TRANSCRIPT

STANDING COMMITTEE ON THE ENVIRONMENT AND PLANNING

Inquiry into rate capping policy

Morwell — 26 September 2016

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

Ms Samantha Dunn
Mr Khalil Eideh
Mr Cesar Melhem
Mr Daniel Young

Participating Members
Mr Greg Barber
Mr Jeff Bourman
Ms Colleen Hartland

Mr James Purcell
Mr Simon Ramsay

Staff
Secretary: Mr Michael Baker

 Witnesses
Mr Tim Tamlin (affirmed), chief executive officer, and
Mr Tom Lovass (affirmed), manager, finance, South Gippsland Shire Council; and
Mr Matthew Rogers (affirmed), manager, finance, Latrobe City Council.
The DEPUTY CHAIR — As Deputy Chair I call this hearing to order and explain that the Standing Committee on the Environment and Planning will be hearing evidence in relation to the inquiry into rate capping and into fire season preparedness here in Morwell, and the evidence is being recorded.

Please note, for witnesses, that we extend a welcome to you to the public hearings of the environment and planning committee. All evidence taken at this hearing is in fact protected by parliamentary privilege. Therefore you are protected against any action for what you say here today in this hearing, but if you do go outside and repeat the same things, those comments may not be similarly protected by this privilege.

I now invite the three witnesses for this morning to address the committee. We have allowed 5 to 10 minutes for an opening presentation, comments and remarks, and then from there we can continue onto questions. So, gentlemen, over to you.

Mr TAMLIN — Where do we want to start? Probably at the beginning.

The DEPUTY CHAIR — It is a very good place to start, Mr Tamlin.

Mr TAMLIN — Yes. We obviously put in a submission. I am not going to go through details of that submission — it is what it is — but I just want to highlight a few little key points on there, in fact the paragraph on the second page reads:

A ratepayer in the inner suburbs of Melbourne with a property valued at $800 000 would pay approximately $900.00 per year in rates for a comprehensive and easily accessible range of services. In South Gippsland a residential property valued at $800 000 would pay $4473.

I think to me that is the underlying driver of why we see a rate cap environment, because the community could not understand why there was such a level of change in the amount of rates charged across the various municipalities. Those numbers came out of a little piece of work I did a couple of years ago in comparing the City of Stonnington with Mornington Peninsula, with South Gippsland and with Buloke Shire. I am almost certain I presented this information at the last hearing.

Ms BATH — You did. I recall it.

Mr TAMLIN — Yes. To me this is the fundamental of why we are sitting here today. For example, South Gippsland is collecting rates and charges income of about $38 million, where we are charging someone $4300 for an $800 000 property, and then you have got the City of Stonnington where they are charging about $962 for a residential property but bringing in an income of $98 million, and they do not have the level of area that we do, with the roads and the infrastructure and the networks. That sort of just puts it in context for me, I think, quite nicely. I do think — this is my personal opinion — that rate capping is a good thing, because it is actually stimulating conversations in local government for looking for efficiencies a lot harder than it would do without it.

That is having some good things for the Gippsland Local Government Network, where the CEOs have signed up an agreement, a charter, to pursue joint services, and that is already starting to come together in various locations and between various shires. For example, South Gippsland and Baw Baw councils now share a risk management coordinator. We have got the same risk management person looking after two risk management offices, one in each shire. We are using the same pieces of software. We have actually gone out to tender, and the audit committee is now being supported by an independent auditor that operates for both shires under one contract. So there are little economies of scale starting to be realised, and we will continue to work with each other to do that sort of thing. That is why I think rate capping has been good, to stimulate that discussion.

But then on the other hand you look at the shires like Buloke, and Towong is a very interesting little case study, where you would no doubt be aware that they applied to get an exemption from the cap, which they did, but then they did not pass on that full exemption to their ratepayers because they said, ‘How is that fair? Why should our ratepayers pay more than everybody else?’, which I thought was a very clever way of demonstrating the difficulties that the rural councils face. My personal view of this is that the metro councils, or the more inner Melbourne councils, are able to be resilient in the rate cap environment more, in a stronger way, than the rural councils are. The further you get away from Melbourne the tougher it gets. Looking at how the rate cap works, having a cap set for everybody being the same, I do not think is quite right.
I think they are basically the points I would like to make this morning. Thank you.

The DEPUTY CHAIR — Next cab off the rank is, Mr Rogers; you look keen.

Mr ROGERS — Yes, keen. Thank you, members. The Latrobe City Council this weekend actually had some news which could have a major impact upon our council and rate capping. We have at the previous meeting discussed the impacts that the generation company agreements have on our rates base and how those generation company increases are linked to CPI rather than rates cap and how that has disadvantaged us in the past also. We will obviously face significant disadvantages if we have closures of any of those facilities in that we are obviously unable to recapture those costs through a rate capping environment.

The DEPUTY CHAIR — Just to cut you off there and ask a question, if I may. Obviously we do not have any announcement yet in relation to Hazelwood. There has been some speculation over the weekend — and I think everybody has done that for many years — and whilst we recognise that there is writing on the wall, we do not yet know what that writing says. Has the council looked into understanding the economic impacts of a partial or full closure as part of its planning for management of assets and income in the context of this rate capping policy already? If you could just detail the work that has been done internally, that would be appreciated. Obviously we are talking about a potentially major event here that is unique to the council and to the LGA.

Mr ROGERS — Yes. Council has engaged CT Management to assist with the undertaking of a financial sustainability review. That review is nearing completion as we speak. However, there is limited analysis in that report in relation to the impacts of a closure of any of our generators. So in terms of the economic impact statements or economic impact works that may have been undertaken, I am not fully aware of any at this point in time. I know that there has been something happening in the background, but am not aware of what amount of work has been undertaken.

The DEPUTY CHAIR — Mr Rogers, I might just interrupt there. It is 11.17 a.m., and we note that the Chair, Mr Davis, has arrived, so on that basis I will hand over my previous deputy chair duties to him to continue. Please continue, Mr Rogers.

Mr ROGERS — In reviewing the previous reports put out by this committee, Latrobe City Council supports the committee’s previous findings in relation to the early announcement of the rate cap being supported, the refinement of requirements relating to the rate cap variation application, certainty around the funding of the Fair Go rating system, clarification being provided in regard to the responsible use of debt by the ESC and continued focus on cost shifting from the state and federal governments.

Our position is that we would like to highlight that we see that the rate cap has actually had limited impact in the initial year. We have been able to continue to maintain the existing amount of services and continue to maintain our existing assets. However, we have identified through our financial sustainability review that we are looking at savings in the vicinity of $6 million over the next four years in order for us to continue to maintain existing services and existing asset structure.

We consider that it is still an issue in relation to our EBA and annual increases in our EBA exceeding those of the rate cap.

Ms SHING — When did you negotiate the most recent EB, Mr Rogers?

Mr ROGERS — I believe our EB is just over 12 months old.

Ms SHING — That is a three-year agreement, is it?

Mr ROGERS — I think it is two years.

We have identified that our asset renewal is currently underfunded in that we are not currently contributing 100 per cent of our depreciation costs around our infrastructure assets. We also identify the requirement to rationalise council’s asset base where we are not directly linked to services, and probably one of the items that the rate capping has highlighted with our council is that we do need to go back and look clearly at what assets we are holding and whether those assets are supporting the services that we provide.
Obviously we just spoke about the high risk in this area in relation to the impending generation companies and their possible closures into the future and how they are excluded from our current rate capping process.

Continuation of cost shifting has come to the party again since the last review. We have just recently made a submission to the inquiry into the sustainability and operational challenges of Victoria’s rural and regional councils, where we highlighted the responsibilities for flood planning and preparation and maintenance of flood mitigation infrastructure, where there appears to be a shift in the areas of responsibilities from current catchment management authorities to council, which could have significant financial impacts on councils.

Going forward, our challenges — we have also made a submission into the regional impact statement for planning and environment fees regulation and subdivision fees regulation. We identified in a previous committee meeting that these fees were identified as not having increased over a long period of time, and we support the review of that increase. However, the findings that have come back from that indicate large increases will severely disadvantage rural areas that rely on planning to drive economic growth. While we support increasing fees, it is not to the magnitude that is suggested through that.

We also highlight the election costs, because we are currently entering into an election, and the increases that they provide each time that we have an election, so we are seeing the increases there in the vicinity of $100 000 from the previous election. We are working closely through our GLGN network into looking at regional procurement solutions and working jointly.

Ms SHING — I have just another question if I may, and I apologise to my colleagues for leaping in throughout the presentation. At the last hearing I suspect it was the Latrobe City Council elected representatives who had referred to the Morwell main drain litigation as being a potentially huge impost on council coffers, following the initial decision. Were funds placed into contingency for the purposes of that litigation, and if so, how much, and what has been the net result of the appeal outcome?

Mr ROGERS — We are happy to say that we were successful in defending that case. We have not had any funds put into contingency. We put some legal funds into contingency, which is in the manner of about half a million dollars for the legal costs associated with that case. Having been successful in defending our position, we are hoping to gather some of those costs back from the other party.

Ms SHING — Thank you very much, Mr Rogers, that is appreciated.

Mr LOVASS — Two hard acts to follow, so I will try to keep it brief. I will just very much focus on the high-level financials of South Gippsland. As Tim mentioned earlier, South Gippsland is financially sustainable at the moment. We prepare our annual budget within a 15-year framework, which has got a series of long-term financial strategies that back it up. In that financial plan the longer term results are trending undesirable, and I am talking about the mid-to-latter years.

Can I go back one step? We are financially sustainable at the moment and we could accommodate rate capping through a series of good plans but also we benefit from having a low-inflation environment. That is really telling when I look at the models. Going forward, our underlying operating result trends into a deficit result. We are still in surplus but the trend is undesirable, which will have flow-on impacts for basically our asset renewal program and so forth which is at the moment funded. I think in the future the rate capping will bite, particularly when the inflationary figures turn around for roads construction and other cost drivers, such as enterprise agreements and so forth.

I guess I am stating the obvious there. What I would just put to the committee is that as an opportunity, rate capping, as Tim says, is good. We can cope with it. It forces efficiencies. I think there is an opportunity for the state government to look at the grant-funding allocations to local government per se, which is a big issue in terms of VGC. Your basis is that large councils, I am guessing, in terms of metros, can cope with it quite easily — that is rate capping at the moment. The larger rural councils can cope for a while, but you are already putting pressure on the smaller ones. It is very telling.

Ms SHING — You do not have that buffer.
Mr LOVASS — I think you have got to look at an incremental change to the grant allocations to stop this gap occurring over the coming years in terms of the financial pressure coming off at the smaller councils. I said that in a roundabout way.

Ms SHING — No, that is very useful.

Mr LOVASS — I think you have really got to look at the funding streams to local government to help councils with the rate capping environment.

The CHAIR — I might kick off with the first of the questions on that exact point. Country roads and bridges was such a grants stream, direct to councils, $1 million a year. What is the impact of that disappearing?

Mr LOVASS — I could not comment. Obviously with the money disappearing it means we have not got the income source for the works associated with that, and that is, I suppose, the contra. When the Victoria Grants Commission grants were frozen for a couple of years we did get this alternate funding stream, so in terms of dollar wise it was a nice little net off. In the future, with that disappearing, it will put further pressure on local government. I think what local governments will be looking for — and I am talking about the rural councils — is a more steady guaranteed cut of the VGC funds going forward without having had these specials come through which are a fortunate — —

The CHAIR — What about a permanent version of a roads and bridges program?

Mr LOVASS — Permanent is consistence.

The CHAIR — So that was an annual program of $1 million a year.

Mr LOVASS — Yes. Permanency, from a bean counter point of view, if we have got permanency guarantee of some sort of funding source, it will help us with our planning.

Ms DUNN — Because you always know it is coming.

Mr LOVASS — Yes. That does help with our modelling. When we look at our budget, I go — —

The CHAIR — So maybe if we just ask Latrobe the same question.

Mr ROGERS — We are in the fortunate position where the majority of our bridges have been upgraded now, so we only have one or two bridges that remain that still require updating, so in terms of funding for us in relation to our bridges — —

The CHAIR — Roads.

Mr ROGERS — Roads is always an issue. We have had double lots of Roads to Recovery the last two years, so that has certainly been a major assistance in our areas and appreciated.

The CHAIR — Federal money.

Mr ROGERS — Yes.

Ms SHING — Plus $20.3 million for Gippsland roads maintenance and upgrades, but anyway.

The CHAIR — But council roads is a separate point. With the roads that you are responsible for, again, the same sort of steady program would assist.

Mr ROGERS — Yes, any steady sort of program would — —

Ms SHING — Any money gratefully received.

Mr ROGERS — It would be gratefully received, yes.

Ms SHING — Mr Tamlin, did you have anything to add to that?
Mr TAMLIN — Yes, just to add to that, I mean you could take, for example, roadside weed management. We are currently managing I think it is around 5 per cent of our road network adequately, but the rest is unfunded. They are the sorts of things that hit, and we just manage with what we can do. So the service standards we provide on roadside weed management are less than desirable, compared with what we would like to do, but you physically just cannot afford it. The state government has helped out with some funding towards that, but still, when you have 2200 kilometres of roadsides the money does not go far. So we just concentrate on preserving and maintaining our high-value roadsides where we have got indigenous plants and tourist areas and the like.

Ms SHING — I just have one further question. It comes off the back of the comments in relation to South Gippsland Shire Council and the way in which rates are gathered. Given that we have got high-population growth in some areas of Gippsland, more specifically than Latrobe — down through Bass Coast shire and Baw Baw but also in pockets of South Gippsland — has rezoning affected the amount of funding anticipated to be received by councils, and if so, to what extent?

Mr TAMLIN — That is a tricky question.

Ms SHING — Sorry, I will not be asking any easy ones today.

The CHAIR — You may not be able to answer it now.

Mr TAMLIN — From what I have seen working back in my metro council days, and just looking at what went on with Casey there, where they were having one new birth every so many hours, or whatever it was, and they were booming, I just recall the actual burden put on the council to deliver services and upgrade infrastructure, and the cost that it took far outstripped any additional costs they got in rates or developer contributions.

Ms SHING — And for the smaller population centres in South Gippsland?

Mr TAMLIN — For us, for example Nyora, there is a rezoning that has gone on around through there. The challenge here too is, how do you ring fence a developer contribution that does not outstrip the viability of going forward with it but then also delivers the benefits to the community through the new assets that it may bring with it? My personal experience is more development actually creates more cost burden to the council. It actually does not give you more rates, therefore make you become more wealthy.

Mr ROGERS — Can I just add to that? We have a number of DCPs, or contribution plans, in place. All of those contribution plans show that we go into negative cash flow for those, and it can be up to 30 years before we recoup those moneys. While it creates growth and that growth obviously builds on itself, it does have a long-term payback. It is very marginal.

The CHAIR — But the DCPs are quite a different matter from the rates per se. When a property is developed you are getting the rates at an earlier point. The DCP phasing issue, which I think you identify, is a separate matter from rates.

Mr ROGERS — It is a separate matter from rates. Those rates are what we need to fund those ongoing services, as well as the ongoing infrastructure costs of those new developments.

The CHAIR — I just wanted to make sure that it was clear.

Ms SHING — Did you have anything to add, Mr Lovass?

Mr LOVASS — I totally agree with the comments. It sounds sort of exciting to get that growth for your rate base to increase, but there is a tipping point where if you have got to tip in basically capital costs to support that population, you actually go backward for a substantial period of time, which will put, again, funding pressures on the plan. Interestingly for South Gippsland, our population I am sure must be in a shadow; we are not experiencing that high growth. We actually had a slight decline in population over the last year or so. So we just want to make it clear that we are not like the Bass Coast.

Ms SHING — No, that is right.
Mr LOVASS — We are sort of in a bit of a shadow.

Ms BATH — Thank you, gentlemen, for appearing today and providing your evidence. My question relates probably straight to Mr Lovass at the minute. With the undesirable holding, maintaining status at the moment, undesirable trending into the future, the decision around services up against asset renewal or asset maintenance, how will that be decided upon?

Mr LOVASS — With our financial strategies we have got a very strong focus on asset renewal, but the asset renewal is part of a service. If I can use the roads for example, we provide a service transport, and it is important that we renew our assets. We have had a strategy for a number of years to actually focus our capital works priorities on renewing assets rather than building new assets; that is why we are in a reasonably good financial position. So when the going gets tough in the future years, again from a bean counter point of view, I will advise councils saying, ‘Okay, we’re running undesirably in terms of our costs increasing’, and I will say to them, ‘What services do you want to cut out on?’, and depending on what service they look at, we will have some asset infrastructure requirements that will sort of be impacted. So I will take a punt. Roads is one that you cannot cut back on, so therefore we will then have a very strong position and say, ‘If you want to maintain your roads, you must replace them’. We will say, ‘Do not compromise on that’, which will then force the issue in terms of, ‘Well what other services, the softer services, will you drop off on?’. Because if you start dropping off on your roads and your maintenance renewals, you will actually have an increasing cost pressure compounded in the later years.

Ms BATH — Sure, and safety and security of residents as well.

Mr LOVASS — Yes. From my side, I do not advise what services they should go for — it is not for me to pick and choose — I just try to advise on the financial implications. But I would suggest the council, roads being a core service, they will not let go of that. They may drop service standards to a point, but they will have to do it very carefully, because otherwise it can actually compound your cost pressures and actually create the problem that we solved many years ago. And why do that? I think that is the advantage of councils. With the Local Government Act changing in the coming year, I am expecting that most — if not all — councils will have to create 10-year financial plans. They will help councils actually see with the financial decisions made now what is the impact for not only this year and the next three, four years of the term but also the longer term.

Ms BATH — Thank you; I appreciate that. Did you want to add anything, Mr Rogers?

Mr ROGERS — No, I think he covered that fairly well.

Ms BATH — He did, yes.

Mr ROGERS — We through our financial sustainability process had reviewed all our services and identified 108 services that we provide at the Latrobe City Council. We are in the process of actually ranking those services in terms of the most important through to those that you would concentrate on if you had to cut services.

Ms BATH — And I am assuming, along with that, the community consultation around that ranking is very important.

Mr ROGERS — It will be, yes. We are not at that stage yet, but yes.

Ms DUNN — Thank you gentlemen for your presentation this morning. I firstly just want to pick up on a couple of points from you, Mr Rogers, when you talked about the generation company agreements. I am just trying to understand the scale of the impact to council if Hazelwood does in fact close and what that means in terms of income to the council, the hit to your budget.

Mr ROGERS — We receive approximately $9 million a year from the generation companies in rating agreements. The impact of one of those closing would be in the vicinity of $2 million, from now.

Ms DUNN — I assume as part of any sort of transition plan for people in the valley there has to be consideration of the Latrobe City Council itself in terms of that hit to your pocket as well?

Mr ROGERS — Yes.
Ms DUNN — I did not think you would argue with me. The other part I just want to pick up from your presentation is that you talked about the ability to rationalise your asset base. I am just wondering if you can give us an idea of what sorts of assets they might be that might come up for consideration for rationalisation?

Mr ROGERS — We have recently had an overview of our open space, as an example, where we have identified developer-contributed open space which does not support our open space strategy. We used to have a situation where developers would maybe provide one block or two blocks within their developments, as they handed them to council, as their open space strategies. We have identified some of those blocks as obviously operational costs for us ongoing that provide no benefit to our community. So we are looking at disposing of those assets and reinvesting that money into better open space infrastructure for our communities.

Ms DUNN — That is great. Thank you. To both councils, I am interested in the overall view in relation to the process around the announcement of the cap, the timing around that and your budget preparations. You are probably pretty much starting already to think about your budget for next year and the fact that you do not know the cap until 31 December and how that impacts on the organisation in terms of it does not work — is the timing right? I am also interested in whether you have seen any new areas of cost shifting, because there are certainly plenty in there that have been there for a long time, but whether there are any emerging areas of cost shift. I know you identified one in terms of emergency management. It is a double-header question.

Mr LOVASS — I will answer the first part because it is easy for me. We actually start our budget process in October. So it does cause us some issues in terms of what the rate capping is. Bear in mind that this is the second year, so the rate cap was announced last year. I have been in contact with Andrew Chow from the Essential Services Commission to try and find out the thinking in terms of what the likely rate cap will be in the future. Obviously he is in a position of guessing also. It causes problems the second year in. When I say problems, I am guesstimating what it will be. We will factor that into the forward plan, then we will have a first-draft budget to council in December prior to rate capping being announced.

Then based on the rate cap being announced, we will have to maybe reconfigure or give them that report. It really gets down to how far was I wrong in my guesstimate of what it is going to be. To me, it causes administrative issues, which I think if they can be overcome somehow in the future years that would be great. We are all creating plans. We are creating 15-year plans. We are going to be creating 10-year plans in the future — I am guessing; this is the industry. It would be nice to get some sort of indicative — —

The CHAIR — It is a bit hard to do that when you do not know what the annual increase is.

Mr LOVASS — Very hard, it is. We are speculating — —

Ms SHING — Planning is inevitably always speculative and difficult in that sense.

Mr LOVASS — We have got indexes that we are working on in terms of inflation and so forth, so some sort of indication a little bit firmer would be nicer from an officer point of view.

Mr ROGERS — We, like South Gippsland, start around November, our budgeting increases. The first year was probably the difficult year, because it was so variable in understanding exactly what that increase was going to be, what the impact was and waiting for the government’s decision as to whether there were going to be variable rates or whether there was going to be a fixed rate. I think going forward it would be nice to know a period of time, lock in some rate increases up-front to be able to assist us with our long-term planning and in particular our major capital projects that we have coming forward.

In terms of the timing, earlier is always better; however, for the immediate year, while minor variations cause us some administrative pain, we are pretty close to where we think we need to be in relation to those in the short-term, early process. But having said that, if we were to know earlier, we also recognise that any variation that we are likely to put in, we are really planning 12 months in advance for those. It is not something that we are going to make a decision on based on the announcement of what the rate increase will be for that year.

Ms DUNN — And the other half of the question — any new and emerging cost-shift areas for either of you?

Mr ROGERS — The only one that I picked up was the one that I mentioned earlier, which was in relation to the floods. There appears to be a shift from the catchment authorities to council in terms of responsibility in that area.
Mr LOVASS — In my mind, I normally do it at the high-level stage. I am not suggesting there are not any; I just cannot think of any.

Ms SHING — If you think of something, then you might provide it on notice.

Mr LOVASS — Can I just take this opportunity to say also about rate capping that even when you are talking about efficiency dividends, which was mentioned in the first year, that makes an important difference to our modelling. Any sort of clarity in terms of what is likely or the direction will help purely from a modelling point of view.

The CHAIR — I thank all of our witnesses and indicate that the secretariat may well be in touch over the next period to follow up a couple of points. We thank you for your testimony.

Witnesses withdrew.