Revenue projections for changes to local government rates and local infrastructure contributions

The NSW Productivity Commission Infrastructure Contributions Review investigated reforms that would impact on the revenue for NSW local councils.[1] These included:

- reform of the local government rate peg to enable rates revenue to grow in line with population. Currently, the rate peg does not allow for any growth in line with population growth in each council area
- adjustments to local infrastructure contributions to restrict the use of planning agreements, increase the threshold for S7.12 levies and allow S7.11 contributions for development-contingent costs only.

This briefing sets out the modelled revenue impacts from the above changes, based on modelling assumptions consistent with the work undertaken for the NSW Productivity Commission. The estimated revenue impacts are shown over a five-year period, from 2022/23 to 2027/28, based on implementing the changes identified by the NSW Productivity Commission on 1 July 2022 for rate pegging and 1 July 2023 for local infrastructure contributions.

Revenue impacts

Revenue impacts for selected council groups are set out in table 1. These are shown as an average over five years, and for the fifth year (i.e. 2027/28). Impacts are reported in millions of dollars, as per cent changes and per capita.

Under the combined set of reforms, councils will gain increased revenue from rates, but decreased revenue from infrastructure contributions, compared to what would be expected with current policy settings. Different council groups are impacted differently:

- Above state-average growth councils tend to have larger positive impacts from aligning the rate peg to population growth, but also have larger reductions in infrastructure contributions. Over a five-year period, above state-average growth metropolitan councils are expected to gain increased revenue of $14 per capita per year above what they would otherwise have received. In the fifth year, the increase is $32 per capita. For above state-average growth regional and non-metro councils, the average increase in revenue is $20 per capita over five years. In the fifth year the increase is $40 per capita.
- Below state-average growth councils as a group also increase their overall revenue, but by smaller amounts. Over a five-year period, below state-average growth metropolitan councils are expected to gain increased revenue of $8 per capita per year. In the fifth year, the increase is $16 per capita. For below state-average growth regional and non-metro councils, the average increase in revenue is $6 per capita over five years. In the fifth year the increase is $12 per capita.

In total, across all NSW councils, the changes are expected to increase revenue by $80 million per year on average over the first five years. The impact gradually increases, because the rate increases are

[1] NSW Productivity Commission Infrastructure Contributions Review website, https://www.productivity.nsw.gov.au/infrastructure-contributions-review.

cumulative, while the reduction from changes to infrastructure contributions remains similar. By the fifth year, the increase in revenue of the changes is estimated at $172 million.

1 Revenue impacts of changes over five years

Council group	Average over five years			In fifth year		
	$m/year	Per cent	$/capita/ year	$m/year	Per cent	$/capita/ year
Below state-average growth metro councils						
Rates	29	1.6	13	51	2.6	22
Contributions	- 11	-6.1	-5	- 14	-7.3	-6
Total	18	0.9	8	37	1.7	16
Above state-average growth metro councils						
Rates	82	4.5	27	147	7.3	49
Contributions	- 39	-6.2	-13	- 52	-7.6	-17
Total	42	1.7	14	96	3.5	32
Below state-average growth regional and non-metro councils						
Rates	23	0.8	8	41	1.3	13
Contributions	- 4	-2.4	-1	- 5	-2.7	-2
Total	19	0.6	6	36	1.1	12
Above state-average growth regional and non-metro councils						
Rates	2	3.2	27	3	5.2	49
Contributions	0	-16.3	-7	- 1	-19.8	-9
Total	1	2.3	20	3	4.1	40
All councils						
Rates	135	2.1	16	243	3.4	29
Contributions	- 55	-5.5	-7	- 71	-6.7	-8
Total	80	1.1	10	172	2.1	20

Note: Starting from 2022/23 for a five year period.
Source: The CIE.

Council groupings

Councils were grouped based on the following criteria.

- Region — councils were identified as either:
  - Metro councils
  - Regional and non-metro councils (which includes Newcastle, Wollongong and the Central Coast)
- Projected population growth — councils were identified as either:
  - Above state-average-growth councils — being all councils with a projected population growth that exceeded the state-wide average (about 1.1 per cent).

– Below state-average-growth councils — being all councils with a projected population growth lower than the state-wide average.

Based on these criteria, the groupings are set out in table 2.

2 Council categories

Category	Councils		
Below state-average-growth metropolitan councils	▪ Bayside ▪ Blue Mountains ▪ Georges River ▪ Hawkesbury ▪ Hornsby ▪ Hunters Hill	▪ Inner West ▪ Ku-ring-gai ▪ Lane Cove ▪ Mosman ▪ North Sydney ▪ Northern Beaches	▪ Randwick ▪ Sutherland Shire ▪ Sydney ▪ Waverley ▪ Woollahra
Above state-average-growth metropolitan councils	▪ Blacktown ▪ Burwood ▪ Camden ▪ Campbelltown ▪ Canada Bay ▪ Fairfield	▪ Canterbury-Bankstown ▪ Cumberland ▪ Liverpool ▪ Parramatta ▪ Penrith	▪ Ryde ▪ Strathfield ▪ The Hills Shire ▪ Willoughby ▪ Wollondilly
Below state-average-growth regional and non-metro councils	▪ Albury ▪ Armidale Regional ▪ Ballina ▪ Bathurst Regional ▪ Bega Valley ▪ Bellingen ▪ Berrigan ▪ Bland ▪ Blayney ▪ Bogan ▪ Bourke ▪ Brewarrina ▪ Broken Hill ▪ Byron ▪ Cabonne ▪ Carrathool ▪ Central Coast ▪ Central Darling ▪ Clarence Valley ▪ Cobar ▪ Coffs Harbour ▪ Coolamon ▪ Coonamble ▪ Cootamundra-Gundagai Regional ▪ Cowra	▪ Gilgandra ▪ Glen Innes Severn ▪ Goulburn Mulwaree ▪ Greater Hume Shire ▪ Griffith ▪ Gunnedah ▪ Gwydir ▪ Hay ▪ Hilltops ▪ Inverell ▪ Junee ▪ Kempsey ▪ Kiama ▪ Kyogle ▪ Lachlan ▪ Lake Macquarie ▪ Leeton ▪ Lismore ▪ Lithgow ▪ Liverpool Plains ▪ Lockhart ▪ Maitland ▪ Mid-Coast ▪ Mid-Western Regional ▪ Moree Plains ▪ Murray River	▪ Newcastle ▪ Oberon ▪ Orange ▪ Parkes ▪ Port Macquarie-Hastings ▪ Port Stephens ▪ Queanbeyan-Palerang Regional ▪ Richmond Valley ▪ Shellharbour ▪ Shoalhaven ▪ Singleton ▪ Snowy Monaro Regional ▪ Snowy Valleys ▪ Tamworth Regional ▪ Temora ▪ Tenterfield ▪ Tweed ▪ Upper Hunter Shire ▪ Upper Lachlan Shire ▪ Uralla ▪ Wagga Wagga ▪ Walcha ▪ Walgett ▪ Warren ▪ Warrumbungle Shire

Category	Councils		
	▪ Dubbo Regional ▪ Dungog ▪ Edward River ▪ Eurobodalla ▪ Federation ▪ Forbes	▪ Murrumbidgee ▪ Muswellbrook ▪ Nambucca ▪ Narrabri ▪ Narrandera ▪ Narromine	▪ Weddin ▪ Wentworth ▪ Wingecarribee ▪ Wollongong ▪ Yass Valley
Above state-average-growth regional and non-metro councils	▪ Balranald ▪ Cessnock		

Source: The CIE.

Approach to rate revenue projections

The general approach to the rate revenue projections is as follows.

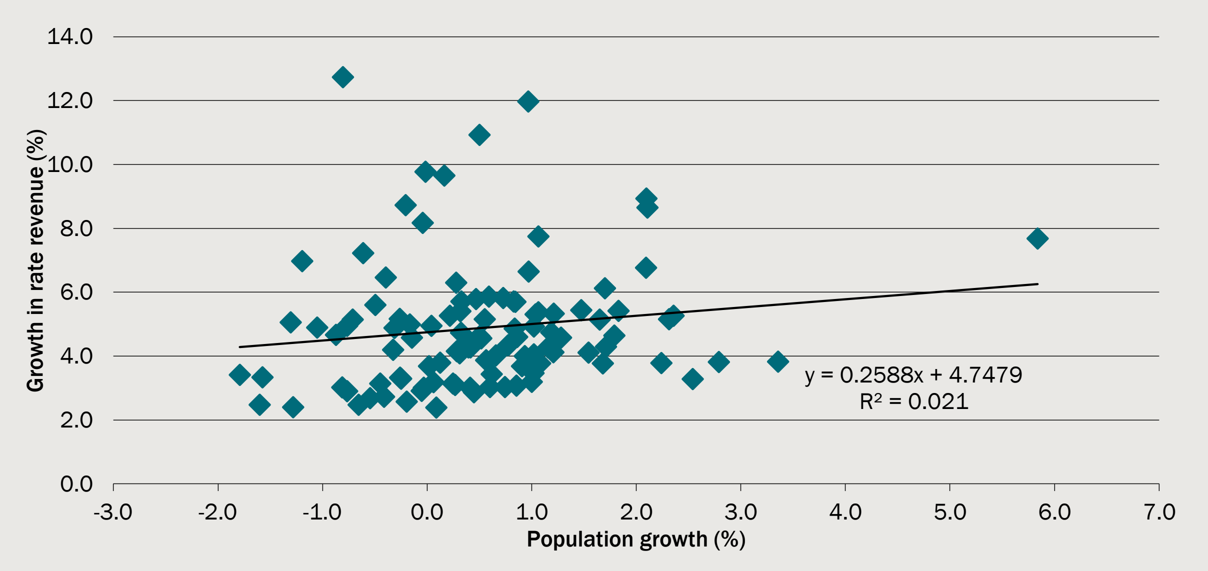
- Rate revenue is projected at the LGA level and then aggregated up.
- The starting point is each council's actual rate revenue in 2018-19.
- Future projections are based on the relationship between population growth and rate revenue (see below).
- The projections are based on NSW Government population projections for each LGA.
- The proposal is implemented from 2022/23 for rate peg adjustments and 2023/24 for local infrastructure contributions reforms.

Growth in rate revenue under baseline scenario

Under the baseline scenario, the growth rate in rate revenue is based on the observed relationship between population growth and growth in rate revenue over the period from 2008-09 to 2018-19. This relationship is weak over this period (not statistically significant) (chart 3), but stronger over a longer period. This relationship implies the following.

- A council with no population growth has on average experienced growth in rates revenue of around 4.9 per cent per year.
- For each percentage point increase in population growth, general income increases by ~¼ percentage point increase in growth in rates revenue, although the relationship is not statistically significant.

3 Relationship between population growth and growth in rates revenue — 2008-09 to 2018-19



Data source: CIE based on OLG data.

Growth in rate revenue under the proposal

Under the proposed changes, we assume that a council's rates revenue would increase by:

- the amount determined by IPART's Local Government Cost Index, plus
- the population growth in the local government area.

Councils would still be permitted to apply for special variations. However, this would be less prevalent, because councils would receive rate increases aligned to their population growth.

Under our baseline assumption, councils were partially compensated for population growth; based on the historical relationship over the 10-year period from 2008-09 to 2018-19, each percentage point increase in population was associated with a ¼ percentage point increase in rates revenue.

Under the proposal, we assume that councils would be fully compensated for population growth (i.e. for each percentage point of population growth, rates revenue would increase by 1 percentage point, rather than ¼ percentage point under the baseline assumption), in addition to the 'base' rate increase of around 4.75 per cent in councils with no population growth.

Changes in infrastructure contributions revenue

Local infrastructure contributions include cash contributions and in-kind works under:

- S7.11 contribution plans
- S7.12 consent levies
- S7.24 planning agreements.

Establishing the baseline

Revenue from infrastructure contributions varies significantly by amount and composition (i.e. the instrument through which contributions are generated) across councils. This reflects differences in the approach to infrastructure contributions taken by councils. As such, infrastructure contributions are difficult to model based on the available data.

- Given the various councils approaches to infrastructure contributions is inherently unpredictable, we based our projections on the average infrastructure contributions (including in-kind contributions) per dwelling approval over the 3-year period to 2018-19.
- The average infrastructure contribution per dwelling for each council is then multiplied by the projected average increase in dwellings for each LGA reflected in the NSW Government dwelling forecasts.
- Total infrastructure contributions were then allocated across the different instruments (S7.11 Plans, S7.12 Plans and planning agreements) based on the share of contributions collected through each instrument over the 3-year period to 2018-19.

This approach effectively assumes that:

- as similar proportion of new dwellings would be covered by infrastructure contributions
- councils would continue with the same approach to infrastructure contributions in the future.

Assumptions for modelling changes to local infrastructure contributions

We have modelled the impacts of the following reforms on local council infrastructure contributions revenue:

- applying the essential works list to all S7.11 contribution plans (rather than just those that go through the IPART approval process) and revisions so the list includes only development-contingent costs
- adjusting the escalation rates applied to local contributions over time
- increasing the maximum S7.12 contribution to the equivalent of 3 per cent of construction value, and
- restricting the use of planning agreements to direct delivery and 'out of sequence' development.

The modelling of changes to S7.11 contributions plans is based on the following:

- Works for community facilities — our estimates assume that this item would be removed from contribution plans completely. Based on the plan composition shown above, this would imply that:
  - contributions from infill S7.11 contribution plans would be reduced by around 9.5 per cent
  - contributions from greenfield S7.11 plans would be reduced by around 1.7 per cent.
- Some works in relation to open space — we understand that councils would be permitted to include basic works (such as the construction of sports fields themselves), but other embellishments (such as seating etc.) would be removed from S7.11 contributions plans. We assume that this would reduce contributions from open space works by around 50 per cent. Based on the plan composition shown above, this would:
  - reduce contributions from infill S7.11 plans by around 11.5 per cent
  - reduce contributions from greenfield S7.11 plans by around 7.8 per cent.

The modelling of changes to S7.12 contributions plans is based on the following.

- The maximum S7.12 levy increases to 3 per cent for new residential development, remains at 1 per cent for commercial and industrial development, and is reduced to zero for alterations and additions (as no new dwellings are produced, it is less likely that this type of development would increase the demand for local infrastructure).

- The levy for lower value developments (less than $200k) change proportionately.

The assumed change in S7.12 contributions are summarised in table 4.

4 Modelled Section 7.12 contribution rates

	Baseline	Proposal
	Per cent	Per cent
Commercial and industrial (<$100k)	0.0	0.0
Commercial and industrial ($100k-$200k)	0.5	0.5
Commercial and industrial ($200k+)	1.0	1.0
New residential (<$100k)	0.0	0.0
New residential ($100k-$200k)	0.5	1.5
New residential ($200k+)	1.0	3.0
Alterations and additions (<$100k)	0.0	0.0
Alterations and additions ($100k-$200k)	0.5	0.0
Alterations and additions ($200k+)	1.0	0.0

Source: The CIE.

The impact of changing the arrangements for S7.12 contribution plans could include the following.

- Councils that would have raised revenue through S7.12 contribution plans under the baseline (including existing S7.12 plans and future plans under the no reform scenario) are likely to raise more revenue. Over the period from 2013-14 to 2018-19, there were 75 councils that collected some revenue from S7.12 contribution plans.
- S7.12 plans would become relatively more attractive to councils, which could encourage some councils that would have raised revenue through a S7.11 plan could potentially move to a S7.12 plan instead.
- The greater potential revenue could encourage some councils that do not raise revenue through S7.12 contributions to do so.

The change in revenue under the changes to S7.12 contribution rates outlined above would depend on the composition of development in areas covered by S7.12 contribution plans.

- To estimate the revenue impact, we assume that the type of development that occurs in areas covered by S7.12 contribution plans reflects the composition of approved DAs in each LGA over the 3-year period from 2016-17 to 2018-19. We assume that 'commercial and industrial' development includes all non-residential development (note: for modelling purposes, we include 'mixed development' in residential development).
- Based on this assumption, the impact on each council's S7.12 varies depending on: whether the council raises revenue through S7.12 contributions; and the composition of development in the LGA. We estimate that the changes to the maximum S7.12 contribution rates set out above would increase aggregate S7.12 revenue by a factor of around 2.2.

The modelling of changes to local planning agreements is based on the following.

- Restricting planning agreements to direct delivery of infrastructure and 'out of sequence' development.
- This is likely to significantly reduce the number of local planning agreements. However, we would expect that in most cases, councils would switch to a S7.11 contribution plan, rather than forego the revenue (including in-kind contributions) altogether.

- We do not have sufficient information to estimate the extent to which moving from a planning agreement to a S7.11 contribution plan would reduce revenue.
- In the absence of data that would enable us to analyse the revenue impact of shifting from a planning agreement to a S7.11 contribution plan, our revenue estimates assume that the revenue (including in-kind works) from planning agreements would decline by 50 per cent.

Further details on the approach to measuring changes in infrastructure contributions revenue is set out on the Productivity Commission's Infrastructure Contributions Review website.[2]

2 NSW Productivity Commission Infrastructure Contributions Review website, https://www.productivity.nsw.gov.au/infrastructure-contributions-review.