



Rate Capping Submission in response to Draft Recommendations – August ‘15

LGPro welcomes the opportunity to make a submission on the Draft Recommendations in A Blue Print for Change, Local Government Rates Capping & Variation Framework Review – Draft Report Volumes 1 & 11.

LGPro made a submission on Local Government Rates Capping & Variation Framework Review in May 2015 and rather than duplicate what was in that, this submission only offers input on those draft recommendations where we have been asked to do so by our members and where we believe it is warranted.

LGPro offers in-principle support to the submissions made by Interface Councils and Rural Councils Victoria as those Councils that stand to be most adversely impacted by the implementation of the framework in its current draft form.

While we believe that there is insufficient evidence to support the introduction of rate capping, we acknowledge the efforts of the Essential Services Commission in undertaking meaningful consultation.

Considerations, Concerns and Risks

- It would be unfair and unreasonable for Local Government to have to pay for any part of the development and implementation of the rates capping and variation framework.
- There is a considerable risk that councillors will be unwilling to seek variations due to a combination of cost to their Council and reputation. The Auditor General has made the point that there is a legacy of underspending on asset renewal. Councils need time to make up the gap and CPI and WPI will not be adequate for Councils to bridge that gap.
- Councils in Victoria collectively spend about \$2Billion per year on infrastructure/capital. This is a very significant amount for the Victorian economy. There is a significant risk that Councils might address the impact of rate capping by decreasing their spend in this area which will have a detrimental affect well beyond Council organisations.
- The same risk, if not greater, applies to investment in staff professional development which, while providing a saving in the short term, will deliver a significant cost as the ability to adapt and perform in a challenging environment will decrease as will organisational performance and the ability to develop and implement productivity initiatives. In addition, professional development plays a significant role in staff attraction and retention with an acknowledgement that high staff turnover, amongst other things, has a high financial cost.

Rate Cap

The recommendation that a single cap be applied to all Councils may very well be simpler but is it fairer?

A single cap for all Councils disregards differences due to the:

- services required by their communities
- state of their infrastructure
- cost of delivering services (which may be constrained and inflated by location)
- availability of other sources of revenue
- demographics and economic circumstances of their communities
- natural environment in which they operate
- existence of two rating systems, i.e. Capital Improved Value (CIV) and Net Annual Value (NAV) with quite different impacts on the two using the proposed approach.

The recommendations provide no acknowledgment or support for the most vulnerable Councils across the state that will struggle to operate under the proposed approach to rate capping and who have little capacity to make applications for variations.

We agree that the rate cap should apply to general rates only and that supplementary rates be excluded from the rate cap in the year they occur.

We also agree that CPI and WPI should be based on *forecasts* produced by the Victorian Department of Treasury and Finance (DTF), but believe that the percentage allocation of each of these should be adjusted. While direct employee costs comprise approximately 40% of Councils' costs, the other major expenditure areas are capital expenses and other non-capital expenses. It is conservatively estimated that approximately 40% of non-capital expenses and 30% of capital expenses are wage related costs. Therefore, the 40% contribution of WPI to the cap formula is understating the wage costs impact on Councils.

We support the recommendation that revenue from special rates and charges, 'revenue in lieu of rates', the fire services levy and service rates and charges should not be included in the rate cap. However no rationale for the ESC to monitor and benchmark service rates and charges has been put forward. In our view this function is completely unnecessary and in the context of rate capping it is incongruous to add another function and cost to this activity.

The rate cap applying to the rates paid by an *average ratepayer* on the face of it seems reasonable but it may well be that rural Councils find themselves disadvantaged under the proposed method due to the nature and quantum of their supplementary rates. Further analysis would need to be done to substantiate that.

The efficiency factor was not part of the consultation that preceded the draft recommendations and there has been no evidence to support its inclusion. The introduction of rate capping is in itself an "efficiency driver". Rather than an efficiency factor it would make more sense to add a percentage to the cap to allow for the backlog of asset renewal expenditure and the cost shifting to Local Government based on evidence of the cost to the sector.

We recommend that:

- ***The framework be amended to provide for 2 caps as a minimum – one for Councils with clear access to generating revenue from other sources and one for those without the same capacity.***
- ***In order to properly account for wage related costs that the cap be based on 40% CPI and 60% WPI.***
- ***The suggestion that the ESC monitor and benchmark service rates and charges is unjustified and should be removed.***
- ***Further and thorough investigation into the impact on different size Councils of using a rate cap based on rates paid by an average ratepayer be undertaken before a rate capping framework is introduced to ensure that small rural Councils that are already significantly disadvantaged aren't further and unintentionally disadvantaged***
- ***The efficiency factor be removed and a percentage be added to the cap to allow for the backlog of asset renewal expenditure and the cost shifting to Local Government based on evidence of the cost to the sector.***

Variation Process

There is a lack of clarity and certainty about the variation process and what Councils will need to provide to support an application. The amount of time and effort that might be required is a significant consideration for smaller, resource strapped Councils. The concerns about the variation process have been compounded by the recent statement by Minister Hutchins in her Ministerial Statement on Local Government on 21 August where she states *“The Essential Services Commission will oversee the implementation of a fair and balanced assessment system including a process for councils to seek authority to raise rates above an annual cap. Such applications will only be supported in exceptional circumstances.”*

We are concerned that the framework as proposed requires that all circumstances would have to be addressed through an application for variation. While we understand that it would be very difficult, if not impossible, to identify and define all circumstances that should not require an application for variation, we believe that this could be covered by a broad definition of “issues beyond a Council’s control such as flood, fire, sector wide superannuation call ...” It would seem to be unnecessarily bureaucratic and very poor use of Councils’ resources particularly at times of crisis to require that a variation application be required.

A recent example of costs beyond Councils’ control is the declaration of a public holiday on 2 October. This would add approximately \$250,000 to the wages bill of a large metropolitan Council to cover the leave and the penalty rates for Council services operating on that day. This expenditure was not provided for, nor predicted when budgets were struck earlier this year.

It appears to be unnecessarily rigid that the ESC will only approve or reject an application for variation and will not be able to negotiate an alternative increase above the cap. This could lead to situations where a Council requesting an increase above the cap is assessed as being eligible for 0.5% less than requested will have the entire claim dismissed.

The timing of the variation application outcomes is problematic. Councils are required to exhibit the draft budget and Strategic Resource Plan for 28 days prior to adoption (per the *Local Government Act*). Should a Council apply for a variation, the proposed notification of the outcome from the ESC in May will not provide sufficient time to update the budget if the outcome is different to the application, publicly advertise, hear submissions and adopt by 30 June (per the *Local Government Act*).

We recommend that:

- ***The ESC or Local Government Victoria develop a template rate cap variation application and consult with LGPro to gain sector wide officer input on it.***
- ***The ESC should have the ability, through the framework, to apply an adjustment to the cap where there are extraordinary matters outside of Councils' control.***
- ***Where an application for a variation above the cap is assessed as worthy of variation, but not at the level requested, that the ESC be able to negotiate an alternative increase above the cap.***
- ***The outcomes of variation applications must be known by no later than the end of March to enable the proposed budget for Councils to be presented in April.***