



Submission to the IPART Review of the Revenue
Framework for Local Government
September 2008

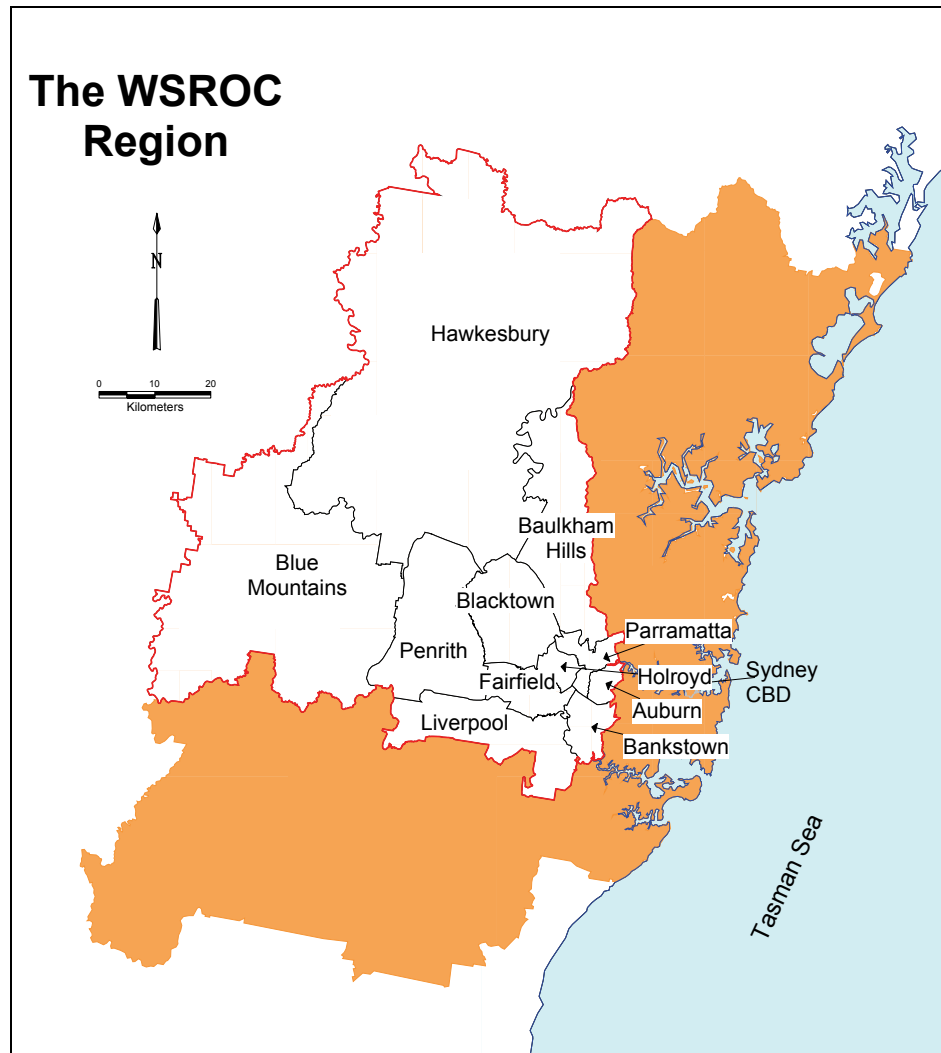
Prepared by the

Western Sydney Regional Organisation of Councils Ltd



Western Sydney Regional Organisation of Councils Ltd

Level 1, WSROC House, 49 Campbell Street
PO Box 63, Blacktown, NSW 2148
Tel (02) 9671 4333 Fax (02) 9621 7741
Email admin@wsroc.com.au www.wsroc.com.au
ABN 16 053 399 983



Auburn
Bankstown
Baulkham Hills
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**SUBMISSION TO THE IPART REVIEW OF THE REVENUE
FRAMEWORK FOR LOCAL GOVERNMENT**

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SUBMISSION TO THE IPART REVIEW OF THE REVENUE FRAMEWORK FOR LOCAL GOVERNMENT

1. INTRODUCTION

This submission has been prepared by the Western Sydney Regional Organisation of Councils Ltd in response to the IPART Review of the revenue framework for Local Government.

WSROC welcomes the opportunity presented by the release of the IPART Issues Paper relating to the above review for public comment. This response draws on WSROC's earlier submissions and research in relation to related policy areas, for example in relation to planning legislation and the recent IPART review of State Government taxation.

In preparing this response WSROC has also consulted with member Councils and reviewed a number of their submissions. It should be noted, however that Councils hold a range of views in relation to some of the questions below and the responses of all WSROC member councils should therefore be read in conjunction with this submission. In addition this submission provides a broad regional response to the nine key questions identified by IPART; more detailed responses to these and the other 43 specific questions outlined in the issues paper are provided in a number of these Council responses

2. RESPONSES TO THE KEY QUESTIONS

2.1 What is the role of local government and how is it determined?

The IPART Issues Paper raises the question of understanding and defining the "appropriate" role of Local Government and uses as a departure point the Allan Report definitions of the "minimalist" and "maximalist" views of this role. The first assumes that the role of Councils is primarily to manage the community's common property and to regulate land use and development; the second that Councils should be concerned with the welfare of the whole community, even if that involves duplication of the roles of State and Federal Governments.

In some respects this is a simplistic and outmoded distinction, especially when the "minimalist" role is expanded by legislative "reforms" and the allocation of responsibilities and costs to councils by other levels of Government, a process over which they have no control.

It is also a mistake to assume that the roles of Councils are determined solely by the 318-page *Local Government Act 1993* (LGA), even if this is the obvious starting point. The LGA includes a Charter for councils which is very broad in scope, stating in part that a council has responsibility to:

"... provide directly or on behalf of other levels of government, after due consultation, adequate, equitable and appropriate services and facilities for the community and to ensure that those services and facilities are managed efficiently and effectively."

Whilst the Act's definition of the functions of Councils is similarly broad (thereby setting the wide parameters for the "maximalist" perspective), it goes on to concentrate mainly on their service and regulatory functions. This can be regarded by default as defining the "minimalist" base of Council activity.

However, the LGA also refers to 20 other Acts which also contribute to defining the functions of councils. In total, around 2,000 pages of legislation regulate Council activity – and this estimate refers just to the LGA itself and the Acts it refers to directly. In the majority of cases, this legislation is not intentionally maximalist, but it does expand the minimalist base by describing – sometimes in great detail – what councils can and cannot do in relation to their regulatory functions and defining how these functions will be done.

For example, the 310 pages of the combined *Environmental Planning and Assessment Act 1979* (EPAA) and the *Environmental Planning and Assessment Amendment Act 2008* have almost as much impact on the role of Councils in NSW as the *Local Government Act*. This is because the amended EPAA largely determines Councils' so-called "minimalist" regulatory functions in respect of the critical areas of land use planning and the control of development. Whilst the EPAA Amendment Act may have removed some of the concurrence requirements in that legislation it has also introduced a range of new requirements for and restrictions on Council operations in these areas.

Compliance with this complex and sometimes conflicting legislative environment imposes a significant cost burden on councils, which is exacerbated by State and to a lesser extent Federal Government cost shifting to Councils. Some of this cost shifting directly relates to the core functions of Councils (for example, arbitrary increases in charges by the Electoral Commission to councils to conduct elections), but other components result from State agencies seeking to expand the roles of councils to suit their policy agendas or for other reasons.

For example IPART itself has previously proposed that the statutory contributions by insurance companies to fund fire services should be replaced by a corresponding increase in the contributions by local councils, with a phased implementation and increases in the rate pegging limit. WSROC has previously expressed concerns that councils will be required to collect these funds while having limited ability to control costs or ensuring the adequacy of the services being provided, as well as the attendant problems that cost shifting always brings. WSROC has called for these costs to be funded centrally by the State Government in the same way as are the NSW Police and Ambulance Services.

In relation to the "maximalist" role of Local Government, it is clear that the Charter referred to earlier does allow Councils very broad scope in determining their activities and in WSROC's view Councils should be free to determine their roles and responsibilities within this framework. Whilst this may have resulted in some cases in inappropriate expansion of Council roles and some duplication of the responsibilities of other levels of Government, this has to be viewed in context.

As pointed out earlier, the expansion of Council roles has been determined to significant extent by State and Federal Governments. Although Councils also respond to community expectations in expanding their services (and sometimes into areas which may be seen as State or Federal responsibilities), there are often very good reasons for doing so.

For example, a Council may come to an evidence-based conclusion that the provision of services or facilities by the responsible level of Government is manifestly inadequate or the delivery model is inappropriate for the particular local area. Other Councils may wish to try an innovative approach to service delivery or to fill a vacuum in which no other Government agency is prepared to take responsibility. A number of Federal and State Government funding programs actively encourage Council participation – even if, unfortunately, these become vehicles for subsequent cost-shifting.

In a fundamental sense the distinction between minimalist and maximalist approaches is being rendered obsolete by other forces. Considerations of sustainability have fundamental impacts on “traditional” Council functions such as land use planning, affecting for example the definition of centres and the locations of shops, services and other facilities. Expanding definitions of corporate responsibility affect Councils much as they do other Government entities and private corporations and in particular Councils will have to respond increasingly to the impact of climate change across all their operations.

In summary, whilst the current IPART inquiry relates specifically to the regulatory framework for Local Government revenues, this cannot be separated easily from the inherent problems caused by the wider legislative framework outlined above.

Recommendation 1: Councils should be free to determine their own roles and responsibilities within the framework of the Charter outlined in the Local Government Act.

Recommendation 2: There should be a comprehensive review conducted jointly by State and Local Government of all legislation and regulations affecting the operations of Councils to remove duplication, conflict and inconsistencies and reduce costs – though not at the expense of Local Government.

Recommendation 3: This review should also aim to prevent future cost-shifting by other levels of Government to Local Government, reduce existing levels of cost-shifting and ensure that where it continues, councils are adequately compensated.

2.2 How effective is rate pegging and what are the implications for councils and ratepayers?

Whilst it may have had some superficial initial impact on rates and managing Council costs, the long-term consequences of rate pegging have been largely negative. Rate pegging has acted as a major constraint on councils in properly managing the provision of infrastructure and services.

The reasons are extensively outlined in a number of submissions prepared by WSROC member Councils, other Councils and other organisations in response to this IPART review and earlier inquiries. In summary, these include:

- Overall, rates revenue in NSW has not kept pace with inflation, rate increases in other States or rising council costs. Furthermore, there is little ability for Councils to offset this shortfall from other sources.
- Rate pegging effectively began by freezing Council rates as they stood at the time of its inception. This might have been excusable if rate pegging had

been introduced to operate for a limited period of, say, three years, but there was no attempt then or since to establish whether these rates were appropriate as a basis for a long-term rates control system, especially one that has remained in place for almost 30 years.

- In particular there was no attempt to review whether the rates then in place were equitable or that they were adequate for council areas with special needs. Whilst special variations in the years since rate pegging was established have softened the resulting distortions to some extent, the underlying inequities still remain.
- As well as the overall shortfall, the “one size fits all” approach combined with the fact that rates are set only on a year-to-year basis means there is little ability for Councils to either use rates proactively to manage anticipated situations, let alone to develop long-term financial plans, unless they are successful in seeking a special variation.
- In particular, there is little capacity for Councils to off-set cost shifting when imposed by other levels of Government by passing on these additional costs through rates. There is also little incentive for Councils to invest in the provision of new infrastructure or the renewal of existing facilities, let alone to meet rising community expectations for services and facilities provision.
- Whilst it may be politically popular, rate pegging removes the fundamental right from local communities to determine – or challenge – their Council’s longer-term rate levels through the ballot box and the responsibility of Councils to answer to their communities for their decisions regarding rates.
- The overall financial result for local government is a massive backlog in local infrastructure investment, which as been estimated conservatively to be around \$6 billion. This threatens the longer-term sustainability of a number of Councils; ultimately, this infrastructure will have to be paid for, either through rates or taxes.
- Councils with communities in rural areas with declining populations, those in urban areas which face major replacement of ageing infrastructure and/or which are undergoing redevelopment as well as those undergoing massive growth are all particularly vulnerable – and several councils in Western Sydney has Councils have elements of all three.
- This problem is exacerbated by the recent changes to Section 94 contributions. In some cases these will directly result in funding shortfalls which will have to be funded through special rate variations – if these are granted.

Recommendation 4: The problems identified with rate-pegging mean that it should be reviewed and discontinued, at least in its current form.

2.3 What are the objectives for a regulatory framework for local government revenues?

The primary objectives for any regulatory framework for council revenues to replace rate pegging should be that it:

- Provides as transparent as possible a process for setting rates and charges;

- Is accountable directly to the affected community, through these rates and charges being set by the level of Government which is levying them and which is answerable to this community through the democratic process;
- Provides a framework for Councils to set rates that meets these two criteria as well as addressing the other principles identified by IPART and others, such as being equitable, efficient and simple;
- Establishes a rate setting system that encourages a sustainable approach to setting rates and charges that will encourage Councils to plan for the long-term provision, renewal and maintenance of infrastructure as well as the equitable delivery of services;
- Creates a climate of community acceptance and understanding of the importance of funding infrastructure and essential services through rates and charges; and
- Where cost shifting cannot be avoided or otherwise compensated, clearly identifies the proportion of rates which will go to the payment for such cost-shifted services.

The current system of rate pegging manifestly fails on all these counts. In effect, the current system is not a regulatory framework, as the State Government has a complete monopoly on the setting of rates. Reforming this system does not mean returning all rates setting to Councils without restriction, rather it involves the creation of a regulatory framework which addresses these basic principles.

2.4 How does the current regulatory framework for council revenue, or any alternative framework support [IPART's objectives]?

- **Promote the effective and efficient provision of services?**
- **Enhance the financial sustainability of local government?**
- **Meet the standard of principles for good regulation and taxation – efficiency, equity, simplicity, transparency?**
- **Enhance the accountability of local government?**

IPART has identified five options for alternative regulatory frameworks, each of which attempts to address the above principles to varying degrees. Whilst the preferred option of WSROC and most member Councils is still that rate-pegging should be abolished entirely, a modified version of IPART's option four is proposed as the most appropriate alternative regulatory framework if some form of rate pegging has to be retained.

Under this proposal, those councils not being exempted from rates pegging would be protected by the use of elements of IPART's options one and two to determine the relevant rates caps. The draft proposal is outlined in the recommendations below:

Several WSROC Councils have raised wider issues regarding the revenue base of Councils. The IPART issues paper notes that only 8.6 per cent of NSW Local Government revenue is from grants and subsidies, mostly from the Federal Government.

There are issues with both the allocation and the total quantum of these funds. Specific purpose grants are allocated for specified projects, for example the road blackspots program. Whilst Councils appreciate these grants, they sometimes

become a “Trojan horse”, where Governments gradually withdraw resources but community expectations oblige Councils to continue the previously-funded service. An example of this is the gradual decline in the provision of State Government library funding in NSW.

General purpose grants are also not without problems. The allocation of these grants between Councils is on the basis of fiscal equalisation methodology which appears to be increasingly complex and sometimes even arbitrary in its outcomes. Perhaps even more significant is the low total amount of these grants, especially in light of the payments which State Governments receive from the Federal Government for productivity reforms and the from the GST.

Unlike some other states, where at least a proportion of the productivity payments are passed on to Local Government, Councils in NSW receive nothing from either source, even though some of the productivity reforms have involved Councils. As several WSROC Councils point out, a revenue sharing arrangement between the three tiers of Government which resulted in a guaranteed income stream for Councils would greatly reduce pressure on the rates system to fund Council services and infrastructure.

Recommendation 5: In principle, the regulatory framework should provide as transparent as possible a process for setting rates and charges and be accountable to the community through the democratic process as well as addressing the other objectives outlined in this submission.

Recommendation 6: A modified version of the option 4 for a new regulatory framework proposed in the IPART issues paper is supported in principle, as follows:

- 1. Exempt individual councils from rate pegging, subject to a mandatory demonstration of:***
 - Financial accountability and governance;***
 - Financial sustainability;***
 - Comparative efficiency and effectiveness indicators (including affordability and availability of local services and facilities);***
 - Ability to achieve the above objective criteria over a 10 year time frame through an approved and independently audited management plan. This audited plan could be tabled in Parliament and made publicly available.***
- 2. In the case of councils which are not exempted, the rates cap determination process should involve the following, based on option 2 in the IPART issues paper:***
 - A more disaggregated form of rate pegging which incorporates cost indices relevant to different council groups based on specific criteria and calculation of a rate peg specific to each grouping;***
 - Publication of the economic indicators or indices to be used in determining these rates caps (i.e., a Local Government Price Index); and***
 - Provision for non-exempted councils to apply for special variations under a modified special variations process which ensures that the process of application and approval is fully transparent.***

Recommendation 7: There should be a review of all Federal and State Government special and general purpose grants with the following aims:

- ***significantly increasing the level of funding to councils, preferably through a guaranteed and consistent share of total taxation revenue;***
- ***making the grants allocation system more transparent and equitable; and***
- ***developing safeguards that prevent special purpose grants being used as a basis for de-facto cost-shifting.***

2.5 What role should IPART play in setting local government rates and charges, including charges for non-business activities? (and)

2.6 Should IPART have a determinative role provided by legislation or should IPART's role be limited to making recommendations?

Rates: Whilst there is broad agreement that IPART through this review and the implementation of its objectives should recommend and oversee the establishment of a new regulatory framework incorporating the principles outlined above, there is a more diverse range of views regarding the nature and extent of IPART's direct involvement in the rates-setting process.

Ideally, the majority of Councils would qualify for exemption under part 1 of the recommendation regarding the rate-setting process outlined above and the rate-pegging mechanism outlined in part 2 would be required for only a small number of Councils and therefore IPART would not be involved. If this is the case then it would seem appropriate for IPART to have a role in setting the rate.

Charges: The strong view of all WSROC Councils is that all charges should be set independently by Councils and that IPART should *not* be involved in this process. IPART's role should be limited to ensure that the system for councils to set such charges is as transparent as possible. This might for example require Councils to establish a consistent policy involving the annual exhibition of its schedule of charges.

Recommendation 8: as an outcome of this review, IPART should design in further consultation with Government, Councils and the community a new regulatory framework as outlined in recommendation 5 and oversee its implementation.

Recommendation 9: IPART should not be involved in setting Council charges but should ensure that any system for setting charges it recommends as an outcome of this review is as transparent as possible.

2.7 To what extent do government authorities – such as SHFA, SOPA, RWA and the GCCs – provide services that duplicate or overlap with those of local government?

WSROC is very concerned at the expanding role of some of these authorities and their current and potential duplication of the functions of Councils.

It appears that decisions to establish these bodies have been made on several occasions in the absence of any direct consultation with or input from the councils affected and without an appreciation of the capacity of these councils to manage the area concerned or to undertake the functions required. It should always be remembered that the extent to which these bodies are delegated the existing function of a council is the extent to which the area under management is removed from the

democratic control of the council concerned. Any such delegation is also likely to have serious financial impacts on the council(s) concerned.

As a matter of principle, the case for the creation of specific authorities to manage particular precincts and to remove certain functions from the affected councils needs to be strongly argued and this process used only as a last resort. When such authorities are established, any functions to be delegated should be strictly defined both in scope and duration, and should not be used as a pretext for the further expansion of the body concerned. The affected councils should also be given strong representation on the authority, which should be required to consult regularly with these councils.

Recommendation 10: The establishment of any statutory authority to manage land and/or take over any other function of Local Government should be undertaken only as a last resort and only after direct consultation with the councils and communities concerned and detailed examination of the financial and other impacts on the affected councils.

2.8 What are the implications for local government rates where these authorities provide services normally provided by local government?

As the IPART issues paper notes, in practice the level of Council-like services provided by these authorities varies considerably, with only the Sydney Harbour Foreshore Authority (SHFA) and the Sydney Olympic Park Authority (SOPA) providing “municipal” services.

However, it should be noted that even these bodies provide only a small, defined subset of the range of services provided by Councils. Indeed, many Councils have had to take on additional responsibilities or fund the provision of additional infrastructure directly or indirectly as a result of the creation and operation of these agencies.

A particular example is provided by SOPA, which manages a significant area within Auburn Council area. Council’s submission outlines the rates revenue foregone and the additional expenditure incurred by Auburn Council as a direct result of the creation of SOPA, for which Council has received little or no compensation. The submission also notes that SOPA provides only a limited range of what could be defined as council services; others are in fact provided by Auburn Council under contract.

Council’s submission details the serious financial consequences for Auburn of the current situation. Council is also deeply concerned at the potential implications in the issues paper on page 67 (in respect of SHFA) and page 70 (in respect of SOPA) that Council’s rates function could be handed over to these authorities.

There are also a number of concerns regarding the role of the Growth Centres Commission (GCC) which affect a number of other WSROC Councils. Whilst these do not have the same municipal functions as the SHFA and SOPA, they still impact on Council operations, particularly through the management of the strategic planning process and the management of the timing of land releases.

Further powers have also been added to the GCC (for example, the GCC will now hold section 94 funds in relation to development in the Growth Centres), whilst the original Commission which had some degree of autonomy has been replaced by a management framework which brings the GCC effectively under Ministerial control.

There are also concerns that the recent cuts to developer charges in Growth Centres and uncertainty regarding the timing of the roll-out of major infrastructure projects will result in the under-provision of infrastructure in these areas with resulting long-term implications for councils.

Recommendation 11: Any council function to be delegated to a statutory authority should be strictly defined both in scope and duration, and should not be used as a pretext for the further expansion of the body concerned. The affected councils should also be given strong representation on the authority, which should be required to consult regularly with these councils.

2.9 Should a common regulatory framework be introduced for these authorities?

As outlined above, there are therefore a number of issues of concern around the IPART proposals for a common legislative framework for these bodies and to remove duplication between their functions and those of councils.

Whilst the establishment of such mechanisms appears to be a logical step, it is supported only if the resulting framework effectively minimises the extent to which these bodies remove these functions from democratic council control. In particular WSROC strongly supports the view of Auburn and other councils that rates collection should remain at all times under Local Government control.

Recommendation 12: The creation of a common legislative or regulatory framework to govern the role of statutory authorities is supported in principle, if and only if it embodies the following principles:

- ***Those outlined in the previous recommendations regarding the establishment of such authorities, the degree of council involvement in their operation and their relationship to affected councils;***
- ***The collection and management of rates income remains under the control of the relevant council(s) at all times;***
- ***Full compensation should be provided to affected councils for any losses directly or indirectly incurred by each affected council resulting from the establishment of the authority and/or the delegation to it of any “municipal” role which would otherwise be undertaken by that council;***
- ***The authority should be required to contract the affected council(s) for the provision of these services at a reasonable cost; and***
- ***Compensation and/or the ability to levy additional rates is guaranteed to affected councils for any infrastructure shortfall or additional maintenance costs resulting from the decisions of the statutory authority.***

3. RESPONSE TO OTHER ISSUES

3.1 Rates Exemption

WSROC supports the argument of a number of member Councils that Federal and State Government properties should no longer be exempt from rates. These properties receive a range of Council services and should therefore not be exempt.

Recommendation 13: Federal and State Government properties should no longer be exempt from council rates.

3.2 Fire Brigade Levy

WSROC has previously expressed concerns at IPART's proposals in its issues paper on state taxation to transfer insurance industry funding and levy collection for the State Fire Brigade services to local councils.

Primarily, WSROC was concerned that councils will be required to collect funding on behalf of the NSW Government while having limited ability to control costs or ensuring the adequacy of the services being provided. In addition, councils were concerned that they would not receive an adequate increase in the annual rate pegging limit, initially or in future years.

Recommendation 14: The existing statutory contributions by insurance companies to fund fire services should be maintained, or alternatively the State Government should fully fund the fire services through consolidated revenue.

3.3 Removal of Payroll Tax Exemption for Local Government

WSROC has also expressed concerns at IPART proposals to remove payroll tax exemption, noting that Councils provide a large number of services and programs for local communities, many of which are not currently or likely to be provided by the private sector. The proposal to offset the removal of the payroll levy by phasing in an increase in the rate pegging limit also raised the same concerns as those outlined above in relation to the proposal to fund fire brigade services through a similar arrangement. The combined effect of these two proposals on the rate-pegging limit would also be very high.

Recommendation 15: Attempts to remove the payroll tax exemption for Local Government (as outlined in IPART's issues paper on State Government taxation) should be formally abandoned.

