



Inquiry into Commonwealth Support for Victoria

Submission

October 2021

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1 Executive summary

The Municipal Association of Victoria (MAV) welcomes the opportunity to provide a submission to the Inquiry into Commonwealth support for Victoria currently being undertaken by the Economy and Infrastructure Committee of Victoria's Legislative Assembly.

The MAV is the peak representative and advocacy body for Victoria's 79 councils. The MAV was formed in 1879 and the Municipal Association Act 1907 appointed the MAV the official voice of local government in Victoria.

Today, the MAV is a driving and influential force behind a strong and strategically positioned local government sector. Our role is to represent and advocate the interests of local government; raise the sector's profile; ensure its long-term security; facilitate effective networks; support councillors; provide policy and strategic advice, capacity building programs, and insurance services to local government.

We understand the inquiry is paying particular attention to Victoria's share of GST funding. At the same time, we feel it is important that other forms of Commonwealth support for Victoria are acknowledged, particularly the financial support for Victoria's 79 councils.

Commonwealth support, most prominently through the Financial Assistance Grants program, is a vital component of the financial sustainability of many Victorian councils. This is particularly true for our rural councils. In 2021-22 Commonwealth Financial Assistance Grants allocations to Victorian councils totaled \$646m. This is broken down into two components - \$478m in General Purpose Grants and \$168m in Local Roads Grants¹.

The Commonwealth also provides significant funding to Victorian councils through various specific purpose grants.

Function	Small Shire	Large Shire	Regional City	Interface	Metropolitan	TOTAL
Governance	\$20,001,619	\$254,301	\$1,597,182	\$295,523	\$11,507,269	\$33,655,894
Families & Community Services	\$1,986,003	\$5,623,002	\$13,145,852	\$16,587,598	\$36,077,162	\$73,419,617
Aged & Disabled Services	\$9,259,537	\$16,531,034	\$37,168,615	\$37,961,929	\$117,283,119	\$218,204,234
Recreation & Culture	\$4,259,633	\$5,189,770	\$13,139,887	\$8,903,753	\$11,826,071	\$43,319,114
Waste Management	\$-	\$-	\$-	\$-	\$17,341	\$17,341
Traffic & Street Management	\$1,292,712	\$1,147,500	\$139,109	\$2,078,885	\$199,206	\$4,857,412
Environment	\$4,485,180	\$489,437	\$1,456,449	\$-	\$190,926	\$6,621,992

¹ Other financial data in this submission has been taken from 2018/19 as the most recent year not impacted by COVID-19. 2018/19 allocations were \$434m in General Purpose Grants and \$154m in Local Roads Grants.

Business & Economic Services	\$162,261	\$3,543,323	\$702,844	\$250,000	\$604,479	\$5,262,907
Local Roads & Bridges	\$15,702,241	\$31,987,452	\$11,280,690	\$8,447,423	\$7,819,460	\$75,237,266
Main Roads	\$1,261,061	\$47,530	\$1,497,429	\$-	\$-	\$2,806,020
Other	\$-	\$-	\$-	\$-	\$851,767	\$851,767
TOTAL	\$58,410,247	\$64,813,349	\$80,128,057	\$74,525,111	\$186,376,800	\$464,253,563

Figure 1 - 2018/19 specific purpose federal grants. Source - VLGGC data

Recommendations:

- That the inquiry report acknowledge the significant role Commonwealth grants play in supporting the financial sustainability of Victorian councils and their communities.
- That the inquiry report acknowledge that the rate cap reduces council control over own-source revenue. This in turn increases their need to seek revenue from other sources, including increasing their fees and charges, and seeking specific-purpose grants from both federal and state governments.
- That the Victorian Government continue to advocate to the Commonwealth to increase the quantum of Financial Assistance Grants and to reverse the impacts of previous freezing of indexation.
- That the Victorian and Commonwealth Governments work together to ensure that Victorian councils are better equipped to maintain their local road networks and community infrastructure through a combination of increased baseline funding and continued specific-purpose programs.
- That the Victorian Government advocate for improvements to the Disaster Recovery Funding Arrangements that would enable councils to incur reasonable recovery costs with greater confidence that funding support will be provided.
- That the Victorian Government advocate for ongoing and sustainable funding for early years programs through the Universal Access National Partnership.
- That the Victorian Government advocate for the Commonwealth to fund councils to improve their capacity to respond to climate change

2 Australia's fiscal system

Australia's fiscal system is designed around vertical fiscal imbalance and horizontal fiscal equalisation. Higher levels of government have greater revenue raising powers than more localised government (vertical fiscal imbalance). In 2018-19, 3.4% of tax revenue was raised by local governments, 15.2% by state and territory governments, and 81.4% by the Commonwealth².

Revenue transfer policies have been instituted to allow sub-national governments to provide similar standards of public services while imposing a similar tax burden on their communities (horizontal fiscal equalisation). This includes allocation of GST revenue, Financial Assistance Grants, and numerous grants for specific purposes.

The need for horizontal fiscal equalisation is driven by the varying economic, social, and demographic settings of different jurisdictions. This affects both their expenditure and their capacity to raise revenue. There is arguably greater diversity between local governments than there is between states and territories, and thus a greater need for horizontal fiscal equalisation to support councils.

3 Council finances

Council revenue can largely be broken up into three categories:

- Rates and charges
- Statutory fees, fines, and user fees
- Grants

Collectively these make up around 97% of council revenue³. This is consistent across the five council comparator types described by Local Government Victoria.

² Taxation Revenue, Australia – Australian Bureau of Statistics

³ This excludes infrastructure contributions

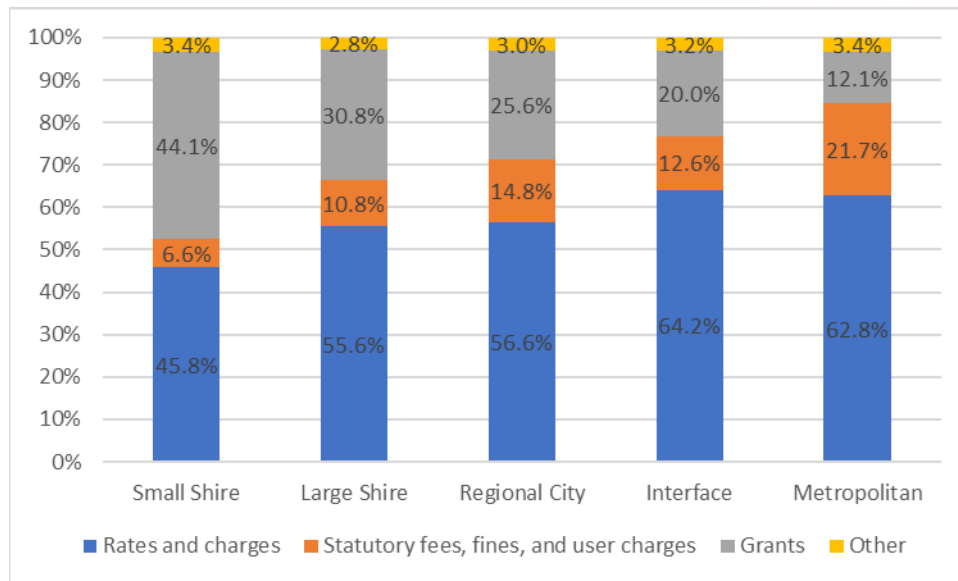


Figure 2 - Council revenue source - VLGGC data for 2018/19 FY

Grants form an important part of the financial sustainability of Victorian councils. Grants are key to implementing goals of horizontal fiscal equalisation.

Rural and regional councils are particularly dependant on equalisation measures. Two factors contribute to this: the capacity of smaller communities to pay, and the often-higher costs in delivering services.

In general, rural and regional communities are more disadvantaged and have lower capacity to pay than metropolitan communities. This limits councils' ability to raise own-source revenue through rates and user fees.

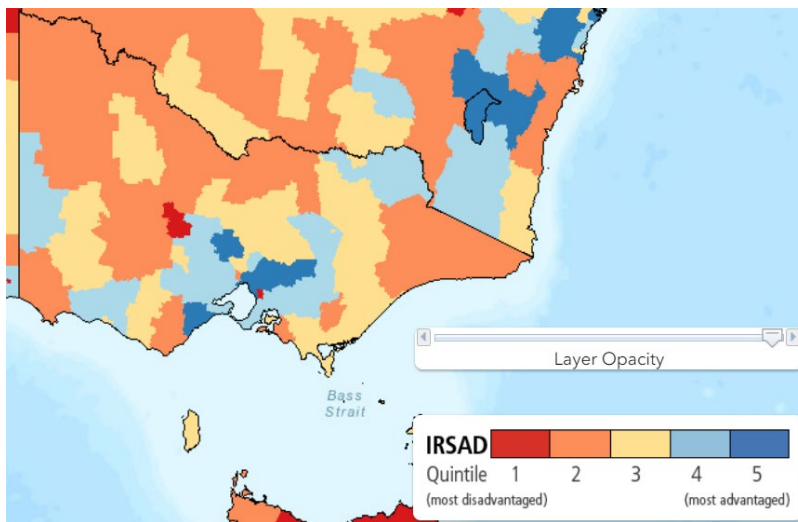


Figure 3 - Census of Population and Housing: Socio-Economic Indexes for Areas (SEIFA) 2016, Australian Bureau of Statistics

Control over own-source revenue is further inhibited for all councils through the year-by-year application of the rate cap. This limits council flexibility in setting rates in response to local conditions. Paradoxically, the current rate cap framework builds in incentives for rates not to be reduced, as doing so in one year will leave a permanent gap in council revenue. This results in reduced investment in community services and infrastructure with long-term negative impacts for Victoria's economy.

Additionally, pressure on council revenues also occurs with executive decisions about property classes to be exempt from the need to pay rates. The current proposal to exempt more than 85,000 dwellings owned and operated by Homes Victoria and community housing associations will cost councils at least \$137 million a year, compounding to \$1.6 billion over a ten-year period. This is despite additional council services needing to be available to support these tenants in need of assistance.

Rural and regional councils face additional factors that increase costs of service and infrastructure delivery. These include:

- Responsibility for maintaining large local road networks
- Geographic expanse of the shire, increasing collection and delivery distances for services such as waste management
- Needing to operate multiple satellite locations for council operations and services
- Relatively smaller populations limiting the ability to benefit from economies of scale
- Increased cost of materials and labour due to distance from population and production centres
- Disadvantaged populations that require additional services

State Governments also regularly place additional responsibilities on councils without a means to resource them. Where resourcing is provided, it will often only cover an implementation or transition period, with councils expected to absorb the long-term operational costs. This has over time increased the dependence of councils on assistance from the Commonwealth.

Councils manage large inventories of assets, particularly when compared to their revenue-raising capacity. Even with grant assistance, many councils struggle to spend on infrastructure faster than depreciation. This is measured through the capital replacement ratio as part of the financial sustainability indicators. The Victorian Auditor General's Office suggest that a ratio of 1.5 or higher represents a low-risk scenario, while a ratio of less than 1.0 indicates high-risk. Taking a five-year average (2014/15 to 2018/19), more than half of Victorian councils had a capital replacement ratio of less than 1.0. This is expanded upon in Figure 4.

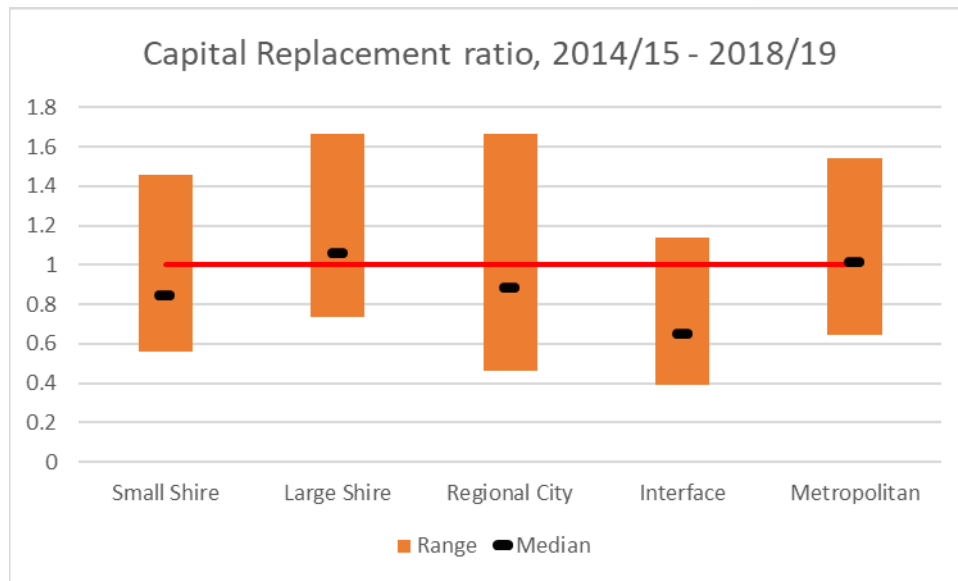


Figure 4 - Capital replacement ratio. Data source - previous year actuals from collated council budgets

4 Financial Assistance Grants

Commonwealth Financial Assistance Grants comprise a significant proportion of council grant funding. Importantly, they are the only major source of untied grants available to Victorian councils. Untied grants, as opposed to specific purpose grants, can be used for any purpose based on local priorities. An important feature of this program is that local government is a genuine partner in the federal system, with the Financial Assistance Grants Program giving local government access to the nation's finances. A fundamental principle in the Local Government (Financial Assistance) Act 1995 is that every municipality receives part of the national tax collection effort.

The allocation of Financial Assistance Grants is split into two methods – General Purpose Grants (also incorporating some disaster assistance funding) and Local Roads Grants. Despite their name, the funding derived from Local Roads Grants is also untied, it is just the method of calculating allocation that varies. In Victoria they are administered through the Victorian Local Government Grants Commission. Allocation is calculated on several factors shown in Figure 5.

The allocation by state grants commissions must abide by principles mandated by the Commonwealth including the minimum grant requirement. The minimum grant requirement currently requires 30% of total allocations to be distributed to councils on a per capita basis. In Victoria this equates to approximately \$21 per capita. 16 councils in metropolitan Melbourne currently receive only this minimum grant amount, totalling just under \$50 million of allocations. That is, if the needs-based allocation were increased and the per capita minimum grant reduced, those councils would receive less funding.

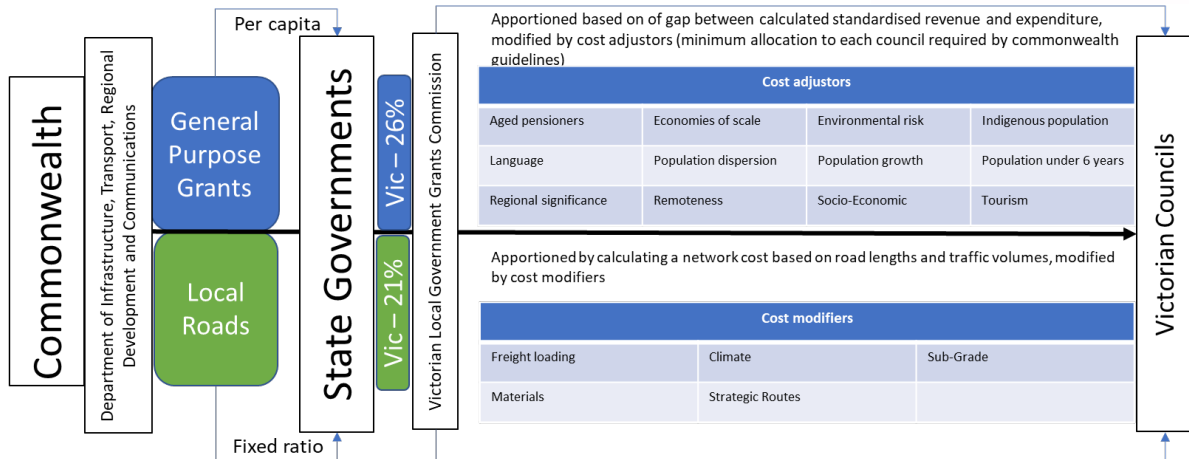


Figure 5 - Financial Assistance Grants structure

In addition to their untied nature, councils also benefit from Financial Assistance Grants being allocated automatically, rather than needing to apply for them. Applying for and reporting on grants is a major administrative burden on councils. For some smaller grant programs, the administrative burden makes the overall value of the grant extremely marginal.

Without the provision of untied grants, rural and regional councils would be unable to sustainably provide a reasonable level of services and infrastructure for their communities.

Financial Assistance Grants allocation 2018-19

Small Shire	\$93,276,727.00
Large Shire	\$156,681,476.00
Regional City	\$111,734,527.00
Interface	\$117,936,965.00
Metropolitan	\$109,048,136.00
TOTAL	\$588,677,831.00

Figure 6 - Financial Assistance Grant allocations to Victorian councils - 2018/19

A 2018 parliamentary inquiry⁴ examined the financial sustainability of Victoria's rural and regional councils. It recommended that the Victorian Government advocate for increased funding through Financial Assistance Grants to address the impacts of a three-year freeze on indexation which commenced in 2014-15. Although this freeze was eventually lifted, it meant that when indexation resumed in 2017-18, grant levels ongoing were from a base some 12.5% lower than they would have been otherwise. Rural councils were particularly impacted by this national decision. Despite the Victorian Government's advocacy, to date no change has been achieved at the federal level to address this shortfall.

⁴ [Inquiry into the Sustainability and Operational Challenges of Victoria's Rural and Regional Councils](#)

5 Infrastructure, roads and assets

Infrastructure grants are one of the most common direct interactions between local government and the Commonwealth. Grants support councils to build and maintain the infrastructure their communities need. Infrastructure grants are also seen as an effective mechanism for localised economic stimulus and to support effective management of the road network.

Victorian councils are responsible for 87 per cent of the state's entire road network – approximately 132,420 kilometres in total (VAGO, 2021) – with a critical role in managing and maintaining safe local networks and associated assets.

Under existing funding arrangements, the relationship between council rate bases and road responsibilities are unbalanced. Many councils, particularly those in rural and regional areas, are unable to deliver on all road priorities. The asset renewal gap also continues to grow.

Due to both legislated restrictions such as the rate cap, and the capacity for rural and regional communities to pay, these challenges require support from State and Commonwealth Governments. There is a need for increased discretionary funding to councils and specific project grant programs (such as the Black Spot removal program which funded Victorian councils \$37.7 million in 2020/21 to address road locations with histories of crashes) to address this. Supporting councils to deliver and maintain high quality infrastructure carries safety and amenity benefits, local stimulus, and whole of economy benefits through more efficient movement of freight and labour.

Roads to Recovery

Roads to Recovery is a longstanding specific purpose grant program for the maintenance of local roads. It is paid by the Commonwealth to local governments (and state/territory governments for roads in unincorporated areas). The Commonwealth has also supplemented amounts available through Roads to Recovery as part of drought recovery.

Councils apply for funding to undertake local road projects. A council must commit an amount of own source revenue equal to their total Roads to Recovery program to road maintenance.

At the outset of a five-year funding period for the program, each council is allocated a lifetime cap. This is the maximum amount of funding that council can receive through the program.

Council group	Lifetime allocation	Estimated 2020-21 allocation
Small Shire	\$ 120,988,243.00	\$ 26,498,131.00
Large Shire	\$ 188,516,851.00	\$ 40,504,080.00
Regional City	\$ 86,151,251.00	\$ 18,767,911.00
Interface	\$ 68,092,969.00	\$ 14,546,635.00
Metropolitan	\$ 63,816,464.00	\$ 13,211,793.00
TOTAL	\$ 527,565,778.00	\$ 113,528,550.00

Figure 7 - Roads to Recovery 2019-24 allocations for Victorian councils

Roads to Recovery represents a significant portion of the \$1.1bn Victorian councils spend on our local road network annually⁵.

Local Roads and Community Infrastructure Program

In May 2022 the Commonwealth announced a \$500 million Local Roads and Community Infrastructure Program. This program provides funding to councils for priority road and infrastructure programs. The focus of the program has been on relatively shovel-ready projects that can also drive economic recovery from the COVID-19 pandemic. Two additional rounds of funding have since been announced for the program, with total allocations to Victorian councils of \$546 million.

As well as road projects, Victorian councils have used this funding for a variety of community infrastructure. This includes active transport, sporting grounds, energy efficient lighting upgrades, and water sensitive urban design.

	Phase 1	Phase 2	Phase 3	TOTAL
Small Shire	\$22,782,614	\$20,106,861	\$45,565,228	\$88,454,703
Large Shire	\$36,186,232	\$39,847,022	\$72,372,464	\$148,405,718
Regional City	\$16,349,269	\$32,211,303	\$32,698,539	\$81,259,111
Interface	\$13,618,594	\$55,273,286	\$27,237,188	\$96,129,068
Metropolitan	\$12,763,296	\$93,727,364	\$25,526,592	\$132,017,252
TOTAL	\$101,700,005	\$241,165,836	\$203,400,011	\$546,265,852

Figure 8 - Victorian council allocations from the Local Roads and Community Infrastructure program – Data source: Department of Infrastructure, Transport, Regional Development and Communications

6 Emergency management

Victorian councils play a critical role in emergency management through mitigation, prevention, support for response, and coordination of relief, and recovery. However, the scope of disasters can exceed the capacity of an individual council to manage. Proactive Commonwealth support is particularly vital in providing financial assistance to allow councils to support their communities and rebuild local infrastructure.

Most disaster support from federal government to local government is through the Disaster Recovery Funding Arrangements, which is a set of joint Australian Government-State cost sharing arrangements. These reimburse councils for some costs incurred via recovery activities following a natural disaster. Disaster-affected councils also receive some additional funding through Financial Assistance Grants.

The MAV has previously identified a number of potential improvements to the Disaster Recovery Funding Arrangements, including in our [Submission to the Royal Commission into National Natural Disaster Arrangements \(RCNNDA\)](#). These include:

⁵ VLGCC data for 2018/19 and 19/20

- Enabling councils to pursue betterment to increase future resilience rather than replacing infrastructure like-for-like
- Funding repair and replacement of a broader range of community facilities
- Better allowing councils to recover costs incurred through resource sharing with other councils, supporting NGO operations, and backfilling council roles to cover for redeployment of staff
- Addressing the high burden of pre- and post-disaster evidence requirements

The MAV is aware that a Commonwealth funding stream for disaster preparedness is being considered, which will include support for projects of local or community significance. This is expected to be welcomed by Victorian councils.

7 Community services

Victorian local government has a long history of delivering community care to older Victorians and people with disability. For the past five years, aged care reforms and the roll out of the NDIS, have resulted in considerable changes to the funding councils receive to deliver services to these groups. The historic partnership model between the Victorian government and councils has been replaced by a market model, reducing local government's ability to influence the quality of care in Victoria.

Councils still providing federally funded services, contribute approximately \$150 million in rate payer funds to continue their high-quality, place-based, accessible services. Current plans by the Commonwealth Government to establish standardised unit pricing could increase gaps between cost of service and actual funding for councils' services and reduce the quality of care in the state.

There is currently limited information available regarding the future of funding for the new 'Support at Home' program, due to begin in July 2023. Significant changes to current arrangements are unlikely to improve councils' capacity to continue service delivery.

In line with these reforms, councils are actively making decisions about their futures in community care service delivery. These changes have the potential to result in a drastically different community care provider landscape and reduce the Victorian Government's oversight of the sector. Ultimately this would limit both levels of government's ability to identify gaps and advocate for service improvements.

Victorian councils also make a significant investment in their children and families. Most councils provide one or more Early Childhood Education and Care Services. The funding for the provision of kindergarten programs in Victoria relies on both the contributions of councils and the Universal Access National Partnership. Since 2009, these Partnership funding Agreements between the Commonwealth and State Government have been short-term.

The MAV has consistently advocated that the funding under the UANP needs to be ongoing and sustainable. A recent review and announcement by the Commonwealth states that from 2022

funding will be available until 2025 but we are yet to see the terms and conditions that are attached to this funding.

8 Climate change

Climate change presents a critical risk to local government and is beyond the financial capacity of councils to address alone.

There are countless projects councils could undertake with funding support that would improve the resilience of their communities to climate change. Future proofing infrastructure from climate risk, improving water security, and making community facilities more energy efficient barely scratches the surface of possibilities for partnership between the Commonwealth and councils in this space.

Accurate and timely information, and access to the expertise to interpret and act upon it is also a barrier for action. The Commonwealth has a role in providing councils with access to local projections on the climate risks their communities face. Support could also be given in the form of best practice guidelines and funding for councils to further develop their own climate action plans.