Dear Mr Delaney

Re: Rate Capping

Please find attached Interface Councils' recent submission to the Essential Services Commission Rate Capping Review which outlines the expected impact of rate capping on Councils.

Yours sincerely,

Interface Councils Secretariat
Submission in response to the Local Government Rates Capping & Variation Framework Consultation Paper (April 2015)

Summary of Interface Councils position

Interface Councils support initiatives that enhance transparency, accountability and efficiency of local government. We would like to work collaboratively with State Government to ensure that the deployment of a rate capping policy will not have long term detrimental impacts on service provision and infrastructure delivery to local communities, particularly those experiencing high rates of growth and change.

Interface Councils does not support a cap based on the consumer price index (CPI). The Interface Councils would welcome further discussion on a model that utilises the Municipal Association of Victoria’s local government cost index instead of CPI.

Interface Councils believe that the variation process should not be onerous and create unnecessary levels of bureaucracy for already financially constrained councils. We propose the establishment of a standard template to ensure that the Essential Services Commission (ESC) has the necessary information to inform their review.

Interface Councils agree that an independent arbiter, such as the ESC, has oversight over the implementation of any rate capping framework. In addition, Local Government Victoria should have a role in providing direct support to councils in reconsidering their financial strategy where business cases are deemed by the ESC to have insufficient merit.

Interface Councils would welcome the opportunity to work with the ESC to scope the ideas and concepts proposed in this submission in more detail to inform a robust and sustainable implementation.
Introduction

In the approach to the 2014 State Government election, the Labor party made a clear commitment to the Victorian community of their intention to introduce a model of rate capping, ensuring that all local governments justify any rate increase above the CPI.

Rates are a key source of local government revenue and are in essence a tax based on asset value, rather than a direct fee for service. Nonetheless, for most councils, and in particular for those outside of inner metropolitan Melbourne, rates represent the largest proportion of council income budget and as a result there is a direct correlation between rating revenue generated and services and infrastructure delivered.

Local government access to alternative sources of revenue is scarce. An initial assessment of the impact of capping rates at CPI rather than at levels forecasted in the Strategic Resource Plans for the ten Interface Councils indicates a total loss of revenue of just under $200 million over the four years to 2020.

There are a number of potential complexities that will need to be considered in designing an appropriate rate capping implementation framework. These include:

- differences between council size, complexity and current financial position
- responsible stewardship of local assets
- growth
- cost pressures on revenue and expenditure unrelated to CPI and outside of local government’s control (such as government charges and levies, utilities, insurances and superannuation calls)
- services that councils deliver on behalf of the State Government which may not be fully funded through grants and or where the price has not been indexed sufficiently
- changing State or Federal Government policy positions which may have flow on cost impacts for local government
- green wedge stewardship
- implementation – timeframes and bureaucracy, and
- Infrastructure delivery – Developer Contribution Plan gap.

This submission provides responses to the questions raised in the consultation paper and highlights the importance to take into consideration the complexities mentioned above in determining a potential rate capping framework, particularly on how it might apply to Interface municipalities.

The Interface Councils released a “Fairer Funding” Report (6 August 2014) that highlights the unique circumstances that apply to their communities and the flow on implications this has and continues to have on Interface Councils’ planning and resourcing. It is highly recommended that the ESC consider this report in determining whether a single cap applies across all councils or a different cap for different groups as well as for the operation of the variation process.
Reponses to questions in the consultation paper

Form of the cap

1. While a cap based on CPI is simple to understand and apply, are there any issues that we should be aware of?

*Interface Councils does not support a cap based on CPI because it is not a relevant indicator for local government costs.*

The use of CPI as a benchmark for local government cost escalation is problematic.

Firstly, while the CPI is a weighted basket of household goods, council services are predominantly made up of salaries, building materials, contracts and utilities, all of which generally exceed other cost increases in the economy.

Secondly, over the last five years there have been increases in government charges, such as the Environment Protection Authority Victoria’s landfill levy and fire services levy, paid by councils that have increased by more than CPI. Levy such as the fire services levy have a much higher impact in municipalities within Country Fire Authority areas, which include Interface Councils, than it did in Metropolitan Fire Brigade areas.

Lastly, another issue to consider is the inability of local government to directly influence fees and charges that are set on its behalf by the State Government such as planning permit fees. A lack of annual indexation on these charges puts pressure on other areas of council budgets.

2. What are some ways to refine the cap (for example, alternative indices), in line with the Government’s objectives?

*Interface Councils strongly support the use of the Municipal Association of Victoria’s local government cost index. The Interface Council would welcome further discussion on a model that utilises a local government cost index instead of CPI.*

A local government cost index would be determined through an independent assessment made by the Australian Bureau of Statistics or similar. The Interface Councils support this approach and would welcome further discussion on a model that utilises the local government cost index.

3. Should the cap be set on a single year basis? Is there any merit in providing an annual cap plus indicative caps for the next two to three years to assist councils to adopt a longer term view in their budgeting and planning, particularly when maintaining and investing in infrastructure often takes a longer term perspective? How should such a multi-year cap work in practice?

*Interface Councils believe that there is merit in providing an annual cap plus indicative caps and that this would both minimise bureaucracy and give greater long term clarity to a council’s financial planning.*
The framework should support councils to take a long term perspective for financial planning. Major capital works projects normally have a multi-year horizon and therefore having a long term outlook on council’s anticipated income would be beneficial.

Councils are required, under legislation, to develop a four-year Strategic Resource Plan and Council Plan in line with the elected council’s terms. It would make sense that any approach to rate capping took that timeframe into consideration.

4. Should the cap be based on historical movements or forecasts of CPI?

*Interface Councils do not support a cap based on CPI because it is not a relevant indicator for local government costs. The Interface Council would welcome further discussion on a model that utilises the local government cost index instead of CPI.*

The Municipal Association of Victoria has flagged their intention to commission an independent analysis to determine a local government cost index which could form the basis for a more relevant starting point than CPI.

The local government cost index would be determined through an independent assessment made by the Australian Bureau of Statistics or similar. The Interface Councils support this approach and would welcome further discussion on a model that utilises the local government cost index.

The Interface Councils further recommend that the ESC provide to all councils the cap level by 30 November each year. Again, this would be the cap level for the next financial year, with an indicative cap level for year two to four. This would allow councils sufficient time to consider their required rate levels that would be the subject of a variation application.

This timing would also allow councils to undertake stakeholder and community engagement and council planning sessions between December and February at a minimum but would not preclude councils undertaking engagement earlier than this. As a result, it is suggested that forecasts are used to generate forecast cap increases for the four years. However, this would be balanced with the option of single year re-calibration to the actual outcome of cap measurement prior to June 30th.

5. Should a single cap apply equally to all councils?

*The Interface Councils believe that a different cap should be applied for different groups of councils. Any rate capping framework should provide a higher cap for the Interface Councils in recognition of the needs and challenges unique to the group.*

There are a number of potential complexities that will need to be considered in designing an appropriate rate capping implementation framework. The Interface Councils include a combination of councils with high levels of growth and development, along with councils with significant responsibility for green wedge conservation and management, particularly Nillumbik, Yarra Ranges and Mornington Peninsula.

Interface Councils are quite different to established metropolitan municipalities characterised by:

- lack of access to non-rate revenue sources such as parking fees and fines
larger geographic areas to service, resulting in additional costs for servicing remote parts of their municipalities
- a higher ratio of local infrastructure assets to state infrastructure assets. For example, Interface municipalities typically have a higher proportion of local roads (sealed and unsealed) and a lower proportion of arterial/main roads when compared to inner/middle metropolitan municipalities. This places extra demands on Interface councils’ finances, relative to the demands placed on inner/middle metropolitan councils, and
- A higher requirement for the provision of new infrastructure.

Additionally, unlike rural councils, Interface councils are not eligible for rural grant programs even though much of their land area is zoned for rural purposes.

During the last 10 years, Interface Councils have accommodated more than 50 per cent of Victoria’s growth. This creates enormous financial strain on council resources. Multiple, concurrent growth fronts and lack of existing infrastructure make it difficult to achieve unit cost efficiencies, meaning that growth in Interface councils costs more than growth in the inner suburbs. Despite this, previous state governments have not allocated a fair share of the allocated capital budget to accommodate and service the growth.

A 2013 report by Essential Economics assessed that significant infrastructure and resources, totalling the equivalent of $9.8 billion by 2026 (expressed in 2011 constant prices), will be required to ensure Interface Council areas are adequately provided with facilities and services to assist in closing the gap with Melbourne’s inner and middle suburbs, and to ensure improved economic, social and liveability outcomes are achieved.

Growth comes at a cost and these costs need to be funded – if not through rates, through some other means. It should be noted that currently, developer contributions provide only a part contribution to the infrastructure costs incurred for new residents. An unintended consequence of the foreshadowed changes to the Development Contributions legislation will be a further reduction of the share of infrastructure costs paid for by Development Contributions with a greater share to be funded by ratepayers in general.

Interface Councils have distinct needs and challenges due to its size, financial position, population growth and green wedge stewardship. Therefore, the Interface Councils advocate that any rate capping framework to provide a higher cap for the Interface Councils in recognition of the needs and challenges unique to the group.

**The base to which the cap applies**

6. What base should the cap apply to? Does it include rates revenue, service rates/charges, municipal charges and special rates/charges?

*Interface Councils recommend that the cap apply only to general rates and the municipal charges and not to charges that are operated on a fee for service or contracting basis.*
The cap should apply only to general rates and the municipal charge (for those councils that still have a municipal charge) and not those charges that are operated on a fee for service or contracting basis such as waste service. These latter services are market tested, subject to cost escalations as outlined in negotiated contracts and often provided on an opt-in or out basis in those municipalities where population density is sufficient to provide economies of scale.

Interface Councils recommend that special rates and charges are not included in the base quantum of the cap calculation, as they normally relate to a special purpose benefit (e.g. new road, footpath or drainage) to a very small number of ratepayers.

The Fire Services Levy should also be excluded from the cap as it is a tax that is collected by local government on behalf of State Government.

It is also important to note that there is no uniformity of the starting position across councils. The average rates and charges per assessment varies widely across municipalities and is based on historical decisions from council to council. It would not be safe to assume that the current levels are an appropriate base on which to assess or cap future movements. Applying a percentage in such circumstances could disadvantage those who have kept rates and charges reasonably low.

7. Should the cap apply to total revenue arising from these categories or on average rates and charges per assessment?

*Interface Councils recommend that the cap should apply to the Total Rate Revenue applying from these categories.*

This is consistent with the strategic element to which all councils determine rate increases, whereas an individual rate assessment is determined by how a Council determines who pays. To explain this further, if the cap is only applied to general rates, then a council could increase its total rate revenue above the cap level, through for example a higher level of increase in its municipal charge, subject to the 20% maximum allowed under Section 159(2) or a higher than cap increase in a service charge or rate.

8. How should we treat supplementary rates? How do they vary from council to council?

*Interface Councils strongly advocate that supplementary rates to be excluded from the rate cap.*

Supplementary rates are indicator of growth that leads to increased service delivery and infrastructure requirements that need to be responded to.

This is due to supplementary rates being an estimate, as required under Regulation 10(2)(q) of the Local Government (Planning and Reporting) Regulations 2014, under which council must include in its rating information of its annual budget, the “estimated total amount to be raised by all rates and charges compared with the previous financial year”. The breakdown of each estimated rate elements are also required under Regulation 10(2)(c,d,l,o).

Furthermore, Interface Councils believe that the objective of rating transparency and accountability would be enhanced through a greater breakdown of the current information reported for Regulation 10(2)(q) within the annual budget. In addition, the transparency of a rating cap should allow a
ratepayer to clearly see the rate calculation as their property existed and was valued in the year prior. Supplementary rates are charged where a property has been subdivided into more than one; a new house has been added to vacant land, an extension to a building on a property, a demolition of a building or a change in the zoning of that property. Any of these changed circumstances would mean that it is impossible to compare the level of rates levied on an individual property with rates in the following year, simply by the addition of the rating cap.

9. What are the challenges arising from the re-valuation of properties every 2 years?

*Interface Councils believe that the challenge will be more significant in the first year of implementation and the perception of benefit gained by the community. By implementing the framework in a revaluation year, the natural shift in relative values, and therefore rates, will mask the real benefit for the average ratepayer.*

The methodology of the local government rating model and how valuations impact the rates paid per property is widely misunderstood in the community. A comprehensive community information campaign will be required to ensure that the benefit is understood.

10. What should the base year be?

*Interface Councils believe that the base year should be 2016/17 with a commencement year of 2017/18.*

Interface Councils recommend that the base year is the year prior to capping commencing, i.e. if the framework commences for the 2016/17 financial year, then 2015/16. However, Interface Councils recommend that the commencement year to be 2017/18 for three reasons:

i. 2016/17 is a revaluation year and this will make the explanation of the first application of the cap very complex, especially at the individual property level

ii. many councils will have completed their existing enterprise bargaining agreements by 30 June 2017, and

iii. council elections will take place in October 2016.

The variation process

11. How should the variation process work?

*The Interface Councils believe that the variation process should not be onerous and create unnecessary levels of bureaucracy for already financially constrained councils. We propose the establishment of a standard template to ensure that the ESC has the necessary information to inform their review.*

The Interface Councils recommend that a standard template to be established for the variation process. This will minimise the cost and administrative burden for councils to apply for a variation and ensure that the ESC has the necessary information to inform their review.

The Interface Councils puts forward the following variation process for consideration:
Councils proposing to apply rate increases in excess of the baseline would need to prepare a variation application for ESC’s consideration. The variation could be prepared on either a four year basis in line with the preparation of councils’ Strategic Resourcing Plans (SRP) or an annual basis in line with council’s annual budget cycle. While either could work, the Interface Councils recommend a four-year model on the basis of minimising bureaucracy and giving greater medium term clarity to a council’s financial planning.

In reviewing each variation application, the ESC would give consideration to the following factors:

- The council has a robust 10 year Long Term Financial Plan and four year SRP in place,
- The council has a clear plan to bring rating increases back in line with the appropriate benchmark baseline for their category within a reasonable timeframe,
- The council can demonstrate clear and transparent communication and consultation with their community in the development of their annual budget and/or four year SRP,
- The council is subject to extraordinary financial drivers that are outside of their control which may include factors such as:
  - Implications of State or Federal Government policy changes,
  - Recovery from emergency or other disaster,
  - Legacy asset management concerns,
  - Shifts in global money markets affecting superannuation calls or other linked investments.
- The rate increase is in direct relationship to increased service and infrastructure provision, for example the introduction of a new green waste service, and the council can demonstrate community consultation and preparedness to pay.

It is critical that the timing and timeliness of ESC’s consideration on a business case does not derail council’s budget preparation and consultation process. The authorisation of a variation would need to be complete by March 31st to enable statutory consultation of four weeks to occur during
April/May, as mandated by the Local Government Act. This challenge lends weight to the option of preparing the business case for a four-year basis in line with SRP.

12. Under what circumstances should councils be able to seek a variation?

*The Interface Councils believe that councils should be able to seek a variation for any purpose following a robust assessment of their financial circumstance, community ambition and consultation.*

The framework should provide guidance about the reasons for variation that are eligible to be approved. However other circumstances may arise which are not anticipated by the framework, and it should be open to councils to seek variations for such other reasons.

13. Apart from the exceptions identified by the Government (namely, new infrastructure needs from a growing population, changes in funding levels from the Commonwealth Government, changes in State Government taxes and levies, increased responsibilities, and unexpected incidents such as natural disasters), are there any other circumstances that would justify a case for above cap increases?

The Interface Councils propose that the following circumstances to be considered for above cap increases:

- overall financial position at the commencement of the framework’s implementation (i.e. some councils are already experiencing financial challenge)
- State and/or Federal Government cuts to grants
- cost shifting by other statutory agencies
- Infrastructure in a Precinct Structure Plan where there is less than 100% contribution
- increases in council responsibilities arising from changes in State or Federal Government legislation or policy
- prevention, mitigation and response to natural disasters
- inability to generate self-sourced revenue
- community asset stewardship (including lack of viable alternatives to council ownership and management)
- proportion of rate base that is exempt from rates in accordance with Section 154 of the Local Government Act
- statutory requirements to fund superannuation shortfalls or increases in the level of the superannuation guarantee
- stewardship of green wedges
- growth, and
- Other extraordinary circumstances outside of local government’s control.

14. What should councils need to demonstrate to get a variation approved? What baseline information should be required for councils to request a variation? A possible set of requirements could include:

- the council has effectively engaged with its community
- there is a legitimate case for additional funds by the council
- the proposed increase in rates and charges is reasonable to meet the need
• the proposed increase in rates and charges fits into its longer term plan for funding and services
• the council has made continuous efforts to keep costs down.

We would like stakeholders’ views on whether the above requirements are adequate.

*Interface Councils strongly recommend that the ESC define what it meant by ‘effective’ and ‘legitimate’.*

Broadly, Interface Councils believe that the requirements outlined by the ESC are appropriate. Councils should demonstrate community consultation and engagement about the variation has been undertaken and that there is community support for a variation. However, we would like to see further clarification on what the ESC sees as effective (“the council has effectively engaged with its community”) and legitimate (“there is legitimate case for additional funds by the council”).

Furthermore, Interface Councils recommend that the assessment of a variation application should consider the relative level of council expenditure on a per capital basis. Rates are a revenue source and the level of rates is a function of the other non-rate revenues available to council. Rates do not reflect the level of expenditure or the level of a council’s efficiency. Hence, we believe that the appropriate measure of efficiency is expenditure per capita.

**Community engagement**

15. What does best practice in community engagement, process and information look like? Are there examples that we can draw from?

*Interface Councils believes that best practice in community engagement require participants to have thorough understanding of the subject matter thus a more in depth community engagement approach needs to be adopted.*

It is critical that the community has a good understanding of rate capping so they are able to provide informed feedback during consultation and community engagement.

Due to the complexity of rates, the usual approach of a single consultation is unlikely to be sufficient for participants develop a thorough understanding of the subject.

Some Interface Councils are adopting a more in-depth approach that comprise of three phases:

i. Three two-hours session with community leaders to develop recommendation(s) for council
ii. Broader engagement with members of the community to test the recommendation(s) of community leaders, and
iii. A statistically valid survey with a representative sample of the community to finalise the recommendation(s).

It should be noted that this approach requires a higher level of councils resources than a typical community consultation process for council budget and thus could not be undertaken on a yearly basis.
Incentives

16. How should the framework be designed to provide councils with incentives to pursue ongoing efficiencies and respond to community needs? How could any unintended consequences be minimised?

Interface Councils believe that the framework should be designed to provide financial sustainability while responding to community needs. We also believe that unintended consequences can be minimised by ensuring a planned and staged implementation in partnership with the sector.

Interface Councils welcome measures to enhance transparency, accountability and community engagement and ownership. We would like to see the State Government share the same principles to financial processes. A level playing field can act as an incentive for both levels of government to pursue ongoing efficiencies and respond to community needs.

Unintended consequences can be minimised by ensuring a planned and staged implementation in partnership with the sector. A fast tracked process will undoubtedly result in unintended consequences that may reflect badly on not only Local Government but also the State. An appropriately comprehensive risk assessment should be commissioned before implementation.

Timing and process

17. A rates capping and variation process should ensure there is enough time for councils to consult with their ratepayers and for ratepayers to provide feedback, and for us to review councils’ applications. To ensure the smooth functioning of the rates capping and variation framework, it is particularly important that it aligns with councils’ budget processes. We are interested in stakeholders’ views on how this can be achieved.

Interface Councils propose that the authorisation of a variation to be completed by March 31st to enable councils to undertake its statutory obligation as mandated by the Local Government Act.

As described previously (see answer to question 11), it is critical that the timing and timeliness of ESC’s consideration on variation applications do not derail councils’ budget preparation and consultation process. The authorisation of a variation would need to be completed by March 31st to enable statutory consultation of four weeks to occur during April/May, consideration of submissions and endorsement by June 30th, as mandated by the Local Government Act.

Transitional arrangements

18. What transitional arrangements are necessary to move to the new rates capping and variation framework? Is there merit in phasing in implementation over a two year period to allow for a smooth transition?
Interface Councils support the idea of phasing the implementation over a two year period. This will allow councils to develop full understanding of how the framework will operate.

The proposed rate capping framework represents a significant change in local government financial planning. A transitional year for application of the framework in 2016/17 would provide scope for councils to fully understand how the framework will operate and its impact on significant projects and regulatory requirements which require funding beyond the existing level of rates and charges.

In addition and further to the response provided to Question 10, Interface Councils believe that councils elected at the October 2012 election were required to develop a Council Plan that encompassed a Strategic Resource Plan for the four-year period 1 July 2013 to 30 June 2017 under the existing parameters of the Local Government Act 1989, including Section 126 Principles of Financial Management. Therefore a commencement year of 2017/18 would allow all newly elected councils to create a Council Plan cognisant of the full operation of the Rate Capping and Variation Framework.

Roles

19. What are stakeholders’ views on the respective roles of the key participants? Should the Commission’s assessment of rates variations be advisory or determinative?

*Interface Councils support the notion that an independent arbiter, such as the ESC, has oversight over the implementation of any rate capping framework. In addition, Local Government Victoria should have a role in providing direct support to councils in reconsidering their financial strategy where business cases are deemed by the ESC to have insufficient merit.*

Interface Councils propose that the Essential Services Commission act as an independent arbiter and perform the following function:

- review variation submissions and council budgets
- authorise rate increases in excess of the baseline where variation applications have sufficient merit in accordance with the established criteria
- provide advice to the Minister for Local Government in circumstances where variation applications are seen to have insufficient merit and other intervention may be required, and
- monitor the implementation of the Rate Capping and Variation Framework and provide advice to the Minister on any review, taking into consideration feedback from the Sector.

Importantly, Local Government Victoria (LGV) should have a role in providing direct support to councils in reconsidering their financial strategy where their variation applications are deemed by the ESC to have insufficient merit.

Over time, the policy parameters to support rate capping must be integrated across Victorian Auditor-General’s Office, LGV and the ESC to ensure maximum public transparency for councils and
for Government. Interface Councils believe that this should also be reflected in the Local Government Performance Reporting Framework.

**Other matters**

20. Is there a need for the framework to be reviewed to assess its effectiveness within three years time?

*Interface Councils believe that a regular cycle of review is imperative.*

A review of the framework should take into consideration feedback from the local government sector and the community. The review should also include a full assessment of the framework’s economic impact on Councils’ financial sustainability and ability to meet asset renewal requirements pre and post rate capping implementation.

21. How should the costs of administrating an ongoing framework be recovered?

*The cost of administering the framework should be borne by the State Government.*

As a State Government policy position, the framework should be fully funded by State Government. Under no circumstances should the cost of administering the framework be applied to local governments.

The State Government can minimise the cost of administering the framework by ensuring that the process is non-bureaucratic, simple to navigate and based on appropriate templates. Other matters raised in earlier chapters

22. We are interested in hearing from stakeholders on:

- whether we have developed appropriate principles for this review
- whether there are other issues related to the design or implementation of the rates capping and variation framework that stakeholders think are important
- supporting information on the major cost pressures faced by councils that are beyond their control and the impact on council rates and charges.

Interface Councils would like to provide further supporting information on some additional major issues faced by Interface Councils that are beyond our control and impact on council rates and charges.

**Responsible stewardship of local assets**

Local government has a key role in establishing and maintaining local assets which make a very real contribution to delivering economic, social and environmental outcomes at local, state, and regional levels. A 2014 report by the Auditor General identified that local government is responsible for $73 billion of community assets.
It is well understood that investment in these important assets has not been able to be sustained at required levels, even with current income and revenue strategies. While some good progress has been made, there is still a pressing need for many councils to address growing asset renewal gaps.

The same 2014 Auditor General report found that councils are generally budgeting less than is required to renew their assets and consequently the funding needed for asset renewal continues to grow each year. The Auditor General went on to assert that without appropriate and concerted corrective action, the provision of council services to communities is likely to be put at risk, and that while this may require some hard financial decisions and trade-offs, failure to address this problem now will only lead to more difficult decisions in the future.

An assessment of rate capping outcomes in New South Wales (NSW) undertaken by NSW Treasury Corporation in 2013 (as reported by Victorian Local Governance Association) identified critical under investment in asset maintenance and deteriorating financial sustainability had arisen during their own rate pegging regime. Their report found that revenue needed to grow to cover not only annual cost increases but the underlying cost of service delivery including progressive elimination of deficits and infrastructure funding needs. This meant that in most cases rates need to rise by substantially more than the current annual peg if councils were to achieve sustainability.

**Green Wedge stewardship**

The Interface Councils have the added responsibility of accommodating 90 per cent of Melbourne’s green wedges. The non-urban green wedge areas located within the Interface municipalities represent some of Melbourne’s most important assets in terms of Melbourne’s liveability, sustainability and prosperity. The green wedges provide vital agricultural, ecosystem, habitat, recreation and tourism values and benefit to all of Melbourne. Whilst the importance and significance of the green wedges to Melbourne’s liveability has been acknowledged by successive governments and the community at large, and has been embedded into the planning scheme as State Planning Policy, the legacy costs associated maintaining and enhancing the green wedges for current and future generations of Victorians comes at a considerable cost to the host councils and this is financially unsustainable long term. Examples include pest and weed management, rural roadside maintenance, and management of significant levels of native vegetation.

**Services that councils deliver on behalf of the State Government which may not be fully funded through grants**

The successful implementation of a rate capping framework must recognise the interdependent financial relationship between all levels of government, but in particular that of State and Local governments. A cut or a restriction in one area can have flow on implications for others.

Local governments typically provide a number of services on behalf of State and or Federal governments which are funded through grant programs. There is evidence that over time grants have not kept pace with the true cost of service delivery. Restricting the ability of Councils to generate revenue through rates will bring increased focus and scrutiny on those areas where local government receives less funding than the cost of delivery of such services. Examples include School Crossing Supervisors, Home and Community Care Services, library services and youth services. An
unintended consequence of rate capping may be a reduction in local government’s ability to subsidise declining real contributions from other levels of government.

Changing State or Federal Government policy positions which may have flow on cost impacts for local government.

From time to time State and Federal Governments introduce changed policy objectives which have flow on implications for local government. Recent examples are the four year old kindergarten universal access policy which has involved considerable expenditure by councils, the restricted breed legislation and the revised emergency management arrangements following the Bushfires Royal Commission resulting in substantial additional costs for many rural and interface municipalities.

Implementation – timeframes and bureaucracy

While Interface Councils welcome initiatives that enhance transparency and accountability, we are concerned that this does not come at the cost of additional layers of administrative burden. We urge the Government to ensure that implementation of proposed changes is done in a way that is well planned, well consulted and communicated, and provides councils with the ability to plan for the consequences and implications.

Conclusion

This submission has been prepared to help inform the development of the local government rate capping and variation framework.

While the objective of any rate capping framework is to limit the growth in rates, it must also ensure that every council is managing its financial undertakings responsibly and that revenue generation through rates is set at appropriate levels, taking into consideration relevant factors such as:

- growth
- ability to generate revenue through other sources
- stewardship responsibilities such as asset maintenance and renewal and management of green wedges
- emergency and other arising circumstances outside of Local Government’s control, and
- community ability to pay having regard to socio-economic or other factors

It is also important that any model does not create unnecessary additional levels of bureaucracy which do not add value or that create additional resource burden for already resource-challenged councils.

Interface Councils are confident that an appropriate framework can be designed to take consideration of and respond to each of these factors outlined above.

We would welcome the opportunity to work with you to scope the ideas and concepts proposed in more detail to inform a robust and sustainable implementation.
Appendix 1: Differences between Council size, complexity and current financial position.

In broad terms, councils can be categorised as:

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<tr>
<th>Type of councils</th>
<th>Characteristics</th>
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<tbody>
<tr>
<td>Inner city</td>
<td>• Average population growth with high density,</td>
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<td>• mature infrastructure,</td>
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<td>• lower service costs per resident,</td>
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<td>• high public transport options,</td>
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<td>• lower infrastructure growth requirements, and</td>
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<td>• an ability to raise revenue through parking and service charges.</td>
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<td>Middle suburbs</td>
<td>• Average population growth,</td>
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<td>• medium service costs per resident,</td>
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<td>• good public transport options,</td>
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<td>• lower infrastructure growth requirements, and</td>
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<td>• an ability to raise revenue through a variety of means such as parking and service charges.</td>
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<td>Interface areas (growth)</td>
<td>• Population growth up to four times the state average,</td>
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<td>• high service costs per resident,</td>
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<td></td>
<td>• new infrastructure in growth areas (PSP’s) requiring Council top-up funding,</td>
</tr>
<tr>
<td></td>
<td>• poor public transport options,</td>
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<tr>
<td></td>
<td>• heavy reliance on cars,</td>
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<tr>
<td></td>
<td>• long distances to employment,</td>
</tr>
<tr>
<td></td>
<td>• high state, regional and local infrastructure requirements and service demands across concurrent growth fronts leading to disjointed and unconnected development and inefficient unit costs,</td>
</tr>
<tr>
<td></td>
<td>• limited ability to raise revenue (no eligibility to rural grants), and</td>
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<tr>
<td></td>
<td>• the lowest allocation per resident of state revenue.</td>
</tr>
<tr>
<td>Interface areas (Green wedge)</td>
<td>• 90% or greater of land area zoned ‘rural’ or ‘green wedge’ with a small number of established urban areas dispersed throughout,</td>
</tr>
<tr>
<td></td>
<td>• Ageing infrastructure and poor public transport</td>
</tr>
<tr>
<td></td>
<td>• Low to average growth (can only accommodate infill housing),</td>
</tr>
<tr>
<td></td>
<td>• disproportionate dependence on residential rate revenue,</td>
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<tr>
<td></td>
<td>• heavy reliance on cars,</td>
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<tr>
<td></td>
<td>• long distances to employment,</td>
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<tr>
<td></td>
<td>• high infrastructure requirements and service demands;</td>
</tr>
<tr>
<td>Type of councils</td>
<td>Characteristics</td>
</tr>
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<td>-----------------</td>
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<tr>
<td></td>
<td>legacy costs associated with custodianship of the green wedges.</td>
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<tr>
<td>Peri-urban areas</td>
<td>• High population growth (in some areas),</td>
</tr>
<tr>
<td></td>
<td>• high service costs per resident,</td>
</tr>
<tr>
<td></td>
<td>• poor public transport options,</td>
</tr>
<tr>
<td></td>
<td>• heavy reliance on cars, long distances to employment,</td>
</tr>
<tr>
<td></td>
<td>• some ability to raise revenue through regional and rural grants.</td>
</tr>
<tr>
<td>Regional centers</td>
<td>• Slow population growth (with the exception of some)</td>
</tr>
<tr>
<td></td>
<td>• Average service costs per resident (suburban subsidy of rural properties),</td>
</tr>
<tr>
<td></td>
<td>• average public transport options,</td>
</tr>
<tr>
<td></td>
<td>• heavy reliance on cars,</td>
</tr>
<tr>
<td></td>
<td>• medium distances to employment,</td>
</tr>
<tr>
<td></td>
<td>• high infrastructure and service growth requirements, and</td>
</tr>
<tr>
<td></td>
<td>• some ability to raise revenue through regional and rural grants.</td>
</tr>
<tr>
<td>Rural areas</td>
<td>• Population decline,</td>
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<td></td>
<td>• lower demand for new or additional infrastructure,</td>
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<td></td>
<td>• poor public transport,</td>
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<tr>
<td></td>
<td>• heavy reliance of cars,</td>
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<tr>
<td></td>
<td>• employment generally close to home (or at home), and</td>
</tr>
<tr>
<td></td>
<td>• some ability to raise revenue through rural grants.</td>
</tr>
</tbody>
</table>
14 May 2015

Mr David Hawkins
Interface Councils
C/- Socom Pty Ltd
Level 2, 377 Lonsdale St
Melbourne VIC 3000

Dear Sir,

Submission in response to the Local Government Rates Capping & Variation Framework Consultation Paper (April 2015)

Mornington Peninsula Shire has reviewed both the Essential Services Commission Local Government – Rates Capping and Variation Framework Consultation Paper (April 2015) and the Interface Councils’ submission.

Due to the compressed timeframe to provide feedback and prepare a submission, the following technical advice has been developed by officers and is not Council’s formally adopted position.

Generally, the Shire supports Interface Councils submission to the Essential Services Commission (ESC).

We submit the following additional points:

- Explanation as to why the Consumer Price Index is not a relevant policy basis for the rate cap; and
- Timing and transition related to the framework implementation and processes.

CPI Vs Cost Index

There appears to be a common acceptance that a cap based on CPI would be simple to understand and apply. We query whether this perception is true and accurate; there are many different components to the CPI that is published by the Australian Bureau of Statistics (ABS). These include the publication of 9 different All Groups CPI figures being one for each of the eight capital cities plus one weighted average of the other eight. Further, each of those nine indices are broken down into component groups such as Education, Transport, Health, Housing, etc. There would need to be a clear definition of which permutation of the CPI is the basis for the cap, and prior to that, robust debate to ensure that the selected option is reflective for the desired purpose of the cap.

The ABS publishes the CPI on a quarterly basis. The measure of the CPI to be utilised for the cap would require definition. For example, the most recent annual movement (since rates are set annually) or an extrapolation based on the most recent quarter movement?
The headline measure of the CPI is the “Weighted Average of Eight Capital Cities” for the “All groups CPI”. Would this be the measure of the CPI utilised for the cap rather than, say, the All Groups CPI for Melbourne? If the headline measure is not utilised there could be confusion amongst ratepayers since the figures they see quoted in the media are almost always the headline measure.

Further, while it could be argued that the capital city measure for Melbourne is more suitable than the Canberra, Perth, Sydney or Darwin measures (because Melbourne is at least in the same state) we question the relevance of the All Groups CPI for Melbourne to the 57 non-Metropolitan (which include the Interface Councils) municipalities.

Given the level of definition that would still be required we therefore don’t accept that utilising CPI does make the cap necessarily easier to understand and apply than utilising any other available index.

The ABS publishes the CPI. The ABS does not produce prospective forecasts for the CPI – only retrospective reports. Therefore, utilising CPI will result in a lag between the measured underlying cost changes and those that are actually to be experienced during the upcoming period for which the rates increase is intended to apply.

The lack of a published forecast CPI figure from the ABS also inhibits its ability to be used for indicative caps (for the entire Strategic Resource Plan period) such as suggested in the Interface Councils response to point 3.

We have made reference to the ABS website page “Topics @ a Glance – Inflation and Price Indexes. Use of Price Indexes in Contracts”; in particular, the comments under the heading “General Matters to Consider When Developing Indexation Clauses Using a Price Index”. We have also referred to the ABS website page “Consumer Price Index FAQs” and the sections entitled “Is the CPI the best measure of inflation?” and “What are some limitations of the CPI?” These sections include the following comments made by the ABS itself:

- The CPI is designed to measure inflation for Australian metropolitan households and thus may not accurately reflect the experience of people living in rural areas.
- There is no single best measure of inflation. Ideally, such an indicator would be comprehensive and cover price changes for all goods and services traded in the economy. However, different measures of price change are suited to analysing different parts of the economy, so the best approach depends on how the data is going to be used.
- The ABS produces a range of price indexes, suited to different parts of the economy. For example:
  - the Consumer Price Index (CPI) is the most comprehensive measure of goods and services price inflation faced by all consumer households;
  - the Selected Living Cost Indexes (SLCIs) are designed to measure changes in living costs for selected population sub–groups. They are particularly suited for assessing whether or not the disposable incomes of households have kept pace with price changes.
  - the Producer Price Index (PPI) measures inflation of products either as they leave the place of production or as they enter the production process;
  - the Wage Price Index (WPI) measures changes in the price of labour in the Australian labour market, and
  - the Domestic Final Demand (DFD) is used as a measure of inflation experienced by consumers, governments and other domestic institutions.

Therefore, we have concerns that - if they were consulted with - the ABS might even suggest that the CPI is not an appropriate index to use as the basis for a local government rates cap.
Timing

- The Shire supports a multi-year cap; notionally fixed for two-years, with indicative caps for a further two years providing guidance for the balance of Council’s four year Strategic Resource Plan horizon. This approach to rate capping aligns with Council’s legislative and financial planning timeframes.

- The Shire recommends a specific cap and forecast guidance to be available to councils by December of the preceding financial year to allow for assessment and planning of non-capped income and setting of capital and operational priorities to formulate a draft budget by no later than April for community review and comment. This allows time for Council to formulate priorities and genuinely engage with the community.

The Shire consents to referencing the content of this letter, or to include as an attachment, within the overall Interface Councils submission to the Essential Services Commission.

The Shire appreciates the work that has been carried out on behalf of Interface Councils and are keen to continue to actively participate in the consultation process with the Essential Services Commission on this very important matter.

Should you wish to discuss any aspect of this submission please do not hesitate to contact the undersigned.

Yours faithfully,

Matt Hubbard
Chief Financial Officer