might need to take a longer term view of the way that we approach that issue. It sounds to me as if we might need to do something similar in relation to the provision of engineering and engineering services within local government. Would that be a reasonable prospect to start this line of questioning?

GORDON MICHAEL BROCK: Yes. If it goes to consistency and predictability about funding, I'd agree with that.

The Hon. WES FANG: Before I get to the question of funding, I'm just going to go more to workforce. I think you've indicated that certainly even if there was an abundance of funds, that securing the appropriate workforce would be challenging in any case. That aspect isn't so much a question of funding; it's a question of time because it takes time to produce somebody who can do the specific tasks that councils require of them. What mechanisms do you think can be employed to ensure that a workforce exists into the future so that local government can continue to provide services? And, putting that to the side and putting another layer over it, is it the case that an outsourced service might ultimately be required, as in things such as roads might not be done in-house; they might be done through third-party contractors et cetera? Are they really the two things we might be faced with here?

GORDON MICHAEL BROCK: The first question is—the solution is, from our perspective, to make sure that local councils are informed purchasers and providers of infrastructure services. If you're building a large bridge that is not something that you would ordinarily do, then you're going to have to engage external providers to assist in the construction and possibly the design of that bridge. But then there's maintenance work and routine work. We believe that it's important that the industry builds its capacity to deliver that in house, and the way in which you would do that from an engineering perspective is to make sure that you've got that engineering capacity to expend or spend any of the funds allocated to maintenance in the best possible way.

I know what you're getting at in terms of timing, but the first thing the Government could do or Parliament could do, in our view, is require that organisations that provide infrastructure services or engineering services actually employ qualified engineers. That gets back to the engineer registration piece we spoke about. Queensland does, the ACT does, Victoria does, South Australia's in the process of doing it, and we're talking to WA. What that then does is it means that, to each council, instead of making decisions around continuing to allocate funds away from that services to property piece that is explained in the Dollery report, it's getting back to having cheap engineers and people in the organisation that can manage that work. If they're in place and the council has the capacity to manage this funding efficiently, you'll save money. There are solutions to it, and they're not solutions that are unknown. They just haven't been adopted.

The Hon. WES FANG: But wouldn't a solution such as that require a lead-in timeframe? Ultimately, a restrictive covenant that says you must employ a qualified engineer may work in some metropolitan councils, and you've already referenced it, but ultimately there may be the lack of an appropriately skilled workforce to be able to hire that labour in. Ultimately, what you're doing is, effectively, delaying or stalling projects at the cost of the community.

GORDON MICHAEL BROCK: The workers are there. They're choosing not to work in local government. In some cases, they're not being encouraged to work in local government because councils don't see it as a priority. When the engineer registration Act was introduced into Victoria, the lead-in time for civil engineers was about 12 months. So the Act was assented to, and then the requirement to have registered engineers as described by that Act was 12 months. Other disciplines followed. Electrical engineering, I think, was next, but from local government's perspective it's mostly structural, civil and geotech engineers. There are other models. We've spoken to the Institute of Public Works Engineering Australasia about this. They're strong supporters of this legislation as well, as I'm sure they've told you or they will tell you, so maybe there's an opportunity for some of the regional councils to find solutions about sharing a professional registered engineer.

But I go back to earlier comments. If you're in the business of building, constructing and maintaining pools, roads, footpaths—a whole host of community infrastructure—you can't afford not to have these people. It's as simple as that. I would say this to the Committee: It's not a matter of us requiring or putting hurdles in this area to delay things; it's about saying there's an urgency, which the industry is not currently recognising. It needs to get on and do it, do it quickly, because the risk to the public and the potential for waste of money is just too high.

The Hon. WES FANG: Have you raised this issue with the Minister, Minister Hoenig?

GORDON MICHAEL BROCK: I've been raising this issue since—I can't remember. I've been raising this issue for a long time. We've raised this issue with the Minister for better regulation. We've raised this issue with the transport Minister. We've raised this issue with local government Ministers of several types.

The Hon. WES FANG: You would suggest, though, that where you've raised it with the transport Minister, you've raised it with the better regulation Minister et cetera, the Minister for Local Government ultimately would, through the Office of Local Government, set the parameters in relation to this?

GORDON MICHAEL BROCK: We've raised it with the Premier. The simple fact is this: The previous Government decided to require registered engineers only in the building industry, in response to some political problems at the time with Mascot Towers and Opal Tower. But you've got to make the point that it's just as important, if not more important to have qualified people working on roads, on electricity systems, on transport systems, on bridges et cetera as it is to build apartment buildings. We see this as a whole-of-government issue. It's not just going to be confined to local government; it has to be a whole-of-government issue.

The Hon. WES FANG: A doctor or a surgeon becomes a member of a college and that's how they receive their accreditation.

GORDON MICHAEL BROCK: There are different ways.

The Hon. WES FANG: Yes. I guess I'm now going down to the weeds of you've got qualifications and you want to be a qualified engineer for local government work. What would that look like?

GORDON MICHAEL BROCK: The assessment scheme that applies in Victoria, Queensland and elsewhere, you require what they call a Washington Accord-recognised degree. It has to come from a degree that's recognised as providing for engineering qualifications, so it's a four-year degree minimum and five years experience. Not everyone working as an engineer in local government will need to be registered, but you need to have registered engineers working in local government. That's how it works. If you're supervised by a registered engineer, you don't have to be registered yourself. So you've got qualifications and experience. The third part is a CPD program. This is the kicker. This is the thing that matters. People need to maintain their skills. They need to be able to demonstrate that they've maintained their skills, and that's an audited process. In those other jurisdictions, that's how it works.

The Hon. WES FANG: What entity overseas—it would be a college in a medical sense, but who does—

GORDON MICHAEL BROCK: No, in Queensland—there is a slight variation in Victoria—it's the Board of Professional Engineers. They are assessing entities. Engineers Australia is an assessment entity, so it does the quals assessment, it does the—

The Hon. WES FANG: CPD?

GORDON MICHAEL BROCK: It provides some CPD; IPWEA provides CPD et cetera. But the registry body is a government body. It's set up as an independent board. It does the registrations and takes action in relation to potential deregistration, because that's got to be an important part of the piece. So it's different to maybe the Law Society; this is a regulator at a government level. It's similar in Victoria. In New South Wales, in the building industry, department of Fair Trading does that.

The Hon. WES FANG: Would you propose the department of Fair Trading would manage—

GORDON MICHAEL BROCK: It could potentially do that. We've written submissions to the bill that was before the Parliament, and there was an inquiry, so all that work's been done. We have a preference for an independent board, only because we think that then has sufficient resource and sufficient specificity in relation to engineering registration rather than being part of a broad regulator. But I think the other thing that works well is a co-reg model: professional bodies do the assessment and then the government does the regulation.

The Hon. WES FANG: Fair. That is interesting. Mr Buttigieg, you're the union man; I'm sure you have some questions.

The Hon. MARK BUTTIGIEG: Mr Brock, in a nutshell, can you just summarise what you're here for? I missed it.

The CHAIR: Or if there's anything else that you wanted to add that you haven't already put on record?

GORDON MICHAEL BROCK: I guess the thing that we wanted to say is that it's construction of new infrastructure and it's maintenance and ongoing maintenance of existing infrastructure. Funding for new infrastructure brings recurrent costs over a long period of time.

The Hon. MARK BUTTIGIEG: I'm sorry, I've remembered something that was pertinent from earlier evidence. I asked a couple of our earlier engineer witnesses what was the catalyst for the denuding of the engineering skills.

The CHAIR: I asked this one.

The Hon. MARK BUTTIGIEG: You did, did you?

The CHAIR: Yes, about the 1993 LG Act.

The Hon. MARK BUTTIGIEG: Yes, that was interesting. Originally the answer was the private sector is too attractive because the money is better, but that would've been the case from time immemorial, I guess. The other answer that then came out was that there was this advent of getting rid of the—

GORDON MICHAEL BROCK: The requirement for the positions. There's no clear career path.

ALYCIA VASILANGOS: Exactly.

The Hon. MARK BUTTIGIEG: Would that be something you think we should recommend?

GORDON MICHAEL BROCK: Absolutely. All we wanted to say is that you need to build capacity to be able to spend money more efficiently, but just doing that is not enough. You have to have the funding model fixed as well so that you've got the additional funds to deal with the infrastructure backlog.

The CHAIR: Thank you so much for appearing today and for giving evidence. The Committee secretariat will be in touch if there are any questions on notice. Thank you so much.

(The witnesses withdrew.)

Mr GRAEME KELLY, General Secretary, United Services Union, sworn and examined

Mr STEPHEN HUGHES, Northern Manager, United Services Union, affirmed and examined

Mr DANIEL PAPPS, Industrial Manager, United Services Union, affirmed and examined

Professor BRIAN DOLLERY, University of New England, sworn and examined

The CHAIR: I welcome the next witnesses to this inquiry. I declare that I am a member of the United Services Union.

The Hon. STEPHEN LAWRENCE: I am also a member of the USU.

The Hon. MARK BUTTIGIEG: I am also a member of the USU.

The CHAIR: Would any of you like to start by making an opening statement?

GRAEME KELLY: Yes, I will, Madam Chair. Thank you. I'm just going to make a statement before Professor Dollery appears before us; Stephen and Daniel will give their own statements a little bit later on. I entered local government the very year that rate capping commenced in 1977, 47 years ago. The reason I raise it is that rate capping was introduced then in New South Wales, and introduced in 2016 in Victoria. They are the only two States in this country that have rate capping. I ask you to think about this for a moment: If every year the rate cap in New South Wales was 3 per cent below every other State in Australia, how much and how far are we behind—the infrastructure that we could have built with those funds? Our desire to become a modern local government, I believe, would've been reached a long time ago.

It's not simply about rate capping, but I believe rate capping is one of the most insidious systems that curb councils' abilities to deliver the modern services that their communities want. I have a certain cynicism about rate capping when you consider last year, in 2023, IPART gave an increase to Hunter Water and to Sydney Water of 7 per cent but capped every council in New South Wales' rates at 3.7 per cent, and every council in the regions, other than the metropolitan area, actually run water as well. That says something about the industry, about IPART's methodology. Couple that with four years ago they were alerted to the fact that they were using inferior rates of pay and industrial rates for their assessments. By that I mean they were applying the Federal modern award rates of pay as their labour costs and not the New South Wales local government labour costs.

It's those types of issues that have driven this union to pursue this inquiry and, at the same time, a Federal inquiry, a standing inquiry, into the financial sustainability of local government. You couple all of this with Federal funding. In 1996, Federal funding, under Bob Hawke, was 1 per cent of GDP or total tax revenue. Currently, today, it sits at 0.2 per cent. When you mould all of that together, local government is haemorrhaging and needs help. Going back to my early days at council—as I said, I started in 1977 on 1 March—I distinctly remember the amount of apprentices; we had 140 apprentices. Local government doesn't employ very many apprentices today, and I hope the current Government heeds that and does something about it.

But what I did see by the time I left council 12 years later, our kerbing and guttering, our road paving, our drainage, our plant workshop and others, were all done by contractors. Why? It was because as early as 1990 the effects of rate capping from 1977, over a 12- or 13-year period, had started to eat away at the fabric of the industry. As I said, it's not simply about rate capping, but you couple that with all of the funding cuts and the industry is in a dire situation. That's all I wanted to say to place that in your mind. I'm going to let Brian, who is an industry specialist and, I might add, someone both sides of politics have used over the past 15 years when they've felt the need to have somebody who is an expert in the field around local government. Thanks for the opportunity.

BRIAN DOLLERY: Good afternoon, ladies and gentlemen. The USU's submission to this Committee consists, amongst other things, of this report to the New South Wales inquiry into the ability of local governments to fund infrastructure and services. This is the report you've all got a copy of. Plus, as an addendum to that, there is a report that I prepared for the USU last year, I think, specifically on rate capping. That report, I think, has quite considerable bearing on the deliberations of this Committee because it examines, fairly exhaustively, international evidence on what they call "tax limitations". The local colloquial expression is, of course, "rate capping". It examines the impact of rate capping on Australian local government, including comparing New South Wales with non-rate-capped States and then New South Wales with other rate-capped States like Victoria, the only other one that's presently rate capped. So you've got quite nice evidence there. You've got rate capped, non rate capped—two systems performing roughly the same function and operating under roughly the same constraints.

In the main document today, in terms of the USU submission, some of the elements that I think are particularly salient to current policy questions in New South Wales local government are special rate variations, and in this report there are specific suggestions—easy, cheap to implement, specific suggestions—on how special rate variations could be improved in New South Wales, most particularly by simply changing the dates, changing the timetable at which it's implemented. Even IPART couldn't really present a sound argument against that, I don't think, because it's that simple. It doesn't cost any money or involve any hassle. In fact, it reduces costs. So I think, from a current policy perspective of something that's pretty easy to change, that would be a really easy matter to tackle. And that would be part of making the rate cut more flexible than it presently is, because presently it's really out of sorts, as you've heard from other people. I'm happy to address any questions anybody may have.

The CHAIR: Thank you. Were there any further opening statements?

STEPHEN HUGHES: If I can, I was listening to the earlier section when you were talking to Mr Brock, and I just wanted to add a few things to that. As I said earlier before I did my affirmation, I started in local government at Narrabri in 1984, when I left the army and started on the old RED scheme. I worked initially in a concrete crew, a bridge crew, and then I was in road construction and quality assurance, looking after quarries and dealing with both day labour and at times, where we had excessive work, some contractors. One of the things that I want to point out, that I need to probably put from a perspective of someone below a professional capacity, like Gordon's members, is the impact on morale and on productivity that the failure to have good qualified leadership in councils can have.

Some of the things that we have seen since the 1993 legislation, which moved away from what we'd done—actually, on 8 June 1992, the three industry unions and the employers association merged half a dozen prescriptive awards that were based on seniority. So the longer you were there, you got promoted. It wasn't on ability. There was no multiskilling. We negotiated an award from 8 June 1992 at the industry level—some of us here worked under that and were around in the industry at that time—which took things away from seniority and prescriptiveness to having a skills-based award based on the acquisition and use of skills, multiskilling and qualifications. Within a year of doing that, the then State Government moved away and then legislated to take away any requirement, when they created this new contract system for senior management, to hold any qualifications whatsoever. That flies in the face of section 349, in particular, of the Local Government Act. Section 348 states that councils shall advertise a position in such a way to attract a suitable pool of applicants at the lower levels, and at the higher levels it actually has to be advertised in a broader way to attract as many suitable applicants as possible.

The problem is, when you go to section 349 that says appointments are to be made on merit, it is at odds with what the then Government did by taking away the requirement to even be qualified for the job they were applying for. I will give you an example. I will name the council; I don't care. Armidale Regional Council, after the last amalgamation, employed a geology teacher to run the engineering department. You actually had to go four levels down from the director, from the head of the engineering department, to find a qualified engineer—that's how far down.

This is the problem. When we're bringing in people outside who are not qualified, they don't feel, I guess, in their DNA—maybe employing someone that's qualified directly as their number two might seem to be a threat to them. Maybe they don't want somebody that actually knows the job better than them to be actually reporting to council to say, "Hang on, you've employed someone as a director that knows nothing about engineering or finance or planning." So they surround themselves—in some cases the problem that we've seen with a lack of qualified engineers has been deliberately as a result of this legislation, where people have come in and deliberately not employed qualified people—in some cases I think fearful because they didn't want to be shown up by people who were actually qualified. An example about the importance—

The Hon. MARK BUTTIGIEG: Sorry, when was that requirement taken out?

STEPHEN HUGHES: That requirement is still there.

The Hon. MARK BUTTIGIEG: No, the requirement for the qualification.

STEPHEN HUGHES: Sorry, in 1993. In 1993 what happened was—when I started, you had a chief health and building surveyor, you had a chief engineer, you had a town clerk or a shire clerk. That all went. Then we wind up with all these funny names and big titles and everything else that came out, with general managers, CEOs, and then we had directors of this, directors of that. Sometimes you can't even tell what job they're in by the titles they've got, unbelievably. But this is what's come in. This is something that's currently before Parliament now—about at least rectifying those under the general manager level, bringing them back in under the award. I believe that—

The Hon. MARK BUTTIGIEG: We passed it last night.

STEPHEN HUGHES: Now that's gone through, you know what's going to have to happen now? As these contracts finish in the future and positions are advertised under sections 348 and 349, councils will be expected to employ people that are qualified. I think it'll go a long way towards bringing that back into the industry. My members—we cover people from all walks. We cover anyone from an apprentice, a trainee right up until senior levels. We've got general managers. We have engineers and we have others as well. Often they're members of both organisations. The USU has very broad coverage—almost 30,000 members in New South Wales local government. What I see, coming from outside construction, is, again, our people need good, qualified leadership above them—people that you know, if you go to them and you've got a problem on the job, can answer the question there and then. That's what we need.

One final example of what a good, qualified engineer will do—there was a guy, a qualified engineer, a director of engineering at Lake Macquarie council, who built Newcastle city airport. Any of you that have been to that, that was built by a council—not by the local council at Port Stephens, not by Newcastle council. There was an engineer that had the fortitude and the ability to motivate his staff, to get his councillors onside, to put in the quote and the bid, and to travel outside their local government area and go and build one of the biggest airports in this country—a good airport, built by council labour under a qualified engineer. I just wanted to put that on record if I could, thanks.

The CHAIR: Noting the time, we'll move to questions. Did you have anything further to say?

STEPHEN HUGHES: I've got other stuff I'll answer later.

The CHAIR: Mr Papps, did you have anything further to add?

DANIEL PAPPS: I'm fine, Chair. Thank you.

Dr AMANDA COHN: Thank you, Professor Dollery, for the work you have put into this really extensive submission. I have a couple of questions about special rate variations. The rate peg is notionally meant to stop bill shock for residents and ratepayers. When you look at some of the special rate variations that we've had in New South Wales over recent years—I'm sure there was bill shock in Strathfield with a 92.83 per cent special rate variation. I'm interested in your perspective on that and whether rate pegging in this instance is actually serving its purpose. Then I have a follow-up question about amalgamated councils.

BRIAN DOLLERY: Yes, rate pegging is, as I argue, a highly questionable process in terms of achieving its intended aims. Lots of people have speculated about the real purpose of the rate pegging regime in New South Wales. It's a useful political tool for State governments of both persuasions. It's an especially useful tool for local councils when criticised by residents because the council always retorts, "Look, you don't look at us. Go and tell the State Government about the rate cap. If we had reasonable funds, we'd be able to address x, y or whatever problems people are raising." To the extent that it addresses rapid price shocks, as you can see, broadly speaking, with a huge lag, rate caps do roughly follow prices, but the problem is the lag is so long. So in the long run, people end up anyway paying, but there's just this massive lag. The lag itself—the people end up paying by having ageing and old infrastructure. So the bill arrives. The local communities pay the bill one way or another.

Dr AMANDA COHN: I was particularly interested with table 2 in your report, which detailed the really whopping SRVs we've seen in the forcibly amalgamated councils. During that amalgamation process, there was some compensation provided by the State Government to those council areas. Do you think that was sufficient in 2016 and do you think that that's sufficient now?

BRIAN DOLLERY: In short, no. The 2016 amalgamation process—as we've demonstrated in other papers in the peer-reviewed literature, it didn't achieve any of its intended aims. In fact, it was supposed to enhance financial sustainability in New South Wales local government. As you can see from this table, it had precisely the opposite effect. You look at some of the amalgamated—Armidale; 58.8 per cent, for example. What do you think is going to happen if you amalgamate Armidale with Guyra, when Guyra is a huge area with ancient infrastructure with largely unsealed roads? That is going to cost someone somewhere something. It was a disastrous thing. I might just remind the Committee that the Coalition never intended that to be a forced amalgamation process in the first place. If you read Don Page, the original Minister that instigated that whole fit-for-the-future process, you will see that he specified in writing that it was supposed to be voluntary amalgamation. Somehow—you guys in the parliamentary system know better than anybody else—that morphed into a forced amalgamation process.

Dr AMANDA COHN: For this Committee in considering our recommendations to address financial sustainability broadly, do we need to be considering some sort of special consideration for those council areas that were subject to forced amalgamation?

BRIAN DOLLERY: Indeed. Certainly, yes. I think the current Minister has recently ruled out—said that councils that want to de-amalgamate have to wear the cost themselves of de-amalgamation. That's an echo from Queensland when they had their infamous 2008 amalgamation process. There was a popular uprising against it, especially in non-metropolitan areas, and the State Government there also said that local governments must, even though they were forcibly amalgamated by the force of law, by the State Government—nevertheless, if they wanted to de-amalgamate, they had to pay for it themselves. I think that runs against natural justice.

Dr AMANDA COHN: Yes, it was the position of the Minister—the bill that passed last week now allows a one-off grant just up to $5 million or an interest-free loan, but it's still up to the council to account for it. I wanted to ask you about interstate comparisons. You've criticised rate pegging, as have many other bodies that have submitted to this inquiry. Obviously, Victoria is the only other State that has a rate peg. I'm interested in your perspective on what's happening in other States and how well that's working. Do ratepayers in other States have catastrophic bill shock as a result?

BRIAN DOLLERY: No, in short. One of the papers that I do have a paragraph on in this report is a comparison between South Australia, un-rate-capped, and New South Wales, a rate-capped State. South Australia attempted to introduce, incidentally, a rate cap there something like 15 years ago. Fortunately for them it was unsuccessful. But that's a nice comparison, because New South Wales has got the longest running rate cap, way back to the early 1970s, as we've heard earlier this afternoon, and South Australia hasn't. So you've got nice long-run comparisons of, for example, infrastructure backlogs and similar kinds of things. I think that paper is particularly salient in regard to your question. What's the difference? The difference is you're much better off not having a rate cap. It isn't the kind of price shocks that people fear.

STEPHEN HUGHES: Can I just quickly add—from our experience, both from the 2004 amalgamations and the 2016 ones, the councils that are most in dire ongoing need of financial support have been the amalgamated councils on average. That's where we also have a much higher level of industrial problems I think as a result of the financial pressures experienced within those councils leading to stress on the staff in relation to unrealistic workloads.

The Hon. MARK BUTTIGIEG: Can I just ask a follow-up? You mightn't remember me, Professor, but you supervised my honours thesis.

The Hon. WES FANG: Did you pass?

The Hon. MARK BUTTIGIEG: Yes, I did.

The Hon. WES FANG: We blame you, Professor.

The Hon. MARK BUTTIGIEG: With the South Australian comparator, is there any regulatory oversight of rates from the State Government, or is it purely on the councils to determine what's required and they're answerable to their electorates, presumably?

BRIAN DOLLERY: In South Australia, yes, the rate setting is a council rate determination.

The Hon. MARK BUTTIGIEG: But there's no State Government regulatory oversight?

BRIAN DOLLERY: There's plenty of regulatory oversight—a myriad of oversight legislation—but nothing that fixes the rate determination.

The Hon. MARK BUTTIGIEG: No, but if a council does something that's deemed a bit out there, in terms of a rate increase or whatever, is there any mechanism at the State level that kicks in and says, "We've got a right to review that or come in over the top"?

BRIAN DOLLERY: There may be but, I'm sorry, I'm not aware of it.

STEPHEN HUGHES: I think what's lacking, if I can, is that OLG are significantly underfunded to conduct the proper auditing that's needed. It's one thing to give the money that's needed, and we know the money is needed. But it's also important to ensure that the money is spent correctly and not wasted by some councils. When you look at the Central Coast Council, which was amalgamated and the council was sacked as a result of a $565 million debt, that debt just didn't build up overnight. If proper measures had been in place, with auditing at the State level through OLG—and I'm not critical of OLG; it's a matter of resourcing—it never would have got to that. As a result, 300 employees were made redundant as a result of what happened at Central Coast Council—300 less employees that don't have jobs anymore because people above them that they relied on ran the council into the record debt for any council in this country, $565 million.

GRAEME KELLY: And the general manager got a $400,000 payout.

STEPHEN HUGHES: Yes, and then he's the general manager elsewhere now. Anyhow.

The CHAIR: Did you have further questions?

The Hon. WES FANG: Are we just airing gripes?

The CHAIR: Order!

The Hon. WES FANG: No, there's a procedural fairness resolution that we're not supposed to be—I'm just making that point.

The CHAIR: Order! Dr Cohn has a question.

Dr AMANDA COHN: I have one last question about cost shifting. People in the local government sector have been talking about cost shifting for a long time. I know there was some detail of that in the report, but my question is to all four of you. Could you share with the Committee and the public some examples of cost shifting across different sectors impacting local government?

BRIAN DOLLERY: Yes, I think that one interesting, at least—my colleagues have other perspectives, but one that strikes me is the pensioner rate concession. If you reflect a little bit on the theory of federalism, which in public economics is a basic theory you can apply to multi-tiered government, distributional questions should be a matter for central Government, certainly not the lowest tier of government, local government, as it is normally in Australia. For example, unemployment is dealt with by the central government, not by State and local governments. All these distributional questions are best dealt with at the highest level.

Under our Federal system presently, State governments force local councils to offer pensioner concessions and then subsidise them. But the degree to which they subsidise comes nowhere near to meeting the full cost of the subsidy, firstly. Secondly, there are terrible distributional consequences because small rural councils have got the greatest proportion of pensioners living in them, so that the poorest councils bear the greatest costs of this redistribution. That's a question that can be addressed at the New South Wales Parliament level, but also pressure should be brought on the Federal Government to step in there. But I'll leave other examples to my colleagues here.

STEPHEN HUGHES: If you want specific examples, I think it's in Gwydir council out at Bingara, in order to attract a local doctor—which a lot of the regional areas have a hard time doing—they actually provide secretarial support and, I think, provide housing in order to attract somebody to town. That's not normally out of council's budget. We've got the councils out there—when COVID hit, the Federal Government of the day jumped in and put out money there to offer money to assist businesses and people that were affected by COVID and not getting to work, but they didn't want to fund councils at all. We had to go to the then State Government because we had childcare centres run by councils who were not going to receive one red cent from the Federal Government.

We were lucky enough—and I'll say this. Shelley Hancock, the Minister for Local Government at the time—we went to her and she intervened. We did the COVID splinter award that we did at our level as well. There was nowhere else in the country that provided job security. We walked away temporarily during that period from some of the things in the award about work locations and the jobs you did in order to keep as many people working as possible and providing services because, without local government, many communities wouldn't survive. But we've got child care and we've got aged care, which generally aren't the responsibilities of local government.

It's not just roads, rates and rubbish. We've got councils that provide the local RMS service out of their front counters. There are more and more things that councils are taking on—public transport in some cases. In order for the council to provide a community with things that people in Sydney and in the big communities expect just for being a local citizen, bush councils, in particular, are having to put their hands in their pockets with a much lower rate base, often with much larger geographical areas, and take on and fund services that other councils don't have to do.

It's a bit like what Graeme touched on earlier. When IPART gave 7 per cent last year to Sydney Water and Hunter Water for their increase in water fees—I'm under Hunter Water up at Cessnock. If I was at Singleton, just up the road, my combined rates and water charges—and I don't have a swimming pool and I'm not running sprinklers. I pay more for water with Hunter Water since it was corporatised, because of the dividends that come out, than I do for my council rates. If I was at Singleton, 50 kays up the road, I'd be paying half of what I'm paying now because my water and sewerage costs would be part of my rate bill.

There are 111 councils in regional New South Wales providing water and sewerage, who also have to provide roads, libraries—not all child care, but roads, rates, rubbish and all the rest of the stuff that councils traditionally provide that got 3.7 per cent because of IPART. They're not only providing the water and sewerage on a much smaller population base, because here's the thing. Governments always come out and the bureaucrats say, "Big is better". If big is better then why is it that Sydney Water, with the amount of customers it's got, and Hunter Water, with the amount of customers they've got, can be given 7 per cent, but a bush council with its own infrastructure that has to provide water and sewerage—plus all the other services—gets 3.7 per cent?

The Hon. WES FANG: Mr Hughes, how did you feel, then, about the fact that Sydney Water and Hunter Water were protected from privatisation by the Labor Government, yet the Labor Government blocked the protections for rural and regional communities?

STEPHEN HUGHES: I'm happy to answer that, and I'm going to say something that's critical of the Labor Party at the time. In 1996 there were 27 power distributors in this State. My wife and my sister worked for NorthPower, whose main office was from Narrabri. It covered out to Bourke, out to Gunnedah and a massive area of the State. It was rated number seven out of 27 power distributors. We had linesmen with local knowledge in every community, like Gwabegar, Pilliga and all that. If a storm hit, there were people that knew the area and could get out and respond very quickly and reconnect the electricity. I will say this. Was it under Michael Egan at the time?

The Hon. WES FANG: Yes.

STEPHEN HUGHES: And I think Costa had a bit to do with it.

The Hon. WES FANG: Probably.

STEPHEN HUGHES: They merged that down to half-a-dozen distributors at the time. At Narrabri, where I lived, they called the staff in. I was an energy organiser, briefly, at the time. They called the staff in and all the regional ones got laid off; they were made redundant. They called the staff in and got rid of most of the staff, and they contracted the work out. Here's the thing when you say about protecting from privatisation. Tell me one area from either side of politics where something has been privatised where it's worked out cheaper. In the power poles, before the last round of power privatisation, everyone drove around and saw on the poles, from the ETU and the USU, "You will pay more". Well, look at what we're doing today.

The Hon. WES FANG: You can thank the Labor Government for that, but also they refused—

The CHAIR: We are straying dangerously outside the terms of reference here. Order!

Dr AMANDA COHN: You've interrupted my time to ask a political pointscoring question without seeking the call from the Chair. Can the witnesses please finish answering the question that I asked?

The Hon. WES FANG: I was just asking for elucidation.

Dr AMANDA COHN: You'll get your own time for questions.

The CHAIR: Order! We'll hand over to Dr Amanda Cohn.

STEPHEN HUGHES: All I've pointed out is that the question about protecting Hunter Water and Sydney Water—privatisation does not lead to a better outcome. What it led to in the power sector was many less jobs—a much inferior system where the people that need to go and reconnect the lines and do the maintenance work are no longer there, so bigger delays. We had the floods in Cessnock. When was the last one? About 10 years. We had the Pasha Bulker, and we had one after that.

The Hon. WES FANG: I was there in Newcastle when it happened.

STEPHEN HUGHES: We went without power for one week in town there, and there's other people. Why is that? It wouldn't have happened 20, 30 years ago.

The Hon. WES FANG: And yet Labor treated us like second-class citizens on water. It was an absolute disgrace.

The CHAIR: Order!

STEPHEN HUGHES: I'll just finish with this. Power was very cheap back then. There were a lot more workers and it was all owned by the local county councils.

The Hon. WES FANG: Labor should just apologise.

Dr AMANDA COHN: Thanks, Mr Hughes. I appreciate you're answering the questions that got asked, but it was an interruption.

STEPHEN HUGHES: No, he's all right.

Dr AMANDA COHN: We had been on cost shifting, and you started with an excellent example. Professor Dollery, just before we go to other members, were there other examples of cost shifting from the—

GRAEME KELLY: Can I just raise one issue: the emergency services levy. Whilst that's under review now and we've put a paper in to that review, there's an additional cost on councils, of 11.7 per cent, and I do recall that it was early last year that the emergency services levy was unfunded in the State Government's budget.

Following the elections, the new State Government issued a requirement to all councils to pay a levy. Whilst my maths mightn't be right, it is just an example. We had a general manager call us to say, "What the hell's going on? Our rates have been set by IPART, and months later we get hit with an emergency services levy that's unfunded—and came up with an answer which led to the review that's taking place now. As you know, councils have the red fleet that they have to account for, when they don't own them. There's a whole myriad of things that are cost-shifted onto local government. When you couple that with the dire straits of their current financial circumstances, it just gets worse. They're just some of the examples.

Dr AMANDA COHN: Thank you. I'm sure we'll have some questions about the red fleet for the Audit Office after the afternoon tea. Did you want to add anything, Mr Papps?

The Hon. STEPHEN LAWRENCE: Does the union support any changes to the Local Government Act to restrict what activities and services and businesses local government should be involved in? Obviously, through the prism of financial sustainability?

DANIEL PAPPS: Does your question go to questions of procurement of services?

The Hon. STEPHEN LAWRENCE: More provision of services and the like to the community. There's been earlier evidence about mission creep, this idea that councils are getting involved in too many things; that's impacting sustainability. Is there any firm policy view about that or would you rather have the view that it's a matter for councils?

DANIEL PAPPS: I think it's a local determination. The needs and services of a community in the eastern suburbs of Sydney might be different from needs and services of a community in rural, regional New South Wales. The point I would make, though, given the shocks of COVID and the views communities have taken about the centrality of local government in delivering services, I think we've seen a general sense or sentiment from the community that there are more things local government can do. I don't think we should be restrictive in a view about there are things they can or shouldn't do.

I think local communities can make those decisions, provided that they're making decisions that are not unduly hampered by what we say is an unfair system of funding. I think that's really the key point. There are probably things that councils want to deliver and services the communities would sorely need, but they feel compelled either not to deliver them or deliver them in a different way because of concerns about funding. So I don't think it would be helpful to be prescriptive about "You can only do roads, rate and rubbish." I think that would be a step backwards rather than a step forwards in embracing the needs of the community and ensuring that those things are funded.

The Hon. STEPHEN LAWRENCE: So there's no real evidence, in your view, that councils are doing a whole lot of profligate things and that's why there's this problem. It's more that there's an artificial cap that, over the years, has compounded and led to this unsustainable situation?

DANIEL PAPPS: I certainly don't have any evidence of any systemic issue about councils doing things they shouldn't be doing. You'll always be able to find an example or two. But, as a general observation, though, there's not a systemic problem with councils over-delivering or over-promising.

The Hon. STEPHEN LAWRENCE: In terms of financial stability, Mr Kelly, is it fundamentally about the formulas for grants from State and Federal governments, as well as the rate-capping system and the special variation rules and so forth? Is that fundamentally the compass of the issues? Is there anything else that we should be aware of, in terms of novel, left-field, maybe international ideas about how local government can be funded?

GRAEME KELLY: No. I think it's central to the problem. As I said earlier today, we're being starved of funds—completely starved. You ask councils that have the bulk of the privatised workforce why they're doing it. It is because they can't afford, they say, to maintain the staffing levels they've got, and it's cheaper to pay contractors, who, a lot of the time, have inferior plant and equipment. I can give an example in the local shire I live in, in Sutherland. I was watching one day, on a particular afternoon when a company come in to town—my wife happens to be the principal of the school. Out the front of the school they were mowing at school finish time. No signage, nobody watching to see that the rotary blades weren't throwing objects out from underneath the vehicles or the plant, no warnings, no street signs—no nothing. They undercut by inferior plant, equipment et cetera, and the council turn a blind eye to that because, simply, they can't maintain their workforces.

The Hon. STEPHEN LAWRENCE: There's no other way of raising money that we should be thinking about? It's fundamentally about rates and State and Federal grant formulas?

DANIEL PAPPS: In addressing that particular question, I think rates and grant formulas are probably the preferred method, from our perspective, of funding, because I think the next obvious option is a user-pays system. If councils can't raise rates to be sustainable—a simple example is they will increase the cost of entry at a pool to cover the cost of that pool. We say that's not an optimal way to fund local services, particularly in a cost-of-living crisis. You've got families and communities who are looking for cheap, affordable, accessible services. So if we shift away from an emphasis on rating, which spreads the costs out across the whole community in, we say, a fairer way to a user-pays system, it is going to disadvantage those people who are least able to afford the services. I think that's probably the opposite of the mission. We spoke about mission earlier. That's the mission of these local councils. So if we're talking about a different system, the next obvious one is user pays and it's not something that we would, in general, be supportive of being a main pillar of council funding.

The Hon. MARK BUTTIGIEG: Let's live in this hypothetical world where the rate cap has gone. Maybe this is for you, Professor. I imagine one of the consequences of that might be that the State and Federal governments will say, "You're accountable to your electorates. If you want more money, keep putting the rates up." This tension between the grants and the rate cap model lifting is—have you given any thought to that? What's the view on that? Would government still have to step in, based on some sort of modelling, and say, "We understand you can increase your rates, but we're still going to give you X amount of money based on X, Y, Z"?

BRIAN DOLLERY: Yes. In Australian government, the most significant form of grants to local government are Federal Government FAGs, financial assistance grants. They've been determined by the Federal Grants Commission, and they use a specific formula. It's actually held up in the public finance literature as the best example of intergovernmental funding, more or less, worldwide because it's outside the political process. There's a formula, and various new governments have come and gone, and they haven't fiddled around with it. What one needs is some system like that, that each council, in accordance with an agreed specific formula, gets what it's due, but then it's got latitude in terms of local autonomy. The local community wants a swimming pool. They want sports fields. They want something extra. Fair enough, but then they must pay for it, because they're getting their fair transfers from other tiers of government.

The CHAIR: Professor Dollery, can I ask—

BRIAN DOLLERY: If I might just address the earlier point, please. There's a myriad of other regulations. This afternoon, we're talk about rate pegging. But there's a myriad of other regulations on local government pricing in New South Wales. For example, as was mentioned earlier, water utilities outside the metropolitan areas are local government operated, and they represent a significant source of revenue to local government. There is some published material on that. Some of you with long memories might remember the attempts at water regionalisation, where they wanted to rip water utilities off local governments. There was a bit of a backlash, so there is published material there.

The Hon. WES FANG: We know.

BRIAN DOLLERY: But, for instance, water tariffs are regulated by the State Government, so local governments don't have latitude there. They can't charge long-run marginal costs, to use econo-speak here. That's the rational way. You want to charge the real long-run cost of the service so that at least it's paying its own way, not being cross-subsidised by other services. Those things could also be addressed.

The Hon. STEPHEN LAWRENCE: Just on that, is there a role for joint organisations in terms of the provision of services in a way that would meet State and Federal government expectations that would then create an environment where you could have more latitude and less concern about things going financially AWOL or—

STEPHEN HUGHES: What should have happened with the joint organisations is—I don't know why they didn't get their buying power together to say, when it comes to supplying fuel and supplying certain things, get together as a group of councils and get the best possible deal for the supplies that councils are purchasing. Some of that is probably due to the fact that those smaller bush councils want to be able to deal with local businesses, which I can understand, that rely on them to purchase their fuel and their protective clothing and various supplies from them. I have raised this in the past, as well, elsewhere in our industry. One of the things I thought the joint organisations could have been handy for out in the bush, in the north-west in particular, would be to look at pooling their resources to actually try and attract some of those professionals, from the engineers, for example, at a regional level. Some of them might want to live—

The Hon. WES FANG: Like an amalgamation?

STEPHEN HUGHES: —full-time out in certain towns in the far west, but may be prepared to live within one of the larger communities within the region and provide that expertise—you know, using the joint organisation to provide that to the councils in the region. That made sense to me. Can I just finish this? You asked about user pays. I'm going to give you a specific example with the problem on that. Not long after the previous Government was elected, Don Page, the Minister, came to us and said Moree council had sought to corporatise and wanted to set up the swimming pool, the Moree aquatic centre, as a corporate entity. We said we didn't see any point to it. We thought it would be more expensive. However, we did get protections, I will say, through the

Minister of the day, even though he was from the other side of politics from what we are using to dealing with. We actually had a good relationship with those Ministers, I will tell you that now.

What he did was make sure that our industrial instrument, our State award, would continue to apply to those staff that were performing those duties that we traditionally perform within local government in the pools. What ended up happening, though, with the person chairing that—so they set up the corporate entity. The person that was chair of it came from Sydney. He would fly to Moree every so often to go and meet with the committee. He wasn't local. They then put the fees up an enormous amount for ordinary pool entry. Now, Moree owned three pools—they owned Mungindi and Boggabilla and Moree. The three communities are largely Indigenous communities. What happened in Moree when they corporatised it, they put the charges up massively and the local Indigenous kids and other kids from families that didn't have the money to pay the much higher charges no longer had a local pool to swim in. Quite frankly, you wouldn't swim in the river out there. I'm not being a leftie greenie on this stuff, in saying this. Sorry, I'm not trying to be critical of anything with it.

Dr AMANDA COHN: Nothing wrong with being a greenie.

STEPHEN HUGHES: I believe in environmental stuff. I believe in conservation as well.

The Hon. WES FANG: Me too.

STEPHEN HUGHES: But the river system out there is full of cotton chemicals—and the cotton industry is important. But the fish that used to exist when I was a young fella out there are gone.

The Hon. WES FANG: Still a young fella.

STEPHEN HUGHES: You wouldn't want—

GRAEME KELLY: That's not what someone said to him coming up here today.

STEPHEN HUGHES: Yes, he called—yes. You wouldn't want the poor kids and those local people in the community that could no longer afford to use the one council-operated pool in Moree having to swim in a river with the problems that you've got there with potential drowning, because of the snags, and other issues that are in there.

GRAEME KELLY: It ultimately went broke.

STEPHEN HUGHES: It went broke—that's correct. It went broke, and it went broke because the cost of running the new board was more money than what they were bringing in, even though they put the charges up.

The Hon. WES FANG: And someone from Sydney as well.

STEPHEN HUGHES: And another one that I'll finally finish with on this is that the State Government itself is complaining, rightfully so, and suffering as a result of having—what is it, $1.6 billion of GST revenue stripped from you? To me, what makes sense is that whether you're State Government—where the Federal Government has got control and where they hand funds to the State Government, and where the State Government controls and also the Federal Government is giving money to local government, there should be a three-year plan in advance. It would only make sense that both the State and local governments relying on that funding collected at that level can plan ahead and plan budgets in future years.

From both sides of politics, whenever they get dudded federally at the State level, they complain. They should realise that the local governments are in the same boat and all they are asking is the same thing the State Government is asking for. Do that for them too, please. Our State award provides council certainty for up to three years as to what staff costs are going to be. It's the only thing they can budget on. How do you think they go when they're asked—and they were asked this under Destination 2036. They were asked to put forward 10-year forward planning estimates on budgets when they didn't even know what rates they were going to get the next year.

If the council can control what it's going to ask from its own community at least three years in advance and let the community know—and if the community don't like it, throw them out—that is what should be going on. It is unfair to expect the State Government to be able to forward plan without knowing what the Feds are going to give them, and it's just as equally unfair that local governments should have it applied to them. I ask you, if you don't like what the Federal Government has just done to this State, don't do it to local government.

The Hon. WES FANG: In relation to the red fleet that you raised earlier, are you aware that there was a bill put forward in this term of Parliament that the Labor Party rejected in relation to that issue?

GRAEME KELLY: No.

The Hon. WES FANG: Okay, I just thought I would raise that. The other thing I wanted to raise was—and I note you said you had 47 years in local government. That was the same year I was born.

GRAEME KELLY: I don't look it, do I?

The Hon. WES FANG: Not at all. That was the year that rate pegging was introduced.

GRAEME KELLY: Yes.

The Hon. WES FANG: Is it fair to say that the issues have been consistent since that time? Have you found that the funding issues have been the same, or have they fluctuated over time?

GRAEME KELLY: I think you can look at that depending on what sort of Federal assistance grants you got at those corresponding times. Some benefited at other times. I haven't got those figures. But this has been a slow and steady deterioration to what I would regard as the worst shape of local government in that 47 years.

The Hon. WES FANG: So you think now is the worst time—

GRAEME KELLY: Yes, the worst. The worst.

The Hon. WES FANG: —that we've seen in that—okay. In your opening statement you said that you have had concerns for some time, but you've been really pushing to have these issues looked at. This hasn't been just a recent thing; you have been pushing for quite a while.

GRAEME KELLY: That Federal inquiry, we have got it up now. I started in 2018 at the ALP conference in Adelaide.

The Hon. WES FANG: What about in relation to this State?

GRAEME KELLY: This issue has been an ongoing concern since not long after—well, around the Bob Carr days. This is something we have agitated for for a long, long time.

The Hon. WES FANG: Did you have engagement with the Minister in the lead-up to this inquiry? Did you propose terms of reference and the like for—

GRAEME KELLY: For this?

The Hon. WES FANG: Yes.

GRAEME KELLY: No. Let me just go back on that first question, though. We were a part of—a lot of people wouldn't know this, but we worked successfully with the Liberal Government from 2011—

STEPHEN HUGHES: The Liberal-Nationals Government.

The Hon. WES FANG: Thank you, Mr Hughes.

GRAEME KELLY: —until recently, when they lost government. We had a relationship with Don Page, Paul Toole—

STEPHEN HUGHES: Shelley.

GRAEME KELLY: —Shelley Hancock—

STEPHEN HUGHES: Wendy.

GRAEME KELLY: —Wendy Tuckerman. We didn't get on too well with—

STEPHEN HUGHES: Gabrielle Upton.

GRAEME KELLY: —Gabrielle Upton. She didn't like us, but that was fine.

The Hon. WES FANG: She didn't like me either, but that's okay.

The Hon. MARK BUTTIGIEG: Can't blame her for that.

GRAEME KELLY: The average is where we did okay. We worked very constructively and there was a ministerial advisory committee set up. The USU had three people on that. That committee was to try to have a forum to raise all of these issues, and we consistently raised the issue around rate capping.

The Hon. WES FANG: Did the Minister promise you that this would be the panacea and this inquiry would be the answers that you're seeking?

GRAEME KELLY: No. I've had no promises whatsoever. I can guarantee you that.

STEPHEN HUGHES: We were working towards trying to do this with the previous Government. Had they have been elected, we would have expected to do the same thing.

GRAEME KELLY: It was always our goal.

The Hon. WES FANG: They probably should have been.

STEPHEN HUGHES: I think that they were surprised—Don Page, Paul Toole, Shelley and by the time that Wendy came along—that our union can work with whoever we need to work with. We care about local government and we come from it. We work with good Ministers and we work with good chiefs of staff. We don't do that just because someone's on one side of politics or another. If someone has the same interests and we're trying to do good, we work with them. That's what we sought to do.

GRAEME KELLY: The end game is a sustainable industry that employs a lot of people and that delivers a modern Local Government NSW. That's all we want.

The CHAIR: In your opinion, Professor Dollery, what are some of the main factors leading you to believe that local government funding is insufficient?

BRIAN DOLLERY: By far the biggest factors are the local infrastructure backlogs. There is, let's say, good political economy grounds for that as well. You hear it often, reading the local press and on local TV and radio stations and things. Infrastructure, maintenance and renewal are largely invisible-type processes from the point of view of the local community, whereas other services, for example, garbage collection—imagine if you cut back on that. Everybody notices it and you are going to get an immediate outcry. Local politicians pay a price immediately, whereas you can defer and delay maintenance and infrastructure upgrades, which are hugely expensive.

Delaying maintenance itself builds up a larger capital cost in the longer run because then it's more expensive to get things back to a satisfactory condition. In that respect, the infrastructure backlogs are a measure or a canary in the coalmine, if you like, for local government because it tells you a larger story. Over the last 30 years I sketched some of this stuff in this report. There have been attempts at measuring the size of the local government infrastructure Australia-wide and for different local government systems, but that's extremely difficult to do. In part, that's difficult because local accounting and auditing practices aren't what they should be and they are getting worse, as we also note in this report. The figures are dicey, but everybody has agreed that it's a massive problem. For me, that's by far the biggest index.

STEPHEN HUGHES: There are two reasons for that, just quickly. You've got, obviously, population growth, which is not consistent and so you need new infrastructure. But one of the biggest problems we're facing regionally, again, where populations are either in decline or static, is ageing infrastructure. Infrastructure doesn't last forever. We need the money to replace what's now coming into disrepair as well.

GRAEME KELLY: Can I make one last comment? You may very well rule this as being insignificant, but one of the things I have just written a report on for my executive is the issue around housing affordability for council workers. I've had many general managers ring me. I know you are a former nurse, Chair, and I mean no disrespect to those who are termed essential services, like nurses, fire, police and all of those. The reality is, as I think COVID demonstrated, that if you don't think a council worker is an essential service, then we're living in fairyland, because they deliver many more services than the average person thinks about.

The Hon. STEPHEN LAWRENCE: Including water.

GRAEME KELLY: Including water, yes.

The Hon. WES FANG: Provided it's not privatised by you lot.

The CHAIR: And sewer, in the regions.

GRAEME KELLY: I did a report at a conference last year to our branch conference where, over the next seven years, 12,500 of the old-time employees are going to leave because they are in the old super scheme. We've got to replenish those. You would ordinarily think that those people would have been around a long time and possibly have been able to afford a home in the day when they were getting married or whatever they were doing. Today, it's a little bit more different. I've got general managers at Randwick, Waverley, northern beaches and others telling me that they won't be able to staff their councils unless something is done about affordable housing and an acknowledgement that council workers are essential to services of every day communities. I can tell you that, in the Sutherland shire, 95 per cent of the outdoor workers come from the South Coast. In Ku-ring-gai Council, there are none from the shire or municipality. They all travel from the Central Coast and north-western Sydney. It is across the board. They are travelling long distances. Some from the Blue Mountains travel from Lithgow to work and it's all because of housing. So if there's any scope—

The Hon. MARK BUTTIGIEG: Presumably, you would like to see one of the recommendations that, along with other essential workers, council workers be included in that category.

GRAEME KELLY: Absolutely.

STEPHEN HUGHES: Someone's got to pick the rubbish up and do the work that needs to be done.

The Hon. STEPHEN LAWRENCE: Is that also an argument for council getting more into property development? That is something that I pushed when I was on Dubbo council because we were facing this acute shortage. It's a profitable industry. We had all the capacity to do it. We had been involved in land development already. Is that an argument for those sorts of factors too?

GRAEME KELLY: It's back to the future, isn't it? We started off under the English system. My boss on Canterbury council was an apprentice electrician working on Sydney city public housing owned by the city council. You know what they have done with most of their buildings. Like all of their work, they contract out literally hundreds of millions of dollars worth of work. They use a company called Skyline Projects. Sutherland council is one of the worst in Sydney—Waratah Group Services, Snippers and a whole heap of others. They just contract it all out. Those people would obviously travel long distances because those companies and their depots aren't in the shire and aren't in the city, unless they are and they have been given the land or the space by the city council. An acknowledgement that council workers are essential, if you could start talking about that, would be very much appreciated, because they are.

STEPHEN HUGHES: Can I just say that I appreciated all the questions from everyone. I thought they were good.

The Hon. MARK BUTTIGIEG: Except Wes.

STEPHEN HUGHES: I thought everyone asked valid questions.

The Hon. MARK BUTTIGIEG: Only kidding.

GRAEME KELLY: I don't think they need us to rate them, Steve.

The Hon. WES FANG: I appreciate the feedback.

The Hon. STEPHEN LAWRENCE: If you want to rate Wes, feel free.

Dr AMANDA COHN: Thank you for your answers.

STEPHEN HUGHES: If we are being evasive and not prepared to answer, that's when you have to worry.

The CHAIR: Thank you so much for your evidence given today. The secretariat will be in touch if there are any questions on notice. We will now have a short break.

(The witnesses withdrew.)

(Short adjournment)

Mr BOLA OYETUNJI, Auditor-General, Audit Office, sworn and examined

Ms CLAUDIA MIGOTTO, Acting Deputy Auditor-General, Audit Office, affirmed and examined

Mr AARON GREEN, Assistant Auditor-General, Audit Office, affirmed and examined

The CHAIR: Welcome to our next witnesses. Thank you for making time to give evidence to this important inquiry. Would you like to start by making a short opening statement?

BOLA OYETUNJI: Thank you for the invitation to provide evidence to this inquiry. This is my first appearance before the parliamentary inquiry as the Auditor-General for New South Wales. I'd like to take this opportunity to acknowledge the substantial and impactful work undertaken by my predecessor, Margaret Crawford, PSM, who tabled in Parliament the reports we will refer to today. Our financial audits of local government entities provide independent opinions on the financial statements of New South Wales councils. Our opinions provide assurance on whether their financial statements comply with accounting standards and relevant laws, regulations and government directions. Our performance audits assess the effectiveness, efficiency and economy of government programs and services, and provide recommendations to assist in improving outcomes.

We do not comment on the merits of policy decisions, including policy decisions relating to funding levels in the local government sector. For example, the Audit Office cannot comment on the merits or otherwise of a council's decision to apply for a special rate variation, nor do we comment on the efficacy of the rate peg. While our financial audits consider each council's ability to meet their existing and ongoing obligations, they do not consider the effectiveness of specific funding and spending decisions. However, the Audit Office has completed several performance audits that provide insights and learnings about how councils assess and plan their resources to respond to service delivery obligations. While the reports are based on audits of the activities of specific councils, many of the insights and recommendations have relevance to the sector more broadly and, as such, may be of assistance to this inquiry. I will briefly mention a couple of them.

Our report on the financial management and governance in MidCoast Council assessed whether MidCoast Council had effective financial management arrangements that supported councillors and management to fulfill their financial stewardship responsibilities. The report found that the council had not effectively carried out long-term financial planning to address its identified long-term financial sustainability challenges. We recommended that the council monitor and address changes in the external environment that would impact on the council's financial sustainability. The report also identified gaps in the reliability of asset condition data, which is required to accurately inform long-term financial planning.

Our 2020 report on *Governance and internal controls over local infrastructure contributions* assessed the effectiveness of governance and internal controls over local infrastructure contributions collected during the 2018 and 2019 financial years by four local councils: Blacktown City Council, Central Coast Council, City of Sydney Council and Liverpool City Council. The report provides insights for the local government sector that outline the importance of sound governance and management reporting so that local councils know whether they are on track to collect sufficient funds to deliver required infrastructure, whether alternative sources of funding need to be considered, or whether other council strategies or policies need to be revised. Findings and recommendations from these reports are directed at the local councils subject to the audit but are relevant to all local government entities.

Finally, I have started engaging with the local government sector to listen and better understand their challenges. So far I have met a couple of CEOs and the OLG and I look forward to catching up with others as I go forward in my term. We are happy to take any questions you may have.

The CHAIR: I might start with some questions. Firstly, can we go through the audit reports released about local government in recent years? You have alluded to it in your opening remarks, but what problems have you identified with the sector?

BOLA OYETUNJI: I will start and I will have my colleagues chip in. One of the things I have seen in the short period of my engagement, and I think it was mentioned earlier, is fundamentally capabilities and skill set. In some areas it is always difficult to engage staff, so the workforce plan needs to be beefed up. When you look at the environment, not only in local government but across government and across businesses, that is a problem worldwide. Specifically for areas of skill set, that is required to make changes in this environment. But I would ask whether there is anything additional.

AARON GREEN: I think our financial audits over the last six or seven years have highlighted a number of observations on the practices at councils. We broadly break those up in our reports to Parliament into categories around governance issues, asset management issues, IT issues. You could argue that it's an evolution. As we report these matters on whether they are high risk or moderate risk, councils are doing work to address some of these issues, and we are finding that as we go through. But a lot of it takes some time. Some of these issues that we identify, especially around information technology systems, are difficult to resolve. A lot of them do require funding to address some of the concerns and the gaps. While the observations in financial audits are broadly related to those areas, I'm not sure, Claudia, if you have any other issues?

CLAUDIA MIGOTTO: It's hard to be general across the sector from the perspective of our findings from performance audits about what might be common gaps or issues that councils face. We have referenced—as the Auditor-General has covered in the opening statement—three performance audits in particular that we think are helpful to the inquiry. They go to similar issues that Mr Green has just outlined: the adequacy of internal governance and controls for the purposes of financial sustainability, really understanding what the obligations are in terms of levels of service delivery and using that to inform long-term financial planning, for example, is something that we found in the MidCoast Council audit report, but I think is something that's probably pertinent across the sector. Really knowing what your costs of service delivery are, knowing what your asset base is and then using that as a basis to identify any needs for additional funding.

The CHAIR: Are the auditing problems, would you say, unique to local government, or is that a problem that you see across other agencies?

AARON GREEN: In terms of the financial audit findings, I would say they are similar because a financial audit looks at similar activities. We look at internal control environments where we are looking for the systems and processes that have been implemented to ensure the reliability of financial reporting. But we see the same types of issues. What we do see is volume. In our most recent report I think it was around 1,100 observations made over the councils, which is quite a sizeable amount of observations to make. But there is progress in addressing those.

The CHAIR: It's good to hear that there is progress, which was my next question—if they were getting worse or better. I'm glad to hear that they are getting better. In terms of these problems, would you say they are more of a resourcing issue or a culture issue?

BOLA OYETUNJI: I believe it's a resourcing issue. When you describe governance, when you describe some of the reports on cybersecurity, when you describe timeliness of reporting, the fundamental of that is capability. That's what I believe. That's why you see some of the metropolitan councils do well. With the rural councils, it's difficult to engage an appropriate level of staff and skills set. We'll always struggle. Again, when I engage across the sector, that's one of the things I'd be wanting to look at and what submissions that we can provide.

The CHAIR: Is there a way that the State Government can work? You're talking about the issues with workforce and the struggle some councils might have. Is there a role for the State in addressing that problem?

BOLA OYETUNJI: I will say there's a role for the local council to leverage expertise. When they collaborate, there is some of the collaboration where they can actually help out. I'm not sure—again, we've not audited this part in what the State Government could do, but one of the things I've been glad about since I started was meeting one of the CEOs and opening the door for me to talk to 36 general managers and CEOs again, and that is when you have a strong council: How do you then help the less strong? That's what I think could be an opportunity in that sector itself first and then, if that doesn't work, of course you look for alternative solutions.

The CHAIR: One of the things mentioned in submissions that we've seen is about the assets that councils have to realise—sorry, value—valuing things that are non-realisable and non-saleable assets, like drains, like roads. Why do they have to value them?

BOLA OYETUNJI: Because I think the code asks them to value them, so it links to the local government code, and that's where this started a few years ago—to starting valuing these assets. Not going into it too technical, but can the standards allow you to use cost or fair value? The local government code chose fair value, again, for whatever reason. We don't comment on that, but that's their choice to give it a value.

The CHAIR: What I'm interested in as well is whether or not the ability of council to fund services and their obligations is impacted by this accounting requirement, and then their requirement to reserve money against depreciating assets, like roads.

BOLA OYETUNJI: Whilst I have not already said that, I would not link the valuation, which is non-cash, to the ability to fund activities.

Dr AMANDA COHN: I want to ask about the red fleet issue, which I'm sure you're familiar with. I understand a significant proportion of councils who receive qualified audit reports are because they've failed to account for the depreciation of RFS assets. I've spoken to a number of those councils. It's certainly not because they're not aware that they should be. They're making a protest, if you will. They are choosing not to account for that depreciation because they don't see it as just that they should have to. It's the requirement to meet other benchmarks of your office that means that having to account for that depreciation has an impact. Has any work been done to look at changes to benchmarks that would improve this problem? I know there's a committee in the Legislative Assembly that's looking at this issue. I'm sure you've already presented to them, but it would be helpful for this Committee as well.

BOLA OYETUNJI: I'll ask Mr Green to answer the question.

AARON GREEN: This has definitely been a difficult issue for the last few years where we have been obtaining the views of the State's Treasury, the Rural Fire Service. We've formed a view and the local councils themselves have formed views around the recognition of rural firefighting equipment. I guess there's a perspective here that there's an element of inconsistency. We've got around 40-odd councils that recognise this equipment. We've then got another 60 or so that don't recognise this equipment, and for whatever reason they've got different views when they look at the legislation which vests these assets over to councils, and then the requirements of the accounting standards take us through a pathway to determine who controls them.

We've ended up in a different place and in some respects that's troubling because we do have councils that are receiving qualified opinions. I think we've reached this point now where we're looking for solutions as well. We do want to work, as Bola suggested, with councils and key stakeholders—both the State Government and the Office of Local Government as the regulator—to look at what other solutions are out there to get some consistency. I think overall the most important part here is the asset management aspect of rural firefighting equipment. They're very important assets that serve a really important purpose. Having this divide over accounting is a bit of a distraction, so we are looking to work with the centre on what the solutions are.

The Hon. WES FANG: Thank you very much for coming and appearing today, and congratulations on the role. It will be lovely to see you coming in, appearing and providing some answers to us, but in relation to this red fleet issue, it is probably one of the biggest issues in relation to local government. You said that you've been looking at solutions, Mr Green. What might that look like? Certainly part of the reason that I think there was concern in the previous term of Parliament was that the State adopting that liability was going to create a huge issue. The councils rightly say, "We have no oversight. We have no responsibility for that asset that has been vested to us, but we have no control over that asset. From that perspective, for us to account for it would be inappropriate." Where are we going to come to in relation to this issue that's actually going to keep everybody happy?

AARON GREEN: I think that's difficult for us to answer, as the Auditor says. I think we can offer up suggestions as to what we see as being the aspects that mean council is controlling. We have some definitive indicators to us. The vesting is really significant to us because that places the red fleet in the ownership of councils, and then with the way the accounting standards work, which is really looking at who has the ability to direct the use of those assets, in our opinion the council does. It would have to be looking at what of those things can change here? Can vesting change? But that's not a decision that the Auditor would obviously make. All we can really do is provide input into the discussion around where are the challenges from our perspective. We can hear the perspectives from other angles and then Government can then determine what options they could take.

The Hon. WES FANG: I'm really keen to drill down on an answer you just gave, which was that councils have the ability to direct the asset.

AARON GREEN: Yes.

The Hon. WES FANG: What led you to come to that determination?

AARON GREEN: This is one of the key points that we have been discussing with the local government sector and councils. It does get a little bit techy, so I'll say that up-front. The ability to direct comes from, in effect, ownership. If you own the asset, you then enter into a service agreement with the Rural Fire Service and you'll basically ask the Rural Fire Service to deliver what has to be done on behalf of the council. The council has the ability to enter into that service agreement. The RFS is not the owner of the asset and can't in itself enter into that agreement because the owner is the one who says, "Okay, I'm willing to enter into it." So you have the ability to enter into that agreement, which is the ability to direct the use. In common sense, you would say, "Well, that means that RFS has everyday access. They've got the keys. They're using them every day," but the reason they have that is because the council elected to enter into the service agreement.

Dr AMANDA COHN: Can I ask a follow-up?

The Hon. WES FANG: Yes. Go for it.

Dr AMANDA COHN: It's just an opportunity to clarify because Mr Fang had brought up the private member's bill earlier.

AARON GREEN: Sure.

Dr AMANDA COHN: That bill proposes to change the vesting in section 119 but it was drafted to omit any changes to section 63, and section 63 is the requirement for landholders, including councils, to conduct things like hazard-reduction burning.

AARON GREEN: Yes.

Dr AMANDA COHN: If the path forward were to be legislative change, do you think that you'd have to change both sections of the Act at the same time? You couldn't just remove the asset and leave the requirement?

BOLA OYETUNJI: I think we can take that off because, as I said before, whether there's a legislative change or not, I'm not sure we have the mandate or the ability to advise on that. But what I would add is that, again, I have received what I call a client survey from councils, and I have seen how passionate they are. I promised them that I will visit them and that I will actually honestly understand, get to the bottom of it. Now, there's always a solution. Also, just for your awareness, accounting standards are principles-based. It's possible for two people to have different views. That's why I think it comes to now how do you then negotiate the best outcome. Once I engage across, I will be able to have a further discussion on how we can resolve this.

The Hon. WES FANG: If I went home I would be hung, drawn and quartered if I didn't ask this question of you now while I have the opportunity, given that you've provided that response to us in relation to this issue, because I live in Wagga Wagga. A lot of the council local government areas around me have all been impacted by this red fleet issue. It's always the number one issue they ask me about when I engage usually with local councils. You've indicated that accounting standards are, effectively, views and one person can have a different view to another. The argument that councils have always given to me is that the entity that uses the asset as opposed to the ownership of the asset is really the entity that should be depreciating that asset. Is it possible that your view might change to the previous AG and that you might adopt the previous position that the red fleet depreciation wasn't on council's books and that we can make this issue disappear?

BOLA OYETUNJI: Until I engage and I discuss with my team and look at the analysis, I wouldn't be able to answer that question directly. But you can be sure that I will visit Wagga. I will visit all the—

The Hon. WES FANG: You are more than welcome. It's a fabulous place. Ignore the Dubbos and the Sydneyites that say otherwise. It is fabulous. You're more than welcome. But in relation to this, there was an adopted view where a different position was then adopted by the Audit Office. Councils felt as if it was all of a sudden foisted upon them. It would solve the problem, if that previous position had gone, we go back to that and then councils aren't forced to account for this depreciation on their books.

BOLA OYETUNJI: Yes. To also make sure there is clarification, accounting for depreciation on the books really does not fix anything than the ratio of OLG.

The Hon. WES FANG: That's exactly their argument.

BOLA OYETUNJI: OLG can actually then, in their guidelines, change whatever ratios you look for. You would use EBITDA before depreciation is committed and amortisation. I wouldn't think depreciation is what—because when you think about it, you get the assets, so the revenue and expenses actually net out over a period. So I'm not sure that will be an argument that is actually complex; I think we can agree on that easily. And it should be easy for—I shouldn't say "easy", but it could be a question to OLG in terms of why there is a pain threshold because you have depreciation on your books. The only reason why there is a pain is that it's affecting such ratios and what do they reduce that ratio for. That's a simpler issue to resolve. But I think what's more complex, really, is—again, at least for my office—we need the assets to be in one book or the other. Now, the fact that it's not in any of the books is a concern for governance and accountability. That is what I will be looking to resolve.

The Hon. WES FANG: I very much appreciate your responses. Thank you so much.

The CHAIR: This is an issue that's being looked at by a lower House committee at the moment, isn't it, the Public Accounts Committee? Is it correct that there's an inquiry?

BOLA OYETUNJI: Yes, that's correct.

The CHAIR: I have a couple of questions now about the Audit Office's services to local government. Why does the Audit Office's service cost so much?

BOLA OYETUNJI: Again, that's a good question. It's one of the questions I'm asking. When you think about it in a broader sense, quality audits cost money and quality leads to accountability. The other aspect—and I will ask Mr Green to add to this—is that the requirement of what needs to be audited and signed off by the Auditor-General is actually broader than what is required by accounting standards. If we then have to provide opinion of another special purpose account and things like that, it costs money. It has been compared to what has happened before, but I need to get more briefing on why. One of the arguments is that, broadly, it doesn't cost much across the board, but there are some outliers. I've actually picked those outliers to investigate and see what could be done.

The CHAIR: Interesting. You talk about good-quality auditing. I suppose there would be an argument about the quality of the auditing that has been done previously, particularly when looking at the example of Central Coast council—but I will leave that comment there for you to make what it is. Are there ways that the cost burden of the Audit Office could be better managed?

BOLA OYETUNJI: We're always looking for improvements. One of the things that would be the hallmark of what I want to achieve across the board, across the State, is the efficient use of taxpayers' money, and I will start from my office.

The CHAIR: Thank you. I'm looking at my colleagues to see if they have any other questions. Was there anyone online—apologies—who had any questions for the Audit Office? I can't see any.

The Hon. WES FANG: I was excited about the red fleet stuff. I got answers, and I'm ecstatic. You couldn't have made me happier.

The CHAIR: That being the case, we'll leave it at that. Thank you so much for your time and for coming to give evidence to this inquiry. The secretariat will provide you with any questions on notice that are given.

(The witnesses withdrew.)

Mr BRETT WHITWORTH, Deputy Secretary, Office of Local Government, Department of Planning, Housing and Infrastructure, affirmed and examined

Mr DOUGLAS WALTHER, Executive Director, Office of Local Government, Department of Planning, Housing and Infrastructure, sworn and examined

Mr KEITH BAXTER, Director, Emergency Recovery and Strategy, Office of Local Government, Department of Planning, Housing and Infrastructure, affirmed and examined

Mr FRANCIS D'LIMA, Manager, Performance, Office of Local Government, Department of Planning, Housing and Infrastructure, sworn and examined

The CHAIR: Thank you and welcome to the inquiry. Would you like to start by making an opening statement?

BRETT WHITWORTH: Thank you, Chair. Firstly, if you hear a bit of nasalness, it's just the remnant of a head cold. I have tested; I don't have COVID. So please be assured on that. There are four key things that I wanted to quickly talk about. In terms of the financial sustainability of councils, there is no simple equation. There is no simple answer to this. It will vary for each council, depending on how that council chooses to apply the principles about financial sustainability from the Local Government Act. The second point that I wanted to make is that, as councils become more dependent on fees and charges and more dependent on grants in terms of their revenue—moving away from being dependent on rates alone—they become more subject to volatility in the economy. They become more subject to the volatility and the decisions of other levels of government for the provision of that funding, particularly in that grant space.

I do think, in terms of the question about cost-shifting—and I know that cost-shifting is something that does get raised quite frequently—that it's something that needs to be looked at from the eye of the beholder. There are arguments on both sides about cost-shifting and what a reasonable expectation is for delivery of local services versus what a new expectation is that a government may put on another level of government. If we're going to dive into the issue of financial sustainability of councils, we've also got to appreciate that we need a high degree of rigour around how you set a budget based on the expectations of service delivery from the community, the expectations of what a council can afford to spend, and what money they are receiving in terms of their various revenue sources. But it's not a set-and-forget exercise; it's something that needs to be continually monitored. That's one of the reasons why we wanted to look at improving the way councillors receive information and the way the Office of Local Government receives that same information.

On a more quarterly basis, we have the quarterly business review statements, but we want to look at making those a more robust tool to ensure that councillors are more able to deal with and understand the financial challenges and the financial progress that the councils will face. We have given a submission that is probably more factual rather than trying to put a particular policy intent one way or the other. We'd be more than happy to work with the Committee in terms of how it might want to progress, because I know that you're going to be hearing from a lot of people and there are a lot of ideas. There will probably need to be a shaping of those ideas, and we're more than happy to help and assist with how those can be embedded into any program for legislative improvement, practice improvements and so forth.

The Hon. WES FANG: Thank you to everyone for appearing today. We very much appreciate it. Mr Whitworth, noting your opening statement, has the Minister provided any guidance or requested any work be done in relation to this matter, or did he just refer it to this Committee to look at?

BRETT WHITWORTH: Well, Mr Fang, I think it's a matter of public record that we had earlier thought that IPART may be a suitable inquiry agency to look at probably a more targeted question around how councils are managing their finances. That flowed from the update to the rate peg methodology that the Independent Pricing and Regulatory Tribunal progressed. So there was obviously a piece of work associated with that. From the very first meeting, almost the very first words that the Minister said to me were, "Brett, I want to see councillors more visibly in control of their councils." From that point of view, he was very clear that it was as much about financial management and budget management of councils, and so it has been an ongoing theme of conversation. As a result of that, we have commissioned various pieces of work. I talked about wanting to update the quarterly business review statement. Mr D'Lima has been working on potential updates to the performance ratios and undertaking consultation with the sector on that as an example of how we go about meeting the Minister's expectations of improving councillor visibility over their finances.

The Hon. WES FANG: It seems to me that this would be an interesting topic to refer to a committee for inquiry. It seems to me as if there are any number of departments—you've already mentioned asking IPART to look at the issue. There's the Office of Local Government, there's Treasury, who will have views and guidance around that. But, instead, the Minister has referred it to this Committee to investigate and make recommendations on the issue. What do you think was the catalyst for that? Why do you think the Minister sought this parliamentary inquiry in relation to this matter over seeking a more targeted approach, say, with a request to the Office of Local Government?

BRETT WHITWORTH: Mr Fang, I think the Minister gave quite a detailed response in budget estimates as to one of the reasons why he wanted to refer the matter to a parliamentary inquiry, so I won't repass that. But I do think that it's important to also think about how one of the fundamental themes of discussion around council finances over the last 15 years has been the rate peg, and whether the rate peg should be lifted. We can come at that from a technical perspective but, fundamentally, there is a political question that goes to what would be the consequences of lifting the rate peg.

Local government is the third tier of our governance system. You have councillors that are democratically elected to represent their community. There is a question as to whether we should give to them the power to set their own rates and revenue and their own—effectively—taxes. Or there is a question as to whether we should continue with a rate cap process, given that local government is created by State statute. The decision as to whether you're going to effectively allow taxation to be set by a tier of government is really probably one for politicians to make. I think that's why he asked this inquiry: to look at those issues as well.

DOUGLAS WALTHER: Also, Mr Fang, if you look at the submission from Justin Clancy, the member for Albury, he actually pointed to the fact that, on a political level, it is easy to take the views of council and acknowledge the rate cap needs to be increased but, at the same time, the residents in that community may feel differently and have certain considerations. I think that submission highlights the fact that it does need a political lens over it, not just an economic or a Treasury one.

The Hon. WES FANG: Yes. I certainly appreciate that. I am trying to understand how the political aspects of this inquiry seem to have trumped a lot of the other aspects over and above the work that was already underway at any number of levels throughout the departments within the Government.

The Hon. STEPHEN LAWRENCE: Point of order: I am unclear how exploration of whether this forum is preferred as opposed to some other forum—the political machinations that might have gone on. I struggle to see how that is relevant to the terms of reference, which are fundamentally about financial sustainability, which is a policy issue and not an issue about how we ended up here.

The Hon. WES FANG: To the point of order: In the terms of reference, reference (g) says "any other related matters", and I would say this is entirely related.

The Hon. STEPHEN LAWRENCE: I think the flavour of "related matters" would be coloured by the other aspects of the terms of reference. It does not mean anything else where some sort of bow could be drawn. It means something that is of a policy nature similar to those specified matters.

The Hon. WES FANG: I am not suggesting to use fish sauce in Italian food, Chair.

The CHAIR: I am prepared to make a ruling on this.

The Hon. WES FANG: I think what I am saying is certainly within the terms of reference.

The CHAIR: In terms of whether or not it is within the terms of reference, I do note that there is the (g). That being said, the question that the Hon. Wes Fang was asking was straying very close to asking a public servant for an opinion on a political matter, and that is completely out of order and not within the remit of this inquiry. Having said that, I will continue and ask him to perhaps rephrase the question.

The Hon. WES FANG: Did the Minister provide any direction to the Office of Local Government to provide detailed work to this Committee in order to guide its deliberations?

BRETT WHITWORTH: We discussed broadly the outline of the submission that we made. We agreed and it was my preference that we provide a factual response to the terms of reference and that we not provide a policy intent for the very reasons that I think the Minister identified when he talked about this in budget estimates—that he wanted a political lens over these issues.

The Hon. WES FANG: Noting the Chair's ruling, I will not ask you to provide an opinion as to my view that the Minister is squibbing his responsibility in relation to having an inquiry like this because he can't make a decision.

The Hon. MARK BUTTIGIEG: Point of order—

The Hon. WES FANG: I have rephrased the question.

The CHAIR: A point of order has been taken.

The Hon. MARK BUTTIGIEG: These forums are not meant for cheap political point scoring.

The Hon. WES FANG: You guys did it for 12 years.

The Hon. MARK BUTTIGIEG: They are meant for interrogation of the witnesses to extract facts so we can come to an informed decision. I ask you to call the member to order and ask him to refrain from political point scoring—which is so transparent as to be ineffective anyway, but I thought I would make the point.

The CHAIR: I uphold the point of order. I note that debate within points of order is not helpful. That being said, the honourable member, in talking about squibbing and other things, was being completely disorderly. I will ask him to rephrase his question again.

The Hon. WES FANG: I think I have made my point. I am happy to pass the questioning over.

Dr AMANDA COHN: I have a question about the code of conduct system which, as you know, is a bugbear of mine. In the context of financial sustainability, you also have councils going out to a panel of private code of conduct reviewers who make an assessment, but often that assessment, as a second step, will then also come to the Office of Local Government and, therefore, be double handled. Is there potentially a more efficient way or are there cost savings that could be found from having a more efficient code of conduct system?

BRETT WHITWORTH: I do note your phrasing of that to give it a financial perspective. Any way that we can reduce the double handling of the code of conduct process would obviously save money. The circumstances where a matter comes to the Office of Local Government as a result of the code of conduct are limited to matters of pecuniary interest and where a code of conduct reviewer has identified a recommendation and the council has chosen to follow a different recommendation, or if the council wants to refer it to the Office of Local Government, having considered the code of conduct reviewer's recommendations. The theory behind the procedures for the administration of the code of conduct is that the code of conduct reviewer's report is sufficient for the Office of Local Government to then determine and identify what next steps it would need to take and that we can build our response on that investigation. I think, with the benefit of practice, we find quite often that we might need to reinvestigate elements, so there are certainly ways in which that can be improved.

Again, I have given evidence and the Minister has given evidence at budget estimates that there are improvements that can be made to the code of conduct process, and looking at the way in which investigations of councillor conduct occurs is quite important there. I do think, though, we need to continually come back to the concept that councils are democratically elected bodies. The responsibility for investigating the behaviour and commenting on the behaviour of a councillor should really rest with the council as a governing body and only come to the Office of Local Government where there are extreme variances from that accepted set of behaviours. So I would prefer that we try and keep that investigation level more at the council level rather than centralising it into a larger agency, in which case we would then have to be talking about funding for the Office of Local Government.

Dr AMANDA COHN: There are all sorts of things wrong with the code of conduct system, but I am trying to stick to the terms of reference of this inquiry. Theoretically, if we were to consider a recommendation around code of conduct reviews being done by the Office of Local Government rather than private providers, whether or not councils would need to partially pay a fee for that service or whether it would be resourced by the State Government, there is obviously a need for resourcing to do that job. But, in your opinion, is there the technical expertise to be able to undertake that function? Is it feasible?

BRETT WHITWORTH: Technical expertise, I suppose, has two elements: There is the capability and the capacity. We certainly have the capacity; we have trained investigators. But the capability comes more from a funding perspective as well, and we would not have that capability unless our funding was increased.

DOUGLAS WALTHER: And the Minister has publicly spoken about the industry that has evolved around code of conduct complaints and investigations. I think, when you look at the benefit, the simplification of the code which the Minister is committed to is probably going to get greater returns than investigations all being done in one place.

Dr AMANDA COHN: We heard from IPART this morning and we had a discussion around their base cost change formula. They were telling us about the metro, regional and rural categories that account for some of the big differences, like how much growth councils have got to look after, but they also talked about how, in their opinion, there is the ability to be more individualised in the application of that algorithm and that calculation that does take into account the extreme diversity in some small councils that have, for example, taken on State government services or have service offerings that are vastly different to other councils. I was wondering if there was an opinion in the Office of Local Government on the base cost change specifically and how well that reflects the diversity of service offerings.

BRETT WHITWORTH: The base cost change model—I don't even think it's a year old yet—was developed as a result of quite an extensive consultation process. I've not had people come to me complaining about the base cost change model but had people complain about the previous local government index—

KEITH BAXTER: Local government cost index.

BRETT WHITWORTH: The local government cost index—and how it was backward-looking and didn't really get the right inputs. I think we've seen a change with that with the base cost change index. The temptation is to come up with an individual rate cap for each council, which also then means: How far away are we from doing an individual financial management plan for each council? Councils are supposed to be independent. They are a democratically elected tier of government that's supposed to take responsibility for their finances. I keep coming back to that. That's an important point because councillors are supposed to be there to understand what service level expectations their community want. Those service level expectations may not be capable of being reduced to an equation because quite often they will be values-driven.

I'd probably put those riders around narrowing the base cost change model down to an individual council but I certainly do see that there is value in being able to distinguish between different types of councils—rural, regional. Rural remote, for example, is an important category of council because we have a number of councils in that category—Central Darling—where their ability to raise rates and own source revenue is approximately $2.5 million yet they run a $27 million operation, effectively. You need the base cost change model to probably differentiate that from, say, Inverell council or Glen Innes, which have a different environment versus a Shoalhaven or a Lake Macquarie.

Dr AMANDA COHN: Thanks, that was comprehensive. You've led well into my last question, which was going to be about own source income. I know that for metropolitan councils there are opportunities in renting out function spaces or meeting rooms in their libraries. I'm very lucky to have been deputy mayor of Albury council where we have an airport and a tip shared with other councils and those opportunities. You named Central Darling as one that has very little opportunity for own source income. Has any work been done to aggregate that information across the State? Is there any way that the Committee could access the various ways or the different examples of councils and their own source income?

BRETT WHITWORTH: We probably have more understanding of the data of how much own source revenue a council will have. We probably don't have the particular examples of how they generate that own source revenue. Mr D'Lima, have I got that right?

FRANCIS D'LIMA: Yes, pretty much. We could tell you how much of the revenue would be rates and how much of that would be charges but whether it's being used in a particular way, that is something on which there would be limits on what we could provide but total amounts and, at a higher level, the categories, yes.

Dr AMANDA COHN: Yes, thanks, that will be helpful. We will at some stage in this inquiry, I'm sure, hear from individual councils where we would have the opportunity to ask directly what those sources are.

KEITH BAXTER: I think the Committee's already heard today about the diversity. You have councils running medical practices, dental practices, post offices, banking services and Service NSW and they'll all generate some level of own source income. You've got a large number of councils that do water and sewer and a local water utility that generates income from service fees and charges, and from waste, which you've mentioned. The variety is huge. Some of them are on a commercial basis and some of them are not on a commercial basis but it is a bit like, "How long's a piece of string" about what they generate. One of the submissions, I think, referenced that the fees and charges policy in one council was 10 pages and in another council it was 130 pages.

DOUGLAS WALTHER: You mentioned Central Darling. One of the interesting things for them is, although not necessarily generating income through hall hire and things like that, that they do have arrangements with Transport for NSW for their roads contract, for example. Councils, where possible, have been looking for those opportunities to do what they can.

The Hon. MARK BUTTIGIEG: I think, Mr Whitworth, you outlined this incompatibility—or tension perhaps is the right word—between the statute provisions and the councils setting their own rates. In other words, local government is a creature of the State Government legally. Could you tease out that tension a bit more in the context of evidence that we heard today that other jurisdictions have done this and there's no issue there? I want to get an understanding of what the issue is.

BRETT WHITWORTH: It is interesting that other jurisdictions—Victoria does have a rate peg; other jurisdictions don't have a rate peg. In South Australia, for example, you have—I will tell you the acronym but

I don't what it means—ESCOSA, which is our IPART equivalent, that does financial sustainability assessments of individual councils, which are there as a guideline for councils. We also have Queensland, which has a local government Minister's forum; they're a senior officers group of local government jurisdictions. Queensland is driving a project at the moment to look at the data behind financial sustainability—not modelling but financial sustainability reporting of councils. I raise that because while some cap rates and some don't, each jurisdiction looks and monitors out of the concern about the extent to which those councils are operating well and also the extent to which there are exceedences and the need for intervention.

Your question also was about the tension that exists. I'm aware of the point that whenever there is, for example, a special rate variation—and this has been happening in an increasing state—you're starting to see community groups come out and say, "We just are really concerned about the impact this is going to have on our capacity to pay."—community, business and the rural sector. Mr Walther pointed out that the submission that we have, for example, from Mr Clancy, the MP for Albury—

The Hon. WES FANG: The great member for Albury.

BRETT WHITWORTH: He raised that very point of that tension—that if you allow rates to go up, you're going to see people that say, "We can't necessarily afford that." In terms of that tension, we probably extend that tension because councils want to set their own development application fees but they can't because they're regulated. They want to set stormwater charges but they can't because they're regulated. We do allow councils to set their water and sewer charges but there are guidelines around that.

The Hon. WES FANG: Unless they privatise it.

BRETT WHITWORTH: There are mechanisms in which the Government provides grants to help identify and provide new infrastructure. We've got an inconsistent array of how councils set their own fees and charges and I think that's a reflection of different perspectives around the many different operational elements of what councils do.

The Hon. MARK BUTTIGIEG: To follow up on that, it seems to me to be somewhat of an academic argument. If you were of the mind—and the logic is, as you pointed out—that the democratic transmission mechanism to the people that you're serving and who elect you is the first layer of protection, presumably if you increase rates out of proportion to what the citizens are getting, then they vote you out. I think the implication is some legal challenge to the State, right? In an extreme situation, the State just steps in and legislates for whatever regulatory oversight it needs to deal with the lifting of the rate peg. Isn't that the case?

BRETT WHITWORTH: In some of those other jurisdictions? Sorry, I'm not—

The Hon. MARK BUTTIGIEG: Hypothetically, in New South Wales. But, yes, if it's happening in other jurisdictions—if they can do it, we can too. If local government is a creature of the State and the State wishes to have them set their own rates, then the State can intervene at any time if it gets out of whack, right?

BRETT WHITWORTH: The State could intervene at any time through legislation if it does get, as you say, out of whack. Yes, that could happen. But the thesis that I'm trying to provide about council financial sustainability is that it really rests with councils to be managing their finances based on that service delivery expenditure-revenue equation. The more risk there is that that will change because of an intervention point from the State through legislation, the harder that makes that job for councils to do. So the more that we can get out of that space and give council some clear air, the better off we'll be. I don't think I'll name and shame them, but I do know that there are—

The Hon. WES FANG: No, go ahead. I'm more than happy.

BRETT WHITWORTH: There are general managers that are quite happy about the rate cap because it gives them an operating environment to say, "These are the efficiencies that we need to manage within our organisation so that we can continue to operate without having to draw too much on the community's capacity to pay additional funds."

The Hon. EMMA HURST: Good afternoon to our witnesses. Admittedly, I had to step away a moment ago, so I hope I'm not asking a question that somebody has already asked. Mr Whitworth, if I do, please let me know. I heard you talking earlier about smaller rural and remote councils, and we've heard quite a bit from them today. I wanted to talk more about the grants and some of the issues that have been raised around access to grants. I'm wondering if the Office of Local Government has done any work already to try to address some of the concerns there?

BRETT WHITWORTH: That's quite a broad question in terms of concerns about grants, and not all—

The Hon. EMMA HURST: A lot of these grants are going to larger councils and some of the regional councils are feeling like they are not getting the same access.

BRETT WHITWORTH: I actually don't think I agree with that proposition. There has been a period where there has been quite a lot of money going into regional New South Wales and that probably is changing. But in terms of things like the financial assistance grants, the identification and the formula for the financial assistance grants is set by the grants commission. It is a challenging space because that's the bulk of where the grant funding goes—the untied grant funding goes to councils from the Commonwealth through the State. We are working on the basis that we have a particular formula about trying to create no disadvantage to councils in terms of the allocation of the grant funding. We have a situation where there is probably an inequality in terms of the need for the access to those grants that exist—so metropolitan councils have far greater capacity to raise their own revenue than regional and rural councils—but we also have limitations set within both the New South Wales legislation and the Commonwealth legislation that sets out how grants commission funds are to occur, so we have to meet those.

For example, there is a weighting around population change and population increase because it's supposed to ensure that those councils that are growing are also getting access to grants to help them manage that growth, which does create that fundamental conflict between regional councils where we're seeing growth is quite steady, if not a modest decline, verses those councils like Blacktown, Lake Macquarie, Newcastle, Shoalhaven where you're seeing quite considerable growth. Answering that question requires an examination of both the Commonwealth legislation and a grants commission that can really push the boundaries on how to allocate that funding.

In terms of other funding that comes from grants, we have been talking with our colleague agencies, particularly with the example of Central Darling, but I think the Premier also looked at this particular issue in the case of Moree. It can be quite difficult to pin down how much money each council is getting from a State Government perspective. Quite often those grants are coming for reasons that are very much driven by those businesses. So maybe delving into the water space—Walgett Council in particular has had money coming to it to address some of its water quality. There is a real challenge in terms of: How do you identify what amount of money you want to give to that council? I was going to hand over to Mr Walther to talk a little bit about some of the grant issues, particularly in the water space.

DOUGLAS WALTHER: Yes, certainly when it comes to programs like Safe and Secure and other grant programs that have gone to some of these councils, it's almost the opposite is true in that the less investment over the years from the council itself, and the lower the health score the greater the need for that State Government investment and intervention. Going more broadly, a lot of the recent grants have been tied to natural disasters. Therefore, they have been allocated based on event rather than capacity of council. Then, at the same time, the nature of a lot of grant programs that require business cases to be done, demonstration of readiness to expend the grants and things like that do favour both metro but also the higher densely populated councils. I don't think you can make the generalisation that all of the grant programs favour the more metro and the higher capacity councils but, at the same time, there is a bit of an example of both.

The Hon. EMMA HURST: Again, using the example of pounds, in the other inquiry that we are doing into pounds, a complaint that has come up from council is that when the rate peg is there, they can't get the money that they need for functioning pounds that are maintained properly. I wanted to hear what work was being done in that space, or what other options are there for councils to be able to run functioning pounds if the rate peg was to stay. Currently, in the situation that we are in, what other options do councils have? My understanding is that there is no way of getting the figures on how much councils are spending on their pounds. Is that something the Office of Local Government has information about?

BRETT WHITWORTH: We don't have more detailed information about how much money councils are spending on individual service areas, unless it's something that they're mandated to report on in their annual report. We have explored the idea of trying to get more detailed data from councils through a more data-driven quarterly business review statement. I would love to be in a situation where we can access council financial information more directly, which would help us do our other job, which is making sure that we're monitoring the financial risk of councils and looking out for those councils that are financially challenged, but at the moment we don't have that information.

In terms of your question about what could be done to improve the accessibility of councils to finance, to fund their pound services, I suppose it comes down to it's either a service that the community pays for out of the rates, it's a service that the customers of a pound pay for as a fee or a charge, or it's something that there is a grant-base program. Again, if it's a grant-based program, okay, that gets you the capital to build the facility but it doesn't necessarily give you the operational expenditure to run the facility. Without wanting to pass judgment on how well councils are managing their pounds or not—and I know that you have a very clear view on that, and I'm looking forward to the inquiry outcome—it does come back to the fact that the operation of a pound probably best comes from the rates, because that's a service that council provides to their community. That's one of the things that, as a ratepayer, you are paying council to manage.

DOUGLAS WALTHER: There's also the companion animal grant payments that go in, so we've got the record of the payments to the councils. But as we touched on at estimates earlier in the year, there is that inequity in that it does favour the higher populations where there are higher registrations et cetera. That's known, in terms of the problems around the way that that's distributed.

The Hon. EMMA HURST: Mr Walther, can you just give me a bit of a scale—in some of these councils that are getting a very small amount from that, how much are they getting if they're getting only small amounts?

DOUGLAS WALTHER: It ranges from less than $100 to tens of thousands of dollars. The variance there is quite significant.

The CHAIR: I might start off with a question around councils and the financial sustainability issues that we've been hearing about. Why is it that councils end up in these precarious situations? Is it a result of them having to enter into a position where they are providing an aged-care facility, for example, or is it because they're building a swimming centre complex that's well beyond their means? Would a perfectly prudent local council still fall off the cliff, I suppose, if there was enough time?

BRETT WHITWORTH: I would argue that a perfectly prudent council would only engage in a decision about that sort of major infrastructure if they thought through the operational costs into the long term and their ability to fund the actual up-front capital. I suppose we were anticipating that you'd ask this question. Without wanting to name particular councils, we'd been thinking that there are some examples of councils that are financially fragile that it's useful to explain. Mr D'Lima, if you could just give us a quick outline?

FRANCIS D'LIMA: There are a number of reasons why, in our experience, councils end up in financial strife. Some of them are the ones you've mentioned, which is they invest without looking at the long-term consequences—in other words, their recurring costs, depreciation et cetera. That is something that a few councils have got into. In some cases, I think there's also the case of transparency of information. Councils, for example, which own aged-care centres or other businesses—and in answer to the previous question, I said we don't have all the data; we do have some break-up of income around aged care, child care et cetera. But councils do not necessarily look at it as separate entities and look and see whether they are cost-neutral or adding to deficit et cetera.

The other areas that we have found to be an issue would be where they get into an investment without considering the long term, as mentioned there already. But in some cases, there are natural disaster relief works which interfere. There are plans to get into areas which require large capital investments, so the question then becomes about borrowing, and committing funds to capital expenditure. These are some of the areas, I think—financial transparency et cetera.

BRETT WHITWORTH: There are examples of those councils that had a high degree of expenditure but they had own-source revenue that enabled them to match that. The pandemic impacted their ability to realise some of the revenue because they were engaging in development activity, for example, to serve the benefit of their community by opening up new land. But where that revenue dropped off, their expenditure remained high and they didn't adjust the expenditure down. That created a particular challenge, or an example of a particular challenge. You've got councils that are unclear on how much money they're spending because their businesses are joined together and they're not separately managed. Then you've got other councils that are simply dealing with the infrastructure increase costs as a result of the pandemic and the supply chain issues that flowed from that, and dealing with natural disaster on top. That has created problems for them in terms of the rapid increase in staffing costs and materials costs to rebuild infrastructure or provide new infrastructure.

KEITH BAXTER: Also, I think the other aspect is there are some councils that have a difficult demographic, economic, geographic environment they're working in. We've used Central Darling as a classic example: very small population, very diverse population spread across three major population centres. But it's a council the size of Tasmania with next to no—I think it was a $2 million rate base. If you think about just trying to manage that as a business, with the sheer volume of roads and things like that, you could be the world's best council and making all the best prudent decisions and you'd struggle in that environment. I think that's what we were trying to do in our submission: to point out that it's not a one-size-fits-all problem so it's not a one-size-fits-all solution. Sometimes it's about a creature of decision. Sometimes it's a creature of the geography, the economics and the demographics of where they are.

The CHAIR: I wanted to ask a question now about developer contributions and voluntary planning agreements. That's come up a bit in the submissions that we've seen to the inquiry. It's a huge source of revenue, as I'm sure you'd know. How can these be better used by councils to ensure their sustainability?

BRETT WHITWORTH: First and foremost, I probably should say that any questions about the policy around development contributions probably should be directed to my Planning colleagues.

The CHAIR: Point taken.

BRETT WHITWORTH: But I'm happy to come at it from a local government perspective, in terms of how should they be used. Perhaps I can give an example of, again, a council that I won't name, but it was a council that I worked in where the interest that they received on their development contributions was a million dollars. If you start putting that together, you'll recognise they had a lot of money in the bank. Unfortunately, the council didn't have enough money to cover the—if everyone came in and said, "We want you to buy the land that you've identified for acquisition," or the delivery of the infrastructure that they'd said they would deliver through the development contributions, their exposure was greater than the amount of money that they had, which talks a little bit about the temporal nature of development contributions. It sometimes looks like there's a lot of money there, but there's a risk that you don't actually have enough because you've over-identified what you want to do.

There are also other councils where the amount of money that comes in and the amount of money that goes out is quite evenly matched. Blacktown, I think it is fair to say, is one of those councils where there is quite a degree of churn around how much development contributions they spend. With the example of Blacktown, they have a very active identification of what they want to deliver. I think that's the critical thing: You've got to have a motivation within the council to say, "We want to pursue a work schedule to deliver on infrastructure, to deliver upgrades to parks," to proactively go out and buy land as early as you possibly can so that you minimise the risk of cost escalation over time. That's probably one of the ways in which you can manage that. It is quite a challenge. I don't want to make it sound like it's really easy and straightforward. It is a real challenge and it's a real budget management exercise as well.

In terms of voluntary planning agreements, probably my only other comment on that is that this is where councils need to be careful. A voluntary planning agreement looks like it's a great thing. A developer is saying, "We'll give you that piece of infrastructure." I don't even want to get into the commentary about voluntary planning agreements, where you are talking about additional development in exchange for a certain amount of money. I'm talking about voluntary planning agreements where, rather than pay the X amount of money that I would pay through a development contribution scheme, I'll give you the cold shell of what could be a library, for example, or I'll provide a road upgrade. If councils can see that and say, "That's great, we're getting this infrastructure"—and it can sometimes look like it's cheap or free infrastructure, but it comes at a cost. You've got to put a library into the cold shell. You've got to be prepared to maintain the road or the park infrastructure that comes along, so I think that is the risk about voluntary planning agreements: They've got to be seen as part of a planned approach to the delivery of services and infrastructure, as a result of growth.

The Hon. MARK BUTTIGIEG: I just wanted to ask a follow-up question on your earlier evidence about the FAGs grants. Are they a discrete mechanism, irrespective of whether or not a regime has rate pegging, or is there a compensation factor for the fact that councils—

BRETT WHITWORTH: No, Mr Buttigieg. The Commonwealth provides an amount of money for each State. It identifies the allocation that it's going to make for each State and then, in order for the State to receive that, they've got to have their own grants commission. It's totally independent from whether there is a rate peg or not.

The CHAIR: I wanted to ask you a couple more questions around financial sustainability, in the time we have left. How many councils are currently in financial trouble? Has this increased over time and has the need for intervention increased over time?

BRETT WHITWORTH: How do you define financial trouble?

The Hon. WES FANG: The Minister should have given you better Dixers.

BRETT WHITWORTH: Some councils are operating at a loss and they're using their reserves, but they're doing that deliberately. Or they may be operating at a loss because the depreciation that they have to use to ensure that they can renew assets into the future is quite high, for example. I think our submission identifies those councils that have positive and negative balances. Do we have a risk-based approach to identifying councils that are financially at risk? Yes, we do. We have regular meetings to discuss those councils.

But, again, one of the examples I gave earlier of the council that had a reduction in its revenue is on that list. That council might manage to make some land sales. That council may see the restart of the fairly significant activity that was generating revenue for it, and it will no longer be on that list. We may have another council that made a decision about a particular service delivery through a particular type of technology, and that type of technology failed. That council will, all of a sudden, go onto our watch list. I probably want to say that it's fact and degree. Having said that, I think about probably 10 councils fairly regularly when I'm out walking around and trying to get away from work.

The CHAIR: I'm just wondering if there are any primary factors or common denominators as to why they're in that difficulty, and thinking about some of the ones that are more likely to be in difficulty are the ones in the large regional centres. Are there any reasons for this?

BRETT WHITWORTH: I think a council being on top of the money that it's expending is critical—I know that sounds self-evident—and being able to understand what your costs are, the extent to which your costs are escalating and the extent to which that escalation in costs is either dependent or relating back to particular projects, or not. There are also challenges for councils that are managing cashflow issues as a result of timing of things like disaster recovery fund payments, timing of the Financial Assistance Grants payments. Those councils run very, very lean in terms of their operation, but they are constantly looking at their liquidity and the amount of cash that they have on hand.

The CHAIR: Did you have any further questions, Dr Cohn? I'm mindful of the amount of time I'm taking up. I have questions, but I'm also—

Dr AMANDA COHN: You go ahead. That's alright.

The Hon. WES FANG: Just noting that we started earlier.

The CHAIR: Yes, I know. We've got about another four minutes, Wes.

The Hon. WES FANG: The Minister's Dixers haven't been that good so far.

The CHAIR: I'm not sure why you're critiquing my questions.

The Hon. WES FANG: The Minister's questions.

The CHAIR: It's very disorderly.

BRETT WHITWORTH: I'm not aware of any Dixers.

The CHAIR: In terms of the grant programs, many of the submissions that we've received have talked about the sugar hit that the grant is. What proportion of council revenue is the capital grants and has this gone up over time?

BRETT WHITWORTH: I'm just wondering whether Mr D'Lima has that at hand; he's looking. But I know roughly that, including the Financial Assistance Grants, about 30 per cent of general council revenue, I think, is grants.

FRANCIS D'LIMA: Total grants for capital purposes would be around 21 to 22 per cent. For operating, it would be around 13 to 14 per cent—across the sector, that is.

The CHAIR: Has that increased, over time, as a percentage?

FRANCIS D'LIMA: Together, yes, they have over the last few years. Earlier, they would account for about 29 per cent together. Now, it's about 34 per cent—so about 3 to 4 per cent, at least, increase over time.

The CHAIR: Thank you. I wanted to ask, just finally, about performance ratios. How do performance ratios fit currently in the way that OLG measures risk?

BRETT WHITWORTH: We definitely use performance ratios. I think Mr D'Lima will attest that I'm not a big fan of performance ratios as they currently stand because they're very much about—when I talk to council general managers, particularly council mayors and rural mayors and I use the words "performance ratios", it brings up for them Fit for the Future connotations, whereas, for me, performance ratios should be a tool that we can use to understand what the liquidity is that that council has. Is there a liquidity risk that the council has? What is that council doing in terms of investing in its infrastructure and renewal of its infrastructure?

How much money is that council making through its own source revenue versus how much it's spending— and moving away from having to factor in grants and so on so that it can survive on its own? I have actually asked that there be a piece of work in which we can renew and revise the performance ratios, so that we can move more to a set of tools that are more about our risk management of councils—and our understanding of how they are operating today, at the end of the year and next year—rather than them being, should we be talking about bigger or smaller councils?

The CHAIR: Thank you. Were there any final questions from my peers? Did you have any final remarks before we finish?

BRETT WHITWORTH: No. Thank you for the opportunity to give evidence. As I said, we are happy to help work through what some of the implementation issues may be of any recommendations. If you want us to come back and give evidence again, we will be happy to do that.

The CHAIR: Thank you so much. The secretariat will be in contact if there are any questions on notice. Thank you for appearing today. That concludes our hearing.

(The witnesses withdrew.)

The Committee adjourned at 16:50.