TRANSCRIPT

STANDING COMMITTEE ON THE ENVIRONMENT AND PLANNING

Inquiry into rate capping policy

Melbourne — 22 March 2017

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Ms Samantha Dunn
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 Witnesses
Mr Rob Spence (affirmed), CEO, and
Mr Owen Harvey-Beavis (affirmed), manager, insurance, research and strategy, Municipal Association of Victoria.
The CHAIR — I declare open the inquiry into rate capping of the environment and planning committee. Evidence given here is protected by parliamentary privilege; outside, of course, it is not. I welcome both representatives of the Municipal Association of Victoria to the inquiry on rate capping and perhaps ask you to make a short introductory statement — an update on the impact of rate capping on local councils and communities.

Mr SPENCE — Okay. Thanks for the opportunity to come and speak to you again. Just to give you a brief overview, we have new councils in place now — about a 50 per cent turnover in councillors — so in a way it is a bit unstable in terms of looking at what is happening with rate capping. At this time, every four years, it is always a bit hard to sort of shake out really what the position is.

Because we are in the first year of rate capping, really, the data is not available to us to actually see the impacts. We are getting a lot of anecdotal advice as to what is happening. As a sort of snapshot view, I think in rural Victoria and particularly in some of the smaller councils, we are getting advice that it is beginning to affect service capacity, particularly in road maintenance and construction, but we are also seeing the smaller councils giving consideration to service reduction — so what they will stay in and what they will not stay in. At the moment school crossings has been a hot topic. SES were negotiating with the state on its future and who funds it, but it is on the agenda. The future of home and community care is again up for grabs, and around some of the other services there are questions.

One of the challenging issues, I think, for the councils to deal with is in the road maintenance area — what is considered to be a reduction. I think it is an actual reduction in funding over time to VicRoads, and then the VicRoads road infrastructure deteriorates, pushing more vehicles onto local roads, and then as a consequence we are seeing rapid deterioration of local roads. Certainly a lot of those roads are not made to the standard of VicRoads roads, so the councils are — —

The CHAIR — They were not intended to be either.

Mr SPENCE — No, they were never intended to carry the sort of loads that they are having to carry. We were in the south-west for a meeting at Warrnambool a week ago, and clearly in that area road infrastructure is a major problem for them. So the ongoing capacity of councils — I think for the small ones we will see the impact of rate capping really start to bite in the next 12 months, in my view.

Mr MELHEM — Just on the road maintenance thing — you talked about VicRoads funding — is that primarily the reason or cause? Is it that generally council has not got enough funding on its own, or is it just that VicRoads is not putting enough resources and money into this sort of thing? Is that what you are saying?

Mr SPENCE — It is both. When you align the capacity of councils to maintain the roads with the fact that VicRoads — I think there is a third bit in it — —

The CHAIR — And the loss of the country roads and bridges program.

Mr SPENCE — Well, the fourth thing, because the weather has been pretty nasty, as Simon would know, in that space and in the south-west. We know that in South Gippsland and in the south-west the road infrastructure has deteriorated really rapidly.

Mr MELHEM — That is why I am trying to distinguish between what is council’s traditional responsibility in maintaining roads — as we know, it is clearly demarcated — and what is VicRoads’s responsibility. I am trying to distinguish between the two. Are you talking about both, or are you talking about — —

Mr SPENCE — I am talking about both. What I am saying is there are multiple impacts leading to the deterioration of the roads. If you look at the situation, for example, in Portland, where you have got —

The CHAIR — Glenelg.

Mr SPENCE — Glenelg shire. You have got timber, you have got mineral sands et cetera being freighted into Portland on both VicRoads roads and local roads. The capacity of those roads to deal with the weight of transport that is coming in now is not there.
Mr HARVEY-BEAVIS — Probably an additional element to that too is that traditionally councils have done work for VicRoads on their roads through minor maintenance agreements, and they have never been agreements that have fully covered the cost of councils’ activities on behalf of VicRoads. But effectively, with more efficient mobilisation of the works team as well as ensuring that the road network is as good as it can be for the community with the deteriorating condition of VicRoads roads, there is additional pressure there as well.

Mr MELHEM — I am just trying to flush out what impact the actual rate capping had on it. There is another argument as to whether or not VicRoads, state government and federal government — all these sorts of government — are actually putting enough money in roads. These roads are deteriorating. You talk about Portland, for example. The Princes Highway is run down, and it is not getting fixed on time et cetera, versus a direct impact of rate capping, which would be reducing the ability of council. This inquiry is focusing on rate capping and what impact that has. Can you actually define or crystallise that rate capping has had an impact on a council’s ability? You have not got any evidence to support it. It is more or less — —

Mr HARVEY-BEAVIS — I think as Rob sort of indicated already, because it is the first year, there is no hard and fast data available yet. We would anticipate that once councils’ 2016–17 accounts are closed and we can analyse them, that evidence would actually begin to mount.

Mr MELHEM — Right. So basically it is guesswork. It is not hard evidence. You cannot support this.

Mr RAMSAY — It is, because they have done surveys of the councils. You were not here for that part of it.

Mr MELHEM — I am sorry. I am not having a go at you. I mean, I know you are doing your job.

Mr SPENCE — No, no. No, I am not taking it as you having a go at me.

Mr MELHEM — I am interested in the facts instead of people guessing and sort of saying, ‘Rate capping is this’. If it is, well, I would like to know, because I am interested, and that is why I am asking that question. I am not saying the problem might not be there. The question is quantifying whether rate capping is the major contributor or a minor contributor, or — —

The CHAIR — As I understand it, what you two are saying is there are actually five factors that are contributing. One is the loss of country roads and bridges, the second is rate capping, the third is the weather, the fourth is the VicRoads wind back and the fifth is the loss of the minor maintenance through VicRoads — —

Mr HARVEY-BEAVIS — It is more than just minor maintenance if it is increasing.

The CHAIR — The occasional maintenance that is done. So there are actually five factors that are interplaying here, and rate capping is the one that has perhaps precipitated that, and the loss of country roads and bridges.

Mr SPENCE — Yes. So the councils would have used rates as the balancing item to try and deal with reductions in revenue in other areas. There is a sixth item that we should have mentioned, and that is the failure to index financial assistance grants by the commonwealth.

The CHAIR — There is probably a seventh, too, which is the commonwealth roads money which has actually gone up.

Mr SPENCE — That is right. So those are sort of offsetting themselves a bit. So there are a number of factors. It is a very hard thing to unscramble at this stage as to what is causing what.

The CHAIR — But Simon, I am sure, would agree with your point that the roads in Glenelg are shocking. We saw this, and we took a lot of evidence on this in that area of the state, and it is pretty clear that there is a declining position for those roads.

Mr SPENCE — That is right.

Mr RAMSAY — Corangamite is indicating about $55 million is needed just to upgrade local roads, and they do not have the capacity to raise that sort of revenue under the present cap.
Mr SPENCE — Yes, that is right. And South Gippsland have got exactly the same issue. In those areas where we had heavy rain — we had a dream period for both the state and local government during the drought in terms of roads; we did not have it in other areas, but we had it on roads. We did not have it with crops or anything, but with roads we had a really good run when there was no rain. But we are back to normalised rainfall, and the roads have been biffed around big-time.

Mr MELHEM — Has there been any improvement in the last three or four months over summer? Has there been some work happening on these roads, do you know?

Mr SPENCE — They are in a pretty bad condition, so all they are doing is deteriorating. No, I meet with John Merritt from VicRoads on a regular basis, where we hold the sort of discussions about what the requirements are to fix it, and it is really a big effort on both sides, but you need the capacity for both organisations — for councils and the state — to be able to do it.

The CHAIR — Because the smaller roads are alternates, but they are less satisfactory alternates because they are not designed to carry the heavy load.

Mr SPENCE — That is right. So there are issues with VicRoads and the state focusing on road safety and so on; well, road safety on the local roads is a major issue given the quality of some of them and their width and so on.

The CHAIR — Do you have a tabulation — just picking up a couple of points you made — of the councils that have stepped out of a number of services, out of school crossings? Is there an update on that?

Mr SPENCE — Northern Grampians are the ones that have stepped out, and others are looking at it but have not. SES — I can give you the list; there is a number of them who have actually stopped funding SES. So we are trying to negotiate with the state an agreement where the state will pay for SES and we will have leases in place for the land.

Mr MELHEM — And how is that going?

Mr SPENCE — Good, yes — progressing.

Mr MELHEM — So we might find a solution for that?

Mr SPENCE — I am optimistic that before 30 June we will get a solution to that one.

The CHAIR — And HACC?

Mr SPENCE — HACC is complicated. The agreement with the commonwealth finishes in June 2019, so the structure for HACC in Victoria stays the way it is until June 2019. We have a tripartite agreement between commonwealth, state and MAV representing local government. We are commencing work with the commonwealth to negotiate through what the model will look like post 2019. I would expect we will need to have that settled by first quarter 2018, because the lead-in then to deal with — —

The CHAIR — But there are a number of councils stepping out of HACC.

Mr SPENCE — They are talking about it. Wodonga is the only one that has made the move.

The CHAIR — Wodonga has, yes.

Mr MELHEM — And what is the reason for that?

Mr SPENCE — Their view is that the funding model is not strong enough to allow them to stay in it.

Mr MELHEM — Is that something to do with the indexation freeze by the commonwealth?

Mr SPENCE — No, it is an indexation issue where the indexation does not really match the cost growth of councils.

Mr MELHEM — But primarily the funding, it is commonwealth funding at this stage?
Mr SPENCE — It used to be commonwealth, state and local — 60 commonwealth, 40 — —

The CHAIR — And about $100 million-odd of council money?

Mr SPENCE — It is $140 million from council.

The CHAIR — How much of that is still there?

Mr SPENCE — A lot of it. The vast majority of it is. It is one to watch, really, as to what the consequences are.

Mr HARVEY-BEAVIS — The other service, Rob, that was mentioned in our regional meetings, fairly surprisingly, was maternal and child health as well. A couple of councils indicated a desire maybe to step out of it.

Mr SPENCE — I will not say anything; I will just roll my eyes.

Mr HARVEY-BEAVIS — We doubt that that will come to pass, but — —

The CHAIR — As a former health minister, I would be very worried if that happened.

Mr HARVEY-BEAVIS — Absolutely, so I am not sure that that was a well-advanced consideration, but it did indicate — —

Mr MELHEM — On that issue, through the association, are you guys working with this council, trying to do something with the commonwealth to overcome that?

The CHAIR — It is state funding too.

Mr MELHEM — And state, yes.

The CHAIR — Maternal and child health is state.

Mr SPENCE — On HACC we are working with the commonwealth. On maternal and child health we are working with the state. The whole health system — almost — in relation to universal service is driven off one point, and that is the birth notices going from the hospital to the maternal and child health service. That is the only point in the whole system where we have control over every child.

The CHAIR — It is an incredibly important strength of Victoria, long term.

Mr SPENCE — It is absolutely critical. That is right. From there you are able to manage the health outcomes of kids, which influences the whole health outcomes of them through their adult life. So it is absolutely critical. It is a major effort from us to make sure councils stay in and provide the appropriate level of service. It is surprising — —

Mr DALLA-RIVA — Who is not providing it now?

Mr SPENCE — Some councils are talking about ‘Why would we stay in it?’, but — —

Mr DALLA-RIVA — Who would then provide it?

Mr SPENCE — Who knows? It might be a local health service or something.

Mr DALLA-RIVA — So the Wodonga one, what was — —

Mr SPENCE — Wodonga is HACC — home and community care.

Mr HARVEY-BEAVIS — Aged care.

Mr DALLA-RIVA — With HACC, did it get withdrawn?
Mr SPENCE — They withdrew, and what they did is they worked for about eight or nine years to establish a local provider network that could provide the service.

Mr DALLA-RIVA — So who is now providing that?

Mr SPENCE — Their local not for profits are providing the service.

Mr DALLA-RIVA — So the slack has been taken up elsewhere?

Mr SPENCE — The slack in Wodonga. If it were Edenhope, nobody is going to take up the slack.

Mr DALLA-RIVA — In terms of the other one, the school crossings, where was that?

Mr SPENCE — That was at Northern Grampians.

Mr DALLA-RIVA — VicRoads are funding it at the moment.

Mr RAMSAY — It is not just Northern Grampians, either. Many councils are looking at reducing services.

The CHAIR — There is a long list of country councils.

Mr SPENCE — They are looking at it, yes.

The CHAIR — It is the direct impact of rate capping that has forced councils to reassess services that are provided by the state government.

Mr MELHEM — Is that a factual thing? Are you saying you cannot support that with the data? That is why I am a bit cautious there with the Chair making an assumption, which you have said is not — —

The CHAIR — You were on the inquiry. We have heard this evidence before.

Mr MELHEM — No, I can actually read reports, David. Are you able to back up what the Chair has said with data?

Mr SPENCE — A council has made a decision based on its view that this is a cost that should not be borne by them because of the impact of rate capping. Whether that is a logical decision, you would leave that to them.

Mr MELHEM — No, that is a fair position to have. I am not arguing that.

Mr SPENCE — That is right. We know what it costs them, but we have not got the data to show that they have not got the capacity to pay.

The CHAIR — We also know that over time state governments have funded less as a share of those particular services and have asked councils to pick up a greater share and that a number of councils have reassessed this on the basis of the impact of rate capping.

Mr SPENCE — Yes, so we now have got an agreement with VicRoads that they will move back to the 50-50 funding for school crossings that fit the agreed criteria. That is a win. If you look at the wins we have had as a result of the rate capping issue, the first one is maternal and child health funding — an extra, I think, $150 million or $160 million in the next four years. Planning fees are another one. These are things we took on as a result of rate capping to resolve issues in the state that remained problematic for councils. We fixed maternal and child health and planning fees. We have got school crossings to deal with and we have got the 50-50, and SES is the next one.

Mr MELHEM — Based on that example you have just given, that is going to be a direct benefit of rate capping by transferring the cost from rate payers in that particular council. Now these services are funded by state government, for example, in this case instead of putting pressure on increasing rates. I suppose the whole idea was to reduce tax and pressure on the ratepayers but not to undermine services. I have got to say you have done a good job so far on these issues, and I am sure there is more to do on others, because the last thing you want to do is cut services.
Mr SPENCE — That is right.

Mr MELHEM — So it is a positive thing, where — —

Mr SPENCE — The outcomes are positive, but we should never have gotten to that point, because we had agreements with the state that the state were not meeting. So what we have done is push them to the point of meeting the agreement. Richard Wynne is different with planning fees because he is the only minister since John Thwaites who has actually been able to deal with the issue, and John Thwaites was a long time ago, so you can see how far the councils were behind in terms of the indexing and planning fees.

Mr MELHEM — There you go — we were given a stamp.

Mr SPENCE — That is right.

Mr MELHEM — My understanding is that about seven councils have applied for or are likely to apply for rate adjustment for this round.

The CHAIR — Variations, I think, is what you are recalling.

Mr MELHEM — Variations of their — —

Mr SPENCE — Small numbers, we expect.

Mr MELHEM — Yes, my understanding is that there are about seven: Casey, Horsham, Hindmarsh, Pyrenees, Queenscliffe, Towong and West Wimmera. Is that your information?

Mr SPENCE — That is my understanding, but it will be a low number, I think.

Mr MELHEM — Is your organisation helping or offering to assist these councils put applications together?

Mr SPENCE — Yes, definitely. I think there are two factors influencing the low take-up this year. One is that we have got a whole lot of new councils. I have not heard of anyone getting elected saying they are going to put rates up. Every one of them gets elected generally by saying they are going to cut rates or that they are going to keep them where they are. To change that strategy is pushing against their political objectives.

I think the second thing that is influencing it is that councils were really nervous after the last round in terms of the complexity of dealing with this with the ESC.

The CHAIR — Some of them got smashed publicly.

Mr SPENCE — Yes, they got smashed publicly, but they also spent a lot of money putting in an application that failed. So some of them are saying, ‘Why spend $60 000 on putting in an application, when all we are going to get back in the increase in rates is $60 000?’ We are working with the ESC to try and improve those processes. The ESC are used to dealing with the water industry, formerly the electricity industry, and so on. They have very rigorous processes to work through, and the ESC has got a very short window to deal with submissions. We have got to get the submission process and so on stripped back so that it is simple and straightforward for the councils.

One of the issues that is bothering me about where we are at at the moment is that if you went back four years or three years, the primary reporting requirements for councils were an annual report — —

The CHAIR — Checked by the auditor.

Mr SPENCE — That is right. There was also the grants commission submission. They were the primary reporting tools. Now we have had added to it the 67 performance indicators that make up the Know Your Council website, and then you have had the ESC’s collection across all councils of another dataset.

The CHAIR — Are they all required to submit to the ESC, even if they do not want variations?

Mr SPENCE — Absolutely. Everyone has got to submit.
The CHAIR — Everyone has got to do it, so it is now four datasets — —

Mr SPENCE — Four datasets instead of two.

The CHAIR — And anything the department asks for too?

Mr SPENCE — That is right. What I am talking to the ESC about is that we need to get this back to two datasets. I am also talking to the red tape commissioner about it, because what is happening is that the level of red tape loaded up on the local government sector is just increasing and increasing and increasing.

Mr MELHEM — What is the feedback you are getting from these agencies in relation to your view — is it positive?

Mr SPENCE — The ESC are interested in resolving it. We did a quick survey last year that indicated that the cost of red tape to councils at the moment is in excess of $40 million, probably closer to $60 million, so we are just picking some targets to see — —

The CHAIR — There is a problem with the recording equipment.

Hearing suspended.

The CHAIR — The hearing is reopened. Rob and Owen, if you could keep going — I am not sure exactly where we were there, but I think we have probably covered most of that topic. I am just looking down the list of things you raised. I might move on to Simon and Richard.

Mr RAMSAY — I just have a question: in light of the government policy in relation to energy, it was brought to my attention by some of your members that in fact many councils are going to face a 300 per cent to 400 per cent increase in energy costs. That is in a lot of their community assets — halls, sportsgrounds, lights. I am just wondering if you are thinking about doing some work in relation to what that impact might mean to your members in relation to costs associated particularly with volunteer groups and community-use assets.

Mr SPENCE — There are two things that we are doing. We are doing a tender for a bulk purchase of electricity, and we will do the same for gas. It is going to take us probably nine months to put all that together, but we believe that will be really competitive through that process. The second thing is that we are working with a number of councils on proposals to put in solar facilities to actually service community facilities and the council offices. That is a piece of work we are doing with some of the regional groupings — environmental groups who sit inside the councils. Those two will help. It is a bit hard to tell where electricity prices are going to go, but it is something we need to get onto reasonably quickly because it is going to put a lot of pressure on all of those clubs and facilities that are supported by councils.

The CHAIR — I have heard a similar point that a number of councils that have had long-term contracts have come to the end or are near the end of their contracts and are now looking at large hikes.

Mr SPENCE — That is right, and what I understand too is that in some circumstances the electricity providers are looking for very short-term contracts, not long-term contracts. That is why a bulk deal is a good way to go because you bring a lot of horsepower to the table.

Mr RAMSAY — One other issue which was brought to my attention over the summer was the lack of capacity to deal with the roadside vegetation. In fact there was quite a significant fire risk to regional Victoria and there are quite substantial or heavy fuel loads along roadsides. Councils say they can slash once but they do not have the funding to be able to slash two or three times in a season like we have had this year. Would you say that councils are under-resourced in funding, material assets and workers so as to be able to reduce the fuel load and reduce the fuel risk to communities in regional Victoria?

Mr SPENCE — I think that in normal weather conditions with the funding they can sort of cope, but with abnormal weather conditions like we have had — that is, heat and rain — I do not think there is enough money in the pot to actually deal with it, and the funding finishes on 30 June this year, so it is an important pressure point for this coming budget, the funding from the state for roadside — —

Mr RAMSAY — And councils are now responsible for roadside control?
Mr SPENCE — No, they are not.

Mr RAMSAY — Weeds?

Mr SPENCE — No, it is part of the conundrum of a poorly drafted piece of legislation.

Mr RAMSAY — So who is?

Mr SPENCE — Nobody, quite. That is why it sits like it does. It used to be the farmer, and then new legislation came in that got it wrong.

Mr RAMSAY — So that councils had to be responsible?

Mr SPENCE — We took advice from Julian Burnside on it, and as a consequence we ended up with a funding pool from the state, so it is questionable. It is a poorly drafted piece of legislation.

The CHAIR — And VicRoads?

Mr SPENCE — VicRoads have got their own challenge in maintaining their roadsides. Yes, absolutely. It is a massive exercise, really. If you think about it, Victorian council roads effectively are long enough to circumnavigate the earth twice. It is a lot of road, and you multiply that by two, because you have got to do both sides. It is a lot of road. The earth is not that big really.

Mr MELHEM — When you look at it that way.

Mr DALLA-RIVA — Thanks, gentlemen. This inquiry has been going for a while now. I am reflecting back, thanks to the secretariat, on one of your early submissions from 13 July 2015. A few issues we have raised tonight I think have been addressed in that letter. There were a range of issues about history, community, local government revenue autonomy and local government revenue raising. So I think we have covered a lot of those issues. The one thing is the uncertainty of the framework. That was your primary concern. You raised it in that submission:

There remains significant uncertainty concerning the detail of the rate capping framework and what effects it will have on the sector.

You raised concerns about how it was going to operate for councils and just generally how that process was going to occur. Then there was the further correspondence to the committee dated 29 July 2016. Again some of those issues we have covered tonight — the emerging consequences of rate capping: SES unit funding, school crossing supervisors and HACC. They are all there, and you have raised your concern, but the major one, which has probably taken up more of your letter than the first one, is the variation process. I think it is fair to say, is it not, that the process of the ESC’s decision-making is perhaps one of the major concerns confronting councils?

Mr SPENCE — Absolutely. But I do not want to be too hard on the ESC in this, because they are working to try and resolve those issues, and we are meeting with them again on Friday of this week.

Mr DALLA-RIVA — We have expanded a lot on the other issues. I guess I have given a long-winded question, but I really wanted to know a lot more detail in terms of the engagement with the ESC, what you have done and how you have communicated with them, what has been the likelihood and the feedback of these communications and are you confident that there is at least some move in the ESC’s mind away from some of those very rigid processes that I think we all saw over the last rate capping process period?

Mr SPENCE — We have a positive and close working relationship with the ESC and have had it for many years. I think the challenge for the ESC in this process was that this was a start-up for them and, as I said before, their experience has been in dealing with the water industry and with the electricity industry and so on historically, and so they have a particular way of approaching things. I think in a way they are light on in knowledge in local government. We have been trying to help them with that. What we have been doing is engaging with them; Owen sits on one of the panels that works through the issues. We are engaging with them to see if we can assist them, and they are very open with this, to improve the processes to make it easier for councils to achieve variations, to make the case simply and to hit the spots that the ESC is interested in. There is a piece of work they are doing at the moment on efficiency in councils, so how do you identify efficiency? Again, a challenging topic. They have got a model that they use in the water industry, but local governments are
79 discreet and quite different entities. They may have a core of services that they provide that are common, but the way they go about delivering them is all different, so it is a complex task. We are trying to help them with that. But the system in my view needs to be stripped back.

I just lost my train of thought, but it will come back at some time tonight.

**Mr DALLA-RIVA** — About the ESC and the variation.

**Mr SPENCE** — About the ESC and the variation process. You do not have to be Einstein to know who needs the capacity on rate increases or needs greater grant funding or support from the commonwealth or the state. The likes of Buloke and so on. Buloke stands out as the flashing night-light of the council in need.

**Mr DALLA-RIVA** — Are they putting a variation in?

**Mr HARVEY BEAVIS** — They were successful in a variation last year.

**Mr SPENCE** — The first time around.

**Mr DALLA-RIVA** — But I was just wondering — Mr Melhem’s checklist — —

**Mr SPENCE** — I do not think they are there.

**Mr MELHEM** — No, I cannot find them here.

**Mr HARVEY BEAVIS** — It is fair to say that they can still put in a variation though.

**Mr MELHEM** — Yes, they have got until the end of May.

**Mr SPENCE** — I think we need to get to a point where the indicators are quite clear as to who should get a variation. You get to the City of Casey — a much more complex environment. They are collecting a lot of developer contributions and so on, so their accounts look incredibly strong, but that money is hypothecated to particular tasks. When you strip all that out, how strong does the business look and what do they need to actually service a community that is in growth mode — like massive growth — and high need?

**Mr DALLA-RIVA** — So the MAV, in terms of its engagement with the ESC, I remember a number of hearings where the councils were bringing in their variation documents. I am exaggerating, but it really required quite a substantial amount of trees being cut down and presentations and documentation required —

**The CHAIR** — Consultants being employed.

**Mr DALLA-RIVA** — and the consultants. I think we had evidence that one of the councils employed a person specifically for that role, and I think $250 000 was mentioned as one of their cost factors. Has that been reflected back to the ESC about the perverse nature of the requirements that outstrip — as you said, $60 000 to spend just to get a $60 000 rate increase back?

**Mr SPENCE** — Yes, we have, and we have made that point loud and clear. I am hopeful that we will get to a point where it is simplified and made a lot easier for councils to make an application. The point we made to the ESC when this process was being implemented was that they should develop a template which is tested with the sector so that the councils know what is expected of them. The first time round no-one knew what was expected of them, and as a consequence you got really comprehensive submissions and you got some that were pretty sketchy. There needs to be a standard in this as to what is expected. I think with rural councils, you have got to deal with them differently to metros. Metro councils are much more complex businesses than the rural ones, and the load on the rurals cannot be high in making submissions. Although the challenge for rural is — —

**The CHAIR** — They cannot rate it anyway. They cannot take — —

**Mr SPENCE** — That is right. If you look at the SEIFA indexes and so on for a lot of the rural councils, you look at the average income of the ratepayers from the ABS datasets — we were looking at one council today; $9700 or something was their average income per head of population for a rural council. That was, I think, the Pyrenees shire — their capacity to rate much harder — —
One of the weaknesses in our model is that the financial assistance grants distribution from the commonwealth is a bit cockeyed, and there needs to be either more money put into the pot or an adjustment to the system to deal with the anomalies that are growing between metro and rural.

Mr DALLA-RIVA — A final question, just in respect of your engagement with the government and the minister, has the minister been receptive to the concerns that you have raised — the specific concerns about the variation process?

Mr SPENCE — Yes.

Mr DALLA-RIVA — And has she considered maybe legislative amendments, or is there something that has been in the discussions — things that you have suggested; probably not the minister’s words, but are there things that you have suggested to the minister to alleviate legislatively some of those pressure points that you have identified over the period of the process so far?

Mr SPENCE — I do not think it is a legislative solution that achieves that resolution; it is actually getting the ESC’s processes right to actually smooth it out, because once it goes from the minister then it is the ESC who determines the model and makes recommendations.

Mr DALLA-RIVA — But is there not within the legislation the modelling of how the rate capping is adjusted?

Mr SPENCE — How the rate cap is adjusted? Yes.

Mr DALLA-RIVA — I know that was a concern. It was not that complex, but there was a complex equation to try and determine the rate cap increase.

Mr SPENCE — Yes.

Mr DALLA-RIVA — So has that been raised by councils — about that formula?

Mr SPENCE — Yes.

Mr DALLA-RIVA — And have there been suggestions? Has the MAV got a suggested or preferred model as to how the rate cap, if it remains, should be?

Mr SPENCE — It is our view that it needs to be, I think, a segregated model, and that is complex to do. It is a difficult one, because you would say that the rural councils, particularly the small ones, need more capacity to raise rates, but then you have got the question of whether the community has got the capacity to pay. Our view is that you would be better with a more sophisticated model that takes into account need and capacity in assessing how much the rate increases.

Mr DALLA-RIVA — Have you done any of that modelling?

Mr SPENCE — We have done some modelling on it but not a significant amount. It is easy enough to do.

Mr HARVEY-BEAVIS — Our modelling tends to be on trying to assess the financial state of the councils, so that we have a good understanding around what is the relative position and what is their absolute financial need. We have got a fairly good understanding both historically and up to the end of 2015–16 which councils are struggling the most.

Mr SPENCE — We have got a dataset that goes back nearly 20 years, so we can follow the history of how it bounces around.

Mr RAMSAY — So they are borrowing more — just out of interest, Chair — because my understanding of Golden Plains, from looking at the longer term of 10 years, was they were having to borrow, I think it was, $13 million to meet the services currently provided to its community but restricted by the cap.

Mr SPENCE — We have not seen it. We run the local government funding vehicle, which takes the councils, if they want to borrow through us, into the wholesale bond market. We have got about $340 million out on bonds at the moment. In this current cycle we have only got bids for $20 million, so it is not significant.
But I think this is all affected by that electoral cycle. People are just getting to grips in the councils; they have only been there for five months or something. They are just getting to grips with the financial conundrum they are in, I think, and I expect we will see in the next budget cycle a growth in the debt numbers or that application for borrowing.

The CHAIR — Has there been movement in debt overall, do you think?

Mr SPENCE — The debt is just about holding. It is just over a billion, I think, the number is at the moment. I think we are holding just about a third of it — something like that.

The CHAIR — Has the ESC continued with its earlier advice just to kind of jack your debt up?

Mr SPENCE — I think what the ESC is trying to do, and it is a reasonable challenge to put to councils, is to leverage the balance sheet a bit more effectively than some of them, the ESC would argue, are doing; whether you leverage it a bit more than it currently is — we have got a lot of councils who are in no debt and then we have got some with significant debt.

The CHAIR — It depends what you use the debt for.

Mr SPENCE — Debt should not be used for recurrent; it should be used for capital. There are a number of processes that we are trying to work through with councils to improve the efficiency of treasury management and so on that we have been doing for a while. The advantage of a pressure point like rate capping is that it forces people to think about these things instead of it being a nice to do.

Mr MELHEM — Just on that, have you noticed any changes within council about trying to improve productivity and cutting costs in-house?

Mr SPENCE — You bet. The last set of data I saw — I am on the super fund — I think the wage rate movements for the last six months were about 1.4 or 1.5 or something. We have got councils like Alpine who have just struck a three-year wage freeze. We are seeing the wage and salary growth come off massively.

The CHAIR — There are still a few that on — —

Mr SPENCE — Quite high ones. As you would you know, there is a lag in the EBA negotiation process, so it depends where they are in the cycle.

Mr MELHEM — Cost of labour is one thing, but I am referring to other areas — service delivery and negotiating a contract with service providers. Like any other business, any business model, you do not want to put out your costs by CPI plus 2 per cent or 3 per cent every year. A successful business will be looking at, ‘If I can maintain my cost at today’s rates for the next few years, I don’t want to increase it’. If we look at the last 10 years, the average rate increase for councils has been about 5 or 6 per cent per annum, and I am not sure that is a good, successful model to go forward if I was a ratepayer.

The CHAIR — CPI is higher too.

Mr MELHEM — Sorry, David, I am not criticising; I am just stating the facts. Let us not get in a tickle about it. I understand council need to provide services and the money has to come from somewhere — it is always an argument. Rates are one and then there are other grants from the commonwealth and the state and various others. There are always the competing interests: which one is it going to be? Rates should be 50 per cent of the income or 60 per cent of the income? It is always an argument. My point here is: have you seen a shift in councils thinking that rate capping is there and we need to look at other ways how we can continue to deliver services that are trying to save costs and improve productivity and efficiency? That is what I am getting at.

Mr SPENCE — Let me deal with it in two bits, because I think I need to deal with the 10 years for this. Ten years is the wrong number to look at. You need to look at from 1993 when Kennett took 20 per cent out of council rates. The impact that had was that councils stopped spending on infrastructure. Then in 1997–98 Rob Macelllan, who was the then minister, recognised that they had created a serious problem, and he started a piece of work to review the infrastructure backlog in local government. As a consequence of that — that was a challenge to the sector to get on top of that — we set up a thing called the STEP Program, started to look at the
infrastructure backlog and the underfunding. As a consequence we saw an adjustment. What I would argue is, and the data is clear, last year we were still collecting less in real terms than we were collecting in 1993–94. I wish the state would do the same. It is easy for the government to talk about 10 years, but let us have a serious look at the actual slice of time.

The second point is there is a lot of effort being put into improving the businesses. We are doing a lot of work in digital transformation. We are doing a lot of work in the procurement space. Our aggregated procurement activities have gone gangbusters, with councils trying to leverage off. We have now entered a national model as well. It is like the state buying: everyone in the one pot. We are doing a lot of work like that, and the councils have got a strong appetite for it.

We are also seeing some shared services in the back end of the business, so you are getting a number of councils working together on providing particular activities. You will see admin driven out of one council, for example, in the future in some areas. There is a lot happening.

Mr MELHEM — What I am getting to is if I am a ratepayer, I would probably say, ‘Look, my rates keep going up, from 5, 6, 7, 8 per cent over the last 20 years’. The point you made about your net income as a council is not necessarily the case. It has become an issue of a funding model and whether the ratepayer wants to continue with 5, 6 per cent or 7 per cent or whatever, or they think that rate capping is good, which I think they do. Will an elected representative have the same view? The question is then what sort of model and how you can balance the books to maintain delivery of services. You talked about, for example, VicRoads stepping in to actually cover the crossing, the SES is not far away and the community care program. It is all about thinking now outside the square: how are we going to continue to provide the service because of this issue of the rate capping? It seems to me there are some positives — it is not all negative — but it still a pressure on the system.

Mr SPENCE — In local government the cycle is not the same as the cycle in the state. The cycle in the state — I have been around the state bureaucracy for over 50 years, that is a long time —

Mr MELHEM — You must have been very young then; you must have been a young boy when you started.

Mr SPENCE — I was only a young boy when I started, you are right. The cycle is government spends and then the next government cuts, and then government spends. That does not happen in local government. It is just a trend. But what we saw in the Kennett era was major reform — we are great supporters of the reform. The 20 per cent rate cut was a blunt instrument that actually had an impact on infrastructure in Victoria that we are still catching up on. That is the point.

The CHAIR — I think we are about done. I thank both of you for your evidence again. It is very helpful to put things in context, and we will certainly be back via the secretariat to follow up on some points.

Mr SPENCE — I think, Chair, too that when we look at this in sort of six months time, we will have a much better picture of what is happening. When we do the data analysis after the annual reports come in and we are doing the surveying of some of the services, we will get a picture of what the movements are, and that will be much more helpful to you, I think.

The CHAIR — Just on the data collection issue, have you costed the impact on the councils of all that data collection?

Mr SPENCE — We have got rough numbers. They are not too sophisticated, but I want to do a piece of work that actually drills down into it a lot more.

The CHAIR — Anything that you thought you could provide we would be happy to look at.

Mr SPENCE — Yes, okay. It has been good to talk to you.

The CHAIR — I appreciate it. Thank you.

Witness withdrew.