TRANSCRIPT

STANDING COMMITTEE ON THE ENVIRONMENT AND PLANNING

Inquiry into rate capping policy

Melbourne — 24 May 2017

Members
Mr David Davis — Chair
Ms Harriet Shing — Deputy Chair
Ms Melina Bath
Mr Richard Dalla-Riva

Ms Samantha Dunn
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Mr Greg Barber
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Witnesses
Dr John Hamill (affirmed), Chief Executive Officer,
Dr Ron Ben-David (affirmed), Chairperson, and
Mr Andrew Chow (affirmed), Director, Local Government, Essential Services Commission.
The CHAIR — I welcome to the inquiry Dr Ron Ben-David, chairperson; Mr Andrew Chow, director of local government; and Dr John Hamill, chief executive officer, Essential Services Commission. I declare open the public hearings on the inquiry into rate capping, noting that evidence given here is protected by parliamentary privilege; comment outside is not. I will have the committee secretariat swear you in first and then ask for a short presentation. This will be followed by questions.

You are familiar with our terms of reference. I understand you have been ill, and I am pleased that you are healthy again.

Dr BEN-DAVID — Yes, it has been a bit of a saga, and I wish you a speedy recovery. Good evening and thank you again to the committee for inviting us to present. We have handed out the notes for my short presentation. The Fair Go Rates system is now in its second year of implementation. I would like to say at the outset that the commission has learned a lot over the past two years. We have listened to, addressed and adapted to feedback from the sector and from this committee as well as the Peter Brown committee, which we initiated, and we will continue to learn. I would like to take just a few moments to go through some of our work since we were last here in October, and I put on the record my thanks to commission CEO Dr John Hamill and our director of local government, Andrew Chow, for appearing before the committee in my absence in October.

The recommendations of the third report from the committee fall into two categories: the government’s commitment to the Fair Go Rates system and the process and cost to local government and the community. The first recommendation relating to the government’s review is entirely a matter for government, so I will not offer any commentary on how that review should be framed or conducted. On the second recommendation for the cap variation process to be simplified and streamlined to reduce costs to local government and the community, I make these observations.

It is our view that councils that are already complying with their statutory obligations in terms of good financial management, budgeting and community engagement will find that the commission’s cap variation process adds minimal additional requirements. This is becoming evident in the first and second-year application process.

Second, the independent review by Peter Brown that we initiated last year highlighted that while the cost of an application in year one varied between $20 000 and $80 000, albeit there was one outlier, Peter noted that the ongoing cost to councils should become negligible if they incorporate the higher cap application process into their normal corporate planning or apply for a four-year cap.

Third, on that point I reiterate the advice we have given the sector on this matter: that applications need to demonstrate a long-term funding need, which is best established through good, long-term financial planning — that is, the cost of an application should relate to the effort in making the case, backed up by the evidence of good planning. I just want to stress that point because really the cost of the Fair Go Rates system is the cost of good financial management practices already. The marginal cost to a council that does that well will be very low; really, as Peter found, it may be as low as $20 000. We also expect the cost of the community engagement required to demonstrate community involvement will reduce as this process is incorporated into council’s planning cycle. In any case, it should be noted that the cost of an effective application is a one-off, whereas a variation permanently increases the rate base.

The fourth and final point I would like to make is that following the Brown review, our own internal review of the first year of implementation and our ongoing discussions with many councils and peak bodies, we have updated our guidance material with a view, where possible, to streamline and clarify our processes and requirements. I will provide more detail on this in a moment.

I would now like to move on to what has changed since the last hearing and what impact those changes might have for the implementation of the Fair Go Rates system. The first change relates to the time frame for applications. This committee, the local government sector and the Brown review all highlighted concerns that the time frame for the application processes places unreasonable and arguably unnecessary constraints on council planning and decision-making.

In December the Minister for Local Government announced an extension to the deadlines for councils wishing to apply for a variation to the cap for this coming year, 2017–18, to 31 May. This was an acknowledgement that many councils had a significant turnover of councillors in the October 2016 elections. The postponed time lines gave councils more time to prepare their applications following the announcement of the minister’s cap in December 2016. We are also open to the possibility of an earlier application date and an earlier determination of
the annual average cap to facilitate councils’ processes in applying for a higher cap. That may, however, require changes to the legislation. In other words it is beyond our control.

I would now like to touch on the work that the commission has been doing since the last hearing to respond to the feedback from the sector, from the committee’s reports and indeed from the Brown review. As well as ongoing advice and support for councils — and I just want to stress this — the team is always taking phone calls from the sector. Just last month Andrew and a couple of the team were out on the road, going around to all the councils that we were expecting to make an application at that stage. We hold workshops. So we are not sitting up in our tower on Lonsdale Street waiting for them to come to us. We are going out and we are working with them as closely as we can.

As well as ongoing advice and support for councils provided by the team, our published guidance material was updated in October 2016 and again in March this year. The guidance material is comprehensive and, in essence, is a living document that will continue to evolve as new issues or requests for clarification emerge. The latest version responded to clarifications requested in community and council workshops with the sector in November and December last year. I just want to stress that this is guidance material. It is advisory. It is not binding on councils. It does not impose any obligations on them. It is just there to advise them of how we think they can make their path through the variation process as smooth as possible.

Since we last spoke the commission has significantly reduced the annual reporting requirements in terms of the information required by us to meet our obligation to report on compliance with the rate cap. Discussions with councils and policy bodies identified a crossover with the data we were seeking in terms of services and infrastructure information, with much of that data already provided to the Victorian Grants Commission. We now access that data via the VGC, relieving councils of having to provide that information to us. This means we only need to ask councils for information directly related to the calculation of the rate cap and the monitoring of service rates and charges.

In summary we are continuing to seek feedback from the sector so we can continually adapt and improve. We also invite councils needing clarification of the system to meet with council staff. Again just reiterating the point I made earlier, we are not trying to trick them in the variation process. It is really about working with us to get the best application possible so that it maximises their chances of successful outcomes.

I would now very quickly like to take you through some new work that we have started since we last presented to the committee to address some of the underlying issues raised at various stages over the past two years. First, we have commenced a productivity study. This study will assist us in developing an efficiency factor if needed for the purposes of the rate cap formula. That goes back to our original work of a few years ago, which recommended that the rate cap be set based on a formula which included an efficiency factor. At the time we said that we did not know what that should be, but we would do a study to inform us. That is this study that is now underway. We have got a technical working group which consists of representatives from councils and peak bodies, and that working group is assisting us with the study and to broaden our collective understanding — that is, ours and the sector’s — of productivity in indeed the local government sector.

Second, we are also undertaking a growth study to improve our understanding of the effects of population growth on the capacity of councils to provide services and infrastructure over time. Six growth councils have participated in the study. They are sharing information and their experiences with us in how they manage growth. What we are trying to get to the bottom of with this study is what we hear of a lot from particularly growth councils: that growth costs a lot of money and that that money needs to be funded by existing ratepayers. What we are trying to understand is why that is the case. Why does growth not basically pay for itself the way it would in other sectors? The important thing is that both studies are being developed collaboratively with the sector and that we will share the results with them, and the final studies will be made public.

Just finally, on the current processes underway, as of today we have received higher cap applications from three councils: Pyrenees, which submitted probably seven or eight weeks ago; Hindmarsh, late last week; and West Wimmera, earlier this week. We expect two more councils to submit by the deadline of 31 May, namely Towong and Queenscliffe, and we expect to make our decision on Pyrenees, given that they submitted earlier, by the end of this month — so hopefully by this time next week. For the other four councils we expect to make our decisions by the end of July.
Finally, just to address the waste charge issue, I would now like to briefly touch on the Yarra council waste service charge proposal, which has attracted significant media coverage in recent weeks. As members of the committee are possibly aware, Yarra City Council proposed to introduce new waste charges in their draft 2017–18 budget. The Minister for Local Government subsequently requested the commission to provide advice on the proposed charges. We provided our advice to the minister on 4 May, and our advice is now available on our website, and we have circulated a copy.

Our advice centred on the concept of revenue neutrality. This is basically a concept explained in our guidance material. Basically it encourages councils to show that when they introduce a new waste charge, it has a neutral impact on their ratepayers, so they are just transferring one source of revenue to another source, but the overall revenue collection is the same.

The CHAIR — Is that the case key here, in Yarra’s situation?

Dr BEN-DAVID — Well, they have not made a final decision yet. What they were proposing, though, was to keep their rate base unchanged and to introduce a new levy. So that would have actually increased their overall revenue take by around $8.5 million.

Mr MELHEM — And the actual rate will go up to reflect that?

Dr BEN-DAVID — No. So what they were proposing to do is — —

The CHAIR — The take from the community would go up.

Dr BEN-DAVID — The total take. So the rate would have gone up by 2 per cent, as per the minister’s rate cap, but then they would have introduced a new charge, which would have been an additional amount of funding. So the overall funding would have increased by about $8.5 million in 2017–18.

The CHAIR — I thank you for your contribution and for the material you have provided, and I put on record the fact that some of the work the committee has done in terms of systematising data collection has actually had some effect, and we are pleased to see less onerous data collection arrangements on councils where the data was already in the public domain in one way or another, or in the provision to one public entity it should not be provided to another one in a process that duplicates. So we are pleased on that. The Brown review: as I understand it, you initiated the Brown review.

Dr BEN-DAVID — Yes, that is right.

The CHAIR — Was there any conversation with the minister’s office at that point?

Dr BEN-DAVID — I cannot recall, but I would imagine we told them that we were planning on initiating a review.

The CHAIR — You told them you were going to do it, or you spoke to them and sought input?

Dr BEN-DAVID — No, I think we would have just told them we were planning it. To be honest — it is a year ago now — but I think that after we made our decisions, we may have met the minister once more after that, and we may have told her we were planning on initiating this review.

The CHAIR — You might want to provide the details of those meetings. That would be helpful — the dates.

Dr BEN-DAVID — Yes, we can look at the dates of that meeting.

The CHAIR — Thank you. And as I understand it, Mr Brown was chosen. How did you arrive at the choice of Mr Brown? I am not reflecting in any way on his capacity. I think he is a knowledgeable individual.

Dr BEN-DAVID — I will have to ask Andrew to answer that.

Mr CHOW — Peter Brown was the ex-CEO of Moreland City Council, as you are aware, and is quite reputable in the sector. We actually asked around both in terms of other CEOs and other people in the peak bodies who they think might be useful to undertake this study, and two names came up. One was Peter Brown,
and the second one was Andrew Newton, whom you know is the ex-CEO of Glen Eira City Council. We spoke to both of them, and Andrew could not make it and Peter was able to undertake the task.

The CHAIR — Peter then undertook a review. It is my understanding that a draft copy of his report was provided to the minister’s office before the report was complete and finalised.

Dr BEN-DAVID — I do not think I recall. Can we confirm that — take it on notice?

The CHAIR — You can. But you are not aware of that?

Dr BEN-DAVID — I do not recall. I honestly do not recall.

Dr HAMIL — It is fairly common practice for us to provide reports to ministers, but it is almost always just for their information.

The CHAIR — Finalised reports?

Dr HAMIL — And it is very rarely for consultation and feedback. So we typically provide the report — —

The CHAIR — My understanding is that this was a yet-to-be-finalised report.

Dr BEN-DAVID — No, my staff is advising that we did not provide a draft report. We provided the final report to the minister office, and I imagine we provided that to the minister — —

The CHAIR — I just advise you, you are under oath.

Dr BEN-DAVID — Yes, I would not say it if I did not believe it.

The CHAIR — Good.

Mr MELHEM — Can I ask the relevance about this to the inquiry, Chair, because the Chair talked about rate capping, and I think the Brown review was not relevant to the rate capping. Would that be correct, Dr Ben-David?

The CHAIR — It is very relevant to the rate capping, and it is a review of the process of assessment and variations.

Dr BEN-DAVID — The review was to assess whether the Essential Services Commission fulfilled its obligations as effectively as possible.

The CHAIR — Under the legislation.

Mr MELHEM — Right.

The CHAIR — That is right. So it is very directly related.

Mr MELHEM — Well, I just find it a bit curious that a year later you are asking this line of questioning, unless you have got something to enlighten all of us about.

The CHAIR — Well, it is my understanding that a draft copy was provided to the minister’s office before it was finalised. So that is why I am asking, and that is why I am asking the question.

Dr BEN-DAVID — I am being advised that it was not, or at least we do not believe it was.

The CHAIR — I am pleased to hear that.

Dr BEN-DAVID — But I would say that the final report would have been provided to the minister’s office — —

The CHAIR — Of course — and the world.
Dr BEN-DAVID — And probably shortly beforehand it would have been released publicly, but it is, as John says, our practice with all reports to provide them to ministers a day or two before they are made public.

The CHAIR — I thank you for that response. The point I would also like to ask about is the City of Yarra and the additional rates that are being sought there, whatever denomination they may put on it, or whatever category they may claim. You are saying $8.5 million extra would have been provided by the ratepayers of the City of Yarra to the council under the proposal.

Dr BEN-DAVID — Yes, if the City of Yarra proceeded with its proposal to introduce the waste charge, as has been presented publicly, that would have resulted in an additional $8.5 million of revenue.

The CHAIR — It is my understanding across the state that a majority of councils, I think, actually have a waste charge, but the waste charge with the basic rate adds up to an aggregate number, and that only a minority of councils — and you might give me the list, Mr Chow, if you have that — do not have such a waste charge but incorporate, in effect, the waste component in their general rate.

Dr BEN-DAVID — That is right. Just bear with me, Chair. There are four councils that we believe wholly recover waste only through general rates as opposed to a waste charge. I can advise you of those: Darebin, Monash, Whitehorse and Whittlesea. Other councils over the last little while have moved from a general rate to a service charge. That includes the Borough of Queenscliffe and Mornington Peninsula Shire Council. They have established a waste charge. Knox has similarly advised us just in the last week or two weeks that it is planning to do the same.

The CHAIR — In those cases it is without an increase in rates beyond the aggregate cap.

Dr BEN-DAVID — Yes, it is what we call a revenue-neutral introduction.

The CHAIR — And you have no objection to that scheme?

Dr BEN-DAVID — No.

Mr MELHEM — A council that applied for a higher cap for more than one year, and I think it would be the first council to do so, can you tell us how you would assess their application? Do you assess it differently than, let us say, a council that only applies for one year? Do you have a certain formula for assessment for one year, two, three or four? I understand you can do up to four years. Would you take a different approach or is your assessment criteria the same?

Dr BEN-DAVID — It is basically the same, but maybe I will let Mr Chow answer that.

Mr CHOW — The basic approach is still the same. In order to apply for a higher cap, they need to demonstrate on the one hand that they have a long-term funding need, and that needs to be demonstrated consistent with their long-term plans, whether you are looking at it in one year or multiple years. You look at a cumulative effect of the four years, if they are applying for four years, or you look at the one year. But in both cases the long-term impacts have to be analysed by the council.

Mr MELHEM — Would that include some sort of long-term project I might have, for example, over a forward estimate, two or three years? They have got to actually convince you. If it was business as usual, there is no medium to long-term project, basically you would not think, ‘I'll put in an application’.

Mr CHOW — Basically you look at the long-term trends on the revenue side versus the expenses side. You know that projects can come in and out, and they can be lumpy — capital projects. But they have got to adopt a long-term view, because a higher cap when it is granted is embedded into the rate base, from the point that it is approved. It has to correspond to the council demonstrating that there is a long-term funding need.

Mr MELHEM — What is the effect? Is it an advantage if a council could consider applying for multiple years, for two or three years, for example? Is there an advantage in doing that? For example, I can think of the cost of putting an application in, even though it is negligible. But what are the advantages?

Mr CHOW — The advantage will be the clarity about the amount of their revenue generated over the four-year period. But in order to do that they have to have supporting evidence in regard to the fact that they
have good financial planning, they have a good long-term financial plan, they have good asset management, they do their service review, they engage with the community. When they are in a position to demonstrate that, in terms of the need for long-term funding, then they would make a case for a higher cap.

Dr HAMIL — I guess — and Andrew or Ron may correct me on this — the advantage for a council in applying for a longer term rate cap would be that it would be given more certainty over a longer term horizon. But I guess it would also consequently rely on them to have a greater deal of sophistication over what their long-term position is really to be able to have — —

Mr MELHEM — And predicting what the CPI would be like.

Dr BEN-DAVID — It is not just that. To be honest, it is probably more the funding from external sources and how predictable that is, and so I suppose their confidence and their ability to manage their finances over a longer period. Let me just give you an example, Mr Melhem. Hindmarsh has applied for a single-year higher rate cap of 4 per cent. Pyrenees, which we have already received, applied for a two-year higher rate cap of 3.5 per cent in each of the years; and West Wimmera has applied for 3.5 per cent in each of the next four years.

Mr MELHEM — So that is one for four years.

Dr BEN-DAVID — We do not tell councils what to do; it is completely up to them in terms of what they see as their risks, their business needs, as to how they structure their applications. We assess each one on its merits.

Ms BATH — I notice that Towong is up near Albury, so it is very rural as well. The last three that you have commented on are quite rural with, I guess, their own issues in relation to potentially a decreasing population base rather than an increasing population base. There is Towong up near Albury, as I said, and then Queenscliffe looks like it would be a solid or increasing population base. I guess in terms of making recommendations for us to consider, and we did not fall on this position, but with a country versus city — I am using city as a very regional and rural space in terms of a rate cap — if population is declining, they are really going to struggle to maintain services and infrastructure and spend et cetera going forward. Can you comment on that?

Dr BEN-DAVID — Yes. Certainly one of the very, very important factors we look at is their financial sustainability. We look at various indicators, and maybe Andrew can comment on that in a moment. Clearly a council in that sort of situation that you described will have or can be expected to have weaker financial indicators, and that will influence our decision. But what we are not in a position to comment on is, shall we say, the affordability of that for the community. That is a matter for council to deal with, not for us. What we have to say is, ‘Have they done the work to support their application? Is the need clearly there?’. Matters of affordability, fairness, equity — they are matters for council and indeed government policy. They are not matters for a regulator to deal with. Do you just want to talk about the sorts of indicators that we use?

Mr CHOW — Yes. Let me go back a step and mention the legislative objectives. It is on the one hand looking at the long-term interests of the ratepayers, the community, in terms of sustainable services and maintenance of critical infrastructure, and on the other hand the financial capacity of the councils to perform their functions and provide services. It is quite important for us to have regard to the differences between the metro councils and the smaller regional councils, and there are clear differences between them. The metro councils have a greater flexibility in terms of alternative sources of income, whereas the rural councils do not. The rural councils are highly dependent on grants, whereas grants make up a smaller proportion of the mix of revenue that the metros collect. The rural councils too are subject to huge infrastructure, many roads — —

Ms BATH — And roads. I was going to say roads, roads and more roads and bridges.

Mr CHOW — Yes, that they have to maintain and operate. They also, as we mentioned before, have a rate base that is either small or shrinking. So in regard to that, in our analysis when they do apply for a higher cap, we look at the number of what we call the LGPRF, the local government performance reporting framework, their financial indicators — looking at their ability to finance operations, cashflow, debt ratios and the leverage ratios, so that we get a good sense about both their starting position and their long-term financial outlook.
Dr BEN-DAVID — Can I just clarify one point? You made reference to capacity to pay. That is, we look at the council’s capacity to fund, not the community’s capacity to pay.

The CHAIR — The councils look at the capacity to pay.

Dr BEN-DAVID — Of course, that is their role.

Ms BATH — A couple of things: with the loss of the country roads and bridges program have you done any analysis, or does that come through when the applications are there? Do they make comment on that in their applications?

Dr BEN-DAVID — The latter; we wait for them to tell us what the impact is rather than us trying to second-guess or model what it might be.

Ms BATH — And based on, from last year, their comments, because — were there nine last year?

Dr BEN-DAVID — Yes.

Ms BATH — And they were regionals, very much, I think. There were predominantly regionals, or a mix, was there not?

Mr CHOW — A mix.

Dr BEN-DAVID — It was a mix last year.

Ms BATH — I think there were five and four, potentially. I am doing that from memory. Can you recall the regional comments around the loss of the country roads and bridges program?

Dr BEN-DAVID — Sorry, I cannot remember. We can take that on notice, but I — —

Ms BATH — Could you do some research? That would be good. Anything available, that would be useful — so if they have made reference to it in their variation, or if they have provided some documents about the impact of the loss of it on their bottom line.

Dr BEN-DAVID — We can get that information quickly, but we just do not have that at hand.

Ms BATH — One last question, Chair. We have got five on the table now, or almost on the table. Do you know if there are any further coming? Do you know if there are any other variations or any metros presenting?

Dr BEN-DAVID — No, we do not.

Ms BATH — It is just still a wait and see this stage.

Dr BEN-DAVID — We would have hoped that by now they would have contacted us given it is a week now until the cut-off.

The CHAIR — So no metros?

Dr BEN-DAVID — No metros, no. Earlier on there was talk of Casey applying, but that dropped off pretty early on.

Mr RAMSAY — There are a couple of issues I wanted to raise with you. The City of Greater Geelong has indicated that they also will be seeking a separate waste levy charge on their ratepayers, which I assume is to be able to access revenue over and above their cap, because it actually previously was incorporated as part of the rate. So it seems to me where one does, others will follow, and it seems like a whole lot of councils now are looking at potentially trying to raise tax levy outside the cap, and the City of Greater Geelong have indicated through letters to their ratepayers this is what their intention is — to have an additional charge, a waste charge. So I am just wondering, as a sort of a corporate policeman of the rate cap, how you would deal with those councils that are trying to weasel their way out of the cap in looking at additional taxes and charges?

Dr BEN-DAVID — I am not aware of that particular Geelong case; are you?
Mr CHOW — I am not.

Dr BEN-DAVID — We have not heard that. First of all, if a council wants to set up one of these service charges, we do not have any jurisdiction over that. What we do after the fact is we monitor. Every two years we will monitor what we are calling outcomes for councils, and that will look at, for example, their overall revenue take. So we would pick up, but that is after the fact. We do not have any role in approving or testing or in any way scrutinising a proposal for council to introduce a service charge. That is exactly what happened with the City of Yarra; they wanted to introduce this. We had no role other than the minister asked us to advise her on what this was all about. So no, we cannot stop that. What we do say in our guidance material, however, is our expectation would be that when a new charge is introduced, it would be introduced on a revenue-neutral basis so the overall take from community was not increased. But that is guidance; it is an expectation. It is not something that we can enforce.

Mr CHOW — We also mention in our guidance that over time where the information becomes better we might look at how those costs move over time and whether there is any possibility of benchmarking those costs between comparable councils. But it is after the event. It is really a monitoring task to see how those costs are travelling over time.

Dr BEN-DAVID — I can provide you with a copy of an extract from the guidance material that goes to this issue of revenue neutrality, if that would be helpful.

Mr RAMSAY — Actually I think I have seen the documentation. I was not convinced it was neutral.

The other question, if I may pose it, Chair, is in relation to sustainability of regional councils, and there is a joint parliamentary committee actually doing an inquiry on that as we speak. If I can use Ararat Rural City Council as an example, their proposal is — farm differentials were to provide equity, particularly for those paying significant amounts of land tax, or rates, for another word, and the differential is applied to provide greater equity for those large ratepayers that have large land for production purposes. So Ararat Rural City Council has seen in their wisdom to remove the 55 per cent differential that the council implemented some years ago, which means now that small section, 24 per cent of the ratepayer base that pays 40 per cent of the total revenue, is looking at a 40 to 50 per cent increase in rate. Also the government’s policy of annual valuations, as I understand from councils that have contacted me, could cost anywhere between $120 000 to $200 000 in additional costs to councils to outsource those annual valuations. So a small council like Ararat city is now looking at trying to meet its cap requirements by taxing a small demographic significantly more — 50 to 60 per cent — to keep within the cap but also keeping the rates low for other demographics because they have only got one pool of money. Then of course they have been challenged by all these additional costs the government are imposing in relation to policy. So the question is: how do you deal with fairness and equity in small, unsustainable councils that are trying to meet cap? They have government policy that is imposing greater costs onto them, yet their only real opportunity is to shift the cost burden across to those ratepayers that they think perhaps could afford more to pay for it.

Mr BEN-DAVID — Okay. There is quite a lot in that question.

Mr RAMSAY — I guess I am flagging you through. This is what is going to happen, particularly with small councils that do not have any flexibility.

Mr BEN-DAVID — Yes. On the issue of the annual valuations and the additional cost to councils, we cannot comment on that. We were not involved in that at all. What I would expect, over the coming years is that if that puts financial pressure on those small councils, they are more likely to apply to us for a variation if the rate cap set by the minister is not high enough. I think that is the only thing I can say in regard to the additional costs that might come with the new valuation methodology or approach. But I do not know anything about that. We were not consulted, so I do not know whether those costs that you cited are reasonable or not. I cannot comment on that.

The CHAIR — On that, just to understand what would happen here, I understand that with the annual variation or the annual rate arrangement, now that this being centralised many of the employed valuers at local councils will no longer be needed, so there may well be redundancies. How would that be treated?
Mr BEN-DAVID — I imagine it will be treated like any one-off cost by council. Again, like any, shall we say, unexpected one-off cost, they will need to demonstrate to us if they cannot meet that cost within their own resources. Then they, I presume, will come to us for an application, and we will have to deal with it.

The CHAIR — For a contractual arrangement a council might have with the valuation consultancy firm which is binding and then they renege on it because of legislative override, would that — —

Mr BEN-DAVID — Look, I cannot comment on all the different possibilities or permutations that could occur out there. The only place we would get involved is if the council had a funding shortfall it could not manage internally. It would make an application to us, and we would have to assess it.

The CHAIR — What about systemically across the state where every council is impacted that employs valuers? Would that count in your base calculations?

Mr BEN-DAVID — Well, remember that the minister sets the whole-of-state cap.

The CHAIR — But you advise.

Mr BEN-DAVID — We would advise; that is right. If it was a significant impost, we may have to have a look at it. I think that is a fair point.

Mr HAMILL — I guess the question that would be quite tricky in that situation would be whether the impost was consistent across the state such that you could really add something into the base rate. It is kind of a fairly common regulatory problem when you are looking at price cap regulation where a cost is introduced of a regulatory nature by whatever government is in place. How you would account for that is very difficult, given that different parts of the sector had a different starting point in terms of their existing cost base.

Mr BEN-DAVID — And then there are the other things. There are swings and roundabouts. If there are additional costs here but there are savings there, as you said, because of redundancies, over the longer term — —

The CHAIR — So redundancy is a cost issue short term?

Mr BEN-DAVID — Short term. I was just going to say in the longer term all of that would have to be taken into account. That is why it is so hard to give a simple answer.

The CHAIR — I think the annual valuation, paid for by council — every council will pay that annual valuation fee. At the moment they have the cost of only buying a valuation.

Mr BEN-DAVID — We would have to have a look at that. But just coming back to Mr Ramsay’s comment on the differentials issue in regard to Ararat, I actually only saw that this morning in the newspaper clippings. That is a matter solely for council. We do not have any role in differentials because that is a matter of equity amongst their ratepayers. What we do is we set the overall amount of revenue — rates. How they are collected from different parts of the community is completely at their discretion.

Mr RAMSAY — Would you advise other tools, like the municipal charge, as a means for councils to use a greater equity share of the pool, if you like?

Mr BEN-DAVID — No, we do not provide any advice along those lines.

Ms HARTLAND — I have got several questions. My first is: how many councils last year applied for an increased rate, and how many were rejected?

Mr BEN-DAVID — Nine applied. Five were approved in full, one was approved in part and three were not approved.

Ms HARTLAND — Has there been any work done on the issue of the fact that some councils are really going to struggle in terms of their major infrastructure work and they are going to have start deciding what it is that they are going to put off so that they can continue with things like Meals on Wheels et cetera? Has there been any work done on that, especially for smaller councils?
Mr BEN-DAVID — Not by us. We would hope that councils are doing that work themselves and then — —

Ms HARTLAND — How do you expect councils to do that work? They clearly will know what they can spend, but this is the thing that has always surprised me about this legislation and is the reason we voted against it. Councils are not going to manage, and footpaths are not going to be done and a whole lot of other work. I am a bit surprised the government or yourself have not actually looked at what is not going to be done because of rate capping.

Dr BEN-DAVID — All I can say is that we have not done that. We were not asked to do that. What our work with the sector has been — and this is regional, rural, metro councils — is that we would expect them to be doing that work. I should say the thing that we have learnt out of all this is the small rural councils are the most innovative. Though they are obviously under the greatest financial — —

Ms BATH — That is country people in general.

Dr BEN-DAVID — Necessity is the mother of invention.

Ms HARTLAND — All right, so they decide to keep home help but they have to start saying, ‘We cannot do roads or footpaths anymore’. Is there any scope for that to be looked at? Because I think it is quite a serious issue for councils, who are going to have to decide which services they are going to keep and which ones they are going to have to give up.

Dr BEN-DAVID — Again that is a matter for them and their ratepayers and then possibly for the state government, but not for the regulator. Where our role comes into it is, as I said a little earlier, every two years we will do a review of the outcomes of the legislation. We recommended that to government nearly three years ago, and the reason we recommended it was because we did not want the consequences of the rate capping framework to be hidden from the community. We wanted them to be seen — for example, what happened in New South Wales in the 1980s when they introduced rate capping was councils just stopped maintaining their assets. Of course that is okay, you can get away with that for a year or two years or a decade or even two decades, but eventually it catches up.

Ms HARTLAND — Where do you expect them to find the money to continue maintaining the assets if they cannot raise higher rates and the state government and federal government are cost shifting all the time to local government, so where will they find the money?

Dr BEN-DAVID — That is not a question I can answer.

Ms HARTLAND — If we could move on to the issue of the City of Yarra, I have some technical questions and you may need to take these on notice. My understanding of this is that on 4 May you wrote to the Minister for Local Government regarding the proposed waste charges that were part of the draft budget for 2017–18 for the City of Yarra, providing advice on the context of rate capping. Could you advise me under what legislation the Essential Services Commission is permitted or required to intervene in a draft budget under development by a local government? As I understand it this was prior to the budget being submitted to the minister for approval.

Dr BEN-DAVID — We were asked by the minister for advice. Given that it was only advice and therefore had no binding effect, as a courtesy we responded to that request.

Ms HARTLAND — It is my understanding that the advice you gave was that it was:

… necessary to distinguish between Yarra’s compliance with the letter of the law versus whether its actions were within the spirit of the law. We believe that our guidance reflects the ‘spirit of the law’.

This is a little bit confusing. I do not want to get into the whole The Castle kind of vibe thing, but is this about the legislation or is it not? What are the requirements of council and what is the requirement of the Essential Services Commission in terms of the advice they give the minister, because that is not terribly clear to me?

Dr BEN-DAVID — We made it very clear. Well I hope the letter is clear, and you should have the letter with you.

Ms HARTLAND — I have it.
Dr BEN-DAVID — We were not in any way suggesting that Yarra’s proposal was contrary to the legislation. What we were saying is our understanding of the legislation, as we reflected in our guidance material — and as I think has been understood by the sector, by their actions — was that if a new charge is to be introduced, it would be introduced on a revenue-neutral basis. That was our understanding of the intention.

Ms HARTLAND — If I can go further — and you wrote to the minister. You wrote:

Based on publicly available information, it appears that Yarra has engaged with its community about the introduction of the new waste charge. We welcome council’s efforts. However, it appears Yarra has not fully explained to its community how they propose to use the additional —

funds raised. Your letter is dated 4 May. The City of Yarra’s online consultation portal was open for most of April, with information as to why the waste services charge would be required. The City of Yarra’s consultation closed on 11 May with a special meeting hearing verbal submissions on 17 May, yet your letter is dated 4 May, so how could you have known when you wrote the letter on 4 May the full extent of the engagement by the City of Yarra?

Dr HAMILL — The advice was written at the time it was written because the minister requested the advice by a particular date, so I guess it was written based on the information that we had to hand at that time.

Ms HARTLAND — Your letter says:

… it appears Yarra has not fully explained to its community how they propose to use the additional —

funds. Yet it is quite clear they have gone through a number of steps, but you wrote this advice before the consultation was finished.

Dr BEN-DAVID — Let us be clear. What we were saying is we were not in any way disputing the fact that the council, the City of Yarra, had consulted its community on the introduction of a waste charge that would raise $8.5 million. We quite openly recognised that. What we were saying though is they had not consulted their community — from anything that we could see that suggested they had consulted their community — on the net increase of revenues of $8.5 million and for what that $8.5 million would be used. That is what we could not see.

Ms HARTLAND — My point is that you wrote that letter on 4 May and that consultation continued until 17 May, so how could you possibly have known what the consultation contained when you wrote the letter on 4 May and it did not finish for almost three weeks afterwards?

Dr BEN-DAVID — Because at that stage everything we could see was around the introduction of the waste charge only, not the increase in overall revenue.

Ms HARTLAND — I am really quite surprised by this — that you would write a letter when the consultation was not finished. I do not understand that. I have got a few more questions, but other people might have some.

Mr CHOW — Can I respond to your earlier question? If you look at the same letter that you quoted, the last sentence states:

We understand that Yarra is currently consulting with its ratepayers on the proposed waste charge and a recommendation to include the waste charge as part of its final adopted budget is yet to be made by the council.

Ms HARTLAND — Then why did you say:

Based on publicly available information, it appears that Yarra has engaged with its community about the introduction of the new waste charge. We welcome council’s efforts. However, it appears Yarra has not fully explained to its community how they — —

So you have got contradictory information in the one letter. I do not understand that.

Dr BEN-DAVID — I do not understand the source of the contradiction, sorry.

Ms HARTLAND — If you do not understand that, I cannot explain it anymore.
We will go on to a few more questions. I have already asked you about what you see in terms of the kinds of services that councils are not going to be able to provide. I am really quite surprised that none of that work has been done, nor has the government done that work.

Can you explain what has been done to develop a monitoring framework for the future in terms of infrastructure and services that are going to have to be dropped because of the rate cap?

Mr CHOW — That work is still being undertaken. What we really like to have is good information on are what we call service impacts, infrastructure impacts and financial impacts. Our outcomes reports aim to look at what are the indicators that help us to see the trend after the rate cap has come in, the impact on services, the impact on infrastructure investment and the impact on the financials of the council. Some of these measures are available in this very sub-elementary form, like the government has developed a local government performance reporting framework and the financial measures are there. The service measures and infrastructure measures are again in a very elementary form in the local government performance reporting framework. We are trying to build on those all the time before we publish a report by the end of next year.

Ms HARTLAND — My final question: I was interested in your comment about the growth areas and why they are not able to match their growth with the income that they will obviously receive from rates. Have you taken into consideration [no audio]?

Dr BEN-DAVID — As a general principle we would expect that when a council builds a facility for a future community, then that future community would contribute to the cost of that. That would be my starting position looking at any business, whether it is local government, a water business, an energy business or the port. If you are building for growth, why does that growth not eventually pay for what you are building? The reason in local government, I think, is that local governments tend to prefer to pay for everything up-front. What that means is that the present ratepayers are paying for assets which future ratepayers are also going to benefit from. We are just trying to understand the economics of all of that. Why is that the way local government works when other businesses do not — —

Ms HARTLAND — Are you suggesting that they should wait before they build the infrastructure?

Dr BEN-DAVID — No, not at all. That is a decision for council. It is a matter of how they finance and fund that infrastructure.

Ms HARTLAND — But if you have got a new estate and there are 1000 houses — and yes, you are receiving rates from them but you have to provide the services to those 1000 people, and you should do it; you would have to do it all at the same time — how could that possibly be delayed or done gradually?

Dr BEN-DAVID — It is the way it is financed that can be spread over time.

Ms HARTLAND — I am sorry; I do not understand.

Dr BEN-DAVID — The bottom line is: is there a role for debt financing of assets that have a long life?

Ms HARTLAND — Having served on a council that had a $28 million debt because of the previous loan speculation, I do not think a lot of councils actually want to get themselves into debt that they cannot service.

Dr BEN-DAVID — And nor would we. That is why, if you go back to our initial inquiry, back almost three years ago, we talked about the need for government to develop guidelines on the appropriate use of debt. Because, no, absolutely it cannot be used for speculative purposes such as those, but for long-lived assets that are going to benefit the community our opening question would be, ‘Well, why doesn’t council fund those through debt?’, or, as Andrew was discussing before, looking at that council’s infrastructure needs over a long term, ‘Why is it not able to manage its overall infrastructure spend in a fairly smooth way?’.

Ms HARTLAND — But it has to create the infrastructure, so it has got to build the community centre or the maternal health centre now. It cannot put them off. You cannot put off the debt, because that infrastructure has to be built.

Dr BEN-DAVID — It is a matter of how that is all phased, and that is why we are so keen on — —
Ms HARTLAND — You cannot phase infrastructure, I am sorry.

Dr BEN-DAVID — No, but you do not have to build everything for everyone on day one.

Ms HARTLAND — If you have got 1000 people in a new estate, are you saying you should phase in the infrastructure?

Dr BEN-DAVID — It depends on what type of infrastructure we are talking about.

Ms HARTLAND — The maternal health centre, the library, the community centre and the playgrounds?

Dr BEN-DAVID — Councils have to work on how they deliver those things in a way that is sustainable.

Ms HARTLAND — You are suggesting in fact that they should just not build them — —

Dr BEN-DAVID — No, please do not put words in my mouth.

Ms HARTLAND — I am actually trying to understand this, and I do not understand what you are saying. You are saying that they should delay the infrastructure, but this is essential infrastructure.

Dr BEN-DAVID — We need to understand why councils are making the case that the present generation of ratepayers should be building assets that are effectively given to the future generation without that future generation contributing their share to those costs. That is what we are trying to understand by this growth study. We are not making any value judgements here; I can assure you of that.

Mr MELHEM — What about other sources, the growth fund, for example, of which $100 million was used very effectively in Wyndham, Melton and Hume. I think in Melton, for example, we got $10 million over the last three years to fund this sort of infrastructure. Do you see a role for councils to better access this sort of funding, whether it is from the Growing Suburbs Fund or other state government funding or federal funding?

Mr BEN-DAVID — Again, we would not comment on any particular source of funding, but external funding and contributions to those, whether state or federal or other, is something that — again, we are trying to understand. You have also got developers contributing assets.

The CHAIR — Let me just understand that a little bit further because the growth fund that has been referred to has been cut in half this year — from $50 million a year to $25 million a year.

Mr MELHEM — No, this year it was $100 million to $50 million — oh, $25 million. You are right.

The CHAIR — It has actually gone to $25 million rather than $50 million a year —

Mr MELHEM — Yes, that is right.

The CHAIR — and there is no funding in the out years. Do you take into account those sorts of cuts when you are looking at the impact on councils? They have expected revenue and it is now no longer there?

Mr BEN-DAVID — Yes, certainly in an individual application we would be looking at — —

The CHAIR — So if a growth area council put an application in and said, ‘We had expected some money and it’s now not there’?

Mr BEN-DAVID — It would be up to them as to how they addressed that.

The CHAIR — And in a similar vein, with developer contributions do you assess the impact on council areas where developer contributions are taken but are not spent? I will be quite blunt about this: if you look to 30 June last year, the state government is sitting on $175 million or $176 million. That is contributions that have come from the growth areas but which have not been put back in. If you look at the budget this year, into the out years, there are four years of growing GAIC, going up to $180 million or $190 million a year, and yet the spending is not matching that. Do you look at the impact of taking those contributions from the growth areas and the non-return of them?
Dr HAMILL — I think the answer then — and Andrew might correct me — is that I would have thought that that unspent revenue would appear on their balance sheet — —

The CHAIR — No, it is taken from the properties in their region — —

Dr HAMILL — Yes, it counts as revenue, but it would appear on their balance sheet because that would — —

Mr BEN-DAVID — No, it goes onto the state balance sheet.

The CHAIR — No, I am talking about the GAIC. I will come to the developer contributions in a moment. The GAIC itself, where that is stripped out of areas but not returned — do you take that into consideration?

Mr BEN-DAVID — What we would be looking at is an individual council’s application and what sources of revenue they are forecasting, whether own source or external — that is all. But we would not look at it in, I think, in the sort of systemic way that you are approaching —

The CHAIR — Even on ex-council — so if an application came in that dealt with the fact that the GAIC had been levied on their area but not returned in terms of need for infrastructure, as Ms Hartland has eloquently outlined.

Mr BEN-DAVID — Again, we would only look at the extent to which it affects the council’s financial position. That is what we would be looking at, because it is council that is applying to us for a higher rate cap because of its financial situation. So we would not be looking at what the state government is doing with that funding or how it is being raised; we would simply be looking at the council — what funds it can raise of its own accord, by whatever means, and what funds it has available to it by other means.

The CHAIR — So you would count out the fact that money is levied from the municipality but not returned? You would not deal with that?

Mr MELHEM — It is not taken into account.

Mr BEN-DAVID — No, it is not.

The CHAIR — That is fine. I am happy to hear that. At least it is clear. I am not saying I support it; I am just saying that at least it is clear.

Mr BEN-DAVID — If council had levied that, then it is a different matter because it is — —

The CHAIR — And then in the case of development contributions, which are levied by council and held by council and reported by council, do you look at the holdings of development contributions in these assessments?

Mr BEN-DAVID — I cannot remember the details, but certainly in one of the applications last year that we dealt with, which was Ballarat, this was a significant issue. But I cannot remember the details.

The CHAIR — Maybe you could take that on advice and come back to us.

Mr BEN-DAVID — The answer is: yes, we do look at it. We can get you the Ballarat decision from last year because that discussed this exact issue.

Mr CHOW — In essence we look at individual councils, the totality of their revenue and the cost, and see whether they have worked out a case for a long-term funding need — so individual councils in totality, in terms of all their revenue sources and all their expenditure, things that are within their control and things that are outside their control.

The CHAIR — I understand the point about the control, but actually it must have an effect on the municipality if there is a tax levied and removed, which is the purpose of infrastructure, but it is not returned.

Mr BEN-DAVID — Again, I would have to refresh myself on this, but in the Ballarat decision that was exactly the issue.
The CHAIR — Well, that was a development contribution, you have been saying, as opposed to the GAIC.

Mr BEN-DAVID — That is right, yes — a developer contribution and then the profile of how that was being spent was something that — again, I cannot remember the detail.

The CHAIR — That you became interested in.

Mr BEN-DAVID — It was an issue that we had to deal with last year.

Mr MELHEM — One last question: have you read the Auditor-General’s report regarding the community consultation and the outcome of that?

Mr BEN-DAVID — I have not — —

Mr MELHEM — Have you got any comments to make on that?

Dr HAMILL — I know Andrew’s team has.

Mr MELHEM — How is that travelling?

Mr CHOW — I think it is undertaking some good work. Community engagement as a subject matter is often challenging — finding when, what to do and how to do it. So I think it is a good report that looks at how councils can actually better engage with their community, and it is based on very sound principles from the profession. So we are working closely with VAGO and the sector to try to converge all these requirements.

Mr MELHEM — One last one: Ms Hartland talked about some projects council from time to time might decide to dump because of financial pressures, but my understanding of the last 12 months is that there have been a number of projects — for example, the SES. From my understanding at one stage there was an argument about funding and now state government has taken over that funding. I think a school crossing was one of them, with VicRoads. What I am saying is: some of these areas that council was 100 percent responsible for, because of the rate capping they have now been taken over by other agencies like state government. So more and more of that is happening. Have you come across any — —

Mr BEN-DAVID — To be honest only from reading the papers. We do not track these things. But we have always said that the benefit of the transparency that the rate-capping framework delivers is that it makes clear where funding pressures are for councils and they can therefore have that discussion with other levels of government, whether state or commonwealth. It depends on their circumstance. So I think that is one of the outcomes of the rate capping framework, yes.

Mr MELHEM — So it is not that you simply just dump a service. We have not seen any evidence where a particular service like Meals on Wheels, for example, has been dumped because of rate capping. We do not know whether any of these services were cut as a result of rate capping.

Mr BEN-DAVID — I cannot comment on that. You have to understand we deal with the sector by and large, other than these two studies we are doing, on an individual application basis, so we only look at that individual council and its circumstances.

Mr MELHEM — No, I appreciate that.

The CHAIR — In conclusion, and just picking up Ms Hartland’s important set of points about the Yarra council waste charge issue, I just put on the record that I do not think Yarra should have been pursuing this in the way they were. But leaving that to one side, it seems to me when you read that letter the second-last paragraph can only be read as a threat:

Should Yarra proceed with this proposal, the commission will seek relevant information to complete its assessment as part of the 2017–18 compliance report to be published in November 2017. At which time, we will also need to assess Yarra’s main reason for requiring the additional $8.5 million for long-term financial sustainability.

It may be that there is a loophole in the legislation or a weakness in the legislation, but I just do not know on what head of power you would be making that sort of statement. I am not opposed to fixing such a loophole, but I just — —
Mr BEN-DAVID — I apologise if it appears to be some sort of threat, because it is definitely not.

The CHAIR — That is the only way I can read it.

Mr BEN-DAVID — No, it is a statement of fact — I will let Andrew explain — because of our reporting obligations.

Mr CHOW — As we have done in the past with Queenscliffe and Mornington when they introduced a new waste charge, they come and talk to us and they provide information once they have adopted the final budget. This is following the same process.

The CHAIR — On what exact head of power, then, do you do that?

Mr CHOW — The compliance reporting.

Mr BEN-DAVID — That is all that was alluding to. Every November we produce a compliance report: have councils complied with their rate cap?

The CHAIR — You would do this anyway, would you not? You would do a compliance report anyway.

Mr BEN-DAVID — That is what we are saying. We do compliance reports across all 79 councils. Have they complied with the minister’s cap or the higher cap that we approved, and all this is saying — —

The CHAIR — If there is weakness in the legislation, you should ask for that to be fixed, as opposed to making a pseudo threat.

Mr BEN-DAVID — It is not; it is merely a statement of what we will be doing in November.

The CHAIR — ‘At which time, we will also need to assess Yarra’s main reason for requiring the additional $8.5 million for long-term financial sustainability’.

Mr CHOW — This is looking from the perspective — —

The CHAIR — I cannot read it any other way.

Ms HARTLAND — Well, you voted for the legislation. We said that this is what would happen.

The CHAIR — The community voted for it actually.

Ms HARTLAND — No, you voted for it.

The CHAIR — The community voted for it actually.

Ms HARTLAND — Do not pretend that you actually — —

The CHAIR — There was a mandate of the government to do it.

Ms HARTLAND — You voted for it.

The CHAIR — We did not like it. It was not our policy.

Ms HARTLAND — You voted for it, and now this is the consequences. Live with it.

Mr BEN-DAVID — No, there is no threat because we have got no power to threaten them with. It is merely a compliance report. I apologise if it reads that way. It was never intended to read that way.

The CHAIR — Whatever the merits of the point, and as I say, I do not agree with Yarra putting up their charge in that way, but it does appear you may have gone beyond you purview, in my view.

Mr CHOW — To reiterate the point, we have got a compliance reporting role, and if you put yourself in the shoes of the ratepayers and community, a change has been made. We need to follow it through to see whether the council have done the whole restructure according to our guidance.
The CHAIR — So the basis for your guidance — which section of the legislation does the guidance — —

Mr CHOW — It is in the legislation that we can issue guidelines.

The CHAIR — Which section, I am just asking.

Mr CHOW — In fact in the first two years we called it guidance.

The CHAIR — It is a guideline, is it?

Mr CHOW — It is not as prescriptive as guidelines. The guidance that we are issuing is really asking the councils to observe and encouraging them to look at some of these key concepts when they are making those changes.

The CHAIR — But it is not binding on them.

Mr BEN-DAVID — No, because it is not a guideline. That is right. That was quite a deliberate strategic decision because once you make it binding, changing it becomes much harder. My very opening comments were, ‘This is a learning phase’. We wanted to have the flexibility to work with the sector, which we do — which Andrew and the team does — so as we learn how to make this work better for us and for councils we can update that guidance. I imagine after two or three years, if necessary, we will actually turn it into guidelines which are binding, which is something that we are empowered to do under the legislation.

The CHAIR — Yes, but the guidance is not binding.

Mr BEN-DAVID — No, and that is the exact point we are making about the spirit of the law versus the letter of the law.

The CHAIR — Thank you. I appreciate it. No doubt the transcript will come in due course. The secretariat may be in contact to follow up some details. Thank you for your evidence.

Mr BEN-DAVID — Thank you.

Committee adjourned.