



MAV Submission to the Rates Capping Inquiry

April 2016

© Copyright Municipal Association of Victoria, 2016.

The Municipal Association of Victoria (MAV) is the owner of the copyright in the publication Submission to Parliamentary Inquiry.

No part of this publication may be reproduced, stored or transmitted in any form or by any means without the prior permission in writing from the Municipal Association of Victoria.

All requests to reproduce, store or transmit material contained in the publication should be addressed to 9667 5555

The MAV does not guarantee the accuracy of this document's contents if retrieved from sources other than its official websites or directly from a MAV employee.

The MAV can provide this publication in an alternative format upon request, including large print, Braille and audio.

Table of contents

1	<i>Introduction</i>	3
2	<i>Expected consequences of the rates capping framework</i>	3
	2.1 <i>Immediate consequences of the rates cap</i>	3
	2.2 <i>Longer-term consequences</i>	4
3	<i>Process issues with the application of the rates capping framework</i>	5
4	<i>MAV Policy response</i>	6
5	<i>Conclusion</i>	6

1 Introduction

The Municipal Association of Victoria (MAV) welcomes the opportunity to provide a submission to the Legislative Council's Environment and Planning Committee's *Inquiry into Rate Capping Policy*.

The purpose of this submission is to provide commentary to the Committee on the current status of the rates capping framework from the perspective of the MAV and provide some guidance around the potential issues and consequences of this policy.

Our position is that the rates capping framework will negatively influence the sector over the medium term, primarily through degradation of the sector's infrastructure, consideration of rationalising councils' services and a reluctance to expand into new service areas.

The consequences of the rates cap are unlikely to be universally felt across the sector; individual councils have differing capacities to respond to the cap.

2 Expected consequences of the rates capping framework

2.1 Immediate consequences of the rates cap

Small rural councils already struggling with cuts to the Financial Assistance Grants (FAGs) program are most likely going to be the most affected by the rates capping framework. This is a consequence of the following factors:

- These councils generally have a strong reliance on rates revenue and external funding, therefore limiting their capacity to utilise other revenue sources, such as fees, fines and charges, to make up any shortfall in core revenue. With per head FAGs grants falling due to the Commonwealth's decision to cease indexation of this program, rural councils will be effectively facing cuts to this program as a consequence of their poor relative population growth.
- Previous MAV analysis has suggested that the small rural councils have a greater susceptibility to financial distress – that is, while there is no obvious causal link between the size or type of council and financial performance, it is also clear that once small rural councils face financial difficulty, it is much more problematic for them to resolve these issues. In effect, the rates capping framework increases the risk that small rural councils will face financial issues in the future.
- The decisions small rural councils need to make in relation to the cap are complex, with many of their communities facing drought conditions and struggling with their own income growth. As a consequence, many small councils may be reluctant to submit an application to increase their rates above the cap due to the potential effects this will have on their ratepayers.

We expect there to be significant diversity on the consequences of the rates cap between individual councils. Some of the tension points previously identified by the

MAV are still relevant to predicting the potential consequences, including population growth far outstripping assessment growth; a high proportion of expenses in direct employee costs; and councils that are effectively 'price takers' in their local markets and will need to respond to broader changes in market input prices that are above the forecast CPI level.

As presented at the Committee hearing, a useful example of the stresses faced by councils in considering whether to apply for a variation is Gannawarra Shire Council. Their rate base is approximately \$10 million and assessment numbers are effectively flat, meaning that the gross increase in rates allowed is around \$250k. Half of this figure — \$125k — will be consumed by banding movements already committed within the award. A further \$25k will be consumed by the increase in postage costs from \$0.70 to \$1, leaving the council \$100k for staffing increases under the EBA and other changes in input costs, such as contract price increases, service expansion, etc. It is estimated by MAV that in order to complete a variation effectively, it will cost in the order of \$40k. Given the lack of knowledge about what will be required to make a successful application, the proportionately high cost of making the application presents an effective barrier to making an application in the first year of the new framework, particularly for a low resource council.

2.2 Longer-term consequences

The MAV expects the rates cap to have negative long-term consequences on local government. The capacity of the sector to manage a cap in the short-term is relatively high. However, insufficient revenue growth will have long-term and catastrophic consequence on the sector as the cumulative effects of small decisions in response to the cap becomes apparent. The following consequences are anticipated:

- An increase in debt levels over time as councils look at alternative funding streams, particularly for long-term assets. This is likely to occur as pressure is placed on the existing infrastructure portfolios of councils and it becomes increasingly apparent that more assets are required. The MAV also notes that the material published by the Essential Services Commission to date appears to support the use of debt within councils, which may prioritise debt before rate increases to fund infrastructure projects.
- The standard of infrastructure is expected to decline over time in response to lower than required revenue. Previous examples of rates capping policies – both in Victoria and in other jurisdictions, such as New South Wales – have suggested that the infrastructure funding (particularly renewal) is susceptible to insufficient funding during times of revenue constraint. While the counter argument is that this will be an aspect monitored by both the Auditor General and the ESC, we do not believe that this will prove to be an effective mechanism.
- There is some discussion within the sector of cuts to services. There is no real evidence of this occurring on a wide-scale basis at this stage, except in some isolated areas for services such as the State Emergency Service and school crossing supervisors. The MAV expects more pressure will be brought to bear on this matter as the cap is in place for several years.

These consequences will have a demonstrable effect on the lives of Victorians. The quality of local infrastructure is important to the liveability of local communities and

their safety. Less renewal capacity will increase accidents on sub-standard infrastructure, while the quality of local facilities – whether public libraries, playgrounds, sporting clubs, shared use pathways or community parks – will gradually reduce.

The threat of increased debt levels and infrastructure gaps will create long-term financial liabilities for the community and hence the beneficiaries of the rate capping framework will be the current community through lower rates, while future ratepayers will be asked to pay higher rate levels to pay down debt and improve run-down local infrastructure.

3 Process issues with the application of the rates capping framework

The MAV believes several process issues are worth raising to the Committee for their consideration.

Uncertainty in relation to the standard required of the ESC to approve a proposed variation to the rates cap is likely to act as an additional barrier to making prudent decisions on appropriate rate increases, at least in the short-term. The evidence presented by the MAV's CEO at the Committee hearings emphasised that the Association has formed the position that it is not our responsibility to tell the ESC how they should judge applications for a rate increase above the cap. Despite this, it is clear that the level of cost associated with the preparation of an application to the ESC, along with the uncertainty in relation to the outcome, presents a barrier. It is the intention of the MAV to provide advice to members on the decisions of the ESC in the framework's initial year to hopefully provide meaningful commentary on the factors that appear to have influenced the ESC's decision.

The structure of the legislation also bears comment. The Minister retains significant discretion in the legislation in the selection of the cap and whether a single or multiple caps are adopted. As such, it is difficult for the sector to predict and plan for future rates caps.

There is also little parliamentary oversight (other than the Committee's inquiry) of the decision on the cap applied each year. It is feasible under this legislation that the Minister may make a determination to cap at wildly different levels. For example, rate increases could be set at zero per cent or at the other extreme it is possible that the Minister may cap rates at a high level (e.g. 10 per cent). This high level of discretion within the legislation suggests the policy intent of reducing councils' rate increases cannot be guaranteed by the legislative instrument that exists.

This issue can be seen by the application of the first year's rate cap. The ESC made a clear recommendation on the appropriate cap level which gave some consideration to the EBA decisions of councils that predated the rates capping policy by incorporating a wage price index component into the rates cap. By ignoring this element of the rates cap, the Government has significantly limited the capacity of councils to plan for the staged implementation of a cap without disruptive influences to their other services.

4 MAV Policy response

The MAV's policy response to the cap has three elements:

1. Identify services provided by the local government sector and advocate for fairer funding outcomes. Examples of this approach include the Maternal and Child Health program, school crossing supervisors program, the SES unit funding, public libraries, etc. The objective of this advocacy is to ensure that appropriate funding underpins those services delivered on behalf of, or in partnership with, the Victorian Government. The MAV believes that the specific purpose funding provided to the sector can be significantly improved by pursuing a wide range of advocacy goals which incrementally improves the funding levels of councils. Further information is provided in the appended brief.
2. MAV is pursuing the Commonwealth through the ALGA for improved Federal funding following the cuts to the FAG program. There has been some success from this advocacy, with the Roads to Recovery program gaining an impressive funding boost with the resumption of the fuel indexation nationally. Our advocacy in partnership with the other state associations will continue with broad goals in relation to increasing federal funding.
3. We have also commenced discussions with our members about establishing a framework for future services delivered in partnership with the State of the Commonwealth. Our recommended principle is that any new function of councils delivered on behalf of the State or Commonwealth should be the subject of a clear funding agreement, with established funding levels and a clear funding duration. At the conclusion of the agreement, the proposal is that the service will stop unless a new funding agreement is entered into. The goal of this advocacy work is to limit the long-term financial consequences to councils of entering new services in partnerships with other levels of government.

As can be seen from these objectives, the MAV is effectively attempting to stabilise and improve the financial position of councils by increasing the funding levels available to councils on a service-by-service basis. This approach is reasonable, as funding from other levels of government has fallen over time relative to service costs.

5 Conclusion

The MAV welcomes the opportunity to provide a submission to the Committee's inquiry into the rate capping policy. We believe that over the next six months an increasing body of evidence will be provided on the initial consequences of the rates capping framework; in particular, we expect to see more evidence about how the ESC considers rates capping variations and hence the likelihood of more applications in the future.

Notwithstanding these matters, the approach of the MAV is to focus on practical efforts it can pursue to improve the financial position of the sector. We believe the sector can make up some of the funding shortfall and reduce the risks of the negative consequences of a rate capping framework by achieving better funding outcomes across a broad range of service areas.

Despite this, the risks from the framework remain significant; ultimately the greatest risk is poor infrastructure combined with higher debt levels within the sector. That is, there is a risk of intergenerational funding inequities, the risk of higher accidents and injuries in the community and of generally poorer quality infrastructure and public spaces. This is a demonstrative and tangible risk to the liveability of Victoria.

MAV Response to Rate Capping

The Municipal Association of Victoria's (MAV) priority actions in responding to the rates capping and variations framework seek to improve the financial position of our member councils. In the current policy environment, our attention is focused on three concurrent strategies:

1. We are seeking to improve the funding for local government by campaigning for a return of indexation for the Financial Assistance Grant program, and through increases in the Roads to Recovery program.
2. The Association is pursuing improved funding in a range of council service areas jointly funded with the State government, including maternal and child health (MCH), the school crossing supervisor program, and public libraries, amongst others.
3. We are advising members to accept any additional service proposals or offerings from the State or Commonwealth without a formal, time-bound funding agreement. Upon expiry of any agreements, we are advising councils to not to continue delivering the service without a new time bounded funding agreement. In the event that funding is cut at any time under the agreement, the service will cease. This approach will require that councils only employ staff for the term of the agreement.

Our immediate focus on the rates capping and variations framework is to assist councils as far as practical to understand the variations process and ensure they are appropriately prepared to make efficient variation proposals.

The MAV has taken a position that the best response to the current financial and political context facing the local government sector is to achieve good negotiated outcomes across a range of council services.

The major headwinds facing local government – the rates capping framework and the cuts to Financial Assistance Grants – are long-term advocacy issues for the MAV. Any positive outcome in these areas will take significant advocacy effort and time to achieve. In particular, the rates capping and variation framework is a key policy of the Andrews Labor Government and has been used politically since the 2014 election campaign as a means of building community support for their government. As such, the policy appears to be a key component of any government led by the current Victorian premier.

Federal Advocacy by MAV

The indexation freeze to Financial Assistance Grants in the 2014-15 Commonwealth Budget, has placed a significant burden on Victoria's councils with an estimated cost of \$134 million over three years. The MAV, as the Victorian member of the Australian Local Government Association (ALGA), has worked with local government associations across Australia to advocate for a return of the indexation.



MEMBERS BRIEF

The MAV has also worked with our interstate peers to advocate for increases and an extension of the Roads to Recovery program to provide additional funding to the benefit of the Victorian local government sector. As part of the policy to commence indexation of fuel excise, the Roads to Recovery program received a significant boost over the 2015-16 and 2016-17 years – councils will receive \$1 billion nationally this year under the program, with Victoria's share estimated at \$203.5m, or an additional \$132.3m over the base funding level. For 2016-17, the estimated funding for Victoria will be \$235.1m, or \$163.9m above normal annual allocation.

Advocacy for better financial support from the Commonwealth Government will continue as part of the ALGA's election campaign. Federal funding of local government will be the primary issue that all parties participating in the 2016 Federal Election will be

State Advocacy

We are continuing in our advocacy against the rates capping framework and will be seeking to build a compelling case in relation to the damage this framework is causing local government and their communities – including deterioration in councils' infrastructure and the related creation of future infrastructure gap, the potential for service levels and quality to decline, and for service innovation to atrophy. This work will collect and analyse the performance and financial data of councils and builds on the Association's almost 20 year time series database of the sector's financial position.

The MAV has been advocating on the following with the State:

Policy area	Advocacy objective	What are we doing?
Maternal and child health	. Sate to meet their agreed commitment to MCH funding of 50%.	The MAV's costing analysis has identified the scale of funding shortfall – the agreed 50/50 funding commitment is now around 60/40 across the sector. The MAV is requiring a major increase in the State's output funding price through the 2016-17 Budget, and is seeking a retrospective payment for the 2015-16 funding year. We have some confidence that the State will respond to the MAV's requests in the upcoming budget.
Home and Community Care program	Support certainty and stability for the HACC program during the transition phase to the Commonwealth	MAV advocacy supported by the State has achieved the Commonwealth's commitment to certainty and stability for councils' Home and Community Care (HACC) program funding until June 2019.



MEMBERS BRIEF

		<p>MAV successfully negotiated with the State to increase the price for HACC services prior to transfer of aged care to the Commonwealth.</p> <p>MAV has successfully negotiated the formation of a 'Trilateral Community Care Officials Group' with the Commonwealth and the State to maintain the strengths of the HACC program in Victoria, This has resulted in a formal agreement through the MAV articulated as a 'Statement of Intent' to be signed shortly at the Ministerial level, recognising the role and investment of local government, and committing the other spheres to consulting with local government on the reforms and transition through to 2019.</p>
School Crossing Supervisor program	Increase the funding for each eligible crossing	<p>MAV is currently completing a costing analysis of the school crossing supervisor program to establish the costs borne by councils for managing the service. This information will be used to advocate for an increase in the program's funding level.</p> <p>The MAV has also advocated for and will be a key partner in, a review of the school crossing supervisor program, which will be undertaken by the Victorian Government and led by VicRoads.</p>
Public libraries	Increase recurrent funding from the State and continue capital funding programs	<p>The MAV has long advocated for improved funding for Victorian's public libraries. Our most recent successes achieved a reversal of funding cuts to the program. We continue to argue that the state's contribution remains inappropriately low and will continue to argue in favour of greater operational funding. We have been successful over time in achieving an improvement in the capital contribution provided by the State and will continue our efforts in this approach in the absence of significant progress being made in recurrent funding.</p>
Planning fees	A review of planning fees to ensure that the level of cost recovery is appropriate	<p>The MAV has advocated for the completion of a review of planning fees, primarily due to the lack of indexation in the planning fees and the view that they have failed to keep pace with the cost of providing planning services. The MAV was successful in securing a review of planning fees in July 2015 through direct advocacy to the Minister for Planning.</p> <p>The MAV has taken a lead role in coordinating the activity-based costing, summarising</p>



MEMBERS BRIEF

		<p>the feedback from council representatives and liaising with the sector on the reform.</p> <p>A draft Regulatory Impact Statement is proposed to be released in April for public comment. The MAV intends to establish a working group to inform our submission to the Regulatory Impact Statement.</p> <p>We believe the current process will provide a positive outcome for the local government sector and will address many of the concerns raised by MAV members.</p>
Distribution of the landfill levy	Allocation of the Sustainability Fund to priority projects	<p>The Sustainability Fund was established in 2010 from excess unspent revenue derived from the State's landfill levy, primarily collected through levies collected by councils. The objective of this fund is to promote waste and resource recovery. Its balance as at 30 June 2015 was \$430m.</p> <p>The MAV is advocating for the significant unspent revenue collected through the landfill levy to be allocated to local government priorities, including for climate change adaptation, and waste and resource recovery initiatives. In line with the Auditor General's report of 2014, some funds should also be directed to rehabilitate closed landfill sites.</p>
SES funding	Establishment of a sustainable and equitable funding model for the SES	<p>Primarily through the historical development of the Victoria SES, local government has provided matched funding for many units. This funding methodology has been haphazard and is inconsistent with other similar statutory authorities, such as the MFESB and CFA, which have operated with clear funding methodologies established through statutes.</p> <p>The MAV's advocacy in relation to the SES funding has focused on:</p> <ul style="list-style-type: none"> • Working with councils to advise them of their responsibilities regarding SES funding. • Direct discussions with SES • Advocacy through MAV's legislated seat on the State Crisis and Resilience Council (and its three sub-committees) - the peak State government emergency



MEMBERS BRIEF

		management policy and reform decision-making committee.
Funding for arts	Increased funding of the arts for local-level projects	<p>MAV has advocated for recognition of the role and investment of local government in arts and culture through national submissions supporting ALGA positions and also the ALGA case for a Community Infrastructure Fund to be established by the Commonwealth.</p> <p>MAV has participated in the National Local Government Cultural Forum over a number of years, representing the interests of Victoria councils to the Australia Council and relevant Federal Government departments.</p> <p>MAV has advocated for more direct funding support and to strengthen the State-local government partnership in our response to the State's Creative Industries Strategy consultation on behalf of councils in 2015.</p>
Roadside weeds and pests	Improved funding for councils' activities	<p>In 2013 the <i>Catchment and Land Protection Act</i> was amended to make councils responsible for roadside weed and pest management. Despite formally assigning councils with the responsibility, the issue of funding for councils went unaddressed. Instead of providing ongoing resourcing, councils found and continue to find themselves fighting to secure short-term funding, which typically only provides one or two years of certainty to the sector.</p> <p>Prior to expiration of the last funding round in mid-2015 the MAV raised the matter in our 2014 State election call to parties, our strategic plan, and in a number of conversations with the State Government. A further two years of funding was subsequently announced. Securing long-term funding will continue to be a priority for the MAV.</p> <p>At its last meeting, the MAV State Council noted that the State's ineffective management of noxious weeds on Crown land and its lack of enforcement action on private land has resulted in many rural areas becoming increasingly infested with noxious weeds.</p>
Local government's role in emergency	Influence the review of local government's emergency	Significant changes to local government's responsibilities in emergency management arose from the Victorian Bushfire Royal Commission. Some of the most emergency-



MEMBERS BRIEF

<p>management</p>	<p>management responsibilities.</p>	<p>prone councils are least resourced to respond to these shifts in responsibilities. Local Government Victoria (LGV) is currently completing a project on councils' emergency management responsibilities. The MAV is working closely with LGV to ensure this project recognises the changing nature of local government since the <i>Emergency Management Act 1986</i> was first introduced.</p> <p>MAV has developed, in consultation with our members, a position paper on the future role of local government in emergency management. This position paper is being used by LGV as an important input into their project.</p> <p>The MAV has successfully advocated for the continuation of the Municipal Emergency Resources Program, which supports councils to access resources required to plan for and support their communities during an emergency</p>
<p>Early years</p>	<p>Improved capital funding support from the Victorian Government</p>	<p>The national 15 hour kindergarten reform was imposed with little if any consultation with the sector, but required councils to invest significantly in infrastructure. Councils had to expand /build new facilities to meet the requirement and are now bearing the ongoing maintenance costs of these facilities.</p> <p>Capital funding provided by government was insufficient. Council rates funded the majority of the infrastructure changes needed – the MAV estimates that \$300m of ratepayer funds was invested between 2009 and 2013, whilst government funding amounted to less than half of councils' investment.</p> <p>Infrastructure costs are a major issue for councils beyond any reform process. With Victoria now having the greatest population growth nationally. Councils, particularly in growth areas, are expected to build maternal and child health facilities and kindergartens to meet new demand.</p> <p>The MAV is continuing to pursue more equitable capital funding contributions from other levels of government to support the significant infrastructure demands required from the State's population growth.</p>

MAV MEMBERS BRIEF

MUNICIPAL ASSOCIATION OF VICTORIA

Prospective Funding Agreements

The MAV has worked with its members to establish a position that the sector should only provide new services on behalf of the Victorian Government in the event that service provision is supported by a time-bound, fully-funded service agreement.

At the conclusion of the service agreement, the local government sector should re-negotiate another agreement with the Victorian Government or conclude the provision of that service. This process is required to ensure that local government is not burdened with new responsibilities that are not appropriately funded.

Advocacy to the Minister for Local Government on this issue is ongoing.

Further information

MAV contact person: Owen Harvey-Beavis

Phone number: [REDACTED]

Email: [REDACTED]