

REROC

RIVERINA EASTERN REGIONAL
ORGANISATION OF COUNCILS

Response Issues Paper Revenue Framework for Local Government

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**RIVERINA EASTERN REGIONAL ORGANISATION OF COUNCILS
RESPONSE
ISSUES PAPER
REVENUE FRAMEWORK FOR LOCAL GOVERNMENT**

The Riverina Eastern Regional Organisation of Councils (REROC) is a voluntary, strategic alliance of 13 General Purpose Councils and two water county councils. The members of REROC are the councils of Bland, Coolamon, Cootamundra, Corowa, Gundagai, Greater Hume, Junee, Lockhart, Temora, Tumbarumba, Tumut, Urana and Wagga Wagga as well as Riverina Water and Goldenfields Water.

Our members believe that a strong and viable local government sector capable of delivering quality services that communities want at the grassroots level is imperative to the economic, social, cultural and environmental well-being of NSW. Underpinning the ability to achieve this goal is an appropriate funding regime that recognises our role as a third tier of government.

Our submission addresses the Issues on which IPART has sought comment but only in the context of the first two matters that IPART has been asked to investigate and make recommendations on:

1. an appropriate inter-governmental and regulatory framework for setting rates and charges that facilitates the effective and efficient provision of local government services:
2. a role for IPART in setting rates and charges in future years.

Role of Local Government

The members of REROC agree that local government faces many challenges. Our members also agree that local government, particularly in rural and regional NSW is about sustaining communities. Our members believe that local councils are the heart of a community and that they are essential to forging the quality of a community's life, we are the foundation on which a community is built. Unfortunately our members are being forced to face the harsh reality that community sustainability is often only achieved when councils step up and provide services that traditionally have been responsibility of state and federal governments.

Therefore our members agree with the conclusions reached by speakers at the Local Government Financial Sustainability Summit held in September 2006, when they stated that they

...were unanimous that councils were in a financial crisis and agreed on its causes: cost-shifting by Federal and state governments, inadequate financial assistance grants and, in many rural shires, small and declining populations, coupled with stagnant property values and long road networks.¹

¹ Max Berry, 'Action on Council Finances Needed', *Government News*, October 2006, 7.

Our members believe that the issue of an appropriate revenue framework for local government can only really be successfully addressed when the issue of what functions, services and infrastructure should realistically fall to local government and which are rightfully the province of state and federal governments. Cost shifting has been identified in successive reports on local government as an issue that is undermining our financial viability as is the question of whether or not local government is receiving its fair share of tax revenues – that is a share that reflects our increasing responsibilities.

Our members strongly support on-going proposals for the establishment of an Intergovernmental agreement on service delivery that is underpinned by appropriate funding for the identified responsibilities.

Ultimately the role of local government is determined by the community it services. It is that community that holds the council accountable for their actions not just at the ballot box but because local government is the government that has the highest level of accessibility, councillors and council staff are held accountable for their actions everyday

It is worth noting that this high level of accountability translates into a high level of constituent satisfaction. An IRIS Study undertaken for the Allan Inquiry, found that 50% of residents across NSW rated their level of satisfaction with their local council as high, 35% as medium and only 15% as low. In addition the Study found that satisfaction levels with rural and regional councils were consistently higher than for metropolitan councils. Our members argue that this demonstrates the ability of local government not only to meet the needs of its constituents but to excel in the role.

There are a number of underlying issues that impact on the ability of local government to fulfil its role as a builder of communities; inadequate funding and the negative impact of rate-pegging, cost-shifting by federal and state governments, the growing problem of being the “last man standing” as federal and state governments decrease their service delivery levels to rural and regional communities, increasing demands by the State on local government for compliance reporting and planning and the increasing reliance of the State on local government to maintain regional and rural road infrastructure.

Rate Pegging

Our members maintain that rate capping has consistently undermined local government’s capacity to achieve financial sustainability. The 2003 Federal Government’s Inquiry into Local Government and Cost Shifting stated that

The rate capping system in NSW exacerbates local government’s inability to raise sufficient revenue. Moreover, it has negative implications on local revenue stability and strategic planning.²

² House of Representatives Standing Committee on Economics, Finance and Public Administration, Commonwealth, *Rates and Taxes: A Fair Share for Responsible Local Government* (2003), [41].

The UTS Centre for Local Government discussion paper, *Advancing Local Government, Partnerships for a New Century* argues that there are frequent cases:

...where adequate provision of services and infrastructure cannot be maintained within rate capping limits, even with efficiency gains, due to special local needs, rapid population growth or other factor.³

The ALGA has estimated that rate capping in NSW cost local government an average of \$200 million per annum, assuming that NSW Councils would have increased rates to the same degree as other states.⁴

At a time when Australian governments everywhere have embraced the concept of user-pays, local government in NSW is trapped in a policy time warp. Residents should be asked to pay higher rates in return for better services and improved facilities but how can this effectively occur when councils must go with a begging bowl to the Minister to request that he or she lift rates above the capped increase.

REROC acknowledges that the Minister can and does approve rate rises above the rate pegged limit. However our members would agree with comments made in the UTS Paper stating that the response to requests is inconsistent stating that “there have been marked differences in receptiveness from year to year”⁵ and noting that for some the approval comes only “after the council concerned has had to devote substantial resources to making its case and has been subjected to intense scrutiny”⁶

IPART suggests that rate pegging encourages councils to find other appropriate sources of revenue such as user fees and charges. Our members would remind IPART that while user fees and charges may be a viable revenue raising alternative for councils that have large and concentrated populations in small urban areas, for rural and regional councils where populations are scattered over hundreds of kilometres it simply does not work. The charges that can be realistically imposed usually don't recover the cost of service delivery and generally the numbers of users are small which further restricts the revenue that can be raised. For example Gundagai Shire Council operates a swimming pool for residents, although it charges fees for use, the Council advises that the net cost of the service is between \$65,000 and \$100,000 per annum.

An economic rationalist would ask, given the circumstances should the service be delivered at all? However if councils are about creating and maintaining communities then the answer is yes, because without the services there is no community.

³ Centre for Local Government, UTS, *Advancing Local Government Partnership for a New Century* (2000), [16].

⁴ House of Representatives Standing Committee on Economics, Finance and Public Administration, above n1, 43.

⁵ Centre for Local Government, above n3, 16

⁶ Ibid.

Our members would not support a great reliance by local government on user charges and fees as we do not believe that in rural and regional areas there is any real prospect of this approach generating sufficient revenues to make any difference. It should also be noted that any discussion about raising fees and charges must also address the issue of the Government setting statutory fees and charges, for example for s149 and s603 certificates, which are not determined on a cost recovery basis. Nevertheless our members believe that increased user charges cannot be used as a replacement for appropriate levels of State and Federal funding and removal of rate pegging.

IPART has also suggested that one of the “pros” of rate pegging is that it ‘limits the ability of councils to divert funds from essential infrastructure to other projects, and spend on marginal services that are better provided by the private sector.’⁷ This is clearly not what is occurring, again the infrastructure maintenance and renewal gaps demonstrate that what actually happens is that councils make a choice between delaying maintenance on essential infrastructure and continuing to deliver services and the imperative for service delivery is winning.

Our members would welcome IPART demonstrating what marginal services councils are now providing that the private sector would be willing to invest in and operate in rural and regional areas. Our experience is that private enterprise is only interested in service provision where there are profits to be made or where a council is willing to subsidise their entry and even their operations.

Our members do not believe that there are any ‘pros’ with regard to rate pegging. It is a political sledgehammer used by the State as a control mechanism on local government. It might be a useful tool for councils if it acted as a benchmark or ceiling for State agencies and departments when they are setting fees and charges that are applied to councils, but it does not. The State Government pays no regard to a Councils’ rate pegging limit when applying levies for functions such as:

- NSW Rural Fire Services
- NSW Fire Brigades
- Department of Lands – Valuation Fees
- State Electoral Office fees
- Planning Panel costs

Our members are at a loss to understand how the State can raise its fees and charges to us with no regard to our financial constraints. For the current round of local government elections the SEO has raised its charges up to threefold for some councils without any significant increase in service provision. It is a monopoly service provider and councils have no choice but to pay.

If rate pegging continues to be a policy of this State then IPART must recommend that State agency and department fees, charges and levies to local government must be reflective of rate pegging – those agencies that

⁷ IPART Issues Paper, 55.

service local government should have to deal with the same financial constraints and budget accordingly.

Cost Shifting

The Issues Paper does not effectively address the issue of cost-shifting and its impact on financial sustainability. The Report from the Upper House Inquiry into Cost Shifting identified that 'much cost shifting has occurred by the level of State's grants failing to keep pace with changing responsibilities and cost increases.'⁸ We note that IPART's Paper does not address the issue of whether or not the State is paying its fair share of the cost of service delivery.

For example, the State Government currently provides approximately \$23 million towards the cost of running 363 libraries in NSW (60% are in rural and regional areas). In 1980, the State Government contributed 23.6% of the total operating costs of public libraries. The State contribution dwindled to 7.8% in 2004-05 with further reductions in years since then, including a massive cut of \$1,023,000 (4.16%) in 2006-07. NSW has the lowest State Government per capita contribution to public libraries of all states and territories in Australia. It is local government that is picking up the funding shortfall of \$265 million, which is coming from rate-pegged, ratepayer funds.

The problem of the State failing to keep pace financially with the cost of service delivery is further supported by the Commonwealth Grants Commission who identified that while the level of State Specific Purpose Payments (SPPs) had increased over time it had actually fallen as a proportion of local government revenue. In 1974-75 State SPPs represented 15% of local government revenue, but by 1997-98 it was about 7%.⁹

In addition our members note that the Paper does not address the cost of compliance, reporting and planning requirements that have been introduced by the State, particularly over the last 10 years. Increasingly, local government is using valuable and limited resources completing reporting and planning requirements established by the State that appear to have no real productive outcomes. The State's failure to rationalise its data capture, which would minimise the reporting costs to local government, is a very real problem.

Local Government Efficiency

The positive spin on this lack of funding is that local government is operating at a highly efficient level – councils are providing far more services than was the case in 1974 but doing it with less funding. An alternative assessment is that this is one of the reasons that local government is facing a financial crisis, councils are being forced to do more with less and consequently the industry is straining at the seams.

⁸ House of Representatives Standing Committee on Economics, Finance and Public Administration, above n2, 36.

⁹ Ibid, 37.

Our members note that IPART has identified that the size of councils influences viability and the Tribunal states it is interested in investigating whether economies of scale exist in the provision of particular services. The successful operation of ROCs such as REROC clearly demonstrates that councils are willing and able to search out opportunities to achieve economies of scale and scope where appropriate. REROC's activities over the last 10 years have generated savings in excess of \$18 million for member councils

IPART raises the issue of whether efficiency improvements can improve council's financial sustainability. Our members would argue that councils are extremely efficient and that the continuing debate about efficiency is masking an underlying failure by the State to provide adequate funding which is further exacerbated by rate capping. The Allan Inquiry Report noted that back office overheads in 58 councils it reviewed ran at only 10% of council operating expenses, whereas the benchmark for operation of similar sized organisations was between 10% and 16%.¹⁰

Our members do not believe that rate pegging or other constraints on revenue raising improve efficiency: the identified shortfalls in funding for infrastructure maintenance and renewal clearly demonstrates what it does result is a failure by local government to meet all its financial obligations because there is insufficient revenue to do so.

The suggestion that local government is more efficient because of rate pegging is a spurious argument. In many ways it makes us less efficient, instead of spending small amounts of money regularly on maintenance we are forced to delay it and consequently need to spend more later, councils cut corners, using cheaper products or services that don't deliver as efficient outcomes as more expensive options would but fit better with the budget. We borrow from tomorrow to pay for today and our members are more than aware that it is catching up with us.

A role for IPART in setting Local government rates and charges

Our members believe that if rate pegging is to persist then it would be preferable for the management of the process to rest with IPART rather than the Minister where political imperatives can impede economically sound decision making. For example in the early 1990's the then Minister, Gerry Peacocke decided that there would be a zero increase, our members argue that there is no justification for such a decision and it was therefore based on political imperatives.

We therefore support IPART's observation that there appears to be no clear basis for determining the level of rate pegging each year. It does not reflect the rising cost of for example salaries or an established benchmark such as the CPI. Similarly, as IPART has noted in its Issues Paper, there is no

¹⁰ Allan, P. Independent Inquiry into the Financial Sustainability of NSW Local Government, *Final Report*, May 2006, 21.

transparent criteria for rate variations. This results in added costs to councils as they attempt to guess what hoops they need to jump through to obtain the rate variation needed.

REROC would support IPART having a determinative role similar to IPART's role pursuant to section 11 of the *IPART Act 1992* which would provide consistent guidelines in relation to the setting of rates, the determination of rate variations and the determination of council prices and charges and removed political intervention in the process.

Conclusion

Our members are concerned that IPART is forced by the Terms of Reference to consider local government's role in isolation to its State and Federal counterparts. We do not believe that a viable outcome can be achieved in relation to establishing a Revenue Framework for Local Government until a Service Delivery Framework for Local Government is established via a Intergovernmental Agreement. It is only when all three tiers of government commit to holistic service delivery where each tier delivers the service for which it has the comparative advantage and is compensated appropriately from taxation revenues that we can hope to achieve sustainable financial results for councils and the State.

Our members note that IPART is looking at local government revenues at the same time it is reviewing State taxes, and we believe that it would have been a more fruitful exercise to consider both issues at the same time and the interplay between each. Considering the socio-economic impacts of raising local government revenues in isolation, without considering at the same time a proposal floated in the State Taxes Inquiry that local government should lose its payroll tax exemption (\$180 million per annum) is of great concern.

Local government and state government do not operate in isolation from each other and our members agree that more collaboration between all three tiers of government would generate significant efficiencies in service delivery. Therefore our members would strongly support a Review into Service Delivery Framework for Local and State government as it is only by identifying where responsibilities lie that we can develop a financial framework that delivers those responsibilities.

Our members would welcome the opportunity to meet with IPART to discuss the issues we have raised.