The Vaucluse Progress Association

Established 1915 ABN 12 756 395 726 P O Box 29, Vaucluse NSW 2030

22 August 2008

RECEIVED
25 AUG 2008
INDEPENDENT PRICING & REGULATORY TRIBUNAL

Review of the Revenue Framework for Local Government
Independent Pricing and Regulatory Tribunal
PO Box Q290
QVB Post Office NSW 1230

Dear Sirs

REVENUE FRAMEWORK FOR LOCAL GOVERNMENT – JULY 2008

The Vaucluse Progress Association is a long established community group representing a substantial membership resident in the Vaucluse and Watsons Bay districts which were previously in the now superseded Vaucluse Council and presently form part of the Woollahra Municipal Council. We have over many years taken considerable interest in local government affairs and in the revenue and expenditure activities of our local council upon which we have frequently commented. ***Attached are extracts of recent newsletters which are relevant and which we ask you to take into consideration in your deliberations.***

ROLE OF LOCAL GOVERNMENT:

The 1993 Local Government Act requires Councils to provide adequate, equitable, appropriate services and facilities for the community. This is a very broad definition and has been so interpreted over the years accordingly.

The effect of this definition has been to move local government away from property based services. It has become more tempting for Councillors and staff to deal with community social services and benefit from their short term popular impact instead of concentrating on the more important but mundane infrastructure requirements. This aspect of Council activity has, of course, been encouraged by State Government in particular, who grasp at any opportunity to transfer financial obligations. Apart from social service type activities, a typical example is that despite over 100 years of State Government funded and maintained public transport street shelters, this has now become a Council responsibility forced, in part, by deliberate neglect (to the extent of structures becoming unsafe) by State agencies.

There is a serious backlog of infrastructure maintenance, asset renewal and their future improvement. Ratepayers and local residents are becoming increasingly aware of this shortcoming due to the poor condition of the roads and other physical features. This is occurring in conjunction with an increase in overall urban population and consequent usage.

In our view the only way to persuade councils to deal with this problem is to re-define their functions by limiting them to property based services for which current rate raising revenues appear to be adequate.

EFFECTIVENESS OF RATE CAPPING:

So long as the definition of Council services remains so broad, rate capping is the most effective restraint on expenditure. Unfortunately it does not direct the capped expenditure into those infrastructure services that have become so neglected. This can only be done by limitation of the duties of Local Government. Such a redefinition involves serious political issues. The burden of social services involving child care, old age and health services should be a Commonwealth or State responsibility. The incidence of demand for such services is not evenly spread on a local council area basis. There is no reason why Councils could not become involved in the implementation of such services but the cost should be directed to Commonwealth or State as appropriate. Any reforms on these lines will result in a marked reduction in Council overhead costs and an improvement in their efficiency in the areas of property based services.

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REGULATION OF COUNCIL FINANCE AND SERVICES

We consider that IPART should play a role in supervising and monitoring (auditing) the financial reports and budgets of Local Councils. However in such processes it is essential that IPART transparently and publicly demonstrate and document any added value its role provides to the process. The present situation makes it difficult for the ratepayers and even the Councillors themselves to comprehend budgetary obligations and the financial position of Councils on an annual basis. The findings of Access Economics as part of the Allan Report in 2006 pointed out the shortcomings in financial governance policies and practices as well as inadequate reporting of Council's financial position and performance. Nothing has been done to implement these findings.

GENERAL COMMENTS:

Our Association are concerned that over a thirty year period and in spite of a fairly static sized local population, we have seen our local Council expenditures increase enormously largely as a result of increasing staff levels and use of consultants which reflect the many and varied additional activities in which the Council is now engaged. This has, of course, resulted in hugely increased rate burdens on residents while the infrastructure quality, such as roads, has deteriorated and is increasingly the cause of resident frustration. The expenditure on non property based services (which are really the responsibility of Commonwealth and State Governments) is the basic cause of shortage of funds which result in efforts to further raise revenue which can only be limited by some form of restraint such as rate capping in such circumstances.

Councils are sometimes seduced into providing non property based services often by seed funding from other levels of Government which then dries up leaving an apparent responsibility to keep providing such services without proper funding.

Rather than constantly maximising the rate revenue it would be well if a harder look be taken to recoup all costs and maximise all possible "user pay" funding by Councils including more appropriate fees for development applications and other areas coming under the planning sections of local government.

We wish to endorse and support the detailed and thoughtful submission dated 10 August 2008 (copy of which was given to us) made to you by Michael Rolfe of Natural Allies who is a long time member and past President of this Association. <u>Your close scrutiny and evaluation of the contents thereof are earnestly solicited.</u>

With regard to IPART's review process we believe, to gain credence, that IPART should transparently demonstrate the use of the public consultation input and reasons for its use/rejection. This should be part of the formal reporting process.

Yours faithfully

Barry Rémond

B M G REMOND
ACTING PRESIDENT

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Newsletter, January 2006

Independent Inquiry into the Financial Sustainability of NSW Local Government

This inquiry, being undertaken by high-powered consultants for the NSW Local Government and Shires Associations, attracted our attention especially as it relates to rating and charging for Council services, and whether and how local councils might be – or become – financially sustainable.

Woollahra Council has a recent history of adopting rate increases set at the maximum increase permitted, and seeking – and usually but not always obtaining – Ministerial approval of special rate increases above that general maximum, and imposing an environmental levy originally approved for three years, and later extended for two additional years; and unsuccessfully seeking Ministerial approval for an infrastructure levy. It has also returned to debt funding in this financial year.

The council's budgetary management has proceeded each year from a base assumption of maintaining service levels; in a situation of general cost increases especially those relating to staff costs, this has occasioned a large and growing burden on ratepayers without any apparent reduction of services.

At the same time, the Council has added a range of new human services and activities, notably including those resulting from the State Government's emphasis on social planning. Local road, footpath, stormwater and similar infrastructure is ageing, and maintenance has not kept pace with its deterioration.

All this looks a bit grim from the ratepayers' and residents' viewpoints: do we expect to face ever-rising rates bills to fund ever-widening activities that we don't even know about for much of the time? And for how long can we do that?

Because the matter is a fundamental one, we report our submission here at rather longer-than-usual length. If it gets tedious, try to visualise your rate notice in ten years' time!

Rating mechanisms: efficiency and equity

Our submission said that there are serious equity and efficiency problems that arise from the current rating mechanism. While they have often been explored in past reviews of local government, many defects remain.

Some progress towards equity was made with the introduction of the *base charge rate* mechanism, which recognises, partially at least, that many council services and works benefit all landowners regardless of the value of their landholding.

However, the 50% restriction on that mechanism retains considerable inequity, especially in council areas where the range of applicable land values is wide for reasons of varying subdivision scale and strata titling of medium and high density dwelling units. Of course the base charge does not fall directly (if at all) upon non-ratepayer residents and visitors who also benefit from such works and services, and so the equity and efficiency of its incidence are compromised to that extent.

The *ad valorem* component of rates is equitable only to the extent that it funds activities that benefit rateable landowners in proportion to the value of their landholdings, and no other activities. Of course, that situation simply does not apply in local government. The reliance of the *ad valorem* mechanism on the flawed land valuation practices and outcomes of the past constitutes a major barrier to the equity and efficiency objectives of local government taxing.

Accepting the (unwelcome) reality of rates on land as a major component of council revenues, we favour the use of rating revenues for those council infrastructure and service activities that cannot sensibly be confined to specific sets of users. For example, we see rate income as being reasonably available for expenditure on parks, road maintenance, drainage and the like, but not for those activities where users can reasonably be identified individually and charged the net cost of the service they are using.

* We think the base rate mechanism should be freed of the 50% restriction contained in S500 of the *Local Government Act 1993.*

Scope of council services

The present legislation enables councils to provide a virtually unfettered range of services.

What is *local* is not at all clear, and so it is not surprising that councils have become active in many fields that seem to have much wider reference frames. For example, most human services now provided by councils fall into categories that were once (and remain formally) the primary responsibility of other levels of government, such as the educational services provided through libraries and the welfare services provided through variously titled community centres.

Clarity of roles would enable issues related to cost shifting and related matters to be more readily distinguished from those related to the observable expansion of local government in a context where there are no formal limits on its scope.

* We advocate revision of the legislative statement of the council charter in S8 of the *Local Government Act 1993*, so that what is considered to be local, and therefore primarily the responsibility of councils, may be readily distinguished from what is undertaken in agency functions for ("*on behalf of*") other levels of government.

* We think the language of S8 should be clarified to ensure that activities undertaken *on behalf of* other levels of government are fully funded by those other levels of government.

Residents' desires and wishes – *wants* – are typically identified by councils by reference to community surveys. When the questions canvassed are wholly or partly unbounded by financial constraints or direct implications for respondents' rate bills (if applicable) or other funding source, the resulting range of nominated wants can be very wide indeed.

People's wants are effectively limitless.

Judging by our Woollahra experience, the wants and wish lists derived from such surveys are then classified by the council as *needs* by a process of mere re-naming, and often funded by diversion of funds from less electorally appealing items like drainage and local road maintenance.

In practice, it seems the high profile human services of councils crowd out the less populist traditional activities from council budgets, even though the former are not primarily council responsibility.

The absence of clear price and cost signals for many council services and activities obscures the assessment by councils and their consultants of community aspirations and the setting of priorities for the outlays intended to meet them.

It also enlarges the potential field of council activity by generating expectations of apparently free or cheap services that councils are (naturally) disinclined to disappoint.

Once installed in a council's catalog of offerings, activities rarely disappear. Ratepayers may perceive at least some nexus between service costs and rate levels, and so moderate their demands on councils to some extent; however, non-ratepayers have no such perception to guide them unless cost-based user charges are imposed.

* Where users do not pay directly for services, shifts in demand are obscured, and the scope (and appropriate standard) of each service lacks an economic basis for assessment.

* Efficiency and adequacy of service provision are unlikely to be achieved where cost-based price signals to users are muted or absent.

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Paying for council services

When the primary providers of human services have withdrawn from the field and/or councils have displaced them, and the scope of human services has been extended - by councils themselves - beyond the range of any incentive grants originally provided by the State/Commonwealth, subsidies provided to councils for these kinds of activities typically do not meet their costs.

The local government sector identifies this as cost shifting by the State and Commonwealth governments. However, to the extent that local councils undertake activities that are primarily the responsibility of other levels of government, they either act as agents – in which case they can and should be reimbursed for their costs – or they assume the burden voluntarily, usually on the ground that no-one else has done so. In the latter instances, the costs of services are shared between users and ratepayers (who may well not be users of the services) according to whatever pricing policy is adopted by the council.

In the absence of a direct cost/price relationship, user demand/want/need for such services is unconstrained by financial practicality, and ratepayer response is muted and ineffectual because the realities are obscured by the diverse nature of the council's activities.

*We advocate a formal agency arrangement for councils in relation to those activities that they provide on behalf of other levels of government to ensure that non-local activities are not a charge on local ratepayers.

* We advocate full net cost recovery from users of those services which fall outside the range of agency services for other levels of government.

* We see council rates on land as being a time-honoured, although not welcome, way of funding local public infrastructure works, but ***not*** human services.

The rate component of particular council service costs and fees/charges made for them is not identified or discernible to ratepayers, and is not of direct interest to non-ratepayers. For that reason, the discipline on rate levels that might otherwise be provided by the electoral process is ineffective.

* We strongly support rate pegging in its role as the only presently available brake on adventurism among councillors whose enthusiasm for being seen to be active is too often not balanced by expertise in matters of public finance.

Unlike other levels of government where Treasury matters are the primary responsibility of a specific Minister accountable to the Parliament as a whole, local rates are determined by councillors as a group, on the basis of simple majority decision-making by people who do not necessarily pay rates themselves anyway, and may not appreciate the influence of the underlying land valuations on the distribution of the rate burdens they impose.

* It is reasonable that councillors should have to make a specific and sound case to a competent authority if they wish rate increases to exceed the general level of price movement in the community they serve.

Loan funding

The Independent Inquiry's Discussion Paper projects an approach that appears strongly to favour council borrowing, partly on the ground of inter-generational equity. We do not think that is a sound basis for councils to assume debt. Our main considerations are set out below.

The life span of municipal assets varies considerably, up to some 80 years or more. The depreciation allowance treatment mandated in local government accounting standards reflects with more or less accuracy the consumption over time of the assets to which depreciation is charged. Equity and accountability are both served by that mechanism.

In practical terms, resort to debt does indeed extend the available resources of a council at the time the debt is assumed. However, it also necessarily depletes the available resources of the council for the future, as interest costs and repayment are serviced. Thus, future generations are burdened with the costs of providing current benefits to the current generation. This is the obverse of the position put in the Discussion Paper. Arguably, both positions might be supportable, but each incorporates significant inequity.

It is salutary to consider why so many councils moved away from indebtedness in recent times.

Part of the collective wisdom appears to have been a sensible reaction to the unsustainable burdens of then-prevailing high interest rates; it appears, too, that local councils realised all too sharply that interest rates vary over time, and over-extended budgets cannot be continually stretched by borrowing.

Part of the reaction also recognised the growing frustration of ratepayers, who saw rising rate burdens allocated not to needed infrastructure and current requirements, but sterilised for debt servicing generated by past profligacy.

Noting that the deductibility of debt servicing costs for income tax purposes is not a matter for local councils, we accept that there may be a theoretical case for councils to assume debt in order to bring forward acquisition of assets/undertake works that are urgently needed now, but which require outlays in excess of those presently available.

Our immediate response to that scenario is a simple one: either the council should insure against the kinds of emergencies envisaged in the argument, or it should provide in its budget for them as a normal prudent financial planning exercise – if necessary by diversion from optional programs.

* We strongly discourage the use of debt funding for municipal purposes.

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Council Management Plan and Budget Consideration

The community consultation implicit in public exhibition of the Council's annual draft Management Plan is reliant on the community's submissions being taken seriously. The fact that there are ordinarily few (if any) companion organisations making such submissions does not indicate any inherent defect in what we say for our Association; rather, we think it suggests a community-wide perception that Budget-related submissions are unwelcome to and perhaps even unconsidered by the Council. When we failed to discover in the current Budget timetable any reference to a promised report on and consideration of our Association's previous (and still un-answered) Budget submissions, we were a bit miffed.

The Council's approach to taxation of ratepayers is specially important at this time when it is looking to introduce new and bigger rating measures (as well as borrowings) ostensibly to deal with an infrastructure backlog that reflects past decisions to spend revenues on more exciting items.... just like the present Council. As usual, we see that services will have to be cut if rates are not increased... and that seems to be the end of the argument. Pity, really: some services could and probably should be cut, but you can hardly expect those who provide them to recommend that. Easier by far to raise the rates, again, and again, and again.

Paying for infrastructure

The Inquiry, ***Are Councils Sustainable***, commissioned by the Local Government and Shires Associations, has reported its findings, and there are no surprises.

Among other things, it advocates a removal or loosening of rate-pegging and smiles kindly on council borrowing in order to overtake the backlog in infrastructure maintenance and provision, and generally says most of the things we are accustomed to hearing from local government.

We had put some views to the Inquiry, but they were swamped by councils and councillors. Ratepayers' interests were definitely a minority.

Essentially, we argued that unless the revenue base of local government is enlarged by the addition of a broad taxation base, the broad slate of activities that it presently pursues should be narrowed to encompass those activities that impact directly on the land that provides the rate revenue, and those that are funded by user charges and agency reimbursements.

This was once the standard role of local councils, before they took on their nanny role to look after everything for everyone.

Despite all the councillor handwringing going on about it, the present unsatisfactory state of council infrastructure reflects the collective decisions of councils to use their available resources for purposes other than the maintenance of infrastructure. Instead, they have chosen to undertake more attractive activities, including the enlargement of their services range.

That kind of thinking may well reflect inadequate accounting information about the state of the roads and drains, but it also reflects deliberate choice by people elected on particular platforms or none.

It is the critically unsatisfactory outcome of that process that leads us to oppose any enhancement of the traditional council roles, and correspondingly to oppose the provision to councils of unfettered access to revenue-raising by rates on land. We want rate pegging to stay.

Having been given the responsibility for local infrastructure, councils have palpably failed to discharge it satisfactorily. It is difficult to see why the electorate should trust them with other responsibilities.

And it is uncomfortably easy to see our point in the current draft budget of Woollahra Council for 2006-2007: after finally attaining debt-free status a few years ago, there is now $194K allowed for interest on loans and $227K for loan repayments – to be funded by ratepayers. It is dead money from some viewpoints.

Looked at another way, close enough to one dollar in every eight dollars to be collected in the new Environmental and Infrastructure Levy next year will be spent not on infrastructure at all, but on that debt servicing.

Happily, no new borrowings are proposed, yet. Only rate increases.

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Newsletter, July 2006

Woollahra Council Management Plan 2006 – 2009

It is history now that Woollahra has gained Ministerial approval for a rates increase this year that is equivalent to 9.58%.

The identification of works for a special levy program separately from other works reflects the directions of the Local Government Minister in relation to special levy approval procedures. As a tactic, it may well make levies more palatable to ratepayers who can at least see something real for the levy money, even though they lack similar comfort in relation to the general rate bill. The technique also makes it less likely that requests for approval of special levies will be disapproved by the Minister, since the relevant works program is carefully chosen to illustrate essentiality.

But the principle of special levies for identified infrastructure programs should not commend itself to ratepayers: the core funding of councils lies in the general rate, and the first call on the general rate revenues should be the essential provision and maintenance of council infrastructure. Under the special levy approach adopted by Woollahra, infrastructure is effectively the last call on the general rate revenue.

Of course all the money can and will be well spent. Someone in the community wants each of the things that it will be spent on and then some more.

As is usually the case, ours was the sole public submission made on the 2006 rate proposal. It is therefore a fair thing for Councillors and the Minister to consider that *a small number of ratepayers were not very positive about it but recognised the downside if this infrastructure work wasn't carried out*, as reported in the *Sydney Morning Herald* on 28 June 2006.

That's true. We **are** a lone voice in bothering to express any concern about the trend of the Council's expansion into optional activities, and we are treated like one. For example, we complained in 2005 that our budget submission had been dismissed in the Council's reports with the remark that it raised matters previously raised by us. Following that complaint, we were assured that a proper examination of the long-standing issues we had raised would be forthcoming. We still await it.

Certainly we can't complain when the Council does not agree with us. Perhaps Council needs to hear more from our individual members.

Do you really care about the cost of rates? Do you want us to continue as we have in the past? Should we (or anyone else) keep trying to persuade the Council to stay with traditional roads and drains and parks things, and leave the State and Commonwealth Governments to do their own thing?

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Newsletter,
November 2006

Informing the ratepayers?

Woollahra's General purpose financial reports for the year ended 30 June 2006 have been published, presented to the public, and signed off. Ours was the only comment on them. Don't ratepayers care?

The reports disclosed a continuation of the trend away from the funding of traditional council services by the ordinary rate. We have previously recorded our discomfort with that trend. It effectively relegates the construction and maintenance of basic community-wide infrastructure to a residual priority, increasingly dependent for funding on the official approval of "special" revenue measures, while optional activities absorb more and more of the ordinary rate revenue.

Broadly, the financial reports show that the Council outlaid some $25m in employee costs to achieve only some $28m worth of outputs of all kinds, including materials purchases – and over $1m-worth of those outputs reflects the special environmental levy works. The employee component of overheads is so large that it implies less and

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less flexibility for the Council in meeting its infrastructure tasks, even though the need for action on the infrastructure backlog is obvious, and is acknowledged by the Council itself, and is common to local government.

The 2006 resort of the Council to $3.07m debt seems perverse in this context, since the borrowing can at best only generate a small works outcome (because of the labour component) and - unfortunately in our view – it provides another vehicle to assist diversion of activity away from the traditional responsibilities of local councils. The practicality of the overheads situation warrants careful consideration of the relative efficiency of the trend of Council's activity towards labour-intensive community service provision.

A Special Schedule attached to the reports disclosed continued unsatisfactory asset conditions for roads, footpaths, kerbs and gutters, and stormwater drainage, with some $20m remedial works indicated to bring them to satisfactory condition. That Schedule has provided that message for too long already, but the Council continues to commit to construction works (such as shopping centre beautification) that are entirely separate from the remedial work indicated for basic public assets.

The issue is one of priorities: we might expect the Council to look to bring its public works assets to a satisfactory condition as a first and over-riding priority, but it clear that it does not do so. This is probably one reflection of the residual nature of infrastructure works funding in the special rate context.

Another explanation might lie in the opportunistic nature of many proposals for other activities, especially in the community services area, such that *ad hoc* decisions accumulate without necessarily having the benefit of a clear policy priority assignment. That possibility is a matter of concern to ratepayers.

The assessment of Council stewardship of resources is not assisted by the Statement of Performance Measurement, which confines itself to some elementary financial ratios only. The performance measures that typically accompany the program budgets throughout the year remain unhelpful for the purposes of objective assessment of task menus and their appropriate resource allocations.

In the absence of a record of works requested but neither done nor committed, the Special Schedule is the only approximation to which ratepayers can resort. Its inadequacies warrant attention in the light of the public accountability objectives that underlie the transparency criteria of council financial reporting to the public.

Council Budget strategy

The presentation of an Overview of the financial position of the Council to its Corporate and Works Committee late last year provided us with an opportunity to remind the Council of the body of opinion in our Association that favours a better match between the Council's ordinary revenue stream and its expenditures than is apparent in the special levy and borrowing program that underlies the report.

We noted that the identified capital works program and infrastructure renewal strategies – which drive the resort to special levies and loans -- are not inherently immovable, and indeed they can be (and have been) adapted and varied according to the Council's wish at any particular time.

The presently-identified projects, especially some of those related to streetscape improvements, exhibit a range of degrees of necessity. Some are merely optional. In the latter cases, resort to loan funding is not supported by

us, and resort to generally-applicable special levies is also not supported.

As noted above in relation to Double Bay and Watsons Bay, we do not object to such projects being funded by rate premiums applicable only in the commercial areas that receive the primary benefit. We requested the Councillors to consider such a mechanism.

It's that time of the year: Woollahra Council's 2007/2008 Draft Budget

The first pass of the draft Budget was again based on the retention of all existing services. at existing service levels *plus* certain increments (about which we had no particular quarrel). This fails to recognise the changing context of public need and opinion. We have long argued that ordinary services should be funded from ordinary revenue, and that services should be adjusted to ensure a proper fit.

After arguing that way for aeons, there just might be some sign of progress. The Council has decided to look at service changes/budget savings – call it what you wish – in a working party to be convened in a couple of months' time. If it's not a nice piece of procrastination, it just might herald the start of serious service reviews and rating discipline at some indefinite time in the future – but not in time for the new rate year.

Just to be sure no-one has forgotten, we have reminded the Council of our support for the retention of the current 50/50 rating structure for residential properties, and our continuing objection to the use of special levies (and loans) to provide funding for works in the absence of a serious review of services.

General Purpose Financial Reports for the year ended 30 June 2007 – Woollahra Council

Public exhibition of the Council's financial reports each year attracts about as much attention among residents as the sound of the first Spring bushfly. Perhaps it is the mind-numbing realisation that they simply embody the results of decisions made in the past that probably will not be re-considered no matter what ratepayers say about them. Perhaps it is just that they so aggregated that the ordinary ratepayer/resident can make little of the statements as they stand.

Nothing daunted, we again offered some observations on the audited reports. Was it worth the effort? Who knows… we are usually the only public contributor to what should be a real dialogue between the Council and its ratepayers about where the district is going. Usually we get the feeling we are talking to ourselves. Not too many arguments that way!

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