



LOCAL GOVERNMENT RATES CAPPING & VARIATION FRAMEWORK REVIEW

Draft Report Volume II — Supporting Material and
Analysis

July 2015

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ABOUT THIS REPORT

In January 2015, the Essential Services Commission (the Commission) received terms of reference (see Appendix A) from the Minister for Finance (in consultation with the Minister for Local Government) to conduct a review and report on a local government rates capping and variation framework. In conducting the review we have had regard to the matters set out in the terms of reference.

We have been asked to design a framework that meets the Government's commitment to cap annual council rate increases as well as to develop a workable process to assess any proposals by councils for above cap increases ('variation process').

This volume of the draft report — Volume II (Supporting Material and Analysis) — outlines the analysis we have undertaken in reaching our proposed framework.

A Blueprint for Change (Volume I) — sets out the key design features of the framework we are proposing. All volumes can be found on our website.

1 LOCAL GOVERNMENT IN VICTORIA

In designing the rates capping and variation framework we accounted for the significance, complexity and diversity of the local government sector.

This chapter outlines:

- our understanding of the sector and the pressures that it faces
- supporting analysis of the matters important to the framework
- our response to the terms of reference relating to:
 - evidence on the magnitude and impact on ratepayers, of Victorian councils' successive rate increases above consumer price index (CPI) increases
 - the differences between rural, regional and metropolitan councils in terms of costs, revenue sources and assets maintained.

1.1 VICTORIA'S LOCAL GOVERNMENT SECTOR AT A GLANCE

Victoria's 79 councils manage around \$78 billion of community infrastructure and assets, generate revenue of \$7.8 billion, incur expenses of \$7.2 billion and employ around 42 500 people.¹

Councils vary in the populations that they serve, from 3 000 (Borough of Queenscliff) to 280 000 (Casey City Council). And their land areas range from 20 (Yarra City Council) to 22 000 square kilometres (Mildura City Council). Each council has elected local representatives that govern its decision-making.

¹ Asset, revenue and expenditure figures are based on council annual reports for 2013-14. Employment figures are for 2012-13 (sourced from Municipal Association of Victoria 2014, *Modest rate rise despite funding cuts*, media release, July).

Councils provide more than 100 services in areas such as social and community services, health, transport and infrastructure, planning and building, environment and emergency services. Service delivery varies across the state reflecting the different composition, expectations and priorities of communities. The types, levels, and quality of service that councils provide also vary depending on the geography and topography of their region, the demographic and economic profile of their communities, their financial circumstances, and the assets and infrastructure at their disposal.

In 2013-14, Victorian councils held \$1.5 billion in borrowings.² In 2013-14, they held borrowings equivalent to 1.5 per cent of their non-financial assets, compared with an average of 3.5 per cent for councils in the other states and territories.³ Councils do not face any legislative restrictions on their ability to borrow.⁴

1.2 LOCAL GOVERNMENT FINANCES

This section provides information on revenues, expenditures and debt management in the local government sector and trends over recent years. Councils have been categorised into groupings (metropolitan, interface, regional centre and small and large rural councils), to help comparisons across the sector.⁵

1.2.1 LOCAL GOVERNMENT REVENUES

Victorian councils' major revenue streams include rates and charges, Commonwealth and State Government grant funding, user fees (such as recreation and leisure centre entry fees), statutory fees and fines (such as statutory planning fees) and developer contributions.

In general, metropolitan and interface councils rely more heavily on rates and charges revenue, whereas regional and rural councils rely more heavily on grant funding, given their lower rates bases and limited alternative revenue sources (table 1.1).

² Based on Local Government Victoria's (LGV) analysis.

³ Based on Local Government Victoria's (LGV) analysis.

⁴ However, their borrowings are subject to a risk assessment as part of the council's annual performance audit by Victorian Auditor-General's Office.

⁵ See Appendix B for definitions of council groupings.

TABLE 1.1 COMPOSITION OF REVENUE BY COUNCIL GROUPING
(2010-11 TO 2013-14)
Per cent

Council groupings	Total rates and charges	Total statutory fees and fines and user fees	Total grants	Other recurrent revenue
All councils	59	16	22	3
Metropolitan	64	18	14	4
Interface	64	13	20	3
Regional centres	54	19	26	2
Large rural	51	12	34	3
Small rural	39	6	51	4

Note: Based on Victoria Grants Commission (VGC) data and council annual reports. If necessary, we adjusted VGC data to be consistent with the audited annual report. Data excludes contributions and non-recurrent revenue (categorised as non-cash revenues in the VGC data).

Metropolitan and interface councils have larger rate bases because they typically have more ratepayers and higher land values than rural councils have. Metropolitan and interface councils also tend to raise more in user fees and statutory fines, possibly because they typically provide a wider range of services.

Table 1.2 shows growth in average annual revenue for each council grouping between 2010-11 and 2013-14. Total rates and charges for all councils increased by an average 7 per cent per year, while revenue from statutory fees and fines and user fees grew by an average 5 per cent per year.

TABLE 1.2 AVERAGE ANNUAL REVENUE GROWTH BY COUNCIL GROUPING
(2010-11 TO 2013-14)
Per cent

Council groupings	Total rates and charges	Total statutory fees and fines and user fees	Total grants	Other recurrent revenue
All councils	7	5	-3	-4
Metropolitan	7	5	-3	-6
Interface	9	5	-2	0
Regional centres	6	4	-4	0
Large rural	8	4	-1	-3
Small rural	6	-3	-6	1

Note: Based on VGC data and council annual reports. If necessary, we adjusted VGC data to be consistent with the audited annual report. Data excludes contributions and non-recurrent revenue (categorised as non-cash revenues in the VGC data).

1.2.2 LOCAL GOVERNMENT EXPENDITURE

The main areas of local government expenditure include employee wages and entitlements, materials and services (council plant, equipment and contracts with external service providers) and capital works (road and building construction).⁶

Councils and peak body groups told us that different council grouping may have fundamental differences in their expenditure patterns — for example, metropolitan councils have a higher proportion of employee expenditure, and interface councils have a higher proportion of capital works expenditure.

Table 1.3 shows the composition of expenditure by council grouping between 2010-11 and 2013-14. On average, employee costs accounted for 37 per cent of total Victorian councils' operating and capital expenditure over the period. Metropolitan councils had the highest share of expenditure on employee costs (41 per cent), while small rural councils had the lowest share (33 per cent).

⁶ The Commission did not consider depreciation in its expenditure analysis because it is a non-cash expense.

**TABLE 1.3 COMPOSITION OF EXPENDITURE BY COUNCIL GROUPING
(2010-11 TO 2013-14)**

Per cent

Council grouping	Employee costs	Materials, services and contract payments	Other operating expenses ^a	Net capital expenditure
All councils	37	33	6	25
Metropolitan	41	29	9	21
Interface	35	38	6	21
Regional centres	37	34	3	25
Large rural	36	33	7	25
Small rural	33	34	4	29

Note: Based on VGC data and council annual reports. If necessary, we adjusted VGC data to be consistent with the audited annual report. Data excludes contributions and non-recurrent revenue (categorised as non-cash revenues in the VGC data). Data on capital expenditure is indicative only. It is based on VGC data and was not reconciled to audited figures. In the VGC data, contract payments over the period were inconsistently reported for materials and services and other operating expense categories.

^a Excludes depreciation.

For interface councils, expenditure on material and services represented 38 per cent of total expenditure. This share was higher than for any other council grouping and for all councils (33 per cent).

Small rural councils spent the largest share of their operating and capital expenditure on capital works (29 per cent compared with 25 per cent for all councils). This finding may reflect the additional challenges faced by rural councils in servicing large road networks and dispersed communities, as well as the capital expenditure required to address the impacts of natural disasters.

Expenditure by all councils grew by an average 5 per cent per year between 2010-11 and 2013-14 (table 1.4).

TABLE 1.4 AVERAGE ANNUAL EXPENDITURE GROWTH BY COUNCIL GROUPING (2010-11 TO 2013-14)
Per cent

Council grouping	Employee costs	Materials services and contract payments ^a	Other operating expenses ^a	Total operating expenses	Net capital expenditure	Total expenditure
All councils	7	4	2	5	8	5
Metropolitan	6	4	-1	4	9	5
Interface	9	4	7	6	5	6
Regional centres	7	6	7	6	7	6
Large rural	7	4	11	5	5	5
Small rural	4	-4	9	0	17	5

Note: Data excludes contributions and non-recurrent revenue (categorised as non-cash revenues in the VGC data). Data on capital expenditure is indicative only. It is based on VGC data and was not reconciled to audited figures. In the VGC data, contract payments over the period were inconsistently reported for materials and services, and other operating expense categories. ^a Excludes depreciation.

Expenditure on employee wages and entitlements grew by an average 9 per cent per year for interface councils, compared with 4 per cent for small rural councils. Net capital expenditure grew by an average 17 per cent per year for small rural councils compared with the state average of 8 per cent. The Victorian Auditor-General's Office (VAGO) noted the higher capital expenditure by small rural councils in recent years was due to their spending to manage the impact of natural disasters.⁷

1.2.3 DEBT MANAGEMENT

Victorian councils held approximately \$1.5 billion in debt in 2013-14.⁸ No legislative limitations inhibit councils' ability to borrow. The Local Government Funding Vehicle, established by Municipal Association of Victoria (MAV), generally provides councils with the ability to borrow funds at lower interest rates than those available if councils individually sought debt financing. In particular, rural councils may not be able to secure the same favourable financing rates offered to large metropolitan councils.

⁷ VAGO 2013, *Local government: results of the 2012-13 audits*, December.

⁸ Based on Local Government Victoria's (LGV) analysis.

The debt ratio (calculated by dividing total liabilities by total assets) measures the proportion of a council's assets that are financed by debt, expressed as a percentage. In general, a higher percentage reflects greater financial risk. Debt ratios across council grouping have been similar at around 3-5 per cent (table 1.5).

TABLE 1.5 DEBT RATIO BY COUNCIL GROUPING
Per cent

Council grouping	2009-10	2010-11	2011-12	2012-13	2013-14	Average
All councils	2.5	2.6	3.4	3.3	3.3	3.0
Metropolitan	4.4	4.5	5.6	4.7	5.2	4.9
Interface	4.6	4.4	4.7	4.0	4.0	4.4
Regional centres	4.3	4.4	5.3	4.6	4.6	4.7
Large rural	3.9	4.1	4.8	3.7	3.9	4.1
Small rural	3.3	3.5	4.2	3.8	3.9	3.7

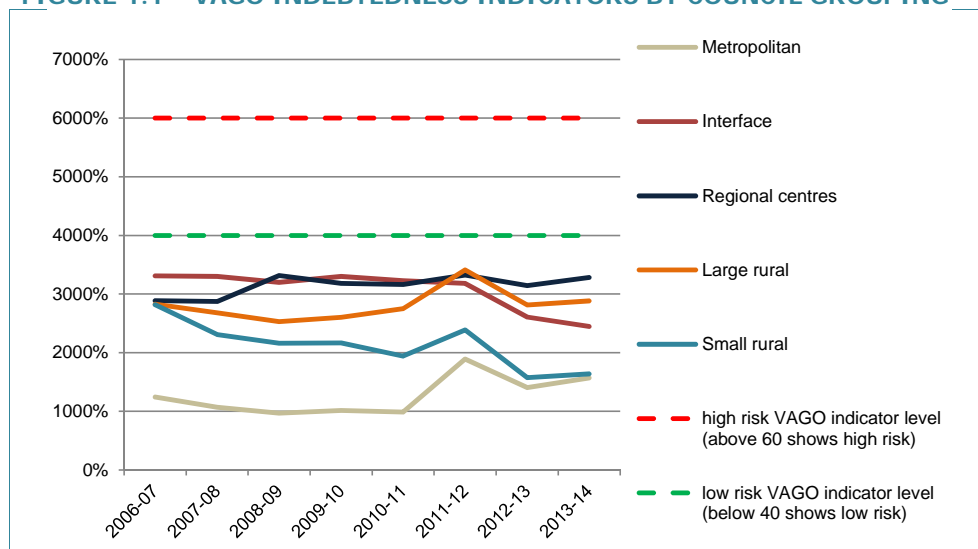
Data source: Annual report.

VAGO also uses an indebtedness indicator to assess a council's level of risk in its ability to repay its long-term debts from its own-source revenue. The indicator compares non-current liabilities (mainly borrowings) to own-source revenue. The higher the percentage, the less able is a council to cover its non-current liabilities from revenue that it generates itself. VAGO considers indebtedness above 60 per cent to be high risk and below 40 per cent to be low risk.

Overall, indebtedness for all councils was below 40 per cent between 2006-07 and 2012-13 (figure 1.1), which indicates no concerns about the ability of councils to repay debt from own-source revenue.⁹ Metropolitan councils had the lowest level of indebtedness.

⁹ Average indebtedness for the sector, which peaked in 2011-12, was affected by the payment options afforded to councils for the defined benefit superannuation funding call. See VAGO 2015, *Local government: results of the 2013-14 audits*, February.

FIGURE 1.1 VAGO INDEBTEDNESS INDICATORS BY COUNCIL GROUPING



Data source: VAGO results of audits reports 2009-10 to 2013-14.

1.3 KEY INFLUENCES ON LOCAL GOVERNMENT COSTS AND REVENUES

This section outlines some of the key factors that influence councils' revenue and costs.

1.3.1 COMMONWEALTH AND STATE GOVERNMENT FUNDING

Each year, councils receive untied Financial Assistance Grants from the Commonwealth Government.¹⁰ In its 2014-15 Budget, the Commonwealth Government announced that indexation of these grants would be paused or 'frozen' for three years from 2014-15 to 2016-17. Figure 1.2 illustrates the impact of this pause, which the VGC estimated will reduce funding by \$64 million (from the 2013-14 base) for councils by the time indexation resumes in 2017-18.¹¹

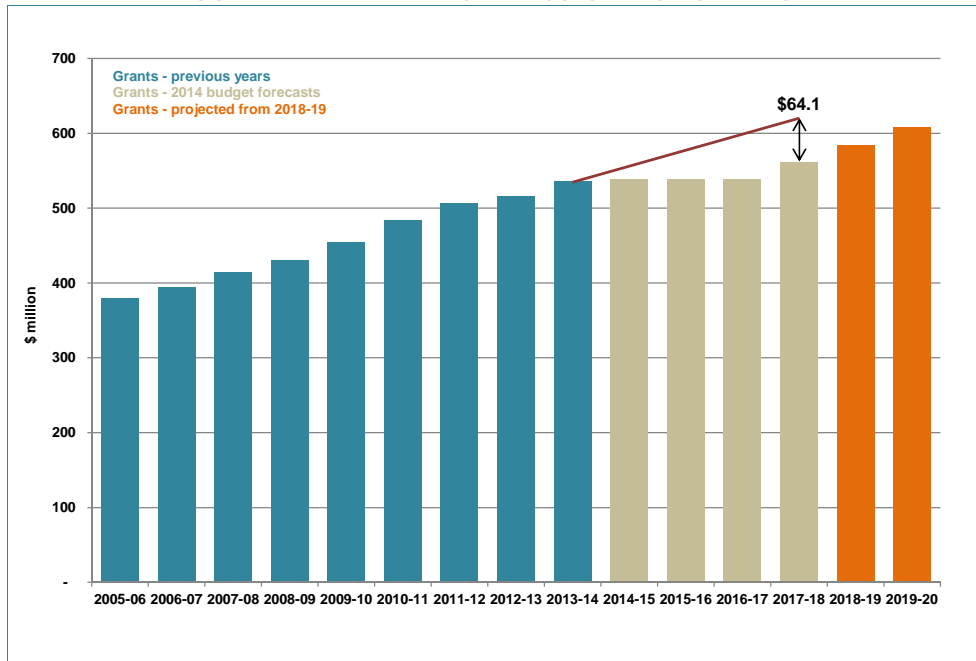
All councils will be affected by the grant freeze but rural councils will be most affected because they have smaller rate bases and rely more heavily on grants. Whittlesea City Council (an interface council), for example, noted in its submission that the freeze will reduce its grant funding by \$1.8 million. Moreland City Council (a metropolitan council), expected its funding to fall by \$1.32 million over the three years.

Councils also have access to other grant funding from the Commonwealth and State Governments (see examples in box 1.1) that is not affected by the grant freeze discussed above.

¹⁰ The VGC allocates these grants across councils.

¹¹ The VGC assumed that grant funding would have continued to increase at 4 per cent per year, similar to the trend over recent years.

FIGURE 1.2 IMPACT OF PAUSED INDEXATION OF COMMONWEALTH GOVERNMENT FINANCIAL ASSISTANCE GRANTS



Data source: VGC analysis, April 2015.

BOX 1.1 EXAMPLES OF COMMONWEALTH AND STATE GOVERNMENTS FUNDING AVAILABLE TO VICTORIAN COUNCILS

Commonwealth funding

- **Regional Development Australia Fund** (\$107.6 million allocated to Victoria) — funding announced in 2011 (and running until 2016-17 to support the infrastructure needs and economic growth of Australia's regional areas. The program funds capital infrastructure projects identified as priorities by local communities.
- **Bridges Renewal Program** (\$300 million committed) — funding for both state and local governments to improve the quality of Australia's bridges. Projects are selected from competitive, merit-based process, and funded for up to 50 per cent of project costs. For Victoria, \$6.4 million was provided under round one.
- **Roads to Recovery** (\$3.2 billion committed from 2014-15 to 2018-19) — funding to support the maintenance of local roads throughout Australia. Victorian councils will receive \$356 million in total over the period.

State funding

- **Interface Growth Fund** (established in 2015-16 with \$50 million initially available) — funding to support local infrastructure needs of communities in Melbourne's outer suburbs or interface councils. It supports infrastructure development, job creation and economic development, and aims to reduce socio-economic disadvantage and improve the environmental resilience of interface councils' communities.
- **Regional Jobs and Infrastructure Fund** (established in 2015-16 with \$500 million committed) — funding to support major projects, create jobs, support population growth and build stronger regional communities.

Source: Department of Infrastructure and Regional Development, Funding programs, www.investment.infrastructure.gov.au/funding, accessed 13 July 2015. Department of Environment, Land, Water and Planning, <http://delwp.vic.gov.au/local-government/council-funding/interface-growth-fund>, accessed 13 July 2015. Regional Development Victoria, <http://www.rdv.vic.gov.au/regional-jobs-and-infrastructure-fund>, accessed 13 July 2015.

1.3.2 COST SHIFTING

The local government sector uses the term ‘cost shifting’ to describe situations where the Commonwealth and State Governments expect or require local governments to deliver services, but do not fully fund service delivery. The sector also considers cost shifting occurs when the State Government sets fees to be charged by local government, but holds the fees below the cost of service delivery (for example, the sector cited planning fees).

Many submissions to our consultation paper argued a rate capping framework should consider this issue because rate revenue is often used to cover shortfalls that result from cost shifting. They identified the following situations as cost shifting:

- when the Commonwealth or state governments confers responsibility for providing a service, asset or regulatory functions on local government without providing corresponding funding
- when another level of government passes on its responsibility for funding a service or function (including concessions and rebates) to local government
- when local government agrees to provide a service or function on behalf of another level of government but funding is subsequently reduced or stopped, and community demand means the council cannot stop the service provision or function.

While we could not directly quantify the extent and impact of cost shifting onto local government, many council submissions included examples of cost shifting in health and aged care, libraries, school crossings, maternal and child care, statutory planning, road-side weed management, immunisation and preschools.

Moreland City Council estimated the impact of cost shifting in maternal and child health was \$193 000 between 2011-12 and 2014-15. Similarly, Whittlesea City Council estimated an impact of \$790 000 between 2010-11 and 2014-15. Over the same period, these councils estimated cost shifting in home and community care cost them \$1.42 million and \$1.7 million, respectively.

Dandenong City Council reported the State Government funded 27 per cent of the costs of school crossings in 2006 and 22 per cent in 2014 (table 1.6), leaving the council to fund the remaining share of the total cost.

TABLE 1.6 DANDENONG CITY COUNCIL COST SHIFTING EXAMPLES
State Government's contribution to the funding required for council services (per cent)

Service	2006	2007	2008	2009	2010	2011	2012	2013	2014	2014-15 (forecast)
School crossings	27	25	22	22	21	24	23	22	22	22
Library services	23	22	21	22	23	21	20	19	19	17
Maternal and child health	52	52	41	37	51	38	36	37	40	36
Statutory planning	54	59	57	47	49	49	43	44	49	43

Source: Dandenong City Council submission to consultation paper, May 2015.

1.3.3 POPULATION GROWTH

Population growth affects councils' ability to manage infrastructure, deliver services and raise revenue. Around 50 per cent of Victoria's population resides in metropolitan municipalities and around 3 per cent reside in small rural municipalities (table 1.7).

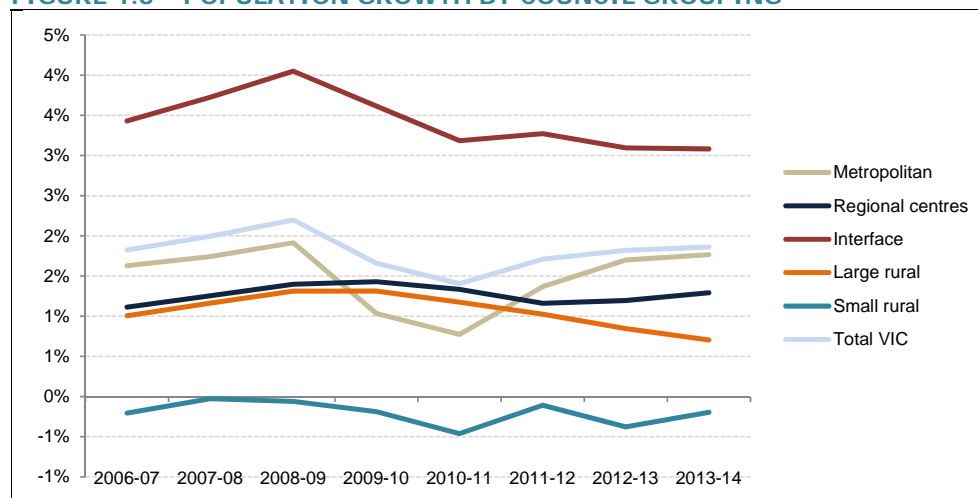
TABLE 1.7 POPULATION BY COUNCIL GROUPING, 2013-14

Council grouping	Population	Per cent
Metropolitan	2 933 748	50
Regional centre	693 770	12
Interface	1 440 423	25
Large rural	593 999	10
Small rural	178 970	3
Total	5 840 910	100

Data Source: Australian Bureau of Statistics, 2015, *Regional population growth*, Australia, 3218.0, March.

From 2006-07 to 2013-14, Victoria's population grew by close to 2 per cent per year (figure 1.3). Population increased in all council grouping except small rural councils, which experienced an average yearly decrease of 0.2 per cent. Interface councils experienced the highest increase in population growth, at around 3- 4 per cent per year. Peri-urban councils, which are predominantly large rural councils on the periphery of Melbourne, were a large contributor to population growth for large rural councils.

FIGURE 1.3 POPULATION GROWTH BY COUNCIL GROUPING



Data source: Australian Bureau of Statistics 2015, Regional population Growth, Australia, 3218.0, March.

1.3.4 INFRASTRUCTURE NEEDS

Victorian councils manage around \$78 billion worth of assets to provide council services. A significant part of their annual expenditure relates to the maintenance, renewal or replacement of infrastructure assets.

The rates capping and variation framework needs to recognise councils' responsibility to maintain and invest in their infrastructure. It also needs to recognise that some councils have spent less than is needed to maintain the service capacity of their infrastructure assets. For this reason, 'robust' indicators are needed to measure councils infrastructure needs. This section summarises how the sector attempts to quantify infrastructure needs.

In 2014, VAGO conducted an audit¹² of council asset management and maintenance. It identified a number of concerns, including:

- deficiencies in renewal planning and practice
- inadequate asset management plans
- poor links between assets and services level
- inadequate asset management information systems and council monitoring, evaluation and reporting of asset management.¹³

Although VAGO found asset management practices were improving, it noted renewal gaps had almost doubled since 1998 and further improvement is needed.¹⁴ The renewal gap seeks to measure the difference between what a council spends on renewing its assets and what it should spend.

The sector mainly uses two measures¹⁵ to assess asset management:

- VAGO's renewal gap
- MAV's STEP program.

These indicators have shown a general improvement in asset renewal in the sector over recent years. However, they may not fully indicate a council's asset renewal performance.

VAGO'S ASSESSMENT OF THE RENEWAL GAP

VAGO defines the renewal gap as the ratio of council expenditure on renewing, restoring and replacing existing assets to asset depreciation (measured on a straight line basis).¹⁶ When a council's spend on renewing assets is higher than the assets' depreciation, a council is sufficiently renewing its assets.¹⁷

¹² The audit focused on five councils (two metropolitan, and one each for interface, regional centre and small rural).

¹³ VAGO 2014, *Asset Management and Maintenance by Councils*, p.iii.

¹⁴ VAGO 2014, *Asset Management and Maintenance by Councils*, p.ix.

¹⁵ Until 2015, LGV also reported a renewal gap indicator. Going forward it will report a new indicator as part of the LGPRF using a renewal gap calculation similar to VAGO's.

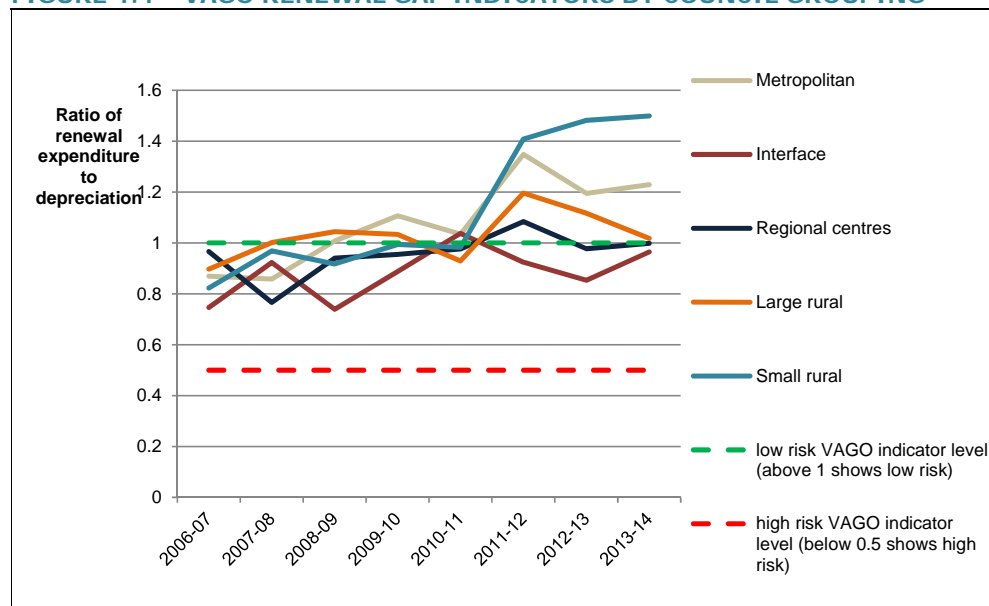
¹⁶ Depreciation is used as a proxy for the rate at which an asset is consumed.

¹⁷ VAGO calculates its renewal gap on renewal expenditure and upgrade expenditure. Asset renewal expenditure refers to expenditure that returns the service potential or life of the asset up to which it had originally, for example, road re-surfacing. Asset upgrade expenditure refers to expenditure which increases the service level or life of an asset above that which it originally had, for example, sealing an existing gravel road.

A large renewal gap (when the ratio is below 0.5) suggests a council's assets will become more costly to maintain (given increased deterioration) and will compromise the delivery of council services that rely on that infrastructure. A renewal gap ratio above 1 suggests a low risk of running down assets.

Between 2008-09 and 2013-14, VAGO's renewal gap indicator remained steady or improved slightly for most council groups (see figure 1.4).¹⁸ In the last 3 years small rural councils have shown a significant improvement in the renewal gap ratio (to 1.5 as shown in figure 1.4), indicating that their renewal expenditure was around 50 per cent more than depreciation.¹⁹ Interface councils have the lowest average renewal gap indicators, likely reflecting the pressures of the high level of capital expenditure necessary to service growing infrastructure demands in their council areas.

FIGURE 1.4 VAGO RENEWAL GAP INDICATORS BY COUNCIL GROUPING



Data source: VAGO results of audit reports

¹⁸ VAGO's capital replacement indicator is a long-term indicator of council asset management and renewals. It has displayed similar trends to the renewal gap indicator, showing a general improvement in councils' renewal management since 2006-07. It is calculated by dividing total capital expenditure by depreciation.

¹⁹ This calculation includes the capital expenditure over the period to restore assets following on from the impact of natural disasters.

VAGO's renewal gap indicator needs to be interpreted carefully, because it may not reflect the true cost of renewing assets. The use of straight-line depreciation may limit the usefulness of the indicator because it does not measure accurately the age or condition of assets or reflect council asset management strategies.

MAV STEP PROGRAM

A number of councils used the MAV's STEP program to improve their asset management and to address renewal gaps.

STEP uses a renewal gap calculation based on an assessment of the asset's condition, in contrast to the accounting approach based on straight-line asset depreciation. While it is a potentially more robust measure of asset management, it requires time and effort to prepare, report and monitor. Not all councils use the STEP program and some who use it, may apply it differently.

While councils using STEP generally improved their asset management and planning, progress has been slow. By December 2013, only 23 of the 79 councils had reached a satisfactory level of asset management and renewal, as measured by the STEP program. Regional councils particularly struggled to improve their asset management performance.²⁰

1.3.5 DEFINED BENEFIT SUPERANNUATION SHORTFALLS

Another cost pressure identified by councils is the funding of defined benefit superannuation shortfalls. Local government's defined benefit superannuation fund is legally required to be 'fully funded', meaning it must have all payments available if all members were to withdraw at once. As a result, councils often have to top-up contributions based on regular actuarial assessments of the liabilities of the defined benefits scheme. Currently, Victorian councils are progressively funding a \$396.9 million shortfall.²¹

²⁰ VAGO 2014, *Asset Management and Maintenance In Councils*, February, p.xi.

²¹ MAV 2013, *About Defined Benefit Superannuation Shortfall fact sheet*.

The City of Greater Bendigo Council, for example, contributed approximately \$23 million in top-up funding to meet its liabilities from 1993 to 2015.²² Additionally, Indigo Shire Council commented in its submission to our consultation paper that their last defined benefits top-up cost over \$1 million.

1.4 RATES AND CHARGES AND THE IMPACTS ON RATEPAYERS

Councils collected a total of \$4.6 billion in rates and charges in 2013-14, comprising rate revenue (85 per cent), garbage charges (10 per cent) and municipal charges (3 per cent). Supplementary rates and charges, special rates and charges, revenue in lieu of rates and revenue from cultural and recreational land, made up the remaining 2 per cent.

Our terms of reference require us to assess the magnitude and impact on ratepayers of Victorian councils' successive above CPI increases in rates and charges. To illustrate this impact, we compared actual increases in the average total charges per assessment for Victoria, between 2005-06 and 2013-14 (eight years), with the increases that would have occurred if rates had increased at:

- the same rate as the CPI
- the rate calculated by the capping approach used in chapter 2 (that is 60 per cent CPI and 40 per cent wage price index).

Between 2005-06 and 2013-14, total rates and charges per assessment increased by around 5.8 per cent per year, compared with an annual CPI increase of 2.7 per cent.²³ Victorian ratepayers paid \$1 448 more over the period than if average rates and charges per assessment had increased at the same rate as the CPI (figure 1.5).²⁴

If our proposed rate cap had applied over the period, ratepayers rates could have been lower by \$1 242 (assuming councils did not apply for a variation during that period).

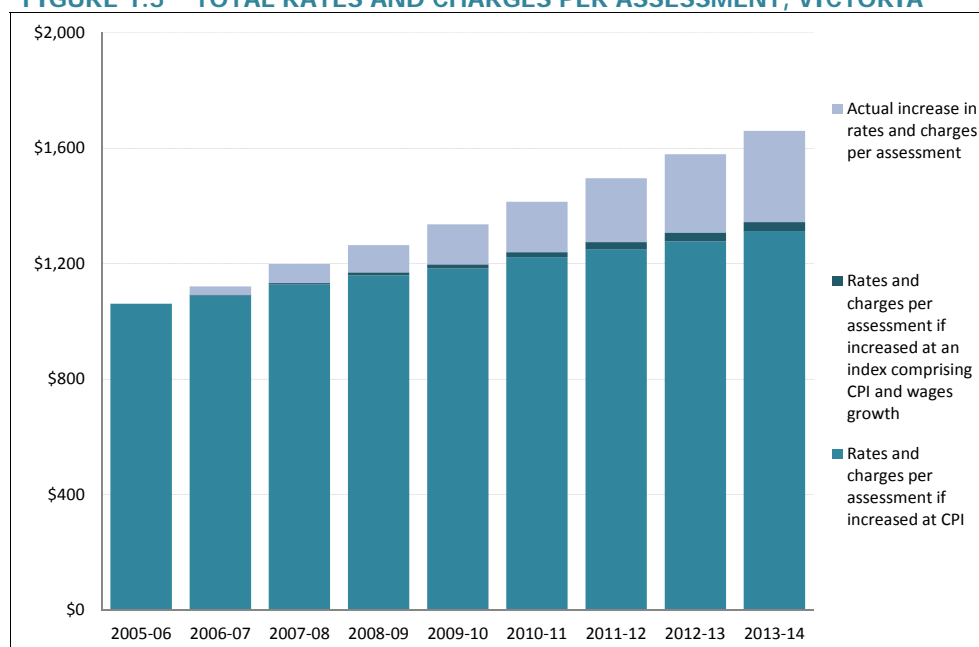
²² The City of Greater Bendigo, *Your questions answered about LASF defined benefits plan*, information sheet.

²³ Although the annual growth in total rates and charges was approximately 7 per cent over recent years, rateable assessments also grew (by approximately 2 per cent) which explains why rates and charges per assessment grew by only 5.8 per cent per year.

²⁴ The figure is an average for all ratepayers whether they be residential, commercial or industrial. The trend for each class of ratepayer is similar to that shown in figure 1.5. there was also little difference in the general trend for council grouping.

We did not seek to assess the reasonableness of the rate of increase in actual rates and charges per assessment. That is, our analysis did not consider any changes in the quality or level of services provided by councils over this period. Moreover, submissions by councils, peak bodies and other council groups argued a portion of the rate and charge increases over the past few years reflected cost pressures beyond councils' control. These pressures included cost shifting, calls on defined benefit superannuation, new obligations, and population growth especially for interface councils.

FIGURE 1.5 TOTAL RATES AND CHARGES PER ASSESSMENT, VICTORIA



Data source: VGC data and council annual reports.

1.5 DIVERSITY IN LOCAL GOVERNMENT

This section further highlights the diversity across the local government sector by drawing on councils' submissions and our analysis of key structural differences across council grouping.

WHAT THE SECTOR HAS SAID

We received submissions from 61 councils in response to our consultation paper. These submissions outlined key features of councils, including the different communities that they serve and the geographic and natural environment of individual municipalities.

Rural councils

- Rural councils have a limited ability to raise revenue through rates, due to their smaller populations, population decline and lower land values, compared with metropolitan councils.
- They rely more heavily on Commonwealth and State Government grants. The current grant freeze has been a large revenue constraint for rural councils.
- They face higher service delivery costs due to disperse communities and large road networks.
- They face more difficulty in managing asset renewals and maintenance back logs due to their limited own-source revenue streams and disperse communities.
- Finding multiple and competitive prices and tenders for services in rural areas is difficult.
- Rural communities have ageing populations, meaning fewer people are in the workforce and more elderly people use health services.
- Residents in rural communities have fewer employment opportunities.
- Public transport options are limited compared with those in metropolitan areas, and rural communities rely more on cars.

Interface councils

- Interface councils mentioned similar concerns to those raised by peri-urban and metropolitan councils.
- They have high demand for their services, community assets and infrastructure due to population growth.
- They manage Melbourne's green wedges, providing vital agriculture, ecosystems, recreation and tourism values for those who live in Melbourne. It is costly for councils to maintain these green wedge areas as required by state planning policy (which requires spending on services such as roadside maintenance, pest and weed management and native vegetation management).
- Like metropolitan councils, they typically provide a larger range of services than other councils.

Peri-urban councils

- Peri-urban councils include rural councils that immediately surround the outer growth ring of metropolitan Melbourne and Geelong. They face significant population growth in some areas as well as population decline in others, which is difficult to manage.
- They raised similar challenges to those raised by rural and interface councils.
- They manage significant planning responsibilities in that they have to balance holding a large portion of the state's agricultural land and farming communities with dealing with high demand for residential development.
- Rural and peri-urban councils face difficulties when large local businesses exit, requiring councils to spend on projects in the community to stimulate the local economy.
- Many rural and peri-urban councils have realised efficiencies and cost savings in recent years. So, under rate capping, they have indicated that they have limited scope to find more efficiencies without council job losses.
- Peri-urban councils have high demand for their services and community assets from tourists visiting country areas.

Regional centres

- The views of regional centres are similar to those of rural councils.
- Regional centres manage large road networks with disperse communities.
- They have a smaller rates base than that of metropolitan councils and a higher reliance on grant funding. Like rural councils, they face significant revenue pressures due to the freeze of Financial Assistance Grants.
- They noted they usually act as a hub for surrounding rural communities and council areas, which creates more demand for council services and community assets.
- Along with rural councils, they are typically constrained in their ability to charge higher user fees, because their communities have lower incomes and are less able to pay.
- They have limited public transport options compared with metropolitan councils.

Metropolitan councils

- Metropolitan councils support highly and densely populated communities.
- They have mature infrastructure assets.
- They typically have good public transport options and can raise revenue through parking fees and fines.
- Like interface councils, they typically provide a larger range of services than do other councils.

1.6.1 ANALYSIS OF COUNCIL DIVERSITY

In considering council diversity, we also examined some structural differences amongst councils. Tables 1.8, 1.9, and 1.10 provide information on the economic, environmental and demographic features of council grouping.

As shown in the tables, small and large rural councils face particular challenges. On average they have the largest road networks and the most bridges. Further, their communities are older, have lower Socio-Economic Indexes for Areas (SEIFA)²⁵ scores and incomes, have the fewest building approvals, and are the most dispersed.

The challenges of a small rate base for small rural councils are illustrated by the impact on ratepayers of a council raising an additional \$1 million through rates and charges (see the last column in table 1.8). If a small rural council were to raise an additional \$1 million in 2013-14, it would have added \$142 to the average assessment (compared with an additional \$56 for ratepayers in large rural councils and \$17 for those in metropolitan councils).

TABLE 1.8 ECONOMIC DIFFERENCES AMONGST COUNCILS

Council grouping	Average wage and salary income, 2011	Average unemployment rate 2011	Average monthly mortgage payment 2011	Average monthly rental payment 2011	Average impact on individual ratepayers in 2013-14 of an additional 1% of total revenue raised through a rates increase	Average impact on individual ratepayers in 2013-14 of an additional \$1 million raised through rates
	(\$)	(%)	(\$)	(\$)	(\$)	(\$)
Metropolitan	55 394	5.5	2 188	1 440	17	17
Interface	48 062	5.2	1 856	1 224	17	15
Regional centres	43 771	5.9	1 471	908	17	23
Large rural	42 298	4.4	1 475	823	17	56
Small rural	38 523	4.4	1 211	666	16	142

Source: ABS 2008-12, *National regional profile*, cat. no. 1379.

²⁵ SEIFA is an ABS index that measure socio-economic advantage and disadvantage by geographic areas in Australia. It is based on household income, education, employment, occupation, housing and other indicators. The higher the index score the more socio-economically advantaged is the area.

TABLE 1.9 STRUCTURAL DIFFERENCES AMONGST COUNCILS

Council grouping	Average council area (km ²)	Average road network length 2013-14 (km)	Average number of bridges 2013-14	Average value of the all new building approvals 2012 (\$ m)	Average number of households 2011
Metropolitan	66	512	8	654	45 039
Interface	820	1 335	72	575	46 661
Regional centre	3 934	2 085	60	287	31 092
Large rural	4 510	2 294	121	22	10 199
Small rural	4 821	2 250	82	89	3 730

Source: VGC data and ABS 2008-12, National Regional Profile. cat. no. 1379.

TABLE 1.10 DEMOGRAPHIC DIFFERENCES AMONGST COUNCILS

Council grouping	Average population size 2014	Average median age 2011	Average SIEFA score ^a 2011	Average percentage of population that is Aboriginal or Torres Strait Islander 2011	Average percentage of population born overseas 2011
Metropolitan	133 352	37	996	0.4	39
Interface	160 047	36	1 038	0.6	30
Regional Centre	86 721	38	979	2.0	16
Large rural	28 286	42	1 002	1.4	15
Small rural	9 419	47	979	1.0	14

^a SEIFA is an ABS index that measures socio-economic advantage and disadvantage by geographic areas in Australia. It is based on household income, education, employment, occupation, housing and other indicators. The higher the index score the more socio-economically advantaged is the area.

Source: ABS, 2008-2012, *National regional profile*, cat no. 1379.

1.6 EXISTING ACCOUNTABILITY AND REPORTING REQUIREMENTS OF LOCAL GOVERNMENT

The local government sector is subject to reporting and accountability requirements. We have been careful to consider these requirements in designing the rates capping and variation framework (chapters 3 and 4). This section summarises aspects of the accountability framework that apply to local government, including roles and responsibilities, reporting requirements and principles that guide service delivery.

Box 1.2 lists the current roles and responsibilities of local government, and explains accountability and oversight.

BOX 1.2 ROLES AND RESPONSIBILITIES

Councils

As a democratically elected tier of government, councils are primarily responsible for providing services to and acting in the long-term interests of their communities. In doing so, councils are obligated by the *Local Government Act 1989* to adhere to the principles of sound financial management and best value principles. Councils also have considerable planning, budgeting and reporting obligations under the Act and Regulations to ensure they are accountable to their communities.

Minister for Local Government

The Minister is responsible for administering the principal legislation relating to local government. While not directly involved in regular management of individual councils, the Minister has broad powers to intervene when a council breaches its obligations under the Act.

Victorian Auditor-General's Office (VAGO)

Empowered by the *Audit Act 1994*, the Auditor-General plays a central role in financial oversight of the sector. VAGO annually audits council financial sustainability and, from 2014-15 council performance against some outcome indicators in the Local Government Performance Reporting Framework. The Auditor-General also undertakes regular performance audits of aspects of the sector, including asset management, rating strategies, performance reporting and financial sustainability.²⁶

Continued next page

²⁶ These reports have identified significant deficiencies in the sector with in terms of performance measurement and reporting, asset management and financial sustainability. Their findings and recommendations have informed the our approach and design of the rate capping and variation framework.

BOX 1.2 (CONTINUED)

Local Government Victoria (LGV)

LGV is a division of the Department of Environment, Land, Water, and Planning, and it oversees administration of the Local Government Act and Regulations. LGV works closely with the sector to provide funding, guidance and support. In particular, it prepares better practice guides covering revenue and rating strategies, financial and performance reporting, and asset management. LGV conducts and collates the annual Community Satisfaction Survey on behalf of participating councils. It also administers the Local Government Performance Reporting Framework, commencing in 2015.

Local Government Investigations and Compliance Inspectorate

The inspectorate was established in 2009 as an independent administrative office to assess compliance with the Local Government Act. The inspectorate has focused its efforts principally on investigating governance issues related to misconduct, fraud, and conflicts of interest.

Municipal Association of Victoria (MAV)

Governed by the *Municipal Association Act 1907*, the MAV is the peak representative body for the local government sector. It also plays an important role in guiding best practice and assisting the sector to build capacity.

The obligations and responsibilities of Victorian local government for planning and accountability are detailed in part 6 of the *Local Government Act 1989* and the *Local Government Regulations (Planning and Reporting) 2014*. Table 1.11 outlines the key features of the accountability and reporting provisions, which include:

- a Council Plan
- a Strategic Resource Plan (SRP)
- an annual budget
- an annual report.

In addition to their formal planning and accountability requirements under part 6 of the Act, local governments must report extensively to various departments and agencies on their service provision.

Further, councils are obliged under part 7 of the Act to apply and adhere to the principles of sound financial management, particularly in their planning, budgeting and reporting practices.

From 1 July 2014, councils are obligated to report on their performance against common service, financial and governance indicators that constitute the Local Government Performance Reporting Framework (LGPRF). The reporting framework covers indicators and measures covering service performance, financial performance and sustainable capacity, and a governance checklist. It includes:

- 53 indicators across 11 service areas
- 12 indicators across five financial performance areas
- six indicators of council capacity and sustainability
- 24 indicators of governance and management.

The reporting framework will replace the performance indicators that LGV reported up to 2014. LGV will publish the service and financial performance data on a new 'MyCouncil' website (under development), allowing some comparisons of performance within council groupings.

TABLE 1.11 COUNCIL PLANNING AND BUDGETARY OBLIGATIONS

Document	Outline	Reporting requirements
Council Plan	Must include the strategic objectives of the council, strategies for achieving the objectives for a minimum of four years, indicators for monitoring the achievement of the objectives, and the strategic resource plan.	<p>Provided to the Minister within six months of a general election or by the next 30 June (whichever is later)</p> <p>Community consultation required.</p>
Strategic Resource Plan	This long-term plan (minimum of four years) must outline the resources needed to achieve the objectives listed in the council plan. It must have regard to all plans adopted by the council, including asset management plans.	<p>Must be reviewed during the preparation of the council plan and adopted no later than 30 June each year. Councils are required to report on any material variation to the plan.</p> <p>Community consultation required.</p>
Annual Budget	The budget must include financial statements, a description of the services and initiatives to be funded, a statement about how these services and initiatives will contribute to the strategic objectives in the council plan, major initiatives, the prescribed indicators of service performance for the services funded in the budget, and the measures relating to those indicators.	<p>Provided to the Minister by 31 August each year (although usually adopted by end of the financial year). Councils must publish a draft annual budget and allow a minimum of 28 days for community consultation.</p> <p>Community consultation required.</p>

Continued next page

TABLE 1.11 (CONTINUED)

Document	Outline	Reporting requirements
Annual Report	<p>For each financial year, councils must prepare an annual report consisting of:</p> <ul style="list-style-type: none"> • a report of operations. It includes a statement of progress for the major initiatives identified in the budget, the performance of the council against the governance and management checklist,^a and results against the prescribed non-audited framework indicators^b and any other strategic indicators in the council plan • a performance statement. It includes audited results achieved against the prescribed performance indicators and measures in schedule 3 of the Regulations. • financial statements. These audited financial statements are prepared in accordance with Australian Accounting Standards. They include a statement of capital works. Income and expenditure must be compared against the budget and any material variation must be explained. Capital expenditure in the statement of capital works must be compared with the statement of capital works in the budget and any material variation must be explained.^c 	<p>Must be submitted to the Minister within three months of the end of the reported financial year (unless permitted otherwise by the Minister).</p>

^a Schedule 1, Local Government (Planning and Reporting) Regulations 2014. ^b Schedule 2, Regulations.

^c Amendments to the Act and Regulations in 2014 mean, from 1 July 2014, councils must structure their annual reports in accordance with the model financial report. These amendments were introduced to help councils be more consistent in how they report on performance and financial position, including capital expenditure.

Councils are obliged to adhere to the Best Value Principles (box 1.3). Introduced in 1999, the best value principles to aim to improve service quality and efficiency, and to ensure service levels are consistent with the community's needs, based on consultation and engagement.

BOX 1.3 BEST VALUE PRINCIPLES

The Best Value Principles are—

- (a) all services provided by a Council must meet the quality and cost standards required by section 208D;
- (b) subject to sections 3C(2)(b) and 3C(2)(e), all services provided by a Council must be responsive to the needs of its community;
- (c) each service provided by a Council must be accessible to those members of the community for whom the service is intended;
- (d) a Council must achieve continuous improvement in the provision of services for its community;
- (e) a Council must develop a program of regular consultation with its community in relation to the services it provides;
- (f) a Council must report regularly to its community on its achievements in relation to the principles set out in paragraphs (a), (b), (c), (d) and (e).

Source: Local Government Act 1989, part 9, division 3

Each year, the VGC requires councils to submit revenue and expenditure data covering 10 broad service areas, for helping determine the annual allocation of Financial Assistance Grants funding.

Further, LGV administers an annual community satisfaction survey on council performance. The survey assesses community satisfaction levels with council performance across a range of areas, including overall performance, community service priorities, service performance community consultation and engagement, decision-making, customer service, general views on the trade-off between increased rates and reduced service levels and overall direction. Participation in the survey is voluntary, with 69 councils using it in 2015. Regardless, the introduction of the LGPRF, councils are now obligated to capture and report on community survey results for a number of service output and outcome indicators.

2 THE RATE CAP

The terms of reference require us to provide advice on how to implement the Government's commitment to cap annual council rate increases. This includes advice on such matters as: whether any refinements are warranted to a cap based solely on the Consumer Price Index (CPI); as well as the base to which the cap should apply.

This chapter considers the following key questions about the proposed approach to setting the cap:

- One cap or many?
- Which revenues come under the rate cap?
- Should the cap be applied to total rate revenue or rate revenue per assessment?
- How should the rate cap be calculated?
- What should be the base year for setting the cap?
- What information should be required each year?

In this chapter, when we say 'capping council rates at CPI' we mean capping increases in council rates at the rate of increase in the CPI.

2.1 ONE CAP OR MANY?

Chapter 1 demonstrated significant differences among Victoria's 79 councils.

2.1.1 STAKEHOLDERS' FEEDBACK

Councils, peak bodies and other council groups identified factors such as growth, population density and dispersion and huge networks of inherited roads, which they suggest should be considered when setting the cap. They suggested that multiple rate caps should be adopted to accommodate these structural differences. Conversely,

ratepayers, some councils and other organisations suggested that applying multiple rate caps across Victoria would lead to ratepayers being treated inequitably depending on the council area in which they lived. They argued for a single cap on the basis that:

- ratepayers should be treated equally²⁷
- different caps for different types of councils might be ‘detrimental to the originally intended outcome that all Victorian ratepayers will have relief from the financial burden of excessive and increasing annual council rates charges’²⁸
- a single cap is simple to administer and to communicate statewide and easier for the community to understand²⁹
- different caps would cause a great deal of inequity and confusion among Victorian ratepayers³⁰
- a single cap would ensure consistency among councils.³¹

Local Government Professionals (LGPro) and a number of councils supported a single cap but only if the variation framework is flexible enough to account for the diverse needs of each council.³² The Municipal Association of Victoria (MAV) acknowledged that council diversity would be more appropriately dealt with through the variation process but suggested the Commission:

*‘may wish to give consideration to whether systematic differences between council cohorts could be more appropriately considered through differentiated caps in the rate capping framework’.*³³

The Victorian Local Governance Association (VLGA) noted that given the diversity of the sector:

²⁷ FINPro 2015, *Submission to the ESC’s consultation paper*, May.

²⁸ Cardinia Shire Ratepayers’ and Residents’ Association Inc. 2015, *Submission to the ESC’s consultation paper*, May.

²⁹ Individual submissions to the ESC’s consultation paper by the Hobsons Bay City Council, Horsham Rural City Council, Whitehorse City Council.

³⁰ Maroondah City Council 2015, *Submission to the ESC’s consultation paper*, May.

³¹ Individual submissionS to the ESC’s consultation paper by the Hume City Council, Bayside City Council, Maribyrnong City Council, Swan Hill Rural City Council, Revenue Management Association.

³² Individual submissionS to the ESC’s consultation paper by the LGPro, Bass Coast Shire Council, Greater Bendigo City Council, Mildura Rural City Council.

³³ MAV 2015, *Submission to the ESC’s consultation paper*, May.

*‘the complexity at stake effectively rules out the possibility of an index able to capture the cost factors relevant to all local governments’... and that ‘the substantive issue is the regime for granting variations. A rate cap must constitute a baseline only, with increase to be granted ‘as course’ where council can make a reasonable case’.*³⁴

2.1.2 DISCUSSION/ANALYSIS

We have considered whether and how structural differences among councils might be taken into account when setting the rate cap. One option we considered was whether separate groups of councils could be subject to different caps. This approach ran into problems.

When we compared the rate of growth of councils’ population (both historical and forecast) we observed that not all interface councils had experienced or will experience significant population growth. Some large rural councils, regional centres and metropolitan councils had also experienced significant growth in the past. We also compared data on road networks and we observed that while most rural councils have huge networks of roads to maintain, some interface and peri-urban councils are facing the same issue. Section 1.6 of volume II summarises the submissions on structural differences among council grouping and it appears that there is no single structural issue which is unique to a single council group.

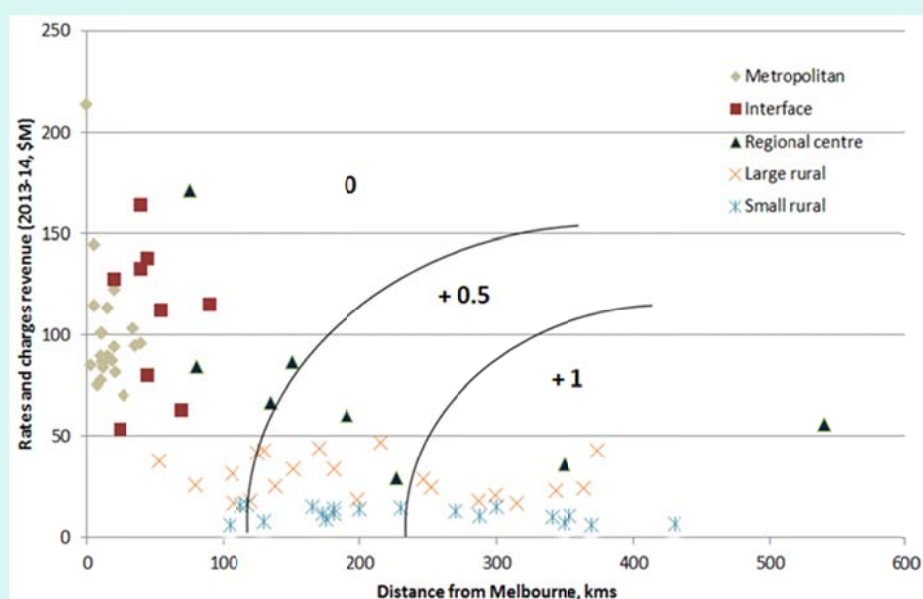
We also examined the merits of an even more tailored approach whereby each council’s rate cap would include adjustments accounting for that council’s resource capacity, its rating history and the extent to which it controlled its costs and revenues. An example is shown in box 2.1.

On balance, we have decided against these approaches for a number of reasons. Our primary concern was the arbitrariness of such arrangements. The adjustments that might be made under either of these approaches are not self-evident and would involve a large degree of judgement. We expect neither the community nor councils would be well served with a capping regime that relied extensively on such subjective assessments. We were also concerned that any effort to tailor the rate cap would suggest a false degree of precision in setting the cap and may lead to confusion in the community.

³⁴ VLGA 2015, *Submission to the ESC consultation paper*, May.

For these reasons, we are recommending that there should be only one rate cap that applies equally to all councils in Victoria. We have concluded that the variation process described in chapter 3 provides a more efficient, transparent and participative mechanism to deal with individual councils' circumstances when the capped increase in rate revenue is considered to be insufficient.

BOX 2.1 PROXY FOR A COUNCIL'S EXPECTED CAPABILITY TO MANAGE ITS BUDGET



In this figure, we adopt two simplistic assumptions. First, the further a council is from Melbourne the fewer its resources to help it manage its budget pressures; and second, the bigger a council's budget the more able it is to manage any budget pressures it may face. In other words, large inner city councils would be assumed to have the most capacity to manage their budgets while small, distant councils would have the least capacity. We then considered whether councils could have their rate cap adjusted depending on where they fell on the graph shown. Small and distant councils would have the largest upward adjustment to their cap (say, by 1 per cent) while bigger and less distant councils would have no adjustment to their cap.

Continued next page

BOX 2.1 (CONTINUED)

This adjustment to the rate cap indirectly accounts for some structural differences among councils but involves some level of arbitrariness in terms of where to place the boundaries and setting the levels of adjustment. Also, data only shows the rates and charges revenue and this provides no indication of a council's revenue raising capacity. Further, in any given boundary, say the +0.5 per cent boundary, there is a high degree of variability among councils. However, any attempt to develop a more refined approach would inject a degree of false precision in setting the rate cap for each council.

DRAFT RECOMMENDATION 1

The Commission recommends that there should be one rate cap that applies equally to all councils in Victoria.

2.2 WHICH REVENUES COME UNDER THE RATE CAP?

The terms of reference require us to provide advice on what would be the composition of the revenue base to be capped. Currently, councils are allowed under the Local Government Act 1989 (the Act) to levy the following rates and charges:³⁵

1. **General rates** — applied as a percentage of each property's valuation; depending on a council's policy this could be a uniform rate, or a number of different rates for different classes of ratepayers such as residential, farms, commercial and industrial enterprises.³⁶

³⁵ Sections 158, 159, 162, 163 of the Act. For more information on the level of rates and charges collected by councils in the past few years, see chapter 1.

³⁶ A number of councils also include recreational and cultural land as one of the differential rating categories.

2. **Municipal charges** — to cover some of the administrative costs of the council and required by the Act to be no more than 20 per cent of the total revenue raised from the combination of municipal charges and general rates.³⁷ Administrative costs are not defined in the Act and not all councils levy municipal charges.
3. **Service rates and charges** — for services to properties such as waste management and water provision. Currently, service rates or charges only refer to waste or garbage management. The Victorian Grants Commission (VGC) data shows that 72 councils levy service charges and six councils levy service rates.³⁸ If levied as charges, they are based on full cost recovery for a number of councils.
4. **Special rates and charges** — For ratepayers specifically benefitting from a service or investment such as; footpaths; kerbs and channels; and arrangements for providing services like promotion, marketing or economic development (such as for commercial businesses).
5. **‘Revenue in lieu of rates’** — Some councils receive ‘revenue in lieu of rates’, which are payments related to unrateable lands such as railway land, Commonwealth and State Government buildings, mining lands, power stations, airports and wind farms, etc.

Items 1 to 3 are the three largest components (98 per cent on average) of councils’ total rates and charges revenue. Under the Act, the Minister for Local Government has the power to limit councils’ income from general rates, municipal charges and service rates and charges.³⁹

2.2.1 STAKEHOLDERS’ FEEDBACK

Stakeholders have different views about the composition of the revenue base that should be capped:

- General rates and municipal charges should be capped because they are not directly linked to specific services or infrastructure projects.

³⁷ 44 councils levied municipal charges in 2013-14.

³⁸ Melbourne City Council noted that its waste related costs are funded as part of the annual budget process and they do not apply a specific garbage/waste/environmental in general rates (Melbourne City Council, response to ESC’s survey of rates and charges).

³⁹ Part 8A of the Act.

- Service charges should be excluded because they can be directly linked to services provided, are based on cost of service, and are market tested. Further, service charges are affected by significant annual increases in the State Government's landfill levy and the costs of specialist private waste contractors. There were suggestions that the Commission monitor service charges if they were not to be included in the revenue base to be capped.
- Special rates and charges should be excluded because they are directly linked to services provided, are based on cost of service and there are clear legislative requirements on councils governing how special rates or charges can be levied.

2.2.2 DISCUSSION/ANALYSIS

For the rate cap to be effective, it should be applied to the bulk of the rates revenue unless there are compelling reasons not to do so. The Commission uses the following considerations in assessing which council rates and charges should be excluded from the rate cap:

1. **Is the charge cost reflective?** — charges, such as garbage charges, are often linked to the costs associated with providing specific services. Capping charges for specific services would make them less cost reflective and could distort price signals for the provision of these services. Further, users of these services can monitor the level and rate of increase of their charges over time and some may compare them with similar councils.
2. **Is the charge market tested?** — if a service that is funded by charges can generally be procured through competitive bidding, this gives some level of assurance that these charges are based on competitive costs.
3. **Are there adequate financial constraints under current legislation?** — it is not necessary to add another layer of financial discipline if the Act or other relevant legislation already provides constraints on how rates or charges are to be set, collected and used; or if there are clear engagement requirements and appeal and/or arbitration processes.
4. **Is the charge a pass through cost?** — levies collected by councils on behalf of the State Government are not within the control of the councils and are direct transfers to government. The State Government normally also sets the annual escalation factor for these levies.

We are recommending that the rate cap should apply to general rates and municipal charges only — noting that these two account for about 88 per cent of the total rate revenue raised by councils.⁴⁰

Based on the above listed considerations, we are recommending that the cap should not apply to service rates and charges, special rates and charges, ‘revenue in lieu of rates’, and the fire services levy. These are discussed in more detail below.

Service rates and charges

Councils’ current service (or garbage) rates and charges appear to partly satisfy criteria 1 and 2. For now, we are recommending that service rates and charges (garbage rates and charges) be excluded from the rate cap.⁴¹ In our survey of council rates and charges, councils reported that their garbage rates and charges are cost reflective and market tested. Capping service rates and charges would make them less cost reflective and could distort price signals for the provision of these services.

Further, users of these services can monitor the level and rate of increase of their charges over time and some may compare them with similar councils.⁴² Therefore, for now, we are not suggesting that these charges be made subject to the rate cap.

Nonetheless, we will monitor and benchmark garbage rates and charges.⁴³ If we find unexplained differences across councils, or if we find that councils are disproportionately allocating their overhead costs to their service rates and charges, then we will make appropriate recommendations to the Government at that time. The Commission notes that in (New South Wales (NSW), the Independent Pricing and Regulatory Tribunal (IPART) has not imposed any annual limit on waste charges since

⁴⁰ Based on 2013-14 rates and charges data collected by the VGC from councils.

⁴¹ There are different practices among councils in covering the cost of garbage services with 72 councils levying a specific garbage charge, while seven councils cover these costs through their general rate revenue (of the seven, six councils recover their waste related costs through general rate revenue. Melbourne City Council noted in its response to the ESC survey on rates and charges that its waste related costs are funded as part of the annual budget process and not through a specific garbage/waste/environmental charge).

⁴² In May 2015, the Commission conducted a survey of council rates and charges. The survey focused on service rates and charges and ‘revenue in lieu of rates’. 62 councils responded to the survey. 38 out of 62 councils reported that they fully outsource their garbage services through competitive bidding, 19 councils partly outsource and 4 councils provide the services in-house (one council did not respond to the specific question about the manner of providing garbage related services). A number of councils are currently locked in to contracts ranging from 2 years to 10 years.

⁴³ Councils’ garbage related costs will be monitored separately from landfill levy related costs.

2010,⁴⁴ but waste related charges are independently audited and monitored by the NSW's Office of Local Government (OLG) annually.

Service charges are affected by the annual increases in the landfill levy set by the Environmental Protection Authority. The landfill levy is a levy on municipal waste going into landfill. As part of our monitoring of service charges we would require councils to provide a breakdown of their garbage costs into council-related costs and the landfill levy.

Two councils noted that those councils which recover garbage related costs through general rates will be disadvantaged if services charges are not capped. It is for these councils (and those councils which levy part service rates and part service charges) to decide whether they want to start levying service charges or separating their service rates from the total general rates going forward to exclude them from being capped.

We believe that there is merit in the Government reviewing the Act's provisions on service rates and charges to increase consistency among councils. In NSW, legislation requires that waste related charges should not exceed the reasonable cost of providing the services and that general rates must not be used to fund the cost of providing waste management services.⁴⁵ And as noted above, councils are required by the OLG to have these charges independently audited each year to determine that they have been calculated on a 'reasonable cost' basis.

Special rates and charges

Special rates or charges are cost reflective and constrained by legislation, therefore the cap need not apply to them. The Act specifies that a special rate or a special charge can only be used to defray expenses or repay loans where there is a special benefit to the persons required to pay the special rate or charge. It also prescribes the formula to be used by councils in setting the maximum special rate or charge including the required engagement and appeal process.⁴⁶ As noted by MAV:

⁴⁴ IPART 2014, *Report on IPART's functions in relation to local government in 2013-14*, October, page 6. The Minister for Local Government has delegated power to specify how councils can vary the charges for waste management services each year to IPART.

⁴⁵ *Local Government Act 1993*, section 504(3). The Act also requires that general rates must not be used to fund the cost of providing waste management services but general rates may be lent (by way of internal loan) for use by the council in meeting the cost of providing waste management services.

⁴⁶ In 2013-14, 23 councils declared special rates/charges. The special rates/charges revenue accounted for 0.22 per cent of Victorian councils' total rates and charges revenue for that year.

projects funded by these revenues relate to specific projects with benefits that are concentrated in a particular group of ratepayers and is delivered over a specific timeline. The current legislative framework for special rates and charges includes appropriate constraints on the use of special rates and charges schemes — such as by clearly defining the benefits derived from the project and polls of the beneficiaries if their contribution is above the threshold level.⁴⁷

Revenue in lieu of rates

‘Revenue in lieu of rates’ is constrained by legislation and should not be capped. Our survey of councils’ rates and charges shows that most ‘revenue in lieu of rates’ comes from power stations.⁴⁸ In this case, the ‘revenue in lieu of rates’ is negotiated by the two parties consistent with section 94 of the Electricity Industry Act 2000 (the EI Act). The EI Act also prescribes an arbitration process.⁴⁹

Fire services levy

Councils currently collect the fire services levy on behalf of the State Government. The fire services levy is a property-based levy collected with council rates. All revenue collected through the fire services levy goes to support the State’s fire services (vital life-saving equipment, firefighters, staff and volunteers, training, infrastructure and community education).⁵⁰ The fire services levy should be excluded from the cap on the grounds that it is not within the control of the councils and is a direct transfer to Government.

SUPPLEMENTARY RATES

Councils also collect supplementary rates. These are additional rates collected during the course of the year if the value of a property is altered after rates notices have been issued. Supplementary valuations may be a result of either changes in the value of

⁴⁷ MAV 2015, *Submission to the ESC’s consultation paper*, May.

⁴⁸ In May, the Commission conducted a survey on councils rates and charges. The survey focused on service rates and charges, ‘revenue in lieu of rates’ and other rates and charges. 62 councils responded to the survey.

⁴⁹ 21 councils received revenue in lieu of rates in 2013-14. This accounted for 0.75 per cent of councils’ total rates and charges revenue for 2013-14.

⁵⁰ <http://www.firelevy.vic.gov.au/>, accessed on 9 July 2015.

existing properties or the entry of new properties — for example, due to renovations or subdivisions, respectively.⁵¹

Supplementary rates accounted for 1 per cent of Victorian councils' total rates and charges revenue in 2013-14. The VGC data shows that interface (growth councils) received the highest supplementary rates but the trend is declining. Regional centres seem to have experienced a 40 per cent increase in supplementary rates for 2013-14.

At the end of each financial year, a council will adjust its valuation base and the base for its general rate revenue, to include the actual supplementary valuation and supplementary rates revenue received in the year just concluded. The adjusted amounts become the basis for determining the next year's rate base. That is, valuations and rates are only treated as 'supplementary' in the year they occur. Thereafter, they are included in the base value and rates of the properties in question.

We are proposing that supplementary rates be excluded from the rate cap in the year they occur.

DRAFT RECOMMENDATION 2

The Commission recommends that:

- revenue from general rates and municipal charges should be subject to the rate cap
- revenue from special rates and charges, 'revenue in lieu of rates' and the fire services levy should not be included in the rate cap and
- service rates and charges should not be included in the rate cap, but be monitored and benchmarked.

⁵¹ Some of the examples cited by councils on their websites of undertaking supplementary valuations include when properties are physically changed (e.g. when buildings are altered, erected or demolished), amalgamated, subdivided, portions sold off, rezoned or are affected by road construction. Supplementary valuations bring the value of the affected properties into line with the valuation of other properties in the municipality. Values are assessed as at the same date of the general valuation for existing properties.

2.3 SHOULD THE CAP BE APPLIED TO TOTAL RATE REVENUE OR AVERAGE RATE REVENUE PER ASSESSMENT?

Rate revenue refers to the total revenue collected from general rates and municipal charges as we have recommended in section 2.2 above. Average rate revenue per assessment refers to the total revenue collected from general rates and municipal charges divided by the total number of assessments.

2.3.1 STAKEHOLDERS' FEEDBACK

In our consultation paper, we asked stakeholders whether the cap should apply to each council's total rate revenue or to average rate revenue per assessment. We raised the same question during many of our meetings with interested parties. Not surprisingly, views were mixed.

Many councils, the Local Government Finance Professionals, the Revenue Management Association (RMA), the Interface Councils Group and a ratepayers association, prefer capping revenue (including supplementary rates) on the basis that:

- a revenue cap is simpler and consistent with council practices in setting rate levels
- it is more transparent and is published in the annual budget. Actual revenue collected is reflected in a council's annual report and therefore easier to monitor
- it provides councils with flexibility to make decisions regarding the equitable distribution of rates burden, and ensures relative valuation movements between properties continue to drive the apportionment of total rate revenue among all ratepayers
- it provides councils with revenue certainty.

Other councils opposed a rate revenue cap on the assumption that supplementary rates would not be added into the base.

Some councils and LGPRO clearly preferred capping average rate revenue per assessment. One council argued that the rates capping objective is 'household affordability', so it makes sense to cap rate revenue per assessment.⁵² The councils supporting capping rate revenue per assessment argued that this would enable easy

⁵² Indigo Shire Council 2015, *Submission to the ESC's consultation paper*, May.

comparison with other councils,⁵³ allow supplementary valuations and revaluations to be factored into the calculation in the most straight forward way,⁵⁴ and allow growth councils to gain additional income from their fast growing areas.⁵⁵

Interestingly, we encountered differing views about why one option might be preferred over another. For example, councils had opposite views about which approach was beneficial to councils experiencing growth.⁵⁶

2.3.2 DISCUSSION/ANALYSIS

Both options are technically viable and relatively straightforward to administer (particularly with the exclusion of supplementary rates). Both options maintain councils' flexibility to adopt or change their rating policies — that is, both options allow councils to rebalance their revenue raising efforts between general rates and municipal charges. Likewise, councils retain the capacity to rebalance between different types of ratepayers (differential rating).⁵⁷

We consider that the Government's objective in establishing a rate cap is to give ratepayers, individual and collectively, confidence in councils' rate setting processes. Most ratepayers are not directly involved in councils' budget and rate setting processes. Rather, they focus on the observed change in the 'amount owing' shown in their annual rates notice. As such, we are proposing that the framework cap rate revenue per assessment rather than total rate revenue as this most closely reflects most ratepayers' experience with council rating.

However, even under a binding rate cap per assessment, individual ratepayers will experience rate changes that differ from the capped rate. There are numerous reasons

⁵³ Individual submissions to the ESC's consultation paper by Moreland City Council and Glen Eira City Council.

⁵⁴ Bayside City Council 2015, *Submission to the ESC's consultation paper*, May. Glen Eira City Council had similar views during our meetings with them.

⁵⁵ Indigo Shire Council 2015, *Submission to the ESC's consultation paper*, May.

⁵⁶ For example, LGPRO considers that capping average rates and charges per assessment is a better option because a revenue cap will be disadvantageous to growth councils. However, the submission from the Interface Council Group, which is comprised of growth councils, supported a revenue cap over capping average rates and charges per assessment. Baw Baw Shire Council also argued that applying the cap to average rates and charges per assessment would be disadvantageous to those councils experiencing growth or significant change.

⁵⁷ Differential rates are where councils set different rates in the dollar for different categories of rateable land. The Council may for example, have differential rates for farm land, various categories of residential property or commercial/industrial properties — each paying a different rate in the dollar.

for these differences that are beyond the control of a rate capping and variation framework. Some of these reasons include:

- market forces altering the relative value of properties within an individual council
- owner actions altering the value of properties, for example, through renovation or subdivision or
- council policies such as altering the differential rates at which different classes of properties are rated.

In light of these uncontrollable factors, we consider that the best option for the rate cap involves applying the rate cap to a 'typical' or 'average' ratepayer — although we recognise that there will be some or many ratepayers who experience higher and lower rate changes than this notional ratepayer.

BOX 2.2 RELATIONSHIP BETWEEN THE RATES BY THE AVERAGE RATEPAYER AND A COUNCIL'S RATE IN THE DOLLAR

The notional 'average ratepayer' is most simply defined as the ratepayer who owns an average valued property in each local government area. The total rates paid by this ratepayer will be the, so called, 'rate in the dollar' applied by the local council multiplied by value of the average ratepayer's property. The simplest possible approach to calculating the value of this average ratepayer's property is to divide the total value of rateable properties by the total number of rateable properties in each council area.

$$\text{Average property value} = \frac{\text{Total value of rateable properties}}{\text{Number of rateable properties}}$$

When determining the 'rate in the dollar' to apply in a particular year, a council will divide the total revenue it requires from rates by the total value of rateable properties in its municipality.⁵⁸

$$\text{Rate in the dollar} = \frac{\text{Total revenue required from rates}}{\text{Total value of rateable properties}}$$

The rates paid by the average ratepayer will be the product of these two factors.

$$\text{Rates paid by average ratepayer} = (\text{Rate in the dollar}) * (\text{Average property value})$$

Substituting the two earlier equations into this relationship and simplifying gives:

$$\text{Rates paid by average ratepayer} = \frac{\text{Total revenue required from rates}}{\text{Number of rateable properties}}$$

which is the measure to which the rate cap will be applied each year.

⁵⁸ For the purpose of simplifying this discussion, 'rates' refers to general and municipal rates. But in practice, some councils levy municipal charges on a property basis.

In other words, we are recommending that the cap should be applied to the rates and charges paid by the average ratepayer and that this is calculated by dividing a council's total required rate revenue in a given year, by the number of properties in that council's area. We expect that both these figures should be readily available to councils and should be readily verifiable.

The rate cap would apply to the year-by-year increase in the rate paid by this average rate payer. Even so, it will be important for councils (and the Commission) to communicate that this is an 'average' outcome and some ratepayers can expect higher increases, while others will experience lower increases for the reasons stated above.

We have also considered whether 'rebalancing constraints' should be applied.⁵⁹ These constraints would limit how far above (or below) the cap an individual ratepayer's rates could be increased (or decreased). For now, we are not proceeding with this idea on the basis that we expect the cost of implementing the required changes to councils' billing systems would outweigh any benefits produced by doing so.

As discussed in section 2.6 below, we will create a working group composed of council representatives to develop the specific information we will collect from councils annually to support the proposed rate capping framework.

DRAFT RECOMMENDATION 3

The Commission recommends that the cap should be applied to the rates and charges paid by the average ratepayer. This is calculated by dividing a council's total revenue required from rates in a given year by the number of rateable properties in that council area at the start of the rate year.

2.4 HOW SHOULD THE RATE CAP BE CALCULATED?

The terms of reference for this review indicate that the annual rate of change in the CPI should be the Commission's starting point when considering the allowable increase in council rates. We are also required to provide advice on 'any refinements to the nature

⁵⁹ The Commission adopted this approach for its decisions on water pricing in 2013. (<http://www.esc.vic.gov.au/Water/Water-Price-Review-2013-18>, Accessed on 23 July 2015).

and application of the cap that could better meet the Government's objectives.' Importantly, the terms of reference require us to have regard to the pressures applying on ratepayers and on councils — for example, through references such as: 'contain[ing] the cost of living' and 'sustainability of councils' financial capacity', respectively.

2.4.1 DISCUSSION / ANALYSIS

In considering how best to balance the requirements of the terms of reference, we have considered which measure of CPI to adopt and which refinements are necessary to address the pressures faced by ratepayers and councils.

There are numerous available measures of CPI (table 2.1) and these can be backward looking (that is, telling us what inflation was in a past period) or forward looking (that is, based on a forecast of what inflation will be in a future period). Each option has its merits and each has its flaws.

TABLE 2.1 CPI ESTIMATES AND SOURCES

Source	Description
Australian Bureau of Statistics	Publishes quarterly estimates of past changes in the CPI and underlying CPI for Australia and Australian capital cities ^a
Victoria's Department of Treasury and Finance	Publishes 4 years forecasts of underlying CPI for Melbourne in May each year ^b Forecasts are updated in December each year
Reserve Bank of Australia	Publishes quarterly estimates of past changes in the underlying CPI ^c for Australia

^a Underlying inflation is based on a trimmed mean (estimated by ordering the seasonally adjusted price changes for all CPI components in any period from lowest to highest, trimming away those that lie at the two outer edges of the distribution of price changes for that period, and then calculating an average inflation rate from the remaining set of price changes and weighted median (the price change at the 50th percentile by weight of the distribution of price changes). ^b Underlying CPI excludes volatile items such as automotive fuel, fruit and vegetables, utilities, property rates and charges, child care, health, other services in respect of motor vehicles, urban transport fares, postal services and education. Source: DTF (2015), *Method for making forecasts of macro-economic indicators*, page 12, May.) ^c Underlying CPI excludes fruit, vegetables and automotive fuel. Source: RBA (2010), *Measures of underlying inflation*, Bulletin-March Quarter).

Source: <http://www.abs.gov.au/ausstats/abs@.nsf/mf/6401.0.55.003>, accessed on 11 July 2015.

Based on our consultations to date, we are recommending that the framework should adopt a cap based on the forecast rate of increase in the CPI for the year in question.⁶⁰ This approach appears to align with councils' current practices of estimating their annual budgets using their forward assumptions of CPI or some other relevant indices. We also recommend that the annual rate cap include forward indicative caps for the next two years to help councils in their strategic resource planning.⁶¹

The CPI forecast we are proposing to adopt is the measure produced by the Victorian Department of Treasury and Finance (DTF) which is published in May as part of the State Budget and it is updated in December. On each occasion, DTF releases its four year forecast of inflation. The CPI forecasts released by DTF are adjusted for volatile items making them more stable than the 'headline' rates of inflation typically reported in the media. We have reviewed the forecasts produced by DTF and found them to be reasonably accurate and unbiased (table 2.2).

⁶⁰ Most councils, the MAV and the RMA supported the use of a forecast rather than an historical index because a forecast aligns more with council budgeting and is more likely to reflect future needs.

⁶¹ Most councils, peak bodies, other council groups, ratepayers and ratepayer associations supported an annual rate cap which includes 3-4 years of indicative caps.

TABLE 2.2 CPI: AVERAGE PERCENTAGE CHANGE

Comparison of DTF's forecast and actual underlying CPI and the ABS's 'headline' CPI

Year	DTF's forecast CPI (average percentage change - financial year end) (per cent)	DTF's actual CPI (average percentage change - financial year end) (per cent)	ABS' headline CPI (average percentage change - financial year end) (per cent)
2010-11	3.00	3.00	3.28
2011-12	2.75	2.25	2.35
2012-13	2.75	2.25	2.20
2013-14	2.50	2.75	2.75
2014-15	1.75		
2015-16	2.75		
2016-17	2.75		
2017-18	2.50		
2018-19	2.50		

Data source: DTF (2015), *Victorian Budget 15/16 For Families: Budget Overview*, page 5 and DTF's spreadsheet on macroeconomic indicators, (<http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators>), Accessed on 17 July 2015.

REFINEMENTS TO THE RATE CAP

A number of councils, peak bodies and other council groups have argued that the rate cap should be refined to account for cost pressures that are beyond councils' control such as cost shifting, defined superannuation benefit shortfalls, reduced Government grants, new legislation, and infrastructure renewal. Some councils also provided us with information about their specific cost pressures. Given the timelines for this review, the Commission was not able to verify the full extent of the impact of these cost pressures on these councils, much less across all councils. It would be difficult to estimate an adjustment factor to account for these costs in the rate cap, and further work would need to be undertaken if this approach were considered appropriate.

Councils' current renewal gaps reflect their policies on investment and financing infrastructure renewal, which in turn were influenced by their communities' needs and their different financial circumstances. Given this, we do not consider a blanket adjustment factor to account for infrastructure renewal is justified. Infrastructure

renewal requirements should be considered on a per council basis and are more appropriately addressed as part of the variation process discussed in chapter 3 of volume II of this report.

Councils and their representative bodies have made repeated representation to the Commission that a cap based solely on changes in the CPI may unduly constrain their operations. Most councils, local government peak bodies, other council groups, unions, service providers and not-for-profit organisations argued that the cap on rate increases should exceed increases in the CPI. They argued that:

- the CPI does not accurately reflect increases in costs faced by local councils, because they have a significantly different composition of expenditure compared to households
- key council expenditures (wages, construction, utilities, others) required to provide council services have been increasing faster than the CPI (also because councils are absorbing the impacts of cost shifting)
- CPI tends to fluctuate in a way that is unrelated to the underlying costs of councils and therefore will introduce undesirable uncertainty
- capping rate increases at the rate of increase of the CPI may lead to most, if not all, councils applying for variations and compromise the variation process, or to job losses, reduced non-core services or a deterioration in the quality of community infrastructure over time.⁶²

They suggested that to refine the cap the Commission should consider applying MAV's local government cost index (LGCI); or developing a LGCI that accounts for changes in wages, construction costs, other operating costs or constructing a simple index of CPI and wages.⁶³

Conversely, most of the ratepayers and ratepayers' associations who responded to our consultation paper supported capping council rates at CPI. But a few acknowledged that the CPI may not be an appropriate index for local government related expenditure.

⁶² Individual submissions on the ESC's consultation paper by the Australian Services Union, Australian Nursing and Midwifery Federation and 2 ratepayers. The comment about cut-back on non-core services was made by the Dandenong Community Advisory Bureau and the Springvale Community Aid and Advisory Bureau in their submissions to the consultation paper.

⁶³ Other suggestions to refine the cap include: setting an upper limit increase of 5 per cent; considering the rate pegging approach in New South Wales (NSW); considering other indices such as ABS's Road and Bridges Construction Index, Wage Price Index (WPI), Average Weekly Earnings; and using the cap to reward those councils which have managed their finances responsibly.

Ratepayers Victoria supported capping rates at CPI but is concerned that 'productive work would be curtailed and the administrative work expanded'. It also pointed out that CPI may not be appropriate when dealing with council costs but 'it is appropriate to use when dealing with the capacity of a community to pay'.⁶⁴ One ratepayer rejected all form of rate capping because it might lead to deterioration in services and infrastructure.⁶⁵

The relatively high proportion of employee costs, and the relatively high rate of increase in those costs in recent years, across the local government sector appears to be the primary cause for capping rates at CPI. These claims are supported by the VGC's data.

Elsewhere in the economy, where prices are regulated, the price regulator will generally not concern itself with an individual service provider's costs of procuring services. Rather, benchmarks for the cost of acquiring those services will be used to inform price decisions. We accept that there are merits for adopting a similar approach within the rate capping and variation framework. On the basis of the evidence before us, we consider that any such refinements to the rate cap should be limited to councils' main source of concern, namely, labour costs.

Councils vary considerably in terms of the composition of their costs and the proportion comprising labour costs. Based on the VGC data, the unweighted average proportion that labour costs represent across the Victorian local government sector is around 40 per cent.⁶⁶ We therefore propose that this proportion be assigned to labour costs when constructing each year's rate cap. In other words, a 60 per cent weighting would be applied to the rate of increase in the CPI and a weighting of 40 per cent would be applied to the benchmark rate of increase in labour costs.

As with CPI, we propose adopting the Wage Price Index (WPI) increases reported by DTF as the benchmark rate for labour costs in the rates capping framework.

Table 2.3 shows the indicative increases in WPI based on DTF's forecasts in May 2015.

⁶⁴ Ratepayers Victoria 2015, *Submission to the ESC's consultation paper*, p.3, May.

⁶⁵ Nina Kelly (2015), *Submission to the ESC's consultation paper*, May.

⁶⁶ 37 per cent rounded up to 40 per cent.

TABLE 2.3 DTF'S FORECASTS OF THE RATE OF INCREASE IN THE WPI
per cent

	2015-16	2016-17	2017-18	2018-19
WPI forecast	3.25	3.5	3.5	3.5

EFFICIENCY FACTOR

While this proposed adjustment for labour accounts for the cost pressures facing local government, it does not address the 'cost of living' pressures faced by ratepayers. The standard approach to creating incentives for service providers to pursue efficiencies in their operations, and then share the benefits of those efficiencies with 'customers', is to impose an efficiency factor on those service providers. Known as the 'efficiency factor', this imposed efficiency requirement can vary significantly from sector to sector. For example, in our water pricing function we impose an efficiency factor of between 1-2 per cent, and for tow trucks pricing, an efficiency factor of as low as 0.5 per cent. The NSW rates capping regime adopts an efficiency factor of 0.04 per cent.⁶⁷

We believe there is merit in adopting an efficiency factor in the proposed rate capping and variation framework.⁶⁸ However, given that at the outset of the new framework councils will have locked in costs under contracts, we propose that the efficiency factor initially be set at zero increasing by 0.05 percentage points each year. We would propose to undertake a detailed productivity analysis of the sector to assess the appropriate long-term rate for the efficiency factor.

On the basis of these refinements, the annual rate cap would be given by:

$$\begin{aligned}
 \text{Annual Rate Cap} &= (0.6 \times \text{increase in CPI}) \\
 &+ (0.4 \times \text{increase in WPI}) \\
 &- (0 \text{ per cent efficiency factor})
 \end{aligned}$$

⁶⁷ Based on the 15-year average of the market sector value-added multi-factor productivity (based on quality-adjusted hours worked in December each year) estimate by the ABS (IPART (2014), Fact sheet - Rate peg for NSW councils for 2015/16. December and IPART (2014), Fact sheet — IPART cost indices — productivity factor, October.

⁶⁸ Views from the sector on the appropriateness of an efficiency factor were mixed. Manningham City council and some ratepayers and ratepayer associations suggested that the cap should include a 'productivity factor'. Moonee Valley City Council suggested that an efficiency measure may be introduced, but only after a transition. The Port Phillip City Council cautioned against the application of arbitrary and/or universal efficiency improvement targets because 'such targets may have unintended consequences, particularly if targets are implemented before councils' individual level of efficiency can be properly determined'.

Table 2.4 shows some indicative forecasts for the Annual Rate Cap (as at July 2015).

**TABLE 2.4 INDICATIVE FORECASTS FOR THE ANNUAL RATE CAP
(AS AT JULY 2015)**
per cent

	2016-17	2017-18	2018-19
Underlying CPI forecast (60 per cent weighting)	2.75	2.5	2.5
<i>Plus</i> WPI forecast (40 per cent weighting)	3.5	3.5	3.5
<i>Less</i> Efficiency factor	0	0.05	0.10
Forecast Annual Rate Cap	3.05	2.85	2.80

We considered that the additional complexity arising from a complex LGCI (similar to IPART's) is not warranted in the current circumstances.⁶⁹ The simplicity of MAV's LGCI measure has merit but we consider that the 80 per cent employee costs share is too high.

As already noted in section 2.1 and in the first part of section 2.4.1, we have not attempted to adjust the cap to account for structural differences between councils, for cost pressures councils are facing and for infrastructure renewal. We consider these matters will be more appropriately dealt with through the variation process described in chapter 3.

⁶⁹ IPART constructs sophisticated LGCI based on 26 cost components, with employee benefits having the largest share at 41 per cent of all costs. IPART uses a combination of indices which include the Labour Price Index, CPI and a range of producer price indices.

DRAFT RECOMMENDATION 4

The Commission recommends that the annual rate cap should be calculated as:

$$\begin{aligned}\text{Annual Rate Cap} &= (0.6 \times \text{increase in CPI}) \\ &+ (0.4 \times \text{increase in WPI}) \\ &- (\text{efficiency factor})\end{aligned}$$

With: CPI = DTF's forecast published in December each year

WPI = DTF's forecast published in December each year

The efficiency factor will initially be set at zero in 2016-17 but increasing by 0.05 percentage points each year from 2017-18. The Commission will undertake a detailed productivity analysis of the sector to assess the appropriate long-term rate for the efficiency factor.

2.5 WHAT SHOULD THE BASE YEAR FOR SETTING THE CAP?

2.5.1 STAKEHOLDERS' FEEDBACK

Most councils, two peak bodies, a council group and a ratepayers association suggested that the starting revenue base for 2016-17 should be the 2015-16 budgeted rates and charges revenue. They argued that 2015-16 budgets include commitments and projects already underway and the consultation they had undertaken on their four year strategic resource plans.

2.5.2 DISCUSSION/ANALYSIS

Our preliminary view is that we will adopt the 2015-16 revenue from general rates and municipal charges as the starting base for 2016-17 and treat all councils similarly. The Minister for Local Government has previously warned councils that any significant increases in 2015-16 may affect a council's application for a variation in 2016-17. This issue is discussed in more detail in chapter 3 (variation process).

DRAFT RECOMMENDATION 5

The Commission recommends that the 2015-16 rates (general rates and municipal charges) levied on an average property should be adopted as the starting base for 2016-17.

2.6 WHAT INFORMATION SHOULD BE REQUIRED EACH YEAR?

As noted in section 2.4 above, in May and December each year the Commission will publish updated forecasts for the annual rate cap as shown in table 2.4. The December forecast would be the binding cap for the following financial year, irrespective of any updated figures published by DTF the following May.

In order to support the rates capping framework, the Commission will collect information from councils each year. We will create a working group composed of council representatives to develop the specific information we will collect from councils annually to support the proposed rate capping framework.

Our initial considerations of this information are discussed in chapter 4 of volume II of this report.

2.7 SHOULD THERE BE GREATER COST REFLECTIVITY IN SOME COUNCIL RATES AND CHARGES?

In section 2.2, we propose that service rates and charges be excluded from the rate cap on the basis of councils' claims that these charges are set on a cost reflective basis. We have not tested these claims. However, we note that, whereas the Act requires that special rates and charges must be cost reflective, there is no corresponding obligation on service rates and charges. The relevant legislation in NSW requires that waste related charges are not to exceed the reasonable cost of providing the services and that general rates must not be used to fund the cost of providing waste management services.

If service rates and charges are to be excluded from the cap, we believe there is merit in the Government reviewing the Act's provisions regarding service rates and charges

to require that these charges must reflect the efficient costs of providing the underlying service.

In some cases, fees associated with statutory services provided by councils (for example, planning fees) are regulated by the Government. It is not necessarily clear how these fees are determined and some have remained unchanged for a number of years. These fees would not be covered by the rate cap.

Following the introduction of the rates capping framework, we consider that councils should be able to recover the efficient costs of providing these statutory services. There is merit in periodically reviewing fees for statutory services to ensure they reflect the efficient cost of providing those services.

MATTERS FOR FURTHER CONSIDERATION

The Commission recommends that the Government consider amending the *Local Government Act 1989* to require that service rates and charges must reflect the efficient costs of providing the underlying service.

The Commission recommends that the Government consider initiating a periodic review to ensure that statutory fees continue to reflect councils' efficient cost of providing statutory services.

3 VARIATION

3.1 WHAT ARE WE REQUIRED TO DO?

This chapter outlines the terms of reference, submissions, research and analysis that has informed the Commission's draft recommendations with respect to the variation component of the rates capping and variation framework.

The terms of reference ask the Commission to ensure that the variation framework:

- provides a mechanism through which councils can justify any proposed increase above the cap
- takes into account factors that impact on local governments' short and long-term financial outlooks and
- specifies any technical requirements (including information requirements) on councils that request exemptions from the cap.

A well-designed variation process will play an important role in ensuring the framework is able to deliver on the policy objectives of the Government. In chapter 2 we describe how it is not practical to design a rate cap that takes into account the diversity, different needs and different legacies faced by individual councils. Nevertheless, the increase permitted by the rate cap represents the annual additional revenue requirement typically expected for councils on a state-wide basis. Some councils may consider this additional revenue insufficient in light of their particular circumstances. A variation process provides a mechanism for individual councils to seek a rate increase in excess of the cap.

The budget pressures facing councils are many. Priorities change over time. New services are introduced, while other services are expanded or discontinued. New infrastructure is built and existing infrastructure needs to be maintained. Revenues fluctuate either because of economic circumstances or following policy decisions by other levels of government. And, on occasion, natural disasters happen.

Sometimes budget pressures will arise due to a specific or one-off expenditure requirement. At other times, budgets will struggle with more generalised cost pressures.

The variation process needs to accommodate different sources of cost pressures and it should be able to respond flexibly in different situations. Likewise, councils should be expected to assess all their options before seeking a rate variation. If this were not the case, the rate cap and variation process would be of little benefit.

When faced with budget pressures, councils can pursue one or more of the following strategies; and the preferred response is likely to depend on the source of the budget pressure and whether it is momentary or structural. The four broad options facing councils include:

- scrutinising the full suite of their operations and planned investments for opportunities to deliver outcomes more efficiently
- ensuring the range of services they are delivering align with their community's highest priorities
- assessing the possibility and merits of alternative funding or financing options for different activities and investments and
- increasing their revenues through higher rates and charges.

The role of representative councils with delegated responsibilities from, and accountable to their communities, is to assess how best to manage the trade-offs between these four options. This responsibility rests inherently with local government. A well-designed variation process will not shift this responsibility away from councils — rather, by promoting transparency and engagement, a variation framework ensures all options are canvassed before rate increases (above the cap) are pursued.

Councils, in demonstrating that there is a justifiable basis to seek a variation, should primarily focus on what positive impacts the above cap increase will have on services, infrastructure and financial outcomes (or what the negative impacts on services, infrastructure and financial outcomes will be if the council is constrained by the cap). Importantly, the major trade-offs between these outcomes should be transparent and councils should have consulted with their communities.

A well-designed variation process should:

- support the autonomy of councils to make decisions in the best interests of their communities
- increase the transparency of council decisions for the community
- complement the cap component of the framework by addressing individual council needs if the cap proves to be overly constraining
- reinforce financial discipline by requiring a council to be transparent in applying for a variation assessed by an independent regulator
- require from councils good information on impacts of cost changes on services, infrastructure and councils' financial sustainability
- require information in proportion to the magnitude of proposed variations above the cap and
- over time, be able to 'reward' those councils that have a proven track record of performance and effective community consultation, with a more 'streamlined' process.

In designing the variation process, the Commission has also sought to ensure that any information requirement:

- can be sourced from existing information databases to avoid imposing another layer of reporting burden
- is aimed at facilitating the assessment process for the benefit of the council and
- creates the right mix of incentives to encourage greater transparency and accountability, efficiency and sustainability.

The Commission is cognisant of the capacity required to seek a variation which could prove challenging for some councils. The Commission intends to assist in this capacity building in the 2016-17 transition year.

This chapter discusses the Commission's draft advice on the following key elements of the variation framework:

- When can councils seek a variation?
- How would a council demonstrate the need for a variation above the rate cap?
- How will the variation process work?

3.2 WHEN CAN COUNCILS SEEK A VARIATION?

This section considers the circumstances that could justify a council seeking a variation from the cap.

3.2.1 BACKGROUND

A key component of the variation framework will be the limits or guidance the Commission puts in place on the circumstances that may justify a variation. The Terms of reference requires us to ensure that a range of events could be accommodated by the variation framework.

3.2.2 STAKEHOLDERS' FEEDBACK

Many councils argued that a list of events that could justify a variation would be unlikely to capture all the relevant variation circumstances and that if good consultation were undertaken, any variation should be justified:

*there should be no defined list.*⁷⁰

*...in providing an exhaustive list of circumstances there will always be an exception. For this reason the circumstances concept should be broad and allow scope for the community to accept or request a variation for any circumstance that the community and council deem necessary.*⁷¹

Where submissions listed specific reasons for possible variations, they focussed on factors outside of councils' control such as the loss of a source of revenue, natural disasters, demographic changes, and superannuation requirements. The broad range of submissions on this question included lists of suggested circumstances for a variation.

⁷⁰ Golden Plains Shire Council 2015, *Submission to the ESC's consultation paper*, May.

⁷¹ Bass Coast Shire Council 2015, *Submission to the ESC's consultation paper*, May.

Typical of submissions from ratepayers groups, the Mornington Peninsula Ratepayers' and Residents' Association stated councils:

- should have to fully justify any variation
- should not be able to subvert the rate cap by unnecessarily increasing borrowings and
- should issue Annual Rates Notices highlighting special charges and indicate when they will cease.

Community groups, service providers and unions did not want the variation process to be too onerous and prevent justified increases to the cap.

3.2.3 DISCUSSION/ANALYSIS

We consider that embedding a list of predetermined triggers (including events) in the rates capping and variation framework would be counterproductive. We propose not to define triggers that would qualify for a variation because:

- in general terms, we consider councils and ratepayers are best placed to decide whether circumstances warrant applying for a variation
- there is no self-evident list of triggers, so any attempt to produce such a list is likely to be a distraction
- disputes are likely to arise about whether particular circumstances conform with the wording of the triggers
- we expect that very few situations will involve single and easily identifiable events that displace all other options
- we believe that situations involving sudden and genuine budget emergencies will be self-evident and that all relevant parties will have a strong incentive to cooperate on quickly identifying a solution and
- we prefer to keep the rules of the framework as simple as possible to make it easy to understand and to avoid a legalistic process.

We also consider there are no circumstances under which councils should be prohibited from seeking a rate variation above the cap. In other words, we do not propose to define situations where a council's application for a variation would be automatically accepted or automatically rejected. We consider that councils should

always have the opportunity to apply for a variation and that each application should be assessed on its merits.

That said, we are likely to have an unfavourable disposition towards applications for higher rates due to unbudgeted increases in controllable costs in the past year (more commonly known as 'cost blow outs').

How we would propose to assess applications is discussed in the following section where we present guidance for councils seeking a variation. When developing this guidance we considered the events listed in the terms of reference to ensure that our framework would allow those events to be considered for a variation.

The items in the terms of reference are:

- actual and projected population growth and any particular service and infrastructure needs
- any relevant Commonwealth Government cuts to local government grants
- any additional taxes, levies or increased statutory responsibilities of local governments as required by the State or Commonwealth Governments
- any extraordinary circumstances (such as natural disasters)
- other sources of income available to councils (for example, ability to raise user fees and charges from non-residents).

Population growth and associated service and infrastructure needs is an obvious factor that could lead to a successful variation application. The Commission would look for evidence of, and robust estimates of, future growth when considering a variation application. Also relevant would be estimates of new sources of income derived from an increasing population such as increases in rates revenue and fees for services. The Commission recognises that some councils cover areas of high population growth and that this could be a likely cause of variation applications.

Changes in grants from the Commonwealth would be recognised in the framework. The key factor the Commission would examine in a variation application based on a change in grant levels would be the extent of engagement with the community undertaken and the options put to the community in terms of increases in rates (or charges) and reductions in service levels.

Additional responsibilities or charges from other levels of government would be recognised by the framework. A variation application based on these responsibilities or charges would require a clear statement of the additional obligations imposed and their costs. If the responsibilities are mandatory then consultation with ratepayers and the community would be necessary on how the burden would be spread between increases in charges or reductions in service. If the responsibilities are voluntary, whether to take them on would first need to be considered.

Extraordinary circumstances such as disasters are accommodated under the framework. Councils could seek a rate variation to recover the efficient costs of dealing with unforeseen events. The amount to be applied for a variation should be net of the funds already received by the council from the Department of Treasury and Finance (DTF) Natural Disaster Financial Assistance and the Victoria Grant Commission's (VGC) Natural Disaster Relief. The framework also allows councils to include reasonable and efficient steps to deal with future disasters through insurance and disaster preparedness.

Revenue other than rates or charges to ratepayers is considered in the Commission's framework and changes to these other sources of revenue available to councils would be considered as a valid justification for a variation.

As a guiding principle, councils should only require an increase in rates above the cap when long run operating revenue is insufficient to offset long run operating expenses. Councils' financial indicator targets will indicate when this is likely. Under this principle there are four main scenarios where a council would seek an increase in rate revenue beyond the set cap. These are to:

- meet high upfront outlays for major new capital or asset renewal projects, where it is unable to increase borrowings (without a detrimental long run impact on its financial sustainability)
- meet additional recurrent operational expenditure for a permanent increase in service levels consistent with community demand
- meet a one-off increase in operational expenditure (e.g. associated with a non-controllable event), where it is appropriate to recover costs from the current ratepayer base or
- address an existing operating deficit which will mean the council is unable to renew assets and/or maintain services over the long-term.

DRAFT RECOMMENDATION 6

The Commission recommends that the framework should not specify individual events that would qualify for a variation. The discretion to apply for a variation should remain with councils.

3.3 HOW WOULD A COUNCIL DEMONSTRATE THE NEED FOR A VARIATION ABOVE THE RATE CAP?

This section considers what would be required for a variation application to succeed, and the variation framework's information requirements.

3.3.1 BACKGROUND

The terms of reference requires the Commission to specify any technical requirements for councils that request variations from the cap.

In our consultation paper we included the following possible set of criteria for a successful variation application:

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

3.3.2 STAKEHOLDERS' FEEDBACK

There was broad agreement with the suggestions in our consultation paper, for example:

The list of requirements appear to be appropriate subject to clear definitions of effectively, reasonable and legitimate.⁷²

Proposed list is appropriate. Key is to have low cost, simple process. Requirements must be well defined — what does effective, reasonable, legitimate mean.⁷³

3.3.3 DISCUSSION/ANALYSIS

There are many reasons a council might consider applying for a variation. Even when we face two applications for seemingly similar reasons, we expect they will differ on the facts when scrutinised more closely. This suggests that different information will probably be required for the purposes of assessing each application. This makes it impossible to establish a single set of information requirements that would be required to accompany each application for a variation. This also suggests that if we attempted to establish a single list of requirements it would probably impose irrelevant (and costly) obligations on most councils seeking a variation.

A more accommodating and flexible approach involves providing guidance to councils on the subject matter areas that will need to be considered when an application for a variation above the cap is being assessed. We propose the following five matters (developed after consideration of submissions on our consultation paper) would need to be addressed in each application:

- **The reason for a rate increase greater than the cap.** The reason for the variation will need to be articulated clearly and the amounts involved will need to be quantified. Reasons could include: changes in costs, a change in asset management, or a change in the services that councils are required to provide. These claims would need to be substantiated.

⁷² Whittlesea City Council 2015, *Submission to the ESC's consultation paper*, May.

⁷³ Moreland City Council 2015, *Submission to the ESC's consultation paper*, May.

- **The application takes account of ratepayers' and communities' views.** The application would need to demonstrate that the views of ratepayers and communities have been identified and describe how their concerns have been addressed. This consultation will need to include the presentation of other realistic options for meeting the funding need, and the trade-offs those options would entail. Importantly, applications will need to account for ratepayers' views on specific expenditure items or cost pressures (where relevant) as well as their impact on the council's overall budget position.

The Commission will not prescribe how councils ought to engage with their communities. Such decisions naturally sit with councils rather than the Commission. Nevertheless, we have developed a set of four key engagement principles which we expect to be reflected in the engagement undertaken in support of an application for variation (see table 3.1).

- **The variation represents good value for money and is an efficient response to the need.** This means that, where additional expenditure is involved, any amount proposed to be recovered through higher rates should represent a good value option for achieving the desired outcome. It would be helpful to submit business cases or cost-benefit analyses where higher rates are being proposed in order to fund the delivery of new or expanded services, or new infrastructure.
- **Service priorities and funding options have been considered.** The application will need to demonstrate that councils have considered reprioritising funding from other areas of expenditure; and the reasons for not proceeding with that reprioritisation (in part or in whole). The application will need to demonstrate whether other suitable funding or financing options have been considered and the decision (and reasoning) reached in relation to those options.
- **The proposal is integrated into the council's long-term strategy.** The matters giving rise to the variation application should be consistently represented and addressed in all of the council's relevant planning instruments — for example: its Council Plan and Asset Management Plan.

In table 3.2, we provide guidance on how we would expect councils to address these five subject matter areas in their applications for a variation. Under each heading, the table sets out:

- questions that councils should ask about whether they require a variation, and if so, what form the proposed variation might take

- actions councils should take when they develop a variation application and
- evidence that councils should provide in their variation applications.

Table 3.2 is for guidance only and the ultimate information requirements will depend on the type of variation sought by councils. Councils will be responsible for providing sufficient information to justify a variation application.

Detailed guidance on how councils could undertake community engagement to take account of ratepayers' and communities' views is provided in Appendix C.

TABLE 3.1 RATEPAYER AND COMMUNITY ENGAGEMENT PRINCIPLES

Principles	
Principle 1	The engagement program must contain clear, accessible and comprehensive information and follow a timely process to engender feedback from the community
Principle 2	The engagement program should be ongoing and tailored to community needs
Principle 3	The engagement program should prioritise matters of significance and impact
Principle 4	The engagement program should lead to communities becoming more informed about council decision-making

TABLE 3.2 QUESTIONS, ACTIONS AND EVIDENCE FOR A VARIATION APPLICATION

Why the Commission needs this information	Questions	Actions	Evidence
The reason a variation from the cap is required			
We need to establish whether there is a need for a rate increase greater than the cap.	<ul style="list-style-type: none"> • What is the underlying driver of the need for an increase in rates above the prescribed cap? • Is the proposed rate increase consistent with the council's revenue strategy and policy on funding and financing? • Has the council taken into account the effects of price shock, and whether a staggered increase in rates would be more appropriate? • Has the council considered spreading the funding needs over time by raising the additional expenditure through borrowings and/or by using existing financial assets; or through user charges, rather than general rates? 	<ul style="list-style-type: none"> • Identify the need for additional revenue. (Is it necessary to meet short-run cash flow needs and/or long-run operating capability?) • Estimate the additional revenue that is required, above the rate cap. • Determine whether the additional revenue requirements are ongoing or temporary. <p>Review the council's policies and practices:</p> <ul style="list-style-type: none"> • revenue raising mix (e.g. taxes and user charges); • revenue target; and • role and use of debt. 	<ul style="list-style-type: none"> • Documents identifying the cause of the variation. • Documents justifying the costs associated with the cause of the variation. • Financial statements showing the council's financial performance and position for previous period.^a • Budgeted financial statements for current period.^a • A strategic resource plan and asset management and long-term financial plans. <p>Documented policies and strategies regarding:</p> <ul style="list-style-type: none"> • mix of own-source revenue-raising; and • funding and financing (role of debt).

^a This may be demonstrated through the baseline information (see Appendix D in Volume II).

Continued next page

TABLE 3.2 (CONTINUED)

Why the Commission needs this information	Questions	Actions	Evidence
The application takes account of ratepayers' and communities' views			
We want to be sure that ratepayers and communities are aware of the variation and that their views have been considered. The Commission provides detailed guidance on community engagement in Appendix C.	<p>All variation applications:</p> <ul style="list-style-type: none"> • How has the council engaged with its ratepayers and communities on the requested rate increase? • What information was provided to ratepayers and community members during the engagement? • How has the engagement impacted the council's decision to seek a rate increase? • Is a rate increase the preferred option of the community? • Have the Commission's four key engagement principles been incorporated into the engagement? <p>Major new projects/material increases in service levels:</p> <ul style="list-style-type: none"> • Has the community been consulted on the proposal including the implications for the council's overall costs and revenue needs? <p>Asset management:</p> <ul style="list-style-type: none"> • Are asset management activities within community expectations and willingness/capacity to pay? • Are asset management expenditure projections based on reasonable and affordable service levels? 	<ul style="list-style-type: none"> • Assess extent of engagement with ratepayers and the community on the options available and justification for the council's proposed option. • Review modelling of financial impacts on asset management need projections with various options in service level specifications from assets. 	<ul style="list-style-type: none"> • A document setting out the council's consultation/engagement processes with ratepayers and communities including how the council gathers, records and incorporates the views gathered. This should include the council's rating strategy. • Information on results of past consultation/engagement relevant to the variation application. • Information on the engagement consultation on the current variation application. • Documented evidence of engagement/ consultation with the community and community satisfaction with the proposed variation. • Evidence of modelling of the financial impacts of asset management needs, including options for varying service level specifications.

Continued next page

TABLE 3.2 (CONTINUED)

Why the Commission needs this information	Questions	Actions	Evidence
The variation represents good value-for-money and is an efficient response to the need			
We want to ensure that the change in costs or services proposed by a council represents good value for ratepayers.	<ul style="list-style-type: none"> • Have sound processes to cost the expenditure been undertaken? • Are there benchmarks from the past or outside the council that demonstrate that costs are appropriate? 	<ul style="list-style-type: none"> • Examine processes to ensure optimal cost/service outcomes when costing capital and operational work. • Gather material that can demonstrate that the variation application is funding items that are fit for purpose and the lowest cost for the selected level of service. 	<ul style="list-style-type: none"> • Information on how the costs that led to the variation were incurred including tender documents if relevant.
Service priorities and funding options have been considered			
We want to know that councils have considered the prioritisation of services and different funding options before seeking a variation. ^a	<ul style="list-style-type: none"> • Why are the existing cost bases increasing? • What other funding options have been considered in addition to a rate increase? • What steps have been pursued to meet preferred expenditure through productivity and efficiency improvements? • Is it appropriate to raise rate revenue rather than reduce other service levels to meet priority needs? • Is the council satisfied the asset management expenditure projections are based on soundly based (cost-effective and timely) treatments for specified service levels? 	<ul style="list-style-type: none"> • Identify drivers of the need for additional revenue. Are they controllable or non-controllable? • Identify all funding options to deal with the new spending priority. • Identify results from productivity and efficiency improvement programs. 	<ul style="list-style-type: none"> • Information showing how the council has considered the possible reprioritisation of services. • Information showing consideration of differing funding options. • Information on councils' processes for seeking efficiencies and information on efficiencies used to offset increases in costs that have led to the variation. • Information showing drivers of cost increases and the extent to which they are non-controllable. • Community survey results showing preference for rate increases relative to service level reductions. • Evidence in asset management plan of rationale for timing and extent of projected asset management outlays (e.g. to minimise whole of lifecycle costs).
The proposal is integrated in the council's long-term strategy			
We want to ensure a proposed variation has been incorporated into a council's plans.	<ul style="list-style-type: none"> • Does the council have an up-to-date Strategic Resource Plan, Asset Management Plan and financial plan? • Is the proposed rate increase consistent with those documents? 	<ul style="list-style-type: none"> • Review the council's Strategic Resource Plan. • Confirm whether the need for additional revenue is identified in the Strategic Resource Plan. 	<ul style="list-style-type: none"> • Demonstrate the variation application is consistent with the council's Strategic Resource Plan and long-term asset management and financial plans.

DRAFT RECOMMENDATION 7

The Commission recommends that the following five matters be addressed in each application for a variation:

- The reason a variation from the cap is required
- The application takes account of ratepayers' and communities' views
- The variation represents good value-for-money and is an efficient response to the budgeting need
- Service priorities and funding options have been considered
- The proposal is integrated into the council's long-term strategy.

3.4 HOW WILL THE VARIATION PROCESS WORK?

3.4.1 WHAT IS THE TIMELINE FOR A VARIATION APPLICATION?

The Commission is required to develop a variation framework that aligns with councils' budgetary and planning processes. The variation framework should allow councils to continue with their existing work schedules without disruption, while at the same time enabling the Commission to robustly assess councils' applications for a variation from the cap.

STAKEHOLDERS FEEDBACK

Many council submissions stated that the variation process should fit with councils' existing planning and budgetary processes. For example:

The timing of any variation process must also work within Councils' budget and planning cycles, and not cause unnecessary delay on the finalisation of annual budgets and rate setting.⁷⁴

⁷⁴ Knox City Council 2015, *Submission to the ESC's consultation paper*, May.

DISCUSSION/ANALYSIS

We have considered various options regarding when councils could apply for a variation. There are several options regarding the possible timing of variation applications.

The first is a fixed annual process for variation of rates. This is the proposal we recommend. A fixed process would provide certainty about the timing for variations and enable councils to continue with their annual planning and budgeting processes. A disadvantage is that costs outside councils' control may arise after rates have been set which would mean the cap might not provide sufficient revenue for councils. To remedy this, we propose that substantial uncontrollable changes in costs in a previous year could be applied for in the following year's variation process.

The second option is to allow councils to apply for variations at any time during the year, in response to unexpected costs. This would remove the need for us to examine distant past costs when considering variations. The difficulties with this option are the unpredictable workload and timing for councils and the Commission. On balance we decided against this option in order to provide for a certain and regular application process.

In developing a timetable for the framework we have sought to:

- provide time for councils to prepare for a variation following the announcement of the cap
- provide time for the Commission to properly consider variation applications and
- fit into the existing timelines for councils' budgetary and planning processes.

Table 3.3 sets out a proposed timeline for next year's capping and variation process.

TABLE 3.3 PROPOSED TIMELINES FOR 2016-17 RATING YEAR

	2015-16
ESC announces cap	December 2015
All councils submit baseline data (budget)	January 2016
Councils notify ESC of intention to seek a variation	January 2016
Council applies for variation, submits baseline data (budget)	March 2016
ESC assesses council variation applications	March-May 2016
ESC notifies councils of decisions	May 2016
Councils consult on draft budget	May 2016
Councils formally adopt budget	June 2016

Another option could involve shifting the beginning and end of the variation process two months later to provide councils with more time for their planning and consultation. This would however, require a later adoption of budgets (say, in August).

3.5 SINGLE OR MULTI-YEAR VARIATION?

3.5.1 BACKGROUND

The terms of reference requires the Commission to ensure that the proposed variation framework takes into account factors that may impact on local governments' short and longer term financial outlooks. This raises the question of whether variations from the cap will be for a single year or for multiple years. Within this question is the other matter of whether variations will always be permanent and if not, how would a variation be finalised once its time period had expired.

3.5.2 STAKEHOLDERS' FEEDBACK

Many council submissions to our consultation paper supported multi-year variations. This was mainly to support councils' longer-term planning and provide them with certainty regarding their revenues, particularly with regard to longer term investments. Many submissions also argued that multi-year variations would reduce regulatory costs for the industry, with fewer variation applications required.

Some submissions argued that variations should not necessarily be permanent and should expire once the need for the variation had passed:

*‘ensure Councils have to justify increase; any such increase should have a ‘sunset clause’.*⁷⁵ City of Glen Eira

3.5.3 DISCUSSION / ANALYSIS

In principle we support the idea of multi-year caps, which could provide councils with revenue certainty over longer periods of time and would reduce the costs associated with more regular applications.

At this initial stage of operation of the variation framework, we think it would be prudent to ensure that single year caps are functioning smoothly before we introduce multi-year caps.

We propose that in the framework’s first year of implementation, the Commission should only be authorised to approve variations for one year. Thereafter, councils should be permitted to submit, and the Commission approve, variations of the length shown in table 3.4. In other words, the length of permissible variations increases as councils and ratepayers become more familiar with the framework. Councils could still apply for shorter variations than the maximum shown in table 3.4. The Commission could be asked to review this timetable for phasing in the variation process after 2-3 years.

TABLE 3.4 MAXIMUM LENGTHS OF VARIATION

First year of variation	Length of permissible variation
2016-17	One year (i.e. 2016-17 <u>only</u>)
2017-18	Up to two years (i.e. 2017-18 only <u>or</u> 2017-18 and 2018-19)
2018-19	Up to three years (i.e. <u>up to</u> 30 June 2021)
2019-20 and beyond	Up to four years (i.e. <u>up to</u> 30 June 2023)

⁷⁵ Glen Eira City Council 2015, *Submission to the ESC’s consultation paper*, May.

We also propose to allow councils to apply for temporary and permanent variations from the cap.

A temporary variation would enable a council to increase its rates above the rate cap for one year. After that one year, rates would be reduced to the level they would have been if the council had been granted the default rate cap one year earlier. A temporary rate cap increase would enable councils to address costs that arise once and were not expected to recur. An example of this type of expense might be a one-off levy by a council to pay for recovery from a natural disaster.

A permanent variation would enable a council to increase its rates above the cap and retain that increase into the future. This might apply to a new recurring cost. An example of this might be a variation to account for a permanent charge levied on councils by another level of government.

DRAFT RECOMMENDATION 8

The Commission recommends that in 2016-17, variations for only one year be permitted. Thereafter, councils should be permitted to submit and the Commission approve, variations of the length set out below.

First year of variation	Length of permissible variation
2016-17	One year (i.e. 2016-17 only)
2017-18	Up to two years (i.e. 2017-18 only or 2017-18 and 2018-19)
2018-19	Up to three years (i.e. up to 30 June 2021)
2019-20 and beyond	Up to four years (i.e. up to 30 June 2023)

3.6 WHO MAKES THE DECISION?

3.6.1 BACKGROUND

The terms of reference requires the Commission to make clear:

the role of councils, the ESC and the Victorian Government in the framework. The key component of this is who makes the decision to approve or reject a variation application.

3.6.2 STAKEHOLDERS' FEEDBACK

Most submissions suggested the Commission should be the decision maker for the variation framework:

*it is recommended that the Commission play a dual role and undertake both advisory and determinative roles at least in the early stages of the new policy. In assessing applications, it should be resourced to provide feedback to councils on the development of their rate variation applications in the initial phase until sufficient applications have been deliberated on by the Commission and the approach taken is well understood...*⁷⁶

Some submissions suggested the Minister should be the decision maker:

*Council considers that the role of the Commission is advisory only. The Minister for Local Government should issue a Ministerial Direction and Order in Council as appropriate.*⁷⁷

Some submissions suggested an appeal process should be available to councils:

*incorporate an independent appeal or review process for rejected applications*⁷⁸

⁷⁶ Rural Councils Victoria 2015, *Submission to the ESC's consultation paper*, May.

⁷⁷ Moonee Valley City Council 2015, *Submission to the ESC's consultation paper*, May.

⁷⁸ Manningham City Council 2015, *Submission to the ESC's consultation paper*, May.

3.6.3 DISCUSSION / ANALYSIS

DECISION MAKER

Some submitters suggested the Commission should only have a role in advising councils on whether their proposed variation is appropriate (leaving councils to decide whether to proceed with the increase). Such a light-handed approach does not appear consistent with the regime envisaged in the terms of reference or in public statements made by the Government.

We consider there are three viable options for who administers the rate variation process. Of course, there are variations on each option.

The first option would involve the Minister for Local Government being responsible for considering each application and deciding whether to approve the application. Under this option, the Minister could seek the advice of her department in relation to each application. The second option is similar to the first but the Commission would be responsible for independently advising the Minister on the appropriate response to each application. Under the third option, the Commission, as an independent and standalone authority, would be responsible for assessing and determining the response to all applications. The Commission could be given this authority directly or under delegation from the Minister.

Public statements from the Government suggest that the third option is preferred.

WHAT DECISIONS SHOULD BE MADE IN RESPONSE TO AN APPLICATION FOR A VARIATION?

If an application for variation were considered and rejected by the Commission, the Commission could:

- only accept or reject an application for variation. In this option, if an application were rejected, the Council's rate increase would be the cap increase for that year
- reject a council's variation application and approve an alternative rates change which the Commission thought appropriate.

Where the Commission determines an application justifies the need for the proposed rate variation, it would simply approve the proposal. However, we expect that some applications will not justify the rate increase they seek. In such situations, we

recommend the Commission only be given the power to reject the application (in which case, the council would be bound by the rate cap).

We do not recommend the Commission be given the power to substitute an alternative rate increase to the one proposed. Nor do we suggest the Commission be given the power to negotiate with the council on an alternative rate increase. Such powers are occasionally given to bodies such as the Commission. In those instances, the regulator collects detailed information about the costs and revenues of the businesses being regulated (and develops detailed financial models of those businesses). We have not considered such a resource intensive approach when designing the rate capping and variation framework outlined in this draft report. These more intrusive options could be considered at a later date if required.

HOW DIFFICULT WILL IT BE TO HAVE A VARIATION APPROVED?

As already noted, we consider each application should be assessed on its merits. In conducting that assessment, it is incumbent upon the Commission to outline its expectations in advance (table 3.2 begins this process). Nonetheless, some degree of judgement will unavoidably need to be exercised by the Commission when assessing how well an application meets those expectations.

In exercising that judgement, we must strike a balance between being too lenient and being too restrictive. Ratepayers would soon lose confidence in the framework's capacity to promote discipline and transparency in the rate setting process if the Commission systematically erred in favour of councils. Conversely, an approach that consistently erred against councils could lead to perverse outcomes and communities could become disillusioned if their councils were prevented from providing sought after services.

All things being equal, we do not expect a large number of applications each year. We will expect however, that when we receive an application, it should reflect a situation of genuine need and it will demonstrate that need rigorously. If these expectations are not met, and if through the variation processes the Commission finds itself routinely becoming involved in councils' rating decisions, we risk becoming a de facto regulator of the local government sector. Such an outcome would be contrary to the autonomy of councils — which is something we have endeavoured to preserve in designing the proposed framework.

CONSULTATION

We propose not to invite public consultation on variation applications. Given that part of the Commission's assessment of variations is councils' consultation with ratepayers, additional consultation would be redundant and might be seen as the Commission placing itself between councils and their ratepayers.

However, the Commission could benefit from submissions on councils' application processes. As part of its variation assessment process, the NSW regulator, Independent Pricing and Regulatory Tribunal (IPART), considers submissions from interested groups or individual ratepayers for up to 4 weeks after the deadline for council variation applications. It does not solicit submissions and does not hold public hearings.

While we do not propose to invite submissions from the public, we will consider submissions that are made.

APPEAL

There is an option for the framework to include a merits review of the Commission's decisions. A merits review would enable a council to have its application re-examined by another body if its application were rejected by the Commission.

With or without a merits review, all the Commission's decisions on variations would be open to judicial review. This means that if the Commission did not give a council a fair hearing on its variation application or made an error of law, the decision could be appealed.

Our view is that a merits appeal process should not be part of the framework. The reasons for this are:

- there is already scope for judicial review, which is a reasonable safeguard
- a merits appeal process would add to the time taken and cost of the framework within an already constrained time period
- another agency re-examining the reasons for a variation after the Commission, would not guarantee an improved decision given the necessary expertise involved in assessments of pricing and
- merits review could lead to additional uncertainty in the framework.

In some other regulatory frameworks where merits review has been allowed, a litigious process has developed and the merits review process has been used as an opportunity to game the framework rather than provide a legal discipline.

DRAFT RECOMMENDATION 9

The Commission recommends that it should be the decision-maker under the framework, but only be empowered to accept or reject (and not to vary) an application for variation.

4 MONITORING AND REPORTING

This chapter outlines the key considerations, research, rationale and recommendations for the monitoring and reporting component of the rates capping framework. The chapter first discusses why the Commission considers monitoring and reporting to be a critical third element of the framework, including the key objectives, stakeholders' feedback, and the potential unintended outcomes the monitoring regime will seek to detect. Section 4.2 assesses the current data available for monitoring and identifies the limitations and gaps that will impact on the capacity of the Commission to monitor the performance of the sector under the framework. Sections 4.3 to 4.6 lay out the options considered by the Commission in designing the monitoring regime, the draft recommendations and the supporting rationale. Section 4.7 outlines the recommended reporting obligations of the Commission in relation to the framework.

4.1 WHAT ARE WE REQUIRED TO DO?

TERMS OF REFERENCE

The terms of reference request the Commission to consider:

- TOR 5 *...how local governments should continue to manage their overall finances on a sustainable basis, including any ongoing monitoring of council service and performance to ensure that any deterioration in the level, quality or sustainability of services and infrastructure and councils' financial position is identified and addressed promptly.*
- TOR 6(d) *any benchmarking or assessment of the effectiveness of the regime, including options to continuously refine the regime and improve council efficiency.*

4.1.1 WHY IS A MONITORING AND REPORTING REGIME IMPORTANT?

Good policy design should always include mechanisms that allow for ongoing monitoring, evaluation and reporting of the impact of the policy and its effectiveness in delivering on the stated objectives.⁷⁹ The Commission considers monitoring and reporting to be a key third element of the rates capping and variation framework that is essential for its long-term success.

Monitoring and reporting should support the integrity of the framework by verifying that local governments are adhering to the rate cap or any conditions of an approved variation above the cap.

Monitoring and reporting should provide timely and credible information about, and a means to assess, the impact of the framework on the sector and its effectiveness in meeting the policy objectives. Crucially, monitoring should also provide an important safeguard against unintended outcomes.⁸⁰ Embedding ongoing monitoring into the design of the framework creates a feedback loop that will allow for continual refinements to the framework over time.

Without a monitoring regime the procedural arrangements of the rates capping and variation processes can remain disconnected from the 'real world' outcomes experienced by ratepayers and communities in their daily lives. Public reporting of these outcomes allows ratepayers to verify the linkages between the rates they pay and the outcomes they observe. In other words, a well-designed monitoring and reporting regime can assist ratepayers to test the value-for-money delivered by their councils as well as how this might change. It can also provide ratepayers with the opportunity to compare their council with other councils in the delivery of value-for-money.

Finally, it is anticipated that the rates capping framework and accompanying monitoring regime will also promote better information gathering, measurement and reporting processes within councils. Continual improvement in this regard will reinforce good

⁷⁹ Department of Treasury and Finance 2014, Victorian Guide to Better Regulation, December, p.35.

⁸⁰ In this regard, the experience and outcomes of rate pegging in NSW have proven instructive for the design of rates capping framework in Victoria. One of the most important lessons from NSW was the need to have ongoing monitoring of council performance outcomes under a rate cap embedded into the policy architecture so that negative outcomes can be identified and addressed in a timely manner.

planning and service delivery and assist councils to make better operational and financially sustainable decisions in the interests of their communities. Further, a good monitoring and reporting regime can assist councils to demonstrate the value-for-money they deliver with the resources they have available; and to benchmark their performance with other like councils. Not only can this support how councils communicate with their communities, but it can also assist them to communicate with other levels of government about the trade-offs faced by local government.

Box 4.1 (below) provides a summary of the key objectives of the monitoring regime.

BOX 4.1 MONITORING AND REPORTING OBJECTIVES

In order to promote transparency of, and accountability for, outcomes under the rate capping and variation framework, the monitoring and reporting regime should:

- provide accurate and reliable information on outcomes
- make findings known publicly and on a regular basis
- present information in a consistent, clear and meaningful manner
- demonstrate whether councils have adhered to the cap or the conditions of an approved variation above the cap
- describe the relationship between rates and council performance in the areas of service and infrastructure delivery, and financial sustainability
- provide councils with the opportunity to explain unexpected or unusual outcomes
- facilitate a process for addressing unusual or unexplained outcomes, where such responses are warranted.

4.1.2 APPROACH

In determining the most appropriate form of monitoring and reporting to support the rate capping and variation framework, the Commission has sought to:

- ensure that any monitoring is integrated with, and adds value to, the existing accountability architecture and sector oversight

- balance the need for monitoring against the reporting burden imposed on councils. The Commission intends to only add requirements where it is absolutely necessary for the integrity of the framework
- use data in relation to service, infrastructure and financial sustainability outcomes that is sufficiently robust, reliable and comprehensive for the Commission to assess the impact of the framework on the sector.

4.1.3 STAKEHOLDERS' FEEDBACK

In response to the consultation paper and in meetings with councils, peak bodies, unions, and ratepayers, the Commission received strong feedback about the potential for unintended consequences and perverse outcomes of the framework should it be insufficiently designed. This would include the need for a monitoring component to identify those consequences and a process to address them.

A common theme, particularly from councils, was the concern that the framework may discourage investment in infrastructure, leading to a subsequent expansion of the renewal gap and reduced services and service levels. Some councils claimed that restricting their capacity to raise revenue would undermine their long-term financial sustainability.

The Australian Services Union and the Australian Nursing and Midwifery Federation both identified the potential for the framework to lead to outsourcing and job losses and cut backs to services. This potential outcome of rate capping was also cited by many councils and community organisations.⁸¹

The Municipal Association of Victoria (MAV) singled out under-funding of infrastructure as the most significant risk, citing the previous experience of rate capping in Victoria in the early 1990s. In order to ensure that these outcomes are not replicated, the MAV recommends that:

[T]he performance of councils in meeting their infrastructure renewal requirement should be monitored by assessing the trend performance against the VAGO indicators. In addition, the ESC may wish to utilise

⁸¹ For example, submissions to the ESC's consultation paper from Regional Cities Victoria, Dandenong Community Advisory Bureau Inc. and the Youth Advocacy and Advisory Group.

*data available directly from councils on the performance of asset renewal.*⁸²

The MAV argued that councils already undertake extensive performance reporting, financial reporting and consultation through their budget development and planning processes. The submission highlighted that the new Local Government Performance Reporting Framework will provide the community with significant data on services, infrastructure and costs.

In their submission to the consultation paper, Local Government Professionals (LGPro) recommended that part of the Commission's role should be to:

*provide advice to the Minister for Local Government in circumstances where Business Cases are seen to have insufficient merit and other intervention may be required.' And to '[m]onitor the success of the implementation of the Rate Capping and Variation Framework and provide advice to the Minister on any review, taking into consideration feedback from the sector.'*⁸³

LGPro also cited the need for Local Government Victoria (LGV) to provide guidance and support to the sector and that over time the policy parameters that support rate capping are integrated across the various agencies with responsibility for sector oversight, namely the Auditor-General, LGV and the Commission, to maximise transparency. The need for adequate guidance and support to assist councils to build capacity and to attract, train and retain qualified staff was a prominent theme among council submissions and also some ratepayers.⁸⁴

The Victorian Civil Construction Industry Alliance recommended that the Commission '[d]evelop performance indicators to monitor/measure efficiencies' in regards to road infrastructure investment and maintenance. And '[a]nalyse the delayed and compounding effect/impact on community infrastructure of reduced asset maintenance and renewal expenditure overtime.'⁸⁵ Similarly, the Institute of Public Works

⁸² The MAV submission to the ESC's consultation paper, pp.5-6 and p.20. According to the MAV, all councils maintain their own assessment of their renewal gap, which may provide a useful source of data to measure the impact of rate capping on infrastructure management.

⁸³ LGRPO 2015, *Submission to ESC's consultation paper*, May, p.8.

⁸⁴ Joe Lenzo 2015, *Submission to ESC's consultation paper*, May.

⁸⁵ VCCIA 2015, *Submission to ESC's consultation paper*, May, p.11.

Engineering Australasia (IPWEA) reiterated the concerns of many stakeholders that the rate cap may reduce expenditure on infrastructure and assets, as well as reductions in technical staff. For this reason, the submission advocated that 'effective performance compliance reporting and auditing is established to ensure these objectives [ESC principles] are sustainably achieved.'⁸⁶

Submissions from LGPro, Mildura City Council and Baw Baw Shire Council also recommended that the framework be subject to a risk assessment prior to implementation.

There was almost universal support for undertaking a review of the framework after a period of time to assess its effectiveness against the Government's policy objectives. Of the 54 submissions received that specifically addressed the question regarding conducting a review, 53 supported it. These submissions included councils, council peak bodies, ratepayer groups and individual ratepayers. The submissions provided valuable guidance on the potential scope and timing of the review.

4.1.4 SUMMARY OF POTENTIAL UNINTENDED OUTCOMES

This section lists some of the unintended outcomes identified in submissions to the consultation paper, through discussions with the sector and relevant stakeholders and the Commission's research. These include:

- the cap is set too low and does not adequately represent council costs, creating negative impacts such as short-term budgeting, reductions in investment and maintenance of infrastructure, and reduced services contrary to the needs of the community
- the cap is set too high and thus ceases to be an effective financial discipline, reducing the potential for improving planning and budgeting, efficiency, and transparency
- the variation process is too complicated and onerous, and not sufficiently integrated with council planning and budgetary processes

⁸⁶ IPWEA 2015, *Submission to ESC's consultation paper*, May, p.2.

- the community develops unrealistic expectations about rate increases never rising above the cap, to the detriment of services, infrastructure or financial sustainability
- the framework encourages short-term, politically expedient decisions to bring budgets under the cap (i.e. reducing expenditure on critical infrastructure maintenance and renewal or outsourcing)
- where councils that need to raise rates do not, leading to a deterioration in services, infrastructure or the financial sustainability (this may be due to the perceived or actual administrative burden imposed by the application process; perceived negative political implications of applying for a variation; or the thresholds for a variation are set too high)
- other fees and charges are increased in excess of the reasonable cost of providing the service to offset any reduction in projected revenue caused by the cap.

4.2 EXISTING DATA AND PERFORMANCE INDICATORS AVAILABLE FOR MONITORING

A key consideration for the Commission in determining the most appropriate monitoring arrangements for the framework is to ensure that, where possible, the framework is integrated with and adds value to the existing planning, budgetary and accountability provisions. As examined in chapter 1 of this volume, there are quite extensive planning, reporting and accountability obligations required of local governments under the *Local Government Act 1989* (the Act) and Regulations. Further, the introduction of rate capping has coincided with a number of important reforms to the sector that encourage more transparent and consistent financial and performance reporting.⁸⁷ Nevertheless, limitations remain that will constrain the capacity of the Commission (or any other agency) to effectively monitor performance outcomes under the framework.

⁸⁷ These include, but are not limited to, the establishment of the LGPRF, improved consistency in financial and performance reporting, and amendments to Section 126(2A)(2B) that require a council's strategic resource plan to take into account any plans adopted by the council and any resources required for plans or initiative adopted by the council to be consistent with the SRP. Local Government Victoria has also released a number of new or updated 'better practice guides' to assist councils in meeting their reporting obligations and build capacity.

By way of comparison, traditional economic price regulation and price monitoring in utility sectors (such as water) typically rely on agreed services and service standards, prescribed financial and operational information (for instance, a chart of accounts which includes unit costs and consistent asset valuation methods) and sector-wide benchmarks to assess performance and efficiency. This provides a much stronger basis to assess how effectively and efficiently an entity has delivered services, maintained assets and managed their overall financial position. As the following analysis indicates, many of these features are only partially captured in, or are largely absent from, the current local government reporting and accountability provisions.

4.2.1 SERVICES

Table 4.1 summarises the available data sources and common performance indicators that could be used to monitor changes in council service outcomes under the framework. Most of these are drawn from council annual reports, including the new reporting obligations under the LGPRF. The Victoria Grants Commission (VGC) also collects revenue and expenditure data disaggregated by 10 broad areas to determine the annual Commonwealth Financial Assistance Grants allocation. Each year LGV also coordinates a community satisfaction survey on council performance. The survey is a useful source of data on broad community satisfaction with council performance.

TABLE 4.1 SERVICES

Victoria Grants Commission	LGPRF (annual report)		Community satisfaction survey
Revenue and expenditure per service area	Service area	Indicators	Community satisfaction per council (69) in relation to:
Governance	Governance	Transparency Consultation and engagement Attendance (Councillor) Service cost Satisfaction (VAGO audited)	Overall performance
Business and economic services	Statutory planning	Timeliness Service standard Service cost Decision-making (VAGO audited)	Community service priorities
Local roads and bridges	Roads	Satisfaction Condition Service cost Satisfaction (VAGO audited)	Community consultation and engagement
Main roads	Libraries	Utilisation Resource standard Service cost Participation (VAGO audited)	Service performance
Recreation and culture	Waste collection	Satisfaction Service standard Service cost Waste diversion (VAGO audited)	Decision-making

Continued next page

TABLE 4.1 (CONTINUED)

VGC	LGPRF (annual report)		Community satisfaction survey
Revenue and expenditure per service area	Service area	Indicators	Community satisfaction per council (69) in relation to:
Waste management	Aquatic facilities	Satisfaction Service standard Service cost Utilisation(VAGO audited)	Customer service
Environment	Animal management	Timeliness Service standard Service cost Health and safety (VAGO audited)	General views on the trade-off between increased rates and reduced service levels
Traffic and street management	Food safety	Timeliness Service standard Service cost Health and safety (VAGO audited)	Overall direction
Aged and disability care	Home and community care	Timeliness Service standard Service cost Participation (VAGO audited)	
Family and community services	Maternal and child health	Satisfaction Service standard Service cost Participation (VAGO audited)	

Capturing consistent information on council performance of service delivery is particularly challenging. Councils typically provide 50 to 120 different services. The mix of services, service levels and the costs of service provision vary greatly from council to council depending on the needs and preferences of the community, the financial capacity of the council and structural factors such as growth, population size and dispersion. Without knowing the relative starting point for each council in respect to the mix and level of services desired by the community, and the effectiveness and efficiency by which a council has been delivering services, it difficult to assess changes in performance or to make comparisons between councils.

Another constraining factor is the quality and consistency of reporting on service delivery and performance. As noted in the most recent Auditor-General report

'reporting of non-financial performance information on services and outcomes has not historically been as robust [as financial reporting]'.¹⁸⁸ Though councils do measure and report on their performance in relation to the strategic objectives and indicators identified in the Council Plan, these are often high level and focus on activities and outputs rather than service outcomes. In this respect, the establishment of the LGPRF is an important reform. However, the indicators and measures used by the framework provide only an indication of performance limited to 10 common service areas.

Within the sector there remains a lack of uniform definitions and standard measures for the inputs used and the outputs produced. Many councils are unable to consistently identify, measure or publicly report on the resources utilised to produce different outputs (for example, unit costs). These deficiencies also limit the capacity of the framework to highlight and drive opportunities for improved efficiency.

4.2.2 ASSETS AND INFRASTRUCTURE

Table 4.2 outlines the current financial data, indicators and measures of local government performance in respect of asset and infrastructure maintenance and renewal.

Councils employ divergent approaches to managing their assets and addressing renewal gaps, including using a variety of different asset information systems and methods for assessing their renewal and maintenance needs. Table 4.2 lists the most common methods used in assessing asset maintenance and renewal need. As would be expected, different definitions and approaches to renewal and asset depreciation and varying standards of intervention levels used by councils can result in divergent estimates of the renewal requirements and asset depreciation.

⁸⁸ VAGO 2015, *Local Government: Results of the 2013-14 Audits*, February, p.x.

TABLE 4.2 ASSETS AND INFRASTRUCTURE

Annual Report	LGPRF	VAGO	MAV STEP ^a
Statement of capital works (from 2014-15)	Asset renewal (renewal expenditure/ depreciation expenditure)	Asset renewal (renewal and upgrade expenditure/ depreciation expenditure)	
Containing: Breakdown of expenditure on property, plant and equipment and major infrastructure classes <ul style="list-style-type: none"> • New asset expenditure • Asset renewal expenditure • Asset expansion expenditure • Asset upgrade expenditure 	Target band 90-110%	Risk Thresholds High risk: less than 0.5 Medium risk: 0.5-1.0 Low risk: more than 1.0 Capital replacement (capital expenditure/depreciation)	Condition-based renewal gap: expenditure on renewal/required expenditure for the period based on the condition assessment of the assets Percentage of assets at intervention level

^a The package of asset management tools developed by the MAV known as the STEP program was created to assist councils to improve their planning and asset management. The STEP program utilises a renewal gap calculation based on an assessment of the condition of the asset, in contrast to the accounting approach based on straight-line asset depreciation. The usefulness of the MAV STEP data as a consistent measure of asset management performance will need to be further evaluated. It is the Commission's understanding that the MAV STEP program is not utilised by all councils and not always applied consistently by those that do.

Because much of the infrastructure under management by local government is long-lived (such as roads, paths, buildings), the impact of under-investment in maintenance and renewal can take a long time to be publicly recognised. Further, capital expenditure on infrastructure can by its nature be lumpy, making it difficult to determine if short-term variations reflect reduced or inadequate infrastructure investment or the normal investment cycle.

Though most local councils are committed to improving their asset management planning and practices and important progress has been made over the past decade, inconsistent management practices and methods for assessing renewal needs, and poor quality information about the condition of assets, make determining the 'true' state of the renewal gap particularly challenging and assessing performance against this

more difficult as a result.⁸⁹ A 2014 audit of asset management and maintenance in local government by the Auditor-General found persistent deficiencies in asset management planning, asset information systems and capital expenditure programs.⁹⁰ In particular, performance has suffered from poor quality data on their assets, including in some instances not having a full inventory of all of the assets under their control, asset condition and anticipated lifetime.⁹¹

Finally, there is limited information available that enables an assessment of how productively a council is using their assets in relation to the services the assets are used to deliver. That is, how well a council has aligned their asset management plans to the mix of services and service levels needed by the community.

4.2.3 FINANCIAL SUSTAINABILITY

The data in relation to financial performance sustainability is the most robust and consistent. The measures and indicators of financial sustainability used by the Auditor-General are well established and broadly accepted by the sector. The recent establishment of the LGPRF also provides additional financial performance indicators that will be consistently applied to the sector (listed in Table 4.3).⁹²

⁸⁹ For example, the widespread adoption of the MAV STEP program and the shift from cash accounting to accrual accounting.

⁹⁰ VAGO 2014, *Asset Management and Maintenance by Councils*, February, found that the majority of councils in Victoria have not made sufficient progress against the National Asset Management Assessment Framework (NAMAF). The NAMAF is a methodology used by local government to assess the level of maturity of their asset management plans and practices. The NAMAF was developed by the Commonwealth Government's Local Government Planning Ministers' Council in 2006, in response to a number of reported issues with local government asset management practices and the potential financial and service impacts of a growing renewal gap.

⁹¹ VAGO 2014, *Asset Management and Maintenance by Councils*, February, p.31. The period of council amalgamations in the 1990s resulted in incomplete or fragmented inventories of council assets and their condition.

⁹² While there is some overlap between these two sets of indicators (VAGO and LGPRF), there are a number of important differences with respect to the specific measures used and the target bands and risk ranges. For example, the target band for indebtedness in the LGPRF is 20 to 60 per cent, while the risk assessment used by the VAGO classifies low risk at less than 40 per cent, medium risk 40 to 60 per cent and high risk greater than 60 per cent.

TABLE 4.3 FINANCIAL SUSTAINABILITY

VAGO		LGPRF (annual report)
Indicator	Dimension	Output Indicators
The underlying result	Operating position	Adjusted underlying result (surplus or deficit)
Liquidity	Liquidity	Working capital
Indebtedness	Obligations	Loans and borrowings Long-term liabilities Asset renewal
Self-financing	Stability	Rates concentration Rates effort
Capital replacement	Efficiency	Expenditure level Revenue level Workforce turnover
Renewal	Sustainable Capacity	Own source revenue Recurrent grants Population Disadvantage

What is missing for the purposes of monitoring the outcomes of the rates capping framework is detailed financial information disaggregated on a per-service basis. The VGC data provides aggregated revenue and expenditure information in terms of ten broad service areas, but the consistency and accuracy of the data becomes less robust when disaggregated by each service. As discussed under section 4.2.1, the sector lacks uniform definitions and standard measures for the inputs they use and the outputs they produce, which cannot readily identify or measure the resources utilised to produce different outputs, and are incapable of generating unit costs for the outputs they produce.

Further, while all councils now required to maintain a long-term financial plan (minimum four-year SRP), the quality of these plans and their capacity to accurately forecast revenue needs, costs and liabilities is variable. In particular, a common finding of VAGO audits in recent years points to the lack of sufficient integration between financial plans and asset management plans. This lack of integration will be further compounded where asset management plans are weak or based on poor quality data.

4.3 WHAT MONITORING SHOULD SUPPORT THE FRAMEWORK?

The following three sections outline the areas the Commission believes should be monitored in the context of the rate capping and variation framework, the options considered for how they should be monitored, and the respective role of the Commission. These are:

1. local government compliance with the rate cap or the conditions of an approved variation above the cap
2. monitoring council performance outcomes (in relation to services, assets and infrastructure and financial sustainability) following the introduction of the framework
3. assessing the overall effectiveness of the framework.

4.4 MONITORING COMPLIANCE WITH THE CAP OR APPROVED VARIATION

The Government has identified rate capping as a key policy for the local government sector. In order to maintain the integrity of the framework designed to implement this policy, the Commission believes that it is necessary to verify that councils adhere to the rate cap or an approved variation above the rate cap.

Accordingly the Commission proposes to monitor that:

- the relevant council rates and charges are set in accordance with the rate cap for the corresponding financial year
- councils with an approval to vary rates above the cap, have set their rates and charges in accordance with the conditions of the approval
- while excluded from the cap, service rates and charges will be monitored and benchmarked to ensure that they remain reflective of the reasonable cost of providing the service.

We would report our findings publicly and on an annual basis. Amongst other things, these reports would address: year-on-year changes in rates, discrepancies between forecast and actual outcomes, and broader trends within and across the local

government sector. Councils would be invited to provide comments explaining any unexpected or unusual findings.

Table 4.4 lists the indicative information the Commission is proposing to collect from councils each year in relation to local government compliance with the rates capping and variation framework.

Minimal additional reporting obligations will be imposed as a result of this monitoring as much of this information is already reported by councils. While the Commission considers this information to be sufficient to monitor compliance, we will continue to consult with the sector before the information requirements are finalised.

TABLE 4.4 INDICATIVE INFORMATION TO BE MONITORED FOR COMPLIANCE WITH THE CAP AND APPROVED VARIATIONS
(\$ million)

	Actual (2015-16)	Forecast (2016-17)	Forecast (2017-18)
Total council revenue requirement (all sources)			
General rates			
Municipal charges			
Service rates & charges			
Special rates & charges			
Supplementary rates			
Statutory fees & fines			
User fees & charges			
Net gain(loss) on disposal of property, infrastructure, plant and property			
Other income			
Grants (all sources)			
Contributions – monetary			
Contributions – non monetary			
Miscellaneous			
Total value of rateable properties^a			
Total number of rateable properties as at 1 July^a (no.)			
Breakdown of garbage related costs:			
Council cost			
Landfill levy			

^a At the commencement of the financial year.

4.4.1 NON-COMPLIANCE

Where monitoring identifies non-compliance with the cap or the conditions of an approved variation above the cap, the Commission has considered three main options to determine the most appropriate response.

Option 1: Direct refund to ratepayers

Councils are obligated to return on a pro rata basis any revenue collected through general rates and municipal charges in excess of the cap or approved variation directly to ratepayers in the subsequent financial year.

Option 2: Reconciliation with base revenue in subsequent financial year

The Commission will seek to reconcile any general rates and municipal charges revenue collected in excess of the cap or approved variation by making a downward adjustment to the council's permissible base revenue the following financial year so that no ongoing financial advantage is obtained. Further consultation guidance would be required to determine the exact formula by which this would take place.

Option 3: Refer matter to the Minister

The Commission will engage with councils to better understand the reasons for any apparent non-compliance and may report to the Minister for Local Government on our findings.

ANALYSIS

Requiring councils to refund ratepayers for any rates revenue in excess of the cap would result in an overly bureaucratic and inefficient process, impose a significant cost and administrative burden on councils regardless of intent and potentially cause confusion for ratepayers. The legislative authority by which option would be enabled and enforced would need to be further considered. The Commission considers that while the framework is in its infancy, this option is too interventionist.

Similarly, making a downward adjustment to the base revenue in the subsequent financial year is considered by the Commission to be too interventionist while the framework is initially being implemented. This option may have merits in the long-term once councils have become familiar with the framework

We therefore recommend that the third option be adopted. We will engage with relevant councils to better understand the reasons for any apparent non-compliance identified in their setting of rates and we will prepare a report to the Minister for Local Government on our findings. Under this option any intervention or enforcement remains the responsibility of the Minister.

DRAFT RECOMMENDATION 10

The Commission recommends that it monitor and publish an annual rates report on councils' adherence to the cap and any approved variation conditions.

4.5 MONITORING OUTCOMES FOR RATEPAYERS AND COMMUNITIES

The Commission considered three possible options when determining the most appropriate monitoring regime to assess the service, infrastructure and financial outcomes for ratepayers and communities, following the introduction of the framework.⁹³

Option 1: No ongoing monitoring

Under this option, the Commission would capture and monitor only the data necessary to set the rates cap and councils' base rates revenue, to assess variation applications and to verify compliance with the cap and conditions of an approved variation. The Commission would have no further role in monitoring service outcomes. This option accepts that while there are limitations in the available data (identified in section 4.2), the current accountability and reporting provisions in the sector and financial sustainability oversight by the Auditor-General provide sufficient assurance that any unintended consequences would be identified and promptly addressed. The overall effectiveness of the framework in meeting the stated policy objectives would be evaluated by conducting a review of the framework after four years (see section 4.6).

Option 2: Ongoing monitoring — risk-based approach

Option two proposes that the Commission assumes a lead role in monitoring both adherence with the cap and approved variations and outcomes for ratepayers and communities under the framework. To minimise the reporting burden on councils and to ensure the regime complements the existing accountability and oversight provisions, the Commission will utilise and consolidate the existing performance data available

⁹³ The Commission notes that the Parliamentary Environment and Planning Committee has been instructed to inquire into and report every six months on the outcome of the State Government policy of local government rate capping on councils' viability, service impacts on local communities and impacts on the provision of local infrastructure. This level of Parliamentary oversight may be an important complementary layer of accountability for the policy.

(section 4.2) into one database. The Commission will use the existing risk thresholds applied by the Auditor-General and the target bands used by the LGPRF. Where appropriate, we may also seek to develop additional risk indicators and thresholds for service, infrastructure and financial outcomes in consultation with the sector.

To address the limitations in the current data and to better enable the Commission to detect a material deterioration in council service, infrastructure or financial outcomes, the Commission proposes two additional features:

- All councils will be required to complete an annual 'baseline information' template. The baseline information would provide additional financial and asset information in relation to council services. The Commission has started developing a pilot template in consultation with a small number of councils and will commence wider consultation following publication of this report. For more information about the baseline information, see Appendix D.
- If a trend is identified through the monitored data indicating a significant deterioration in performance outcomes for ratepayers and the community or financial sustainability in relation to a council or group of councils, the Commission may conduct a further assessment to determine materiality of the trend and its consistency with long-term planning and public consultation. In conducting this assessment, councils will be invited to provide an explanation for the identified trend. A report may be provided to the Minister detailing the findings of the assessment, where a trend is found to be inconsistent with planning and consultation. The council or councils in question would be invited to provide comment on the findings of any report.

Option 3: Ongoing monitoring — strengthened regulatory obligations

Option three proposes that the Government strengthen council performance and financial reporting obligations in support of the rates capping and variation framework, and provide the Commission with a stronger role in regulatory oversight. The proposed model would be broadly similar to price regulation used in utility sectors. The new regulatory framework would include: defined services and service standards and consistent performance measures; mandatory asset management methods; and prescriptions about what financial information must be collected and reported on, such as a chart of accounts that captures detailed costs (direct and indirect) per service. This option would enable more robust and consistent information to be reported by councils and monitored by the Commission about council performance under the

framework. This option would also impose the greatest regulatory burden on the sector. A report may be provided to the Minister detailing the findings of the assessment where a trend is found to be inconsistent with planning and consultation. The council or councils in question would be invited to provide comment on the findings of any report.

ANALYSIS

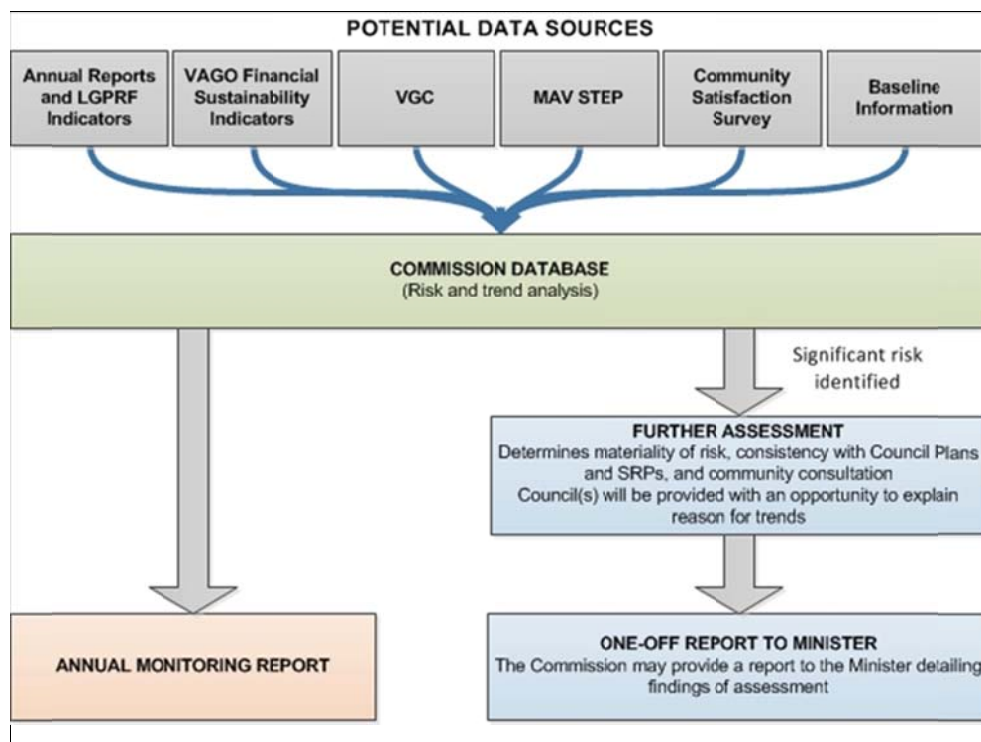
The Commission considers that option one would result in a potential disconnect between the operation of the framework and the outcomes experienced by ratepayers and communities. This would also present an unacceptable risk that any potential unintended consequences (such as under investment in infrastructure) may not be identified and addressed in a timely fashion, as required by the terms of reference.

Establishing a stronger regulatory regime contemplated in option three is also considered to be inappropriate in the current context. While clear service standards and financial and performance reporting obligations would provide the most reliable and consistent information about performance outcomes under the framework (including opportunities for benchmarking efficiency and effectiveness), they would also impose a significant cost and resource burden on councils and on the Commission to administer. This option would also see the Commission assume a far more intrusive regulatory role than envisaged for this framework. It is also questionable whether such a rigid form of regulatory oversight is practical for the sector given the diverse mix of services and service levels provided by councils relative to community need and affordability. Finally, this option would also represent a significant change from, and potential clash with, some of the existing accountability and reporting obligations, the most significant of which is the new LGPRF.

The Commission does however recognise the need for further improvement in how councils monitor, evaluate and report on their performance, particularly with respect to service performance, efficiency, and asset management. It is hoped that the framework will encourage councils to improve their practices in this regard, particularly through the introduction of the baseline information and recommended public reporting.

The Commission's preferred approach to monitoring is option two, represented in figure 4.2.

FIGURE 4.2 ONGOING MONITORING OF OUTCOMES FOR RATEPAYERS AND COMMUNITIES



This risk-based approach allows the Commission to partially address some of the current limitations in the data available on council performance without imposing an excessive regulatory burden. To a large extent, this option uses existing council performance data and complements the current accountability and reporting provisions. The additional information required by the Commission (the baseline information) is comprised of information that councils should already capture in order to meet their planning and accountability obligations under the Act.⁹⁴

⁹⁴ Councils are obliged to set strategic objectives in their Council Plans, budgets and annual reports, and identify and report on the specific initiatives and priority services that will enable the council to meet those objectives. The Best Value Principles require councils to develop cost and quality standards for each service. To achieve this, councils are expected to be capturing and monitoring the costs of providing a service, and any associated assets necessary to deliver the service.

Further rationale for the Commission recommending this approach is captured below.

- Having responsibility for monitoring sitting with the Commission provides clear continuity of responsibility through the three key elements of the framework (cap, variation process, monitoring) and will establish a feedback mechanism to allow for refinements to the elements of the framework over time.
- This option facilitates a process by which any unintended negative outcomes for ratepayers and communities can be promptly addressed.
- This option respects council autonomy by limiting the Commission's role to information gathering, evaluation and reporting. Powers of intervention remain with the Minister for Local Government.
- This option reinforces good practices by providing credible and impartial information about performance outcomes under the framework. While not designed to be a punitive measure, the transparency and accountability promoted by ongoing monitoring by the Commission may discourage some councils from taking short-term or politically expedient decisions under the cap.

DRAFT RECOMMENDATION 11

The commission recommends that it monitor and publish an annual monitoring report on the overall outcomes for ratepayers and communities.

4.6 FRAMEWORK REVIEW

As with any regulatory arrangements, the rates capping and variation framework should be subjected to periodic review. The ongoing monitoring regime detailed above provides assurance that the key elements of the framework are adhered to and a means of identifying and addressing significant deteriorations in performance or unintended consequences at the council level.

However, there is a need to conduct a more extensive review of the framework on a periodic basis in order to monitor, evaluate and report on how effectively it has achieved the intended policy objectives. The review should identify any necessary refinements to the legislative or regulatory architecture so that it remains capable of meeting the objectives of the policy into the future. Including a formal review

mechanism into the design of the framework that is consistent with best practice public policy design and program delivery principles.

Wide support for a review of the framework was evidenced in the submissions received in response to the consultation paper. Stakeholders recommended a range of review periods (1 to 5 years) for a framework review. Several submissions also recommended aligning the review with the Council election and planning cycles.

In other regulatory and legislative contexts, review periods typically range from 2 to 10 years. In this context, the Commission considers 4 years to be an appropriate timeframe. This provides sufficient time for councils to familiarise themselves with the requirements of the framework and make any necessary adjustments to their systems and processes. A 4 year review period will also enable a more comprehensive data set (including trends) to be established, and for the effectiveness of the framework to be assessed. In the long-term, this will also provide for closer alignment with council planning and election cycles.

MATTERS FOR FURTHER CONSIDERATION

The Commission recommends that the Government consider making a formal review of the rates capping and variation framework a statutory obligation. The review should draw on any data and trends identified through the ongoing monitoring regime and all interested parties should have an opportunity for the sector to provide input to that review. The Commission considers a review period of 4 years to be appropriate.

4.7 COMMISSION REPORTING OBLIGATIONS UNDER THE FRAMEWORK

Transparent reporting is central to maintaining the integrity of the framework and the accountability of the sector, the Commission and the Government. Table 4.5 outlines the recommended reporting obligations with respect to the operation of the framework.

TABLE 4.5 FRAMEWORK REPORTING
Key Reports

Report	Description
Setting the rate cap (Chapter 2)	In May, the Commission will issue a statement with its forecast for the rates cap for the next financial year and the following two years. In December, the next year's rates cap will be finalised and published together with the forecast for the two following years.
Variation Applications (Chapter 3)	At the conclusion of the application period for rate variations, the Commission will issue a statement summarising details of each application received for a rate variation above the cap.
Variation Decisions (Chapter 3)	The Commission will publish reports detailing the outcome of each application for a variation above the rates cap (approval or refusal). Each report will detail the basis for the Commission's decision.
Annual Rates Report (Chapter 4)	Each year, the Commission will publish a report into councils' adherence with the rates cap or relevant variation conditions in the financial year just completed.
Annual Monitoring Report (chapter 4)	The Commission will release a report on the performance of the framework. The report will bring together information about the cap and variations, with key findings from the monitoring regime. We initially expect this report will be available in February each year but will endeavour to bring forward its publication as the framework matures.
One-off reports	From time to time, the Commission may issue one-off reports into matters pertaining to the operation of the framework.

4.7.1 BENCHMARKING

The terms of reference requested that the Commission consider any benchmarking in relation to the effectiveness of the framework and also council efficiency. In light of the current gaps and consistency issues in the data available and the short timeframe for implementing the framework, the Commission's initial position is to use existing performance benchmarking captured in the VAGO annual audits and the LGPRF. The exception to this position is monitoring of service charges. The Commission will monitor and benchmark service rates and charges from the commencement of the framework to ensure they are reflective of the reasonable cost of providing the service.

As the framework evolves, the Commission will seek to develop additional benchmarks, where the data is sufficiently robust and meaningful comparisons can be made. A working group will be established to identify and refine these benchmarks in consultation with the sector, as well as any additional thresholds and risk flags necessary to support the monitoring regime.

In the interim, when applying for a variation above the cap councils are encouraged to provide any benchmarking they may have undertaken in relation to like or neighbouring councils as evidence of a demonstrated effort to pursue efficiency and reduce costs.

APPENDIX A — TERMS OF REFERENCE

Local Government Rates Capping Framework

Terms of Reference

I, Robin Scott MP, Minister for Finance, under section 41 of the *Essential Services Commission Act 2001* (the 'ESC Act'), refer to the Essential Services Commission (ESC) the development of a rates capping framework for local government.

As provided for by section 185b of the *Local Government Act 1989*, the Minister for Local Government can cap council general income. The Government has announced a commitment to cap annual council rate increases¹ and has also provided additional guidance on factors to be considered during the implementation of the cap².

The State Government's objective is to contain the cost of living in Victoria while supporting council autonomy and ensuring greater accountability and transparency in local government budgeting and service delivery. The Government intends to promote rates and charges that are efficient, stable and reflective of services that the community needs and demands, and set at a level that ensures the sustainability of the councils' financial capacity and council infrastructure, thereby promoting the best outcomes for all Victorians.

The ESC is asked to inquire into and advise the Ministers for Finance and Local Government on options and a recommended approach for a rates capping framework for implementation from the 2016-17 financial year. Advice should include and/or take into account the following matters:

- 1) Available evidence on the magnitude and impact of successive above-CPI rate increases by Victorian councils on ratepayers.
- 2) Implementation of the Government's commitment to cap annual council rate increases at the Consumer Price Index (CPI) with councils to justify any proposed increases beyond the cap, including advice on the base to which the cap should apply (e.g. whether to rates or to general income).
- 3) Any refinements to the nature and application of the cap that could better meet the Government's objectives.
- 4) Options for the rate capping framework should be simple to understand and administer, and be tailored to the needs of the highly diverse local government sector. The framework should take into account factors that may impact on local governments' short and longer term financial outlook, such as:
 - a) actual and projected population growth and any particular service and infrastructure needs;
 - b) any relevant Commonwealth Government cuts to Local Government grants;
 - c) any additional taxes, levies or increased statutory responsibilities of local governments as required by the State or Commonwealth Governments;

¹ Media release by Daniel Andrews, *Andrew Announces Fair Go for Ratepayers*, 5 May 2014.

² ALP's response to MAV's *Local Government Call to Political Parties*, p.1, November 2014.

- d) any extraordinary circumstances (such as natural disasters); and
 - e) other sources of income available to councils (for example, ability to raise user fees and charges from non-residents).
- 5) Consider how local governments should continue to manage their overall finances on a sustainable basis, including any additional ongoing monitoring of council service and financial performance to ensure that any deterioration in the level, quality or sustainability of services and infrastructure and councils' financial position is identified and addressed promptly.
 - 6) The processes and guidance to best give effect to the recommended approach for the rates capping framework and a practical timetable for implementation, including:
 - a) the role of councils, the ESC and the Victorian Government and the expected time taken by local governments and by the Victorian Government or its agencies, for each step in the rate capping process;
 - b) any technical requirements including the information requirements on councils that request exemptions from the cap;
 - c) any guidance required to give effect to the rate capping options (including in relation to consultation with ratepayers) and to improve accountability and transparency; and
 - d) any benchmarking or assessment of the effectiveness of the regime, including options to continuously refine the regime and improve council incentives for efficiency.
 - 7) Options for ongoing funding to administer the rate capping framework, including the potential for cost recovery.

In conducting the inquiry and providing its advice, the ESC will have regard to:

- the role of local government in the provision of infrastructure and services to the community and the general efficacy with which they currently perform this task;
- the differences between rural, regional and metropolitan local councils in terms of costs, revenue sources and assets maintained;
- the Revenue and Rating Strategy guide and Local Government Performance Reporting Framework to be administered by the Department of Environment, Land, Water and Planning;
- matters regarding rating practices and asset renewal gap raised by the Victorian Auditor-General's Office (VAGO);
- Department of Treasury and Finance's Victorian Guide to Regulation and Victorian Cost Recovery Guidelines; and

- any relevant insights from the experience of rate pegging in New South Wales, including any reviews or evaluations that can suggest ways to minimise any unintended consequences.

In conducting this independent inquiry, the ESC will be informed by wide consultation. This will include, but is not limited to: councillors and officials from local government; representative bodies such as Municipal Association of Victoria, Victorian Local Government Association and LGPro; unions; VAGO; and relevant government agencies and departments. In addition, the ESC will consult regularly throughout the course of the inquiry with a sector consultative panel established by the Minister for Local Government. The ESC's consultation will be guided by its Charter of Consultation and Regulatory Practice.

The ESC will publish a draft report on the rates capping framework no later than six months after receipt of these terms of reference. The draft report must be made publicly available and invite comments from local governments and other interested parties. A final framework report along with draft guidance material will be provided to the Minister for Finance and Minister for Local Government no later than 31 October 2015.

ROBIN SCOTT
Minister for Finance
Dated: 19 January 2015

APPENDIX B — COUNCIL GROUPINGS

Metropolitan	Interface	Regional centres	Large Rural	Small rural
Banyule	Cardinia	Ballarat	Colac Otway	Bennalla
Bayside	Casey	Greater Geelong	Corangamite	Gannawarra
Boroondara	Hume	Warrnambool	Golden Plains	Hepburn
Brimbank	Mornington	Greater Bendigo	Moirā	Mansfield
Darebin	Nillumbik	Greater Shepparton	Moorabool	Murrindindi
Frankston	Whittlesea	Latrobe	Mount Alexander	Strathbogie
Glen Eira	Melton	Mildura	Bass Coast	Alpine
Greater Dandenong	Wyndham	Wodonga	Baw Baw	Ararat
Hobsons Bay	Yarra Ranges		Campaspe	Buloke
Kingston			East Gippsland	Central Goldfields
Knox			Glenelg	Hindmarsh
Manningham			Horsham	Indigo
Maribyrnong			Macedon Ranges	Loddon
Maroondah			Mitchell	Northern Grampians
Melbourne			Moyne	Pyrenees
Monash			South Gippsland	Queenscliffe
Mooney Valley			Southern Grampians	Towong
Moreland			Surf Coast	West Wimmera
Port Phillip			Swan Hill	Yarriambiack
Stonnington			Wangaratta	
Whitehorse			Wellington	
Yarra				
22	9	8	21	19

APPENDIX C — COMMUNITY ENGAGEMENT

The terms of reference for this review state that the Government intends to promote rates and charges that are efficient, stable and reflective of services that the community needs and demands. The Commission is asked to advise on the processes and guidance to best give effect to the rate capping options, including in relation to consultation with ratepayers. In applying for a variation, the Commission is recommending that councils wishing to increase their rates above the cap must show evidence of an effective engagement process with their ratepayers and communities. The engagement process should be designed to facilitate transparent and shared decision-making, leading to mutually beneficial outcomes for councils and their ratepayers and communities.

According to the *Local Government Act 1989* (the LG Act), councils must comply with Best Value Principles which include the need for a council to develop a program of regular consultation with its community in relation to the services it provides and must report regularly (at least once every year) on its achievements in relation to the Best Value principles.⁹⁵ In applying Best Value Principles, councils may take into account community expectations and values as well as other factors.⁹⁶ Councils must also make public their Council Plans and annual budgets for 28 days and receive submissions in that time.

⁹⁵ Sections 208B (e) and 208B (f), *The Local Government Act 1989*.

⁹⁶ Section 208C, *The Local Government Act 1989*.

C.2 STAKEHOLDERS' FEEDBACK

Many of the submissions from councils and council groups, local government peak bodies, unions, community organisations and service providers stressed that councils already undertake extensive community consultation in the development of their budgets and council plans and do so in accordance to, or go beyond, legislative requirements. Responses from ratepayers and ratepayer associations were mixed. Some cited examples of good engagement occurring in their communities⁹⁷, where there have been improvements⁹⁸ or what good engagement could look like⁹⁹. Others indicated dissatisfaction with the level of engagement undertaken by their respective councils.¹⁰⁰ Some of these submissions cited a perceived lack of transparency and of opportunities to have their perspectives heard and taken account of.

Submissions outlined that Councils generally undertake community consultation in three general ways:

- during the development of the Council Plan and Budget (including the Strategic Resource Plan)
- during the development of councils' long-term plans, which then inform councils' SRPs and budgets
- during the development of other specific strategies and policies such as service delivery and infrastructure strategies and key project proposals

A few submissions noted that there were ways to improve community engagement without being overly burdensome or through strengthening existing engagement processes (such as those undertaken in the development of council plans, strategic resource plans and budgets).¹⁰¹ Several were supportive of the rates capping and

⁹⁷ Alistair Rowe 2015, *Submission to the ESC's consultation paper*, May.

⁹⁸ Mornington Peninsula Ratepayers' & Residents' Association Inc. 2015, *Submission to the ESC's consultation paper*, May

⁹⁹ Joe Lenzo 2015, *Submission to the ESC's consultation paper*, May; Trevor Dance and Arnie Anzaris 2015, *Submission to the ESC's consultation paper*, May; Ratepayer Groups (Knox, Monash and Ratepayers Victoria) 2015, *Submission to the ESC's consultation paper*, May; Sunbury Residents Association 2015, *Submission to the ESC's consultation paper*, May.

¹⁰⁰ Murray Nicholas 2015, *Submission to the ESC's consultation paper*, May; Adrian Jackson 2015, *Submission to the ESC's consultation paper*, May; Nina Kelly 2015, *Submission to the ESC's consultation paper*, May; Ken Dyer, *Submission to the ESC's consultation paper*, May; Eastern Melbourne and state-wide Ratepayers Groups 2015, *Submission to the ESC's consultation paper*, May.

¹⁰¹ City of Port Phillip 2015, *Submission to the ESC's consultation paper*, May; Manningham City Council 2015, *Submission to the ESC's consultation paper*, May; Northern Grampians Shire Council 2015, *Submission to the ESC's consultation paper*, May; Knox 2015, *Submission to the ESC's consultation paper*, May.

variation framework providing guidance on best practice in engagement.¹⁰² The many submissions that commented on what good engagement looks like noted features such as:

- being based on reasonable expectations
- being proportionate, relevant and suitable to needs of community
- tailored to each council
- being open, flexible and responsive
- containing guidance on prioritisation and what the community has an opportunity to influence
- being representative
- involving multiple mechanisms
- occurring at the macro and micro levels
- including clear and accessible information needed for the community to base their feedback on ensuring community has adequate time and opportunity to engage with the process
- ensuring that the final decision, once made, is clearly communicated to the community, including the reasons for it

Many submissions provided examples for the Commission to consider as good/best practice community engagement, including the work of individual councils in Victoria and in other states. Examples of the approaches or guidance councils use or recommended to us and various tools and techniques undertaken in the engagement process by councils identified in submissions are shown in table 6.1.

¹⁰² Murrumbidgee Shire Council 2015, *Submission to the ESC's consultation paper*, May; Golden Plains Shire Council 2015, *Submission to the ESC's consultation paper*, May; East Gippsland Shire Council 2015, *Submission to the ESC's consultation paper*, May; LGPro 2015, *Submission to the ESC's consultation paper*, May; East Gippsland 2015, *Submission to the ESC's consultation paper*, May.

TABLE C.1 ENGAGEMENT APPROACHES AND TOOLS & TECHNIQUES
Examples provided by submissions to the Consultation Paper

Approaches or guidance used or suggested by councils

The International Association for Public Participation's (IAP2) Public Participation Spectrum
Oregon Model of Community Visioning
IPART's guidelines on community engagement
Victorian Auditor-General's Office's guidance on Public Participation in Government Decision-making

Tools & techniques used to capture community opinions and feedback

'Have your say' campaigns and online forums
Use of social media
Surveys or polls
Community events
Storytelling through words and visual art
Community panels or forums
Focus groups
'World café' community discussions
Participatory budgeting
Zero (activity) based budgeting
Citizen juries

Other issues raised in some submissions include the need for the Commission to clearly articulate our expectations around the quality and quantity of community engagement to be undertaken; how councils manage prudent but unpopular decisions within the proposed framework; the need for the framework to ensure that councils give adequate weight to minority preferences for services and infrastructure; and, the need for regular community engagement to occur about the new framework both prior and during the early stages of its implementation.¹⁰³

¹⁰³ City of Port Phillip 2015, *Submission to the ESC's consultation paper*, May; MAV 2015, *Submission to the ESC's consultation paper*, May.

C.3 DISCUSSION/ANALYSIS

Where councils are already undertaking good consultation and engagement with their ratepayers and communities will be reflected in the quality of their strategic resource plans, budgetary and planning decisions, financial and services outcomes as well as community satisfaction. The Commission will seek, through this framework, to reinforce these practices.

The diversity in the local government sector means there will be variability in how well councils consult and engage with their ratepayers and communities. In facilitating better engagement practices, the Commission will:

- not mandate specific engagement techniques or require prescriptive standards, as these will not be useful or helpful given the sector's diversity, and the different needs of individual councils
- encourage greater sharing amongst councils on good and effective experiences on community engagement
- encourage peak industry bodies (such as the VLGA and MAV) to work closely with the sector to enhance the different means to consult and engage effectively with ratepayers and community
- outline clearly the principles that exemplify good outcomes in community engagement that we expect to see reflected in applications for variation.

C.4 THE FRAMEWORK'S COMMUNITY ENGAGEMENT PRINCIPLES

The Commission has developed four key engagement principles based on what various submissions have told us good engagement should look like. These have been tested against various national and international approaches or standards for engagement.¹⁰⁴

¹⁰⁴ International Association for Public Participation Australasia, 2015, The IAP2 Public Participation Spectrum, <http://www.iap2.org.au/resources/iap2s-public-participation-spectrum>; *Victorian Auditor-General's Office January 2015*, Public Participation in Government Decision-making, Melbourne, <http://www.audit.vic.gov.au/publications/20150130-Public-Participation-BPG/20150130-Public-Participation-BPG.pdf>; IPART, October 2014, Community awareness and engagement for special variation applications, Fact sheet for councils; <http://www.ipart.nsw.gov.au>

The Commission will not assess an engagement program based on a single criterion or technique. Good engagement is not necessarily demonstrated by the absence of community objection or by survey results demonstrating majority support for a proposal. Councils may sometimes decide to implement options that do not have majority support. Before such decisions are made, however, the engagement program should focus on keeping the community well informed.

The tools used should be effective, accessible, transparent and adopt a long-term view.

Principle 1: The engagement program must contain clear, accessible and comprehensive information and follow a timely process to engender feedback from the community

Councils need to provide their ratepayers and communities with clear, accessible and comprehensive information about the need for, and the extent of, proposed rate variations. This should also include information on the major trade-offs involved in the options that the community is being asked to consider.

The community should have adequate opportunities to consider an issue and provide feedback in a timely manner.

Principle 2: The engagement program should be ongoing and tailored to community needs

The program must take into account the characteristics of the community and aim to be as representative of the community's diversity as practicable.

It should be a two way dialogue which occurs on an ongoing process either through regular council planning or designed to address specific issues as they arise.

Its success is measured in how the engagement has impacted the decisions a council has made in regards to setting their rates. Councils should be able to demonstrate how, in making their decisions, they have considered information gathered during the engagement process.

Principle 3: The engagement program should prioritise matters of significance and impact

The engagement program should be fit for purpose, having regard to the significance of the matter at hand, and should demonstrate good value for money.

The focus of the engagement program should be on a discussion between councils and their ratepayers and communities about how rate levels impact on services, and their prioritisation, as part of the Strategic Resource Plan. Engagement with communities in relation to a proposed rate rise should be proportionate to the size and impact of the rise proposed.

Principle 4: The engagement program should lead to communities becoming more informed about council decision-making

Councils should be open and transparent about how rate levels impact on services and about how efficient they are in delivering those services the community needs, and in managing assets necessary for providing those services.

The role of the Commission, in assessing applications for rate variations, will include the consideration of ratepayers' and communities' responses to councils' proposals. The Commission will need to understand whether councils are meeting the reasonable expectations of their ratepayers and communities and how they have considered and responded to issues of common concern to its ratepayers and community.

How the engagement process has considered the following questions will be important:

- What services does the community value most?
- What services does the community want and how much is it prepared to pay for them?
- Does the community understand the level of services that are available with current rates?
- Does the community understand what the level of services would be with higher rates?
- Does the community understand how much the Council needs to spend to implement the services and why?

Councils will have to provide a narrative in their applications for variation, supported by and including references to appropriate supporting documentation.

C.5 COMMUNITY ENGAGEMENT GUIDANCE MATERIAL

To assist councils in considering how these principles could be reflected in their community engagement strategies and to assist with variation applications we have started to put together a reference tool including engagement tools and techniques, reference points and case studies. The examples presented are not intended to be prescriptive but aim to assist councils in thinking about the types of engagement they could consider undertaking with their communities.

We expect to continue working with the sector to further develop this guidance material and that it will evolve and be updated as the framework is implemented.

Table C.2 sets out some examples of potential approaches for councils engaging with their communities and ratepayers on variations from the rates cap. Table C.3 sets out some of the tools and techniques that could be used.

TABLE C.2 EXAMPLES OF POTENTIAL ENGAGEMENT APPROACHES TO RATE VARIATION APPLICATIONS

The Framework's Community Engagement Principles	Engagement		Responsibilities	
	Aim	Examples of Tools and Techniques	Council	Community
Principle 1: The engagement program must contain comprehensive information and follow a timely process to engender feedback from the community	<ul style="list-style-type: none"> Talking with, not to, communities Finding a common ground 	<ul style="list-style-type: none"> Community consultative committee Advisory committee Round tables Briefing sessions Public meetings Workshops Interviews Charrettes (a public meeting/workshop devoted to a concerted effort to solve a problem or plan the design of something) 	<ul style="list-style-type: none"> Be prepared to be influenced by your community Establish internal systems and decision-making processes to deal with community input Choose effective and practical tools and techniques then commit to them Share information and data 	<ul style="list-style-type: none"> Be willing to be involved and accept joint responsibility for outcomes Be willing to participate in new engagement techniques – try something new
Principle 2: The engagement program should be ongoing and tailored to community needs	<ul style="list-style-type: none"> Providing opportunities for all to participate regardless of language, geographic, physical or technological barriers Building a partnership 	<ul style="list-style-type: none"> Websites Social media channels and discussion forums Printed materials (leaflets, newsletters, letters, flyers, advertisements) Focus groups (where appropriate) 	<ul style="list-style-type: none"> Effective and up to date website Reach out to the community and extend the invitation to participate Skilled staff to provide information in community languages, plain English, graphic visualisations, technical support 	<ul style="list-style-type: none"> Be prepared to respond and provide feedback Spread the word within the community and through networks

Continued next page

TABLE C.2 (CONTINUED)

The Framework's Community Engagement Principles	Engagement		Responsibilities	
	Aim	Examples of Tools and Techniques	Council	Community
Principle 3: The engagement program should prioritise matters of significance and impact	<ul style="list-style-type: none"> • A factual and clear understanding of the situation and priorities of the council and the community • Building consensus 	<ul style="list-style-type: none"> • Workshops • Field trips • Round tables • World café • Community consultative committee • Steering committees • Focus groups (where appropriate) • Planning simulation tools (where possible) 	<ul style="list-style-type: none"> • Use appropriate tools and techniques, including something new to excite interest, particularly among groups not usually involved • Make it engaging • Make clear what the community can and can't influence • Provide an evaluation tool e.g. a short participant survey 	<ul style="list-style-type: none"> • Take the opportunity to be heard • Share local knowledge • Voice ideas and concerns • Be prepared for your views to be weighed and balanced against the views of others
Principle 4: The engagement program should lead to communities becoming more informed about council decision-making	<ul style="list-style-type: none"> • A recommendation with reasons • A decision process that is accepted as having been fair and open by the community. 	<ul style="list-style-type: none"> • Publication of decisions and policies • Printed materials (leaflets, newsletters, letters, flyers, advertisements) 	<ul style="list-style-type: none"> • Share not only the recommendation or decision but the information base • Explain how stakeholder input was gathered and used • Document and report on the community input 	<ul style="list-style-type: none"> • Stay informed of issues and decisions
Principle 5: The Commission will not assess an engagement program based on a single criteria or technique	<ul style="list-style-type: none"> • Endorsement of the outcome by the community 	<ul style="list-style-type: none"> • Feedback reports 	<ul style="list-style-type: none"> • As outlined in the previous Principles 	<ul style="list-style-type: none"> • As outlined in the previous Principles

TABLE C.3 EXAMPLES OF ENGAGEMENT TOOLS AND TECHNIQUES

Tool	Tips for using	Why you might use it	Why you might not use it
Printed materials Include fact sheets, newsletters, newspaper advertising, brochures, flyers, leaflets, reports, letterbox drops, personalised invitations	<ul style="list-style-type: none"> • Use clear, plain English or translate as required • Be brief and direct but not simplistic • Make it visually interesting but not busy or slick • Use language that is inclusive and jargon free • Provide contact details (phone, email, web address) • Offer translation services • Maintain an up to date mailing list 	<ul style="list-style-type: none"> • Can reach a large target audience • Community information in regular place and format • Allows for technical and legal reviews • Documentation of community involvement facilitated 	<ul style="list-style-type: none"> • Distribution planning inadequate • Materials do not reach the mark • Materials not read • Limited capacity to communicate complicated concepts • Information misinterpreted
Information sessions Public gatherings where people can engage at their own pace, drop in individually to view plans, ask questions, provide feedback	<ul style="list-style-type: none"> • Method and content should be tailored to the stakeholder group. 	<ul style="list-style-type: none"> • Able to reach a large number of stakeholders. • Can be targeted to specific stakeholder groups 	<ul style="list-style-type: none"> • Written material may not be accessible to people with visual impairment or low literacy levels
Displays Often located in public libraries or community centres, they can also be permanently located in a shopfront, or mobile and used in shopping centres.	<ul style="list-style-type: none"> • To draw attention to a display, use inventive formats such as a colourfully painted bus or a pop up cart. 	<ul style="list-style-type: none"> • To take participation to hard to reach communities, and provide a less formal format for interaction with the community. 	<ul style="list-style-type: none"> • Essentially a one way communication tool.
Briefings Short presentations to key stakeholders, peak bodies, agencies and community groups to share information and respond to questions.	<ul style="list-style-type: none"> • Used to provide an overview or update on a project. • Presentation may be delivered by an agency representative and followed by detailed discussions in a question-and-answer format. 	<ul style="list-style-type: none"> • Can also be used as a forum for feedback, and to uncover preliminary community issues and values. • Less formal and expensive process than large public meetings. • Help to build community good will and create a more effective atmosphere for dialogue. 	<ul style="list-style-type: none"> • Make sure that all groups are treated equally. • Individuals conducting briefings should be well versed and able to answer questions, but also open and approachable to help build community relationships

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TABLE C.3 (CONTINUED)

Tool	Tips for using	Why you might use it	Why you might not use it
Workshops Small and large workshops where participants work in small groups. These may include guest speakers, general discussion, or more targeted tasks for participants such as visioning and prioritising.	<ul style="list-style-type: none"> • Need to be well designed and prepared for. • Make sure the purpose is clear to all participants and that their level of interest is equal to the level of participation required. • Table scribes are often needed to document the proceedings and tables also report back as part of facilitated meeting management. 	<ul style="list-style-type: none"> • An opportunity to provide information and personalise contact with the community. • Workshops encourage involvement and interaction and allow the gathering of community feedback. • Discussing complex issues, analysing competing options and generating ideas • Encourages joint working and problem solving Builds ownership of results. 	<ul style="list-style-type: none"> • Can be costly due to need to hire venues, independent facilitators and provide refreshments etc. • Can also expose poor preparation.
Interviews One-on-one discussion with community members or groups to gain detailed information on their views and attitudes.	<ul style="list-style-type: none"> • Use to obtain qualitative information from an individual. 	<ul style="list-style-type: none"> • Can produce highly accurate results • Adds a personal dimension • Might be used where there are sensitivities associated with privacy or concerns about security. 	<ul style="list-style-type: none"> • Necessitates more sensitivity than other methods • May raise expectations among some people or groups • May ignite community rivalry or raise allegations of special treatment • Careful preparation necessary
Field trips Guided site visits or tours of areas under discussion	<ul style="list-style-type: none"> • Involve key stakeholders. 	<ul style="list-style-type: none"> • Helps build relationships and trust. • Useful for building capacity of communities to participate in complex discussions. 	<ul style="list-style-type: none"> • Can be costly to arrange and require time commitment from both organisers and participants.
Charrettes Typically involves intense and possibly multi-day meetings that bring together a wide range of participants to generate ideas, responses and plans.	<ul style="list-style-type: none"> • Work best when focused on technical aspects of planning and can be a catalyst for cooperation among key decision-makers. 	<ul style="list-style-type: none"> • The time required to prepare, participate and report make this a process that works best in longer term engagements. • Can also be used to promote joint ownership of solutions and to defuse confrontational attitudes. 	<ul style="list-style-type: none"> • Requires considerable preparation, time and resources.

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TABLE C.3 (CONTINUED)

Tool	Tips for using	Why you might use it	Why you might not use it
Round tables Round tables are one of the more flexible engagement formats and differ from session to session.	<ul style="list-style-type: none"> • Participants may be selected for the particular perspective or understanding that they bring. • The format usually includes a presentation followed by in-depth discussion. 	<ul style="list-style-type: none"> • Allows for extended discussion and are often designed to solve a challenge. • Enables participants to hear multiple points of view through open discussion • Encourages community participants to think 'outside the square' and find common ground 	<ul style="list-style-type: none"> • Some participants may try to dominate a table discussion
'Town Hall' meetings Traditional 'town hall' style meetings are familiar, established ways for people to come together to express their opinions, hear a public speaker or proposed plan, engage in shared learning about a topic, or work together to develop solutions	<ul style="list-style-type: none"> • Do not hold a town hall style public meeting if you are not willing to allow anyone to attend, including media. A public meeting must be open to anyone. • Engage an independent chair to host and moderate • Make sure you provide for attendees who need assistance getting to and around the venue, hearing what's said, seeing what's presented, etc. • Consider childcare facilities to make it easier for people with young children to attend. 	<ul style="list-style-type: none"> • Introduces a project or issue to a community. • Provides all participants a chance to voice their concerns, issues, and ideas. • Participants need to be willing to listen to each other, which can be useful for exploring alternative strategies and building consensus. • Also useful for reaching larger numbers of people. 	<ul style="list-style-type: none"> • Unless carefully planned and well facilitated, town hall events can be high risk because they provide a platform for the loudest and most negative voices. • Many community members, especially those who fear being shouted down, will either not attend or not participate.
World Cafe This is a deliberative concept where participants work in small groups simultaneously on questions and change tables during the process, refining their understanding of an issue and working to find common ground as a community.	<ul style="list-style-type: none"> • Provide a scribe for each table to assist in keeping the conversation on track and moving. • A central moderator needs to keep the process fluid with summary thoughts captured so that a full report can be compiled after the event. 	<ul style="list-style-type: none"> • This process fosters open discussion and empathy. • World Cafe events benefit from involving larger numbers (more than 60) because they are dynamic. • Different points of view and life experience emerge very naturally. 	<ul style="list-style-type: none"> • Works best with large numbers and for deliberative formats only. • Dependent on a competent facilitator and participants willing to invest the time.

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TABLE C.3 (CONTINUED)

Tool	Tips for using	Why you might use it	Why you might not use it
Participatory budgeting Participatory budgeting is a process for involving citizens in setting priorities in the context of resource constraints, often through a working group format.	<ul style="list-style-type: none"> Need to have the councils' real budget on the table for these processes to be rewarding, constructive and enlightening. 	<ul style="list-style-type: none"> Can be used to educate the community in the difficulty of making decisions about how public funds are spent and the trade-offs that arise. 	<ul style="list-style-type: none"> Do not use this process unless you are willing to follow through on the community's preferences.
Focus groups Originally a market research tool, focus groups are small facilitated discussions involving carefully selected individuals.	<ul style="list-style-type: none"> Use to test opinion on a particular issue prior to undertaking more widespread engagement. Payment to participants is likely to be required 	<ul style="list-style-type: none"> Useful when used early in a decision-making process or when time is limited. 	<ul style="list-style-type: none"> May not be truly representative of views across the community. May be criticised because participation has been rewarded with payment.
Surveys and polls A quantitative research method to gauge views, experiences and behaviours. A research method used to extrapolate results and determine what people think about an issue.	<ul style="list-style-type: none"> Always include open-ended questions and space for fuller comments. Ensure that the questions are thoroughly tested in-house before they go public. Be prepared to spend time on drafting and refining the questions and on compiling, interpreting and analysing the results. Use digital survey tools wherever possible in large scale consultations. 	<ul style="list-style-type: none"> Straightforward Focussed and specific Can gauge a large number of opinions Easily adapted Quick and cheap Provides a snapshot of opinions at a certain time Straightforward and accurate 	<ul style="list-style-type: none"> Difficult to gather qualitative information Answers may be irrelevant Delivery methods can affect results May be too brief for people to provide their full opinions Results may be affected by poorly conceived or worded questions. Large numbers of responses, particularly on paper-based surveys, can create handling and processing burdens.

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TABLE C.3 (CONTINUED)

Tool	Tips for using	Why you might use it	Why you might not use it
Community Consultative Committee (CCC) Forum for open discussion between representatives of the community, council and other stakeholders.	<ul style="list-style-type: none"> • Ensure that membership is representative. • Assign senior participants from your own organisation. • Make sure that community participants are aware of the commitment required prior to joining. • Be prepared to be open with information. • Consider an independent chair or facilitator. • Publish minutes of all meetings in a timely fashion. • 	<ul style="list-style-type: none"> • Can be a powerful tool to demonstrate transparency and for frank and open discussions. 	<ul style="list-style-type: none"> • May be criticised because of the small number of people involved. • Can be a risk for community participants who may be seen as having compromised their positions by being too close to a process or unpopular project.
Public Notices Ad placed in local newspaper, notice boards, etc, informing the community of ways to participate, or of decisions made.	<ul style="list-style-type: none"> • A basic pre-requisite for all public policy decision-making. 	<ul style="list-style-type: none"> • Community members will look for them to know they can participate. 	<ul style="list-style-type: none"> • Public notices are not a good way to reach community members who do not normally participate, or do not have access to newspapers etc.
Partnerships Councils work together with communities to plan	<ul style="list-style-type: none"> • Make sure the governance arrangements are in place first. These can take some time to set up, but are well worth it for building trust and commitment. 	<ul style="list-style-type: none"> • Require both communities and consent authorities to work closely and transparently to reach agreed outcomes. 	<ul style="list-style-type: none"> • Not appropriate for all engagements or communities. It also may not always be possible to reach this level of trust and co-operation.
Advisory groups A group of representatives or informed individuals convened to meet regularly as a sounding board for a decision-maker.	<ul style="list-style-type: none"> • Very useful for organisations that need to build relationships and communications channels with new communities. 	<ul style="list-style-type: none"> • Advisory groups have value where an external viewpoint is needed or for when a 'temperature check' of the mood of the community on a particular issue is required. 	<ul style="list-style-type: none"> • Limited in the amount of representation they provide

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TABLE C.3 (CONTINUED)

Tool	Tips for using	Why you might use it	Why you might not use it
Expert Panel Used to gather concentrated opinions from a range of experts on a particular issue.	<ul style="list-style-type: none"> • Use to produce in-depth analysis on technical matters. 	<ul style="list-style-type: none"> • Focus intently on a specific subject. Draws on experts who can often be objective 	<ul style="list-style-type: none"> • The process needs to be carefully focussed • Breadth may be limited • May be too 'exclusive'
Resident panels and precinct committees	<ul style="list-style-type: none"> • Resident panels and precinct committees can be used to seek views on a variety of themes and can also be conducted in conjunction with other forms of engagement. • A source of local knowledge 	<ul style="list-style-type: none"> • Can be a vehicle for establishing long running forms of participation that go beyond single, issue-specific consultations. 	<ul style="list-style-type: none"> • Limited in the amount of representation they provide
Steering Committees A group of people who take responsibility for the success of a project, usually representative of the sponsors of the project.	<ul style="list-style-type: none"> • Participants need to have a good understanding of the issues and could be drawn from community leaders, elected representatives, individuals and members of groups involved in community initiatives. 	<ul style="list-style-type: none"> • Typically a group of between six and 10 people, the committee should be composed of representatives of the sponsoring organisations or agencies. 	<ul style="list-style-type: none"> • Can take on a life of their own and become adversarial if roles become blurred or if there is serious dissent.

TABLE C.4 EXAMPLES OF POTENTIAL DIGITAL ENGAGEMENT TOOLS AND TECHNIQUES

Tool	Tips for using	Why you would use it	Why would you NOT use it
Websites and web forums Websites are used to provide information about, and links to, policy proposals as well as any other information a community may need to participate. Web sites allow for the use of a wide variety of media formats, including video	<ul style="list-style-type: none"> • Can be as simple as a single page on an organisation's website with a link to a specifically designed and separately hosted community engagement website that allows viewers to participate in online surveys, contribute to online forums, post a message, view interactive videos and documents and make submissions. 	<ul style="list-style-type: none"> • Community members will often look to your website as the most obvious place to obtain information, and for many community members, it could be the only way for them to participate due to time, geographical and other constraints. 	<ul style="list-style-type: none"> • A proportion of people still struggle with the internet because of access constraints or because they are not web users. It should therefore not be the only tool you use. • Anonymous internet users may present challenges for honest, civil and open interaction.
Email Direct and efficient method of engagement	<ul style="list-style-type: none"> • Proactive, personal and powerful as a means of communicating directly with the community. • Protocols must be set regarding style, language, tone of voice, response times and privacy. 	<ul style="list-style-type: none"> • Allows you to establish a personality, or 'tone of voice', that feels personal. • As a means of responding to questions, email is immediate and efficient. 	<ul style="list-style-type: none"> • Can become devalued by overuse or by sending trivial information.
Smartphones Almost 70 per cent of Australian social media users access sites using a smartphone.	<ul style="list-style-type: none"> • Ensure that any content can adapt to different screen sizes, for example if including 3D design and game-style simulations in consultation exercises. 	<ul style="list-style-type: none"> • When you want to ensure the widest participation possible and allow people to access information and engage anytime, anywhere. 	<ul style="list-style-type: none"> • Requires specialist screen design to ensure readability and facilitate interaction.
Applications (apps) An app – short for application – is a piece of software that runs on a computer or phone and enables a program to be run on that particular device.	<ul style="list-style-type: none"> • Apps are a fun and efficient way to engage. There are apps that put the user in charge of planning for a community, to give them a sense of the pressures of decision-making. 	<ul style="list-style-type: none"> • Free apps are becoming part of the community expectation and can be a fresh way to engage, particularly with young people. 	<ul style="list-style-type: none"> • May alienate some members of the community who do not have the right equipment or cannot download the app.
Simulation tools Software to explain, describe and support a new policy or planning mechanism.	<ul style="list-style-type: none"> • Enable the user to investigate options and to visualise or experience likely consequences and impacts. 	<ul style="list-style-type: none"> • Useful where participants can have a 'hands on' experience. • Attractive to participants who are tired of old engagement techniques. 	<ul style="list-style-type: none"> • Can be expensive and may put some participants off due to being overly complex.

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TABLE C.4 (CONTINUED)

Tool	Tips for using	Why you would use it	Why would you NOT use it
YouTube Short (typically one to three minute) videos or series of photos posted on and accessed via the internet.	<ul style="list-style-type: none"> Used in conjunction with Facebook, this is proving to be a highly popular way to summarise a proposal and for community participants to inexpensively express their views and put forward their own ideas. 	<ul style="list-style-type: none"> With 11 million users, YouTube is the second strongest Australian online channel. It is a story telling medium that is accessible and inexpensive. 	<ul style="list-style-type: none"> YouTube requires that users are 13 years old and must be 18 years old to view some content.
Instagram Instagram is an online photo and video sharing social networking site.	<ul style="list-style-type: none"> Use to extend your reach into the community, and to encourage young people to participate. 	<ul style="list-style-type: none"> Inexpensive, immediate platform for sharing photos and videos of events, for example. 	<ul style="list-style-type: none"> As a platform that is often used by celebrities, and with a minimum age requirement of 13 years, this tool may have limited application.

The following reference points and case studies provide additional resources for councils to consider in developing their community engagement. These examples are not comprehensive of all the available resources for councils to guide their community engagement approaches, however, they provide a useful starting point for readers wishing to gain further knowledge on the subject of community engagement.

REFERENCE POINTS

Victorian Local Governance Association (VLGA)

The VLGA is a peak body that links local government, councillors and community leaders to collaboratively build and strengthen local governance and democracy.

The VLGA website includes resources that aim to provide local governments with the information, tools and support to consult effectively.

The VLGA has two tools for local governments and their communities to use – its ‘Let’s Talk: a Consultation Framework’ guide and the International Association for Public Participation (IAP2) Toolkit.

‘Let’s Talk: a Consultation Framework’ was produced in 2007 to provide a starting point for beginning community consultation and engagement.

The IAP2 framework and toolkit is based on the spectrum model that is used to determine the scope, tools and techniques for conducting public participation in each of the following areas:

- Inform
- Consult
- Involve
- Collaborate
- Empower

The website contains additional resources on a range of engagement topics, including pre-consultation methods, two-way or interactive consultation, choosing a method, engaging hard-to-reach groups, planning and process design and preparing a consultation strategy.

Further information: http://www.vlga.org.au/Resources/Consultation_and_Engagement.aspx

City of Melbourne

The City of Melbourne is the municipality which covers the central city of Melbourne and 16 inner-city suburbs. More than 116,000 people call the municipality home and a further 728,000 people visit the central city every day for work and leisure.

'Participate Melbourne' was launched in July 2013 to provide an additional online way for members of the community to understand and contribute to the decisions that shape Melbourne's future.

The online community complements the Council's existing engagement activities and is a key part of its commitment to being a more accessible, transparent and responsive organisation. Through Participate Melbourne, Council improves the opportunities for the community to participate in and engage with its activities and decision-making. Information about Council's decisions and performance is shared and feedback is provided to let the community know how its views have influenced Council decisions.

The City's website includes links to the details of all of its major previous engagement processes dating back to 2009-10. The City also uses social media, in addition to traditional methods, as an effective way of connecting with its many audiences.

Further information: <http://participate.melbourne.vic.gov.au/> and <http://www.melbourne.vic.gov.au/getinvolved/PastConsultations/Pages/PastConsultations.aspx>

Municipal Association of Victoria

The MAV is the legislated peak body for Victoria's 79 councils which, among other aims, has a role to advocate local government interests and build the capacity of councils.

The MAV negotiates with the Victorian and Australian Governments and other stakeholders for funding and assistance in the provision of council-provided social and community services by developing planning frameworks and capacity-building initiatives.

An example of this role includes research that aimed to improve the design and delivery of government services such as Medicare, Centrelink and the Child Support Agency as part of the Australian Government-funded Community Engagement Co-Design Prototype Project.

The research was the first phase of a co-design model used successfully overseas to engage local government, community organisations and end-use customers with the Australian and Victorian Governments to be part of the solution to improve the delivery of services.

Representatives from councils, community organisations and residents participated in workshops held in six areas which aimed to identify how services delivered by Centrelink, Medicare, the Child Support Agency, state and local governments and community organisations could be improved.

Each of the areas addressed a particular client group which included:

- older Australians (Rosebud)
- families looking for work (Fountain Gate)
- families (Epping)
- young single parents (Benalla)
- young people (Ballarat)
- families (Maryborough)

The key questions asked of the community at these workshops included:

- Where can improvements to services be made?
- Would co-located services improve delivery?
- Do services require better design to respond to the needs of service users?

The involvement of all levels of government and the community is expected to result in options for service improvements. Key outcomes included identifying agreed actions in a number of areas to enable governments and community agencies to respond in a more coordinated way to the specific service needs and expectations of those who use services in these locations.

Further information:

<http://www.mav.asn.au/policy-services/social-community/community-engagement/Pages/default.aspx>

Local Government Association UK

The LGA is the national voice of local government in the United Kingdom, working with councils to support, promote and improve local government.

Amongst the resources available on the LGA UK website is a guide, Integrating community engagement and service delivery – pointers to good practice. This was produced in 2010 to help local authorities ensure that the results of their community engagement processes are built into their service plans and the ways that they deliver services.

A guide on developing a neighbourhood empowerment plan is also available, with a template to produce a plan based on the outcomes of two empowerment mapping tools.

This guide draws heavily on case study material provided by a range of councils who have outlined their approach to connecting the views of communities to service planning and delivery.

In making the case for community engagement, the guide notes: 'It is clear that councils that develop a meaningful dialogue with their residents, in good times and in difficult ones, find community engagement and empowerment saves them time and money, creating more satisfied communities.'

The guide outlines seven key ingredients that can help lay a foundation for responsive service planning and delivery influenced by the priorities and genuine needs of local people.

- An organisational culture where councillors, directors, service managers and frontline staff value engagement
- A locally based planning mechanism that feeds into service planning
- An identifiable staff resource to link community planning to operational management
- An accessible way for residents to raise and track issues of concern, demonstrating how services have responded to their influence
- A strong message within corporately produced guidance on service planning
- A commitment to using the experience from everyday transactions (engagement between frontline staff and those who use services) to help shape those services
- An openness to considering and developing new ways to deliver services

The 2013 publication, *Our Place! Community Engagement A guide to what we learnt*, provides tips on delivering broad engagement (such as covering information that's already available, informal events, innovative mechanisms and established research techniques); three different methods in conducting more detailed work (e.g. having residents on working and steering groups and full community management of the process); ideas to maintain enthusiasm (e.g. developing a vision for a neighbourhood, reporting back on results, continuing to build capacity).

Further information: <http://www.local.gov.uk>

CASE STUDIES

Case study: Empowering communities in South Somerset

South Somerset District Council in the United Kingdom is nationally recognised for its community engagement.

The Council uses a range of community engagement tools depending on the issue in hand. Amongst these are an annual 'you decide' meeting where 100 members of the public come and have their say on alternative ways that the council could allocate its spending.

'This is a way of finding out what people do want the council to spend money on and what they do not. It is exploring the difficult decisions we constantly have to make,' said Rina Singh, Deputy Chief Executive, South Somerset District Council.

In some localities, the Council has gone further and held forums where people vote on projects that the community has put forward. Area forums are a mechanism to involve 'natural' communities in decision-making about a variety of issues. The South Somerset district area is divided into four sub-district areas, each serving about 40,000 residents.

Currently, forums are being used for prioritising projects, making decisions about the funding of projects, planning and buying in enhancements to service delivery, should the community desire them. The Council has allocated £40,000 to each of the four areas and the area forums can then engage with the public to get a consensus on what the money needs to be spent on.

HOW THE AREA FORUMS OPERATE

Residents and stakeholders in an area are invited to come to an evening session and participate in the decision-making. The heads of service, members and the portfolio-holders from Council also attend so people can speak to them about service provision.

Engagement at sub-forum level takes place in a number of ways, depending on what is the most appropriate method of bringing flexibility around engagement. The focus can be on a particular service issue and a vote taken to aid in tailoring local services.

However, the results of these engagement activities are supplemented by statistical data and information from other sources. They can then be presented to members at area committees.

OUTCOMES AND IMPACT

According to Rina Singh, the benefits of this approach to community engagement is that decision-making on council matters is seen to be within the community, which can have a say on service enhancements.

'Feedback from participation events has been extremely positive. Attendance has increased each year, which shows an engaged community. Residents feel engaged and able to influence services,' she said.

'It is human nature for people to want everything. But when people feel involved they are more likely to understand that there isn't a bottomless well. It helps people understand the reasons why a particular thing is being done and why something else isn't. Without that understanding, people are less tolerant.'

South Somerset has built on this success and taken this to the next level through:

- Engaging the community in design and delivery of services;
- Enhancing participatory budgeting, enabling larger 'community kitties';
- Developing a commissioning role for local services; and
- Securing decision-making at a local level through joint agency committees.

KEY LEARNINGS

- Know your community. Try different approaches as one size doesn't fit all. Thought needs to be given to what needs to be achieved by the end of the evening session so that the most suitable method is applied.
- Be clear about the level of empowerment on offer. Managing expectations is the key to successful engagement.
- Be prepared on the day. A slick operation goes a long way.
- Close the loop. Always ensure that outcomes actions from the event are followed through and communicated. Absence of this can damage reputations and relationships with the community.

More details are available at:

http://www.local.gov.uk/localism-act/-/journal_content/56/10180/3511155/ARTICLE

Case study: Handing decision-making back to the community

In Western Australia, Melville City Council's experience in handing decision-making back to its community led to its Project Robin Hood being highly commended in the capacity building category of the 2014 Core Values Awards, run by the International Association of Public Participation Australasia (IAP2).

Project Robin Hood provided an opportunity for community members to develop projects that contribute to their well-being, allowing them to vote on the projects they wanted to progress and then providing funding for this to occur.

Based on the principles of participatory funding, the project aimed to:

- provide an opportunity to deepen citizenship and democracy
- empower citizens to influence public decisions that directly affect their lives
- enhance government responsiveness and accountability to citizens
- enhance citizen understanding of public budgets and budget constraints, creating more realistic expectations
- enhance citizen confidence in Council
- promote greater democracy and equity in the allocation of public resources
- encourage community cohesion and help build understanding, trust and consensus among citizens
- promote productive dialogue and constructive working relationships between City staff, elected Members, citizens and communities.

The process was led, developed and owned by the community, represented by the Youth Advisory Council (a group open to all young people aged 12 to 25 years who live, work, play or study in the City of Melville). The Youth Advisory Council was given a \$100,000 budget for the community to vote to spend on projects initiated by the community. Their task was to develop a transparent, open process that provided the community with equal opportunity to participate.

This presented a major shift in usual practice. Historically, local government processes for budget expenditure are controlled by the organisation, thereby mitigating any risk. Project Robin Hood turned this upside down with control being handed to the community to not only develop the projects, but also vote on the ones to be implemented.

To maintain a purity of the process, organisational staff was deliberately 'hands off' in the design of the process to spend the allocated \$100,000. Training, workshop attendance, participation of organisational technical experts and criteria to support the decision-making was incorporated into the project process.

The \$100,000 was distributed amongst a number of small grants (\$1,000 - \$20,000) for projects presented by the community. Unlike traditional grant funding, the decision-making for the allocation of the budget to those proposed projects was made by the community through an online voting process.

A major marketing and communications strategy was developed and implemented by the Youth Advisory Council project members, which centred on the Robin Hood theme. This included a highly visible presence at places such as State Government election polling booths (with an election in the middle of the project), major music events, cafes and shopping centres.

Half a million dollars' worth of applications were received from the community, 50 + projects, 1,379 individual voters, and 674 comments recorded online. The community selected 12 projects on which to spend the \$100,000. Cheques have been issued and handed directly to the community members with some projects now complete and all commenced.

More details are available at:

<https://www.iap2.org.au/awards/2014-core-values-awards>

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APPENDIX D — PROPOSED ANNUAL COUNCIL INFORMATION REQUIREMENTS

D.1 OVERVIEW

This appendix details the Commission's proposed annual reporting requirements with respect to compliance with the cap and council baseline information. At this stage the requirements discussed below are indicative only. The Commission will continue to refine these requirements over the coming months in consultation with the sector. A draft of these requirements will be included in the final report.

D.2 MONITORING THE CAP AND VARIATION CONDITIONS

Table C.1 below lists the indicative information the Commission is proposing to monitor each year in relation to local government compliance with the rates capping and variation framework and to identify discrepancies between forecast and actual outcomes.

With the exception of the forecasting of supplementary revenue and the breakdown of costs that constitute service rates and charges, much of the information below is already reported by councils in their annual reports, Strategic Resource Plans (SRPs) or in submissions to the Victorian Grants Commission (VGC). Monitoring this information should therefore not impose an additional reporting burden on the sector. The Commission will consult with the sector (through a working group) to determine the most efficient way to collect this information, while ensuring the robustness of the data.

TABLE D.1 INDICATIVE INFORMATION TO BE MONITORED FOR COMPLIANCE WITH THE CAP AND APPROVED VARIATIONS
(\$ million)

	Actual (2015-16)	Forecast (2016-17)	Forecast (2017-18)
Total council revenue requirement (all sources)			
General rates			
Municipal charges			
Service rates & charges			
Special rates & charges			
Supplementary rates			
Statutory fees & fines			
User fees & charges			
Net gain(loss) on disposal of property, infrastructure, plant and property			
Other income			
Grants (all sources)			
Contributions – monetary			
Contributions – non monetary			
Miscellaneous			
Total value of rateable properties^a			
Total number of rateable properties as at 1 July^a (no.)			
Breakdown of garbage related costs:			
Council cost			
Landfill Levy			

^a At the commencement of the financial year

D.3 BASELINE INFORMATION

As discussed in chapter 4, the Commission is proposing that councils complete a baseline information template on an annual basis. The purpose of the baseline information is to provide a more detailed picture of each council's starting point with respect to services, assets and infrastructure, financial position and how this might change over time.

The baseline information is intended to assist councils to demonstrate both to their communities and subsequently to the Commission, the need for a variation above the rate cap in relation to the key areas of council operation, and the potential trade-offs and impacts associated with different options to addressing the need.

It will also assist the Commission to monitor the service and performance outcomes for ratepayers and communities under the framework and to detect unintended consequences or deterioration.

While the baseline information will initially only be used to assess changes within a council, the Commission anticipates that over time it will form a valuable database on council performance, from which further opportunities for benchmarking and trend analysis can be explored.

D.3.1 WHAT WILL BE REQUIRED?

It is anticipated that the baseline information will require councils to provide integrated information about:

- council services, including priority services (consistent with Council Plans and SRPs)
- the outputs and outcomes used to measure performance in these priority services
- the revenues and expenditures for these services (reconciled to audited annual reports)
- the capital works used to support these prioritised services and how this expenditure relates to the councils' asset renewal needs.

It is proposed that the information will be populated using council budgets, based on the current financial year, on an annual basis starting from 2015-16. As with other information discussed in section 1.1 above, much of the anticipated information to be included in the baseline template is already reported by councils in their annual budgets and SRPs. To minimise the burden on councils, one option being considered by the Commission is that, where possible, we will pre-fill sections of the template using the existing reported information. To ensure that the collated information is accurate, the Commission will require each council to verify its contents, including reconciling figures back to annual budgets.

For councils that apply for variations to the rate cap, the template will need to be provided on two scenarios which is discussed in table D.2. This will help enable the Commission to directly observe the impacts of variations.

TABLE D.2 BASELINE INFORMATION TEMPLATE REQUIREMENTS

Council intentions	Requirement
No intention to apply for variation	Submit baseline information template with budget data by January 2015.
Intention to apply for variation	Councils must submit two baseline information templates. One showing adherence to the cap and the other showing the impact of the variation. These can be provided between January 2015 – March 2015.

D.3.2 PILOT TEMPLATE

The Commission is working with a group of six councils (two metropolitan, one interface, one regional city, and two rural) to design a pilot template of the baseline information. During the consultation, councils have been able to populate early drafts and have provided valuable feedback. Preliminary feedback indicates that the proposed information requirements can be both useful to the councils and do not result in an onerous reporting burden. The Commission will establish a working group to obtain wider feedback from the sector and refine the template further before a draft is published in the final report.

D.4 PROCESS FOR FORMALISING REQUIREMENTS

A transitional approach to implementing the annual reporting requirements for councils under the framework will be necessary to provide sufficient time for consultation with the sector and to provide time for councils to develop the systems and processes to capture all of the required data. The Commission will provide guidance to councils on how to prepare the information. An indicative timetable is set out in table D.3.

TABLE D.3 TIMELINE FOR FORMALISING COUNCIL REPORTING REQUIREMENTS

Indicative dates	Activity
August-September 2015	The Commission will establish a working group to refine and formalise the reporting requirements for monitoring the cap and baseline information template
September 2015	Draft information for the cap and baseline information template released with final report
November 2015	Finalise baseline information template
January to March 2016 (transitional date)	Councils return populated baseline information template (year 1). Support and guidance will be provided to populate the data, to those councils that need it
November 2016	Councils provide the baseline information

APPENDIX E — SUMMARY OF CONSULTATION

E.1 MEETINGS

PRE-DRAFT REPORT CONSULTATION

In the period prior to the release of this Draft Report, the Commission has undertaken wide consultation with those who will be affected by the introduction of the rates capping and variation framework. The purpose of this initial consultation period was to gather information, data and ideas from the sector, ratepayers and other interested parties. We also used this time to test ideas and options as we were formulating them.

During this time we held and attended meetings with ratepayers and representatives from ratepayer associations; local government councillors, officials and staff; representative bodies such as VLGA, MAV, LGPro, FinPro; and unions such as the ASU, ANMF and Professionals Australia. We have had ongoing discussions with VAGO and other state government agencies including LGV. We have met bodies such as the VFF and interested parties from the private sector. We have also spoken to our colleagues in New South Wales at IPART and OLG about rate pegging in NSW.

Dr Ron Ben-David and Andrew Chow have presented at several forums including the LGPro CEO Forum, VLGA Rate Capping Forum and the 2015 ALGWA Conference. To date the number of meetings, forums and presentations we have undertaken exceeds 55. We have engaged with representatives from most Victorian councils via individual meetings, forums and workshops. We also released our first newsletter in June as an update on our review for interested parties.

TABLE E.1 CONSULTATION PRE-DRAFT REPORT
Meetings and Events

November 2014	
Meetings	DTPLI (now DELWP)
February 2015	
Meetings	VLGA DELWP/LGV DTF Randwick City Council (NSW) Warringah Council (NSW) IPART (NSW) Office of Local Government (NSW)
March 2015	
Meetings	MAV Strathbogie Shire Council VAGO VGC DELWP/LGV Hume City Council LGPro Wangaratta City Council Greater Dandenong Shire Council
Presentations/Forums	LGPro CEO Forum
April 2015	
Meetings	VFF Minister for Local Government's Mayoral Advisory Panel Manningham City Council DELWP Professionals Australia CT Management Group
Presentations/Forums	Great South Coast Group VLGA Rate Capping Forum

Continued next page

TABLE E.1 (CONTINUED)

May 2015	
Meetings	<p>DELWP</p> <p>Trevor Dance (Sunbury Ratepayers)</p> <p>ANMF</p> <p>ASU</p> <p>VLGA</p> <p>Ratepayer Associations including Ratepayers Victoria, Monash Ratepayers Association, Mornington Peninsula Council Watch, Mornington Peninsula Ratepayers Association, Monash Ratepayers Association, Knox Ratepayers Association, Sunbury Residents Association</p> <p>Baw Baw Shire Council</p> <p>Cardinia Shire Council</p> <p>Kingston City Council</p> <p>VCCIA</p> <p>Strathbogie Shire Council</p> <p>Bayside City Council</p> <p>Glen Eira City Council</p> <p>CT Management Group</p>
Presentations/Forums	<p>MAV Board Meeting</p> <p>Inner Southern Metropolitan Mayor's Forum (including Bayside, Boroondara, Glen Eira, Kingston, Stonnington and Yarra City Councils)</p> <p>LGPro Corporate Planners Network Special Interest Group</p> <p>RCV Mayors, Councillors and CEOs Forum</p> <p>2015 ALGWA Conference</p> <p>IPWEA Rate Capping Information Session and Workshop</p>
June 2015	
Meetings	<p>Local Government Sector Reference Group</p> <p>Interface Councils Group including Hume City, Mitchell Shire, City of Whittlesea</p> <p>Baw Baw Shire Council</p> <p>Hume City Council</p> <p>Boroondara City Council</p> <p>LGV</p> <p>Inner Southern Metropolitan Mayor's Forum (including Bayside, Boroondara, Glen Eira, Kingston, Port Phillip, Stonnington and Yarra City Councils)</p> <p>Greater Dandenong City Council</p> <p>Merv and Rohan Whelan</p>
July 2015	
Meetings	TBC
Presentations/Forums	TBC

POST-DRAFT CONSULTATION

We will continue our consultation with the sector and interested parties following the release of this draft report. We will be seeking feedback on the proposed framework as it is outlined and aiming to canvas the full range of perspectives ensuring we hear a balance of views.

We will be holding a number of public information sessions throughout the month of August as detailed in the table below. These sessions are intended to clearly articulate the framework, explaining our observations and recommendations, and explain our process of analysis. These sessions will be open to anyone who is interested in the framework and provide opportunities for them to their feedback to us directly. The details for the public information sessions will also be placed on our website.

E.2 WHAT IS THE FEEDBACK FROM THE COMMUNITY AND THE SECTOR?

Our consultation paper released in April 2015 asked interested parties to make submissions in response to a number of questions and any other matters they believed important for us to consider in designing and implementing a rates capping and variation framework. We received 287 submissions from ratepayers, ratepayer associations, councils, council service providers, sector peak bodies, unions and community organisations. The submissions have provided us with insights into how the sector and the broader community think the local government rates capping and variation framework should work.

The following section outlines some of the key issues identified in submissions (a summary of the submissions can be found in table E.2 to E.23).

E.3 RATEPAYER'S VIEWS

We received 187 submissions from ratepayers and ratepayer associations. The majority of which supported the introduction of a rate capping and variation framework. Those who were opposed were concerned with the potential for deterioration in council service provision and asset management and maintenance under the framework.

It was commonly viewed that while a consumer price index (CPI) cap may not accurately reflect council costs, it reflects the communities' ability to pay. Some ratepayers suggested a cap based on the local government cost index (LGCI).

Some ratepayers suggested that the rates cap should apply differently to councils to account for cost pressures specific to them, for example interface councils facing high infrastructure and service demand or rural councils with smaller rate bases and large road networks. Other ratepayers suggested that if this were the case, ratepayers across Victoria would be inequitably treated based on the council area in which they live.

A number of ratepayers suggested that it is important for the Commission to include a productivity factor into the cap to ensure councils continuously strive to achieve efficiencies in their operations. It was suggested that rate increases above the cap should be once-off and not become part of council rate bases (that is, rates and charges in the long-term should grow in line with inflation). Some ratepayers also argued that councils should not be able to unnecessarily increase borrowings in lieu of rates increases.

Regarding the variation process, ratepayers generally emphasised the need for a robust and systematic approach. Suggestions to ensure variations were justified included:

- incorporating variations into long-term plans
- sufficient community engagement
- sunset clauses for variations, and
- different approaches for controllable and non-controllable costs.

Most ratepayer submissions supported greater transparency and more meaningful engagement between councils and ratepayers.

Some ratepayers also suggested that indicative forecasts be given to councils for planning purposes, that there be a review of the framework in two years' time and that the Commission be given a determinative role under the rate capping and variation framework.

E.4 COUNCILS, COUNCIL GROUPS, COUNCIL SERVICE PROVIDERS AND COMMUNITY BASED ORGANISATIONS VIEWS

Submissions from most local councils raised concerns about the appropriateness of using the CPI to cap rates. They argued that CPI does not reflect movements in the costs of delivering council services and that the wages, construction costs and utility costs have all been typically growing above CPI. It was suggested that capping rates at the CPI would result in perverse outcomes for service provision and asset renewal. They advocated for a different basis for the cap, mainly referring to adoption of a LGCI.

These stakeholders also supported indicative cap forecasts and the ability of councils to apply for multiple years of above rate cap increases. Most councils also supported the use of a forecast rather than an historical index in setting the rate cap. Eight councils disagreed with this and preferred the use of a historical index.

A near universal message in council and council affiliated groups' submissions was that the variation process should be simple, clear, inexpensive and not administratively difficult. Many submissions suggested the variation process should run in line with councils' four year council plan and strategic resources process. It was noted that an onerous variation process would discourage some councils from applying even when their case may otherwise be justified.

Most councils and council affiliated groups were concerned that if a cap were set too low, there would be incentives for councils to let infrastructure deteriorate and service levels fall. Many not-for-profit community groups and council service providers were concerned that if this were the case, job losses could also occur, especially in council services, such as health and family care.

Most councils and other council affiliated groups suggested that the framework should align with the current community engagement process used by councils. It was suggested that there was ample community consultation at present, and that any additional community engagement on top of the existing requirements could diminish the clarity and usefulness of information being delivered to the community.

A number of councils commented that the Commission should have a monitoring and advisory role in the framework. Some councils indicated that they should have the final say in what level rates are set at. On the other hand, there were a few councils and service providers who supported the Commission having a determinative role,

commonly citing the independence of the Commission and the need to avoid political interference in the process.

The submissions from councils, council groups, service providers and community organisations also identified a number of the unique features of councils, which are discussed below.

RURAL COUNCILS

Rural councils stated that they face various challenges in service delivery and asset management compared to larger and metropolitan councils. Rural councils have less capacity to increase rates revenue due to their smaller populations, and are the most reliant on Commonwealth and State Government grant funding.¹⁰⁵ They have larger road networks to manage, more disperse and older communities to support, fewer staff and resources to manage their operations, and are most susceptible to natural disasters such as bush fires and floods.

REGIONAL CITIES

Like rural councils, regional cities have commented that they typically have large road networks to manage with more disperse communities relative to metropolitan councils. Regional cities also act as a hub for surrounding areas which place greater demand on their infrastructure and services.

PERI-URBAN COUNCILS¹⁰⁶

Peri-urban councils stated that they face a rapidly increasing population and the challenge for them is to fund growth related infrastructure and services while maintaining basic and improved levels of services and infrastructure to their smaller towns. They also need to manage important agricultural and natural environment resources. Like rural councils and regional cities, peri-urban councils have generally disperse communities, large road networks, fewer council staff and resources and a greater susceptibility to natural disasters.

¹⁰⁵ Rural councils are reliant on the Financial Assistance Grant from the Commonwealth Government. Grants are indexed annually in line with population growth and inflation forecasts but the indexation has been 'paused' for 3 years (from 2014-15 to 2016-17). Rural councils reported that they have been affected significantly by this development.

¹⁰⁶ These include the shires of Bass Coast, Baw Baw, Golden Plains, Macedon Ranges, Moorabool, Murrindindi and Surf Coast. These councils are located on Melbourne's growth corridor and the regional cities of Geelong, Ballarat and Bendigo.

INTERFACE COUNCILS¹⁰⁷

Interface councils, like peri-urban councils, have commented that they face challenges with population growth and high demand for services and community assets. They incur significant maintaining Melbourne's green wedges, including services such as pest and weed management and native vegetation management.

METROPOLITAN COUNCILS

Metropolitan councils have commented that they have high population and very diverse communities. They also have to manage some of Victoria's green wedges and maintain assets which are matured and of very high value.

E.5 PEAK BODIES

Like councils and council affiliated groups, the submissions from the peak bodies argued that CPI would be an impractical and potentially detrimental cap for local government. It does not account for the true costs of councils; mainly comprised of wages, materials and services and construction and in rural and regional areas, transportation costs and a lack of competition means that increases in costs can be much higher than CPI. There was strong support for the use of an LGCI or for a mechanism that accounted for structural differences in councils.

The peak bodies favoured a rate cap based on a forecast rather than an historical index. They also preferred multiple year forecasts of the cap. Most peak bodies suggested a single cap approach would be the best solution, given the potential inequities to ratepayers across the state depending upon their location, that a single cap would be clear and simple, and that the variation process may be better suited to handle council diversity.

In general, most peak bodies identified rate revenue or rate revenue plus municipal charges as the base to which the cap should apply, citing the difficulties of capping

¹⁰⁷ The Interface Councils lie at the interface of metropolitan Melbourne and rural Victoria, sharing aspects of both urban and rural communities. Characteristically, the population dispersion across the municipalities is concentrated around urban areas, with significant numbers of people living in rural townships. In all of the municipalities, approximately 70 per cent of the population live in about 30 per cent of the area. The interface councils are Cardinia Shire Council, City of Casey, Hume City Council, Melton City Council, Mitchell Shire Council, Mornington Peninsula Shire Council, Nillumbik Shire Council, City of Whittlesea, Wyndham City Council and Yarra Ranges Council.

user charges such as waste. There were differing opinions on whether total rates revenue should be capped or a rates-per-assessment cap be adopted. One body mentioned that a rates-per-assessment approach would be unfair to growth councils. Another mentioned a per-head of population would be more reflective of costs than a per-property assessment.

For the variation process, peak bodies supported a clear process with variation thresholds. Most peak bodies thought the variation should be open to all councils for a variety of reasons including renewal gap problems, new capital projects, cost shifting, financial sustainability, grant funding cuts and many more. They wanted the variation process to have as little administrative burden on councils as possible and for there to be a tiered approach to the scrutiny of applications.

It was suggested that community engagement for rates capping should align with councils' current processes and existing examples of good engagement. It was mentioned that sometimes there is not a great level of interest from the community for some councils' engagements, such as annual budget setting. Most peak bodies supported a review of the rates capping and variation framework at some stage or on a regular basis in the future and for the costs of the regime to be borne by the State Government.

E.6 UNIONS

Unions did not consider CPI to be a reasonable cap on local government. It was mentioned that enterprise bargaining agreements have included average wage increases of 4 per cent each year, which is far greater than average annual CPI increase of 2.8 per cent. The cap should be set as an index which better reflects council wages, and infrastructure and asset renewal. There was fear that a low cap will cause job losses and the outsourcing of council services, and that if the variation process was too onerous it may act as a disincentive for applications.

In terms of community engagement, it was suggested that local governments already consult considerably with communities and that the new framework would add needless administrative burden to councils' budgeting processes. It was recommended that the Commission should consider ways to ensure that the process is fast and economical for councils.

TABLE E.2 QUESTION 1: WHILE A CAP BASED ON CPI IS SIMPLE TO UNDERSTAND AND APPLY, ARE THERE ANY ISSUES THAT WE SHOULD BE AWARE OF?

All respondents, with the exception of two councils and majority of ratepayers/Ratepayers associations, do not support capping rates at CPI. The main argument against CPI is that it is not an appropriate measure of the movements in costs of the delivery of council services; and key council expenditures (wages, construction, utilities, etc.) have been increasing more than CPI. They consider the likely outcomes of capping rates at CPI to be: all councils applying for variations, large reduction in services and deterioration in quality of vital community infrastructure over time, difficulty in retaining staff, job losses and cutbacks on non-core services.

Councils

Majority's response:

- CPI is not an appropriate measure of the movements in costs of the delivery of council services and therefore should not be the cap.
- CPI represents only a small proportion of local government costs.
- Key local government expenditure are related to wages/salaries, construction and utilities and they are all increasing above CPI.

Capping rates at CPI will result in:

- Large reduction in services and deterioration in quality of vital community infrastructure over time (and rural councils will be most affected).
- All councils seeking variations above the cap.

Councils also consider that CPI is not stable.

Other responses from councils

A council supports CPI as a cap if it's the RBA's target of 2.5 to 3 per cent.

A council questions the reliability of an LGCI to accurately reflect the cost pressures on all councils evenly given the diverse nature of councils. Considers CPI as widely understood and is calculated by a trusted, reliable and independent agency; if transparency is a key principle underpinning the framework then CPI should be used and not LGCI which may lend itself to perceptions of self-interest.

A council is asking which CPI will be used.

One council does not support rate capping at all.

Peak Bodies

Peak bodies do not consider CPI as adequate or appropriate for local government cost escalation.

Costs shifting and road and building construction costs have more bearing than CPI.

In rural and regional areas, material and transportation costs and reduced competition means costs can be much higher; also, these councils have significantly greater restraints on their revenue raising capacity due to their dependency on grants and their limited opportunities to recoup funding via charges and fees and low and fixed income base of many communities.

Other council groups

Other council groups consider CPI as not reflective of changes in the input prices of council services.

Continued next page

TABLE E.2 (CONTINUED)

Ratepayers /Ratepayers Associations

Majority of ratepayers and Ratepayers Associations support capping rates at CPI.

Additional comments/suggestions:

- Review the cap every 2 years.
- CPI may be not appropriate when dealing with council costs but appropriate to use when dealing with the communities' capacity to pay.

Other responses from Ratepayers / Ratepayers Associations

Some ratepayers considered that CPI is not an appropriate index for LG.

A small number reject any form of rate capping; do not want services and infrastructure to deteriorate.

Not-for-profit community groups

Do not support capping at CPI.

At CPI cap, councils might start to cut back on non-core services.

Service Providers

Service providers do not support capping rates at CPI.

Council costs are driven by employment costs.

Capping at CPI may adversely impact on the essential delivery of Maternal and Child Health and Immunisation Services to local communities.

Capping rates fails to account for the diverse needs of different communities. Arbitrary caps, without proper consideration of each individual Council's infrastructure needs and capacity to pay are detrimental to the quality of Local Government.

Unions

Both ASU and AEU do not support capping rates at CPI.

Education and training wage increased by an average of 4% compared to the average annual increase of 2.8% for CPI over the last ten years; if councils cannot offer comparative salaries of teachers and educators then councils will not be able to retain their early education staff.

CPI does not measure Council costs; likely consequences of using CPI are: cut back on the services, run down of asset renewals exacerbating the already sizable asset-renewal backlog, councils exit some services; councils contract out services to the lowest bidder.

TABLE E.3 QUESTION 2: WHAT ARE SOME WAYS TO REFINE THE CAP (FOR EXAMPLE, ALTERNATIVE INDICES), IN LINE WITH THE GOVERNMENT'S OBJECTIVES?

Except for some Ratepayers Associations and ratepayers, majority of respondents support the development by an independent agency of an LGCI. However, their recommended LGCI tries to capture almost all cost pressures being faced by councils. They consider that LGCI should not only account for movement in wages and construction costs but there should be an additional x% to account for cost shifting; defined benefits; renewal gaps; new obligations; growth; levies; council location, dispersion, capacity to raise revenues and dependence on grants, etc.

There were mentions of an efficiency measure: (1) arbitrary efficiency measures may have unintended consequences particularly if targets are implemented before councils' individual level of efficiency can be properly determined; (2) a productivity factor may be introduced after the transition.

Councils

Majority's response:

- Develop local government cost index or consider MAV's LGCI.

Two of the suggested variations on the LGCI are:

- A core LGCI that accounts for changes in wages, construction costs, other operating costs plus an additional factor to account for cost pressures that are beyond their control such as cost shifting, defined benefits, reduced grants, new legislation.
- A core LGCI plus an additional factor to account for infrastructure renewal.

The LGCI should be developed and verified by an independent agency.

Other responses from councils

RBA's underlying CPI.

RBA's 2-3% CPI forecast.

Combination of CPI and AWE; this will have more credibility in the community than a LGCI; infrastructure maintenance and renewal gap must be a key factor in the ESC's consideration of rate variations and also given much more prominences in council reporting.

ESC to set an upper limit of 5%.

Consider IPART's rate peg.

Consider other indices such as ABS's Road and Bridges Construction Index, WPI, AWE.

Base cap should be RBA's CPI forecast of 2-3% plus 1 to 2% to account for state government imposed obligations or cost shifting; above this base, cap councils will need to apply for variations.

Cap should reward those who have managed their finances responsibly.

On a productivity measure:

- Arbitrary efficiency measures may have unintended consequences particularly if targets are implemented before council's individual level of efficiency can be properly determined.
- A productivity factor may be introduced after the transition.

Continued next page

TABLE E.3 (CONTINUED)**Peak Bodies**

There are strong suggestions for an LGCI which is independently developed and verified

Said index should:

- take into account new obligations imposed, cost shifting, geographical location, average weekly earnings, defined benefits and reliance on rates as a proportion of income
- consider a core LGCI, an adjustment factor (for new regulations, defined super, new obligations imposed by State) and an infrastructure renewal factor (to recognise the relative starting point for a council)

MAV's LGCI is more closely aligned with council costs

Any restrictions on rates revenue needs to account for local government diversity and be accompanied by measures to particularly protect those councils that will be substantially affected

Other council groups

ABS-developed index for Victorian local governments

LGCI

The application of a rate cap on rural councils must be attended with greater sensitivity and flexibility for councils to meet their already over committed financial position; recommended that a financial model is constructed to test the combined impact of freezing commonwealth grants and rate capping on small rural councils as well as their capacity to absorb further shocks

Ratepayers / Ratepayers Associations

Should be consistent with VAGO's recommendation of a suitable and agreed sector cost index; some commented it should also have a productivity factor

Whilst there was some support to use NSW as a workable model using MAV's LGCI, many did not support for MAV's LGCI:

- MAV's LGCI too high
- MAV's LGCI is not an appropriate index; ABS produces Selected Living Cost Indexes, PPI, WPI, Domestic Final Demand which are all unbiased, proven and robust compared to MAV's LGCI.
- LGCI's reported weaknesses (not reflective of growth, better quality of services and new services) are inaccurate: growth in local government brings extra rates in proportion to the costs of the population growth; improved quality should mean reduced waste and lower cost; increased scope of services should not be indexed as this is optional not mandatory

Other comments:

- IPART's rate peg, ESC should allow also for productivity factor.
- Government should first review councils financial position before determining what framework should be introduced.
- Those on Centrelink payment should pay only ten per cent of their annual income for rates.

Not-for-profit community groups

There should be weights for things like disadvantaged and cultural diversity such that councils with such challenges will have higher caps

Continued next page

TABLE E.3 (CONTINUED)**Service Providers**

Alternative indices:

- Real wage growth or MAV (or other's) LGCI; a wage growth based cap; cap that averages CPI/Wage trends; multiple caps.

Unions

- Index should reflect the expenditure of councils on wages, infrastructure and asset renewal; criteria must acknowledge LG's role as a partner with Commonwealth and State Governments in service provision to the Victorian community and the expectations and obligations that entails.
- If the ESC or the State government attempts to modify a certified enterprise agreement lawfully entered into by the Council and the ASU, with the objective of bringing it within the rate cap, such a move will fly in the face of the objectives of the Fair Work Act and would, at any rate, be of questionable legality.
- At a minimum, it should cover each councils' infrastructure needs and must take into account the differing requirements of different councils.

TABLE E.4 QUESTION 3: SHOULD THE CAP BE SET ON A SINGLE YEAR BASIS?

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

Majority of respondents supported an annual cap plus indicative caps for the next 2 to three years to help them plan. But there are also a few councils which favour setting multi-year caps aligned with Strategic Resource Plans (SRPs) for certainty (with a mechanism to review rates increases during the life of the SRP when circumstances changed).

Councils

Majority's response:

- Annual cap plus indicative caps for the next two to three years to align with SRP.

Other responses from councils

- Multiple caps aligned with SRP to allow certainty; with a mechanism to review rates increases during the life of SRP should circumstances changed.
- 2 years cap plus 2 years indicative caps.
- A 'minimum' annual cap for the duration of SRP.
- Single cap only

Peak Bodies

- 2 years cap plus indicative caps for the next two years.
- Agree to multi-year caps; should align with SRP.

Other responses from peak bodies

- Variation should be applied for multiple years given the council plan and SRP extend for the term of the council; this promotes more effective infrastructure planning and delivers and identifies the plan of the council for its entire term

Other council groups

- Annual cap plus indicative caps for the next years.
- The cap should be multi-year with the opportunity to return to the ESC to make a case for changes during the term of the agreed cap.
- Implies support for a multi-year cap.

Ratepayer /Ratepayers Association

- Annual cap for the term of SRP subject to yearly change; also provide 10 year CPI forecast for the LTFFP.
- Annual cap plus indicative caps for the next three years; should align with SRP.

TABLE E.5 QUESTION 4: SHOULD THE CAP BE BASED ON HISTORICAL MOVEMENTS OR FORECASTS OF CPI?

Majority of respondents recommended that the cap be based on forecasts of CPI/alternative index because they are more likely to reflect their future needs. Eight councils favour historical figures because they can be fairly established and removes uncertainty.

Councils

- Forecast - aligns with council budgeting; more likely to reflect future needs; minimises any mismatch between price changes being experienced as they are being incurred.
- Some councils further suggested that there be a true up.
- Suggested sources are DTF, commonwealth and state governments' Budget, RBA, ABS.

Other responses from councils

- Historical - can be fairly established and removes uncertainty; also argued that forecasts are subjective and open to debate.
- Consider both forecast and historical.
- Use the December quarter.

Peak Bodies

- MAV recommended DTF's forecast and noted that historical numbers will lead to inappropriate cap and variation regime.
- The Revenue Management Association suggested forecast.

Other council groups

- Cap should be announced by 30 November each year.

Ratepayers / Ratepayers Associations

- Forecast with true up.

TABLE E.6 QUESTION 5: SHOULD A SINGLE CAP APPLY EQUALLY TO ALL COUNCILS?

Majority of councils prefer a different cap per council group but there are also strong suggestions for a single cap combined with a more flexible and straightforward variations framework. Most peak bodies support a single cap for various reasons (consistency across councils, equal treatment of ratepayers, and a sufficiently flexible variations framework). MAV acknowledged that some of the diversity factors may be better addressed in the variations framework but asked ESC to consider whether systematic differences between groups could be more appropriately considered through differential caps.

It is suggested that ESC looks into the VGC adjustment factors when taking into account diversity.

Councils

It should not be a single cap. Options suggested are:

- Different for interface (1.5 per cent higher to account for growth) and rural councils (huge network of roads to maintain, low rate base and no alternative sources of income).
- Different for metro councils (large population) and rural councils (huge network of roads).
- Set on a per region basis.

Factors that ESC needs to consider:

- location, isolation, dispersion
- road length per capita vs. own source revenue
- council's revenue raising capacity
- population
- VGC adjustments (population dispersal and road length, etc.) to account for diversity
- reliance on rates revenue.

Other responses from councils

A number said it should be a single cap.

Ensures consistency among councils.

Easy to understand, apply and communicate state-wide; allows community to understand what is being proposed; avoids debates.

If the variations framework is sufficiently flexible to meet the diverse needs of each council then a single cap is easy and simple to administer.

Different caps would cause a great deal of inequity and confusion among Victorian ratepayers.

Did not state preference but made the following comments:

- Tiered approach – below or equal to cap no review; a certain % above the cap light review; more rigorous review for higher percentage increases above the cap.
- A one per cent increase for Towong is less than \$50k while for a metro it could equate to \$1m.
- There should be equity in how the cap is adjusted.
- Multiple caps not easy to understand; a single cap may be too simplistic.
- Each council must be assessed in setting a cap.

Continued next page

TABLE E.6 (CONTINUED)**Peak Bodies**

Most stated it should be a single cap:

- Should be consistent across councils.
- Ratepayers should be treated equally although a single cap would be inconsistent with Principle 1.
- If the variation framework is sufficiently flexible to meet the diverse needs and circumstances of councils then a single cap would be the simplest to administer.

Given the diversity of the sector, the complexity at stake effectively rules out the possibility of an index able to capture the cost factors relevant to all councils. For VLGA, the substantive issue is the regime for granting variations. A rate cap must constitute a baseline only, with increase to be granted 'as course' where council can make a reasonable case.

Different cap per council group:

- Framework must be sufficiently flexible to be able to respond to the specific circumstances of each but recognised that while these issues may be considered within the variations, the ESC may wish to give consideration to whether systematic differences between groups could be more appropriately considered through differential caps.

Other responses from peak bodies

If different per group then ESC should consider: inner city, middle suburbs, interface areas (growth), interface areas (green wedges), peri urban areas, regional centres, rural; also a more sophisticated multi- cap model would recognise the relative starting point for each council based on financial sustainability

If a state-wide LGCI is adopted plus adjustment factor (such as infrastructure levy) the rationale for the differences should be made clear to the community

Other council groups

A few stated the cap should be different per council group:

- Higher cap for interface councils due to their distinct needs and challenges due to their size, financial position, population growth and green wedge stewardship.
- Smaller councils should be subject to a higher than CPI cap unless they choose to apply for an alternative level of rates above this level.

Ratepayers / Ratepayers Associations

A small number of ratepayers' or ratepayer associations' submissions responded to this question. A few stated there should be different cap per council group:

- Metro - no greater than CPI plus 1 per cent; outer metro, regionals and rural: CPI plus 1.5 per cent.
- Some considerations may be given to special circumstances due to different demographics of councils.
- State Government should review councils' financial statements then adopt a different cap per group based on the results of the review.

A few stated there should be a single cap:

- Differences in rating requirements should be addressed in the variation process.
- Having different caps per group will not lead to the intended outcome that all ratepayers will have relief from excessive rates burden.

Continued next page

TABLE E.6 (CONTINUED)

Service Providers
No cap would be appropriate across all councils due to the diverse range of needs, diverse revenue bases and widely differing infrastructure needs.
Metro councils typically manage mature infrastructure networks, with the support of a large rate base.
Interface councils need to cater for the growing urban sprawl.
Unions
Rural councils, both small and large, are required to manage infrastructure across a much larger geographical area, with a much smaller rate base.

TABLE E.7 QUESTION 6: WHAT BASE SHOULD THE CAP APPLY TO?

Does it include rates revenue, service (waste) rates/charges, municipal charges and special rates/charges?

There are mixed views about the composition of the base but the majority of respondents consider that:

- the base should include revenue from general rates and municipal charges because these two are not directly linked with specific services or infrastructure projects.
- services rates and charges should not be capped for various reasons - it can be directly linked to service provided, based on cost of service, market tested, driven by significant annual increases in landfill levy and costs of specialist private waste contractors).
- special rates and charges should not be capped because it is directly linked to service provided, based on cost of service and there are check and balance already in place in the legislation.

There were suggestions for the ESC to monitor the movement of service rates and charges if they were not to be capped.

Councils

- Cap general rates and municipal charges only; do not cap service (waste) charges for various reasons (fee for service, market tested, driven by landfill levy and specialist private waste contractors).
- A council suggested that ESC may wish to monitor the movement of service rates/charges separately.
- Almost all submitters responding to this question agree that special rates/charges should not be capped given the check and balance already in place in the legislation.

Other responses from councils

- Cap general rates only.
- General rates, municipal charges and service rates/charges; if not then councils adopting NAV and levy general rates only as a result will be disadvantaged.
- Government levies should be excluded from the base.
- It would not be safe to assume that the current levels are an appropriate base from which to cap future movements.

Peak Bodies

- General rates only.
- General rates and municipal charges.
- General rates, municipal charges and service rates/charges, but noted the issues with capping the latter.
- Service charges are based on cost of service
 - to cap it would force local governments to conduct activities at a loss
 - ESC may wish to satisfy itself that service rates/charges do not exceed the full cost recovery.
- Exclude special rates and charges because there are appropriate constraints on the use of these rates under the legislation.

Continued next page

TABLE E.7 (CONTINUED)

Other responses from peak bodies

For councils that levy general rates only, the cap should not be applied to the proportion of waste and environmental management costs.

Other council groups

- General rates only.
- The base should not be fixed.

Ratepayers / Ratepayers Associations

A few submissions responded to this question with varying thoughts:

- General rates and municipal charges; exclude service rates/charges and special rates/charges.
- General rates, municipal charges and service rates and charges.
- General rates only for simplicity
- All rates and charges.

TABLE E.8 QUESTION 7: SHOULD THE CAP APPLY TO TOTAL REVENUE ARISING FROM THESE CATEGORIES OR ON AVERAGE RATES AND CHARGES PER ASSESSMENT?

Majority of respondents consider that the cap should apply to revenue including supplementary rates (to account for growth). It is observed that some submitters assumed that the revenue cap will not include supplementary rates and therefore suggested per assessment capping given its ability to factor in the effect of supplementary valuation in a straightforward manner. See table below for the pros and cons of each option.

Councils

Cap should apply to revenue plus supplementary rates revenue (to account for growth).

Arguments for a revenue cap:

- Simplest option.
- Consistent with council practices in setting rate levels.
- More transparent, published in the annual budget documentation as the rates are levied.
- Provides councils flexibility to make decisions re equitable distribution of rates burden.
- Ensures relative valuation movements between properties continue to drive the apportionment of total rate revenue among all ratepayers.
- More fair; differential rating, revaluations and supplementary rates will distort the outcome if applied to an average per assessment.
- Minimises confusion during revaluation years.
- Cap should apply to revenue not per assessment on the basis that property subdivisions and consolidations could have unintended perverse outcomes.

Arguments against per assessment cap:

- This would represent an unwarranted interference in the legitimate decision-making role of the council in rate setting; will restrict councils to alter rating strategies around municipal charges and differential rates.
- Will result to potential complexities and confusion in a general valuation year where differential rates are present and there is not an absolutely uniform movement in valuations between different classes of ratepayers.
- It may also result to reduced rate base if there are negative outcomes for supplementary valuations.
- It adds additional layer of administrative complexity and effectively make the biennial general valuation process superfluous as rate increases will be pegged to a base year.
- Per assessment is how the total increase in own source revenue is distributed; it is not a driver of the increase.
- Per assessment has the advantage of simple messaging but does not take into account the financial realities of council's cost structure.

Continued next page

TABLE E.8 (CONTINUED)

<i>Other responses from councils</i>
Cap should apply to per assessment
Arguments for per assessment cap:
<ul style="list-style-type: none"> • Allows the effect of supplementary valuations and the revaluation process to be factored into the calculation in the most straight forward way. • Growth in number of assessment must result in increased rate revenue as it will lead to increased demand for service. • Objective is household affordability so it makes sense to cap per assessment; it also allows growth councils to gain additional income. • Would enable comparisons within council groups.
Arguments against revenue cap:
<ul style="list-style-type: none"> • Revenue (without including supplementary rates) is not fair to growth councils. • Cap rate in the dollar; cap either revenue or per assessment; cap rate in the dollar in a non-valuation year and revenue in a general valuation year.
Peak Bodies
Revenue with supplementary rates.
<i>Other responses from peak bodies</i>
Per assessment; revenue would be grossly disadvantageous to growth councils.
Per head of population because services are provided to people not to property and population growth is therefore highly correlated to service cost increases. Regardless, since the apparent objective is cost of living challenges whatever base is adopted should include an automatic provision for automatic cost growth.
Other council groups
Should be revenue.
Ratepayers / Ratepayers Associations
Revenue should be capped; councils should be given leeway to determine their revenue mix and rates pricing levels; per assessment should only be used for comparative purposes.
Victorian Farmers Association further suggested capping revenue per group of rate payers although noted that councils will lose flexibility to adjust rates burden among group of ratepayers.
<i>Other responses from Ratepayers / Ratepayers Associations</i>
Per assessment.

TABLE E.9 QUESTION 8: HOW SHOULD WE TREAT SUPPLEMENTARY RATES? HOW DO THEY VARY FROM COUNCIL TO COUNCIL?

There are mixed views about treatment of supplementary rates but majority of council respondents consider that it should be included in the rates based and capped. Two methods of accounting for supplementary rates in the rates base were also given (see below). Peak bodies, except for FINPro, also consider that supplementary rates should be part of the rate base to be capped.

MAV and two councils noted that if the cap is applied on rates per assessment the issues relating to how to account for supplementary rates are eliminated.

Councils

A number of submissions argued to include supplementary rates

Two methods of accounting were suggested:

- **Suggestion 1:** The rate base for the current year should be the previous year's rate base including the annualised supplementary rates for that previous year; the forecast supplementary rates for the current year is excluded.
- **Suggestion 2:** Same as Suggestion 1 except that the forecast supplementary rates for the current year is also included.

Other responses from councils

Exclude totally.

Hard to estimate/forecast accurately.

Peak Bodies

Exclude from the rates base for the current year but include in the rates base the following year and capped.

Supplementary rates to be added should be the annualised amount (full-year rates) for the previous year not the budgeted (part- year rates).

Other responses from peak bodies

Must fall outside of any cap regime.

Other council groups

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

They should be excluded from rate capping; they are only an estimate.

Ratepayers / Ratepayers Associations

Exclude from the calculations.

Should be considered in the development of the framework.

TABLE E.10 QUESTION 9: WHAT ARE THE CHALLENGES ARISING FROM THE GENERAL VALUATION OF PROPERTIES EVERY 2 YEARS?

Majority of respondents believed that ratepayers will be confused during general valuation years because changes in valuation will lead to changes in rates that are higher or lower than the declared cap. They consider that a comprehensive community information campaign will be necessary to explain the methodology and the State Government should help in this campaign.

Councils

Confusion among ratepayers because revaluation will lead to changes in annual rates which are higher or lower than the declared cap.

Communication strategies would need to be prepared in advance to explain this (by Government, ESC and councils).

Other responses from councils

The valuation is costly for councils and should be done every 3-4 years.

There are no issues with revaluations.

Peak Bodies

All commented that ratepayers will be confused.

A comprehensive community information campaign will be necessary to ensure the methodology and benefits are understood.

Other council groups

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

Ratepayers / Ratepayers Associations

Revaluation does not result in additional rates and municipal charges; individual ratepayers will experience rate increases or decreases depending on the movement in individual valuations (ratepayer).

Will result in variations in rate rises, ESC should cap revenue for each group of ratepayers

TABLE E.11 QUESTION 10: WHAT SHOULD THE BASE YEAR BE?

Majority of respondents suggested the base year to be 2015-16. Other councils prefer that the rate capping and variation framework commences in 2017-18 given that 2016 is an election and general valuation year.

Councils

2015-16.

The year includes commitments and projects already underway and the consultation they had undertaken on their 4 year SRPs.

Should be budgeted.

Other responses from councils

2016-17/2017-18.

Have for the last 3 years or the last 10 years.

Councils' efforts to increase efficiency and effectiveness prior to this policy announcement should be recognised in the rate capping framework.

Peak Bodies

- 2015-16
- 2017-18

Other council groups

2015-16

Ratepayers / Ratepayers Associations

2015-16

TABLE E.12 QUESTION 11: HOW SHOULD THE VARIATION PROCESS WORK?

There was a clear preference from Councils and peak bodies for the variation process to be clear, simple and low cost, with assistance from the ESC to make the process manageable. There was particular concern raised about the capacity of small and rural councils to participate in the variation process. A tiered variation process with increasing levels of scrutiny was suggested by many submitters.

Ratepayers and ratepayer organisations emphasised the need for rigour in the variation process.

Community groups, service providers and unions were concerned that services would suffer under the framework and that the framework should not prevent justified variations to the cap.

Councils

Councils want a simple and inexpensive variation process. Some councils suggest this could be achieved by the ESC providing a template for councils to fill in.

Many submissions recommended the variation process should: work within councils' existing budget process; be set for four years to align with the strategic resources plan; use existing material and documents; and that thresholds should exist to allow for different levels of scrutiny according to the size of the variation requested.

Many councils highlighted the needs of smaller, rural councils which have limited resources to make detailed applications.

Some councils suggested various means of the ESC assisting councils including information sessions, written guidelines, assistance with variation applications.

Some submissions called for: an automatic approval for variations outside the control of councils; an appeal or review process; the ability to apply for variations through the year and deadlines on ESC decision-making.

Peak Bodies

Peak bodies support a clear process, an application template, and variation thresholds.

Most peak bodies believe variation should be open to all, including financially strained, smaller councils; the process should not be burdensome; a tiered approach to scrutiny of different levels of variation.

The MAV submitted a three tiered approach to the variation process which would minimise the total cost of the ESC review for all parties, while maintaining the original policy intent – minimising unnecessary rate increases.

FinPro suggested that: criteria should be clear and known in advance; template for requests should be developed; definition of best practice community consultation should be clarified.

LGPro suggested the ESC prepare a template for a variation application, and favoured a tiered approach to scrutiny.

The RMA sought a simple template and for councils to provide documentation such as Annual Budget, LTFP, Rating Strategy, and SRP. It emphasised the importance of timing and approval of applications.

Other council groups

Other council groups consider the variation process should consider the differing resources of councils and be a clear, flexible and simple process.

Consideration of smaller, lower-resourced councils was a key feature:

- A 'flying squad' could assist smaller councils with applications.
- Process should not be onerous and create bureaucracy for financially constrained councils.
- Clear criteria for applications and simple transparent, efficient and equitable process.

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TABLE E.12 (CONTINUED)

Ratepayers / Ratepayers Associations

Ratepayer associations and ratepayers emphasised the need for a robust variation process.

Suggestions to ensure variations were justified included:

- Rigorous requirements to justify a variation.
- Sunset clauses for variations.
- Rates notices that itemise variations.
- Separating cost in those that were and were not controllable.
- Incorporating variations into long-term plans.
- ESC use of efficiency indicators in variation assessment.

There was broad agreement among ratepayers that a systematic approach to assessment of variations should be undertaken.

One submission was concerned that the cost of the framework would increase.

A ratepayers peak body was suggested in one submission.

Not-for-profit community groups

Community groups do not want the variation process to be too onerous and prevent justified increases to the cap.

For example, the Springvale Community Aid and Advice Bureau do not want the variation process to be too onerous, particularly with regard to consultation.

Service Providers

Service providers and unions were concerned that the variation process might prevent justified rate increases.

Professionals Australia considers that the proposed framework for variation poses a significant burden on Councils, and does not adequately cater for additional rate rises, even where demonstrably necessary. The ESC should consider ways to ensure that the process is fast and economical for Councils.

Unions

The ASU fears that some councils may merely adopt a CPI rate increase, ignore the variation process and use the CPI cap as an excuse to get out of some service delivery.

TABLE E.13 QUESTION 12: UNDER WHAT CIRCUMSTANCES SHOULD COUNCILS BE ABLE TO SEEK A VARIATION?

Councils and council groups listed circumstances that should allow for a variation many of which could be divided into uncontrollable items and changes desired by the community. The emphasised the costs that apply to councils which Councils cannot anticipate and which require financial action. Also emphasised was the importance to autonomy of councils responding to changes in community preferences and needs.

Ratepayers and their associations highlighted the need to have a robust framework to prevent unjustified rises in rates and charges. They also raised transparency as an important factor, emphasising that rate payers should be informed of changes.

Community groups, service providers and unions emphasised that variation criteria should not limit the provision of services to community members, particularly vulnerable members.

Councils

The key elements of almost all council submissions are that councils should be able to seek variations for:

- events outside councils' control
- changes in community demand for services
- financial sustainability
- infrastructure renewal
- cost shifting.

Many councils argued that broad criterion should be adopted to capture all the relevant variation circumstances and that if good consultation were undertaken then a variation could be justified for any purpose.

Other reasons for variation suggested were loss of a source of revenue, natural disasters, demographic changes, superannuation requirements.

Some councils gave reasons for variation including:

- Levels of socio-economic disadvantage.
- Capacity to generate non-rate revenue.
- Economic development programs for small rural councils.
- Servicing loan for infrastructure.

Peak Bodies

Peak bodies argued for broad scope of justifications for variation, particularly for items outside councils' control.

One argued variations should be allowed for:

- renewal gaps
- costs of major new infrastructure
- new and 'shifted' services
- financial sustainability according to VAGO; implementing SRPs.

One argued for variations where, after financial assessment and community consultation, it is determined that a rate rise is warranted.

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TABLE E.13 (CONTINUED)**Peak Bodies (continued)**

One said matters considered should include:

- Cuts to grants.
- Cost shifting.
- Extraordinary circumstances.
- Sources of income available and overall financial position.
- Maintenance of services, including infrastructure.

Other council groups

Specific council groups highlighted the need for inclusive reasons for variation and guidance in making submission.

Highlighted points include:

- Councils should be able to seek a variation for any purpose following a robust assessment of their financial circumstance, community ambition and consultation.
- The ESC should provide certainty to struggling Councils working through the system. Guidance on specific categories such as: natural disasters, community wellbeing, population decline, significant economic downturn – where a significant local employer has closed down and investment is required to stimulate the town's economy.

Ratepayers / Ratepayers Associations

Ratepayers and ratepayer associations highlighted the need for full justification of any changes.

- have to fully justify any variation
- not be able to subvert the rate cap by unnecessarily increasing borrowings
- issue Annual Rates Notices highlighting special charges and indicate when they will cease.

Not-for-profit community groups

Community groups did not want the variation process to be too onerous and prevent justified increases to the cap.

Service Providers and Unions

Community groups did not want the variation process to be too onerous and prevent justified increases to the cap.

TABLE E.14 QUESTION 13: APART FROM THE EXCEPTIONS IDENTIFIED BY THE GOVERNMENT (NAMELY, NEW INFRASTRUCTURE NEEDS FROM A GROWING POPULATION, CHANGES IN FUNDING LEVELS FROM THE COMMONWEALTH GOVERNMENT, CHANGES IN STATE GOVERNMENT TAXES AND LEVIES, INCREASED RESPONSIBILITIES, AND UNEXPECTED INCIDENTS SUCH AS NATURAL DISASTERS), ARE THERE ANY OTHER CIRCUMSTANCES THAT WOULD JUSTIFY A CASE FOR ABOVE CAP INCREASES?

<p>Most respondents had addressed this question in earlier responses on the variation framework. Councils and council groups listed the factors that they argued should be allowed for variations. They also argued that given that an exhaustive list was not possible, broader non-specific criteria would be more appropriate.</p>
<p>Councils</p> <p>Councils proposed a number of circumstances in addition to those listed the most widely cited of which were:</p> <ul style="list-style-type: none"> • Cost shifting • Infrastructure renewal • Superannuation requirements • Long-term contracts indexed above CPI • Financial sustainability • Charges fixed by other governments • State cuts to grants • Prevention of natural disasters • Impact of tourism • Addressing disadvantage • Provision of service over disbursed population • Above CPI utility bills • Workcover insurance premiums • Change in municipal boundaries • Landfill rehabilitation projects • Uninsured losses arising from force majeure. <p>Several councils identified diminishing economies of scale or loss of industry for councils as a relevant circumstance for a variation.</p> <p>Some submissions recommended that variations be automatic for circumstances outside councils' control.</p> <p>Some submissions suggested the criteria had been well identified in the consultation paper.</p>

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TABLE E.14 (CONTINUED)

Peak Bodies
<p>The Council peak bodies listed a number of circumstances that would justify a case for above cap increases:</p> <ul style="list-style-type: none"> • Local community support for investment. • Overall financial position at commencement of framework. • Factors outside of council control Bridging asset renewal gaps. • Continued freezing of statutory fees. • Cost Shifting. • Higher than CPI increases in Utility charges. • Changes in legislation requiring. • Costs for legal issues. • Changes in grant programs. • Increased property density leading to changes in demand for services. • Council elections. • Prevention, mitigation and response to natural disasters. • Inability to generate self-sourced revenue. • Other circumstances outside council control. <p>Some consideration should be given to the 'catch ups' when new responsibilities have a greater cost that estimated.</p>
Other council groups
<p>Council groups emphasised that the variation process should not rely on fixed predetermined criteria because reasons for rate increases were not always predictable.</p> <p>However, they listed the following as circumstances that should be allowable for successful variations:</p> <ul style="list-style-type: none"> • Overall financial position at the commencement of the framework. • Cuts to grants. • Cost shifting. • Changes in legislated council responsibilities. • Prevention, mitigation and response to natural disasters. • Inability to generate self-sourced revenue. • Economic downturn – where a significant local employer closes and investment is required to stimulate the town's economy. • Community asset stewardship. • Change in population. • Proportion of rate base that is exempt from rates. • Superannuation requirements. • Stewardship of green wedges. • Growth. • Circumstances outside of councils' control.

Continued next page

TABLE E.14 (CONTINUED)

Ratepayers / Ratepayers Associations

Ratepayers and ratepayer associations highlighted the need for full justification of any changes.

Councils should

- have to fully justify any variation,
- not be able to subvert the rate cap by unnecessarily increasing borrowings,
- issue Annual Rates Notices highlighting special charges and indicate when they will cease.

Not-for-profit community groups

Community groups did not want the variation process to be too onerous and prevent justified increases to the cap.

Service Providers and Unions

Service providers and unions were concerned that the variation process might prevent justified rate increases.

TABLE E.15 QUESTION 14: WHAT SHOULD COUNCILS NEED TO DEMONSTRATE TO GET A VARIATION APPROVED?

A possible set of requirements could include whether:

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

Councils and local government bodies expressed broad agreement with the proposed requirements but raised questions around the information required. Suggestions were also made on the types of events that should qualify for a variation.

Councils

Many councils expressed broad agreement with the suggested set of requirements although sought clarity around what supporting information would be required. Some also set out their own suggested supporting evidence.

One set of suggestions were that the Council:

- has a robust 10 year Financial Plan and 4 year SRP;
- has a clear plan to bring rating increases back in line with appropriate levels within a reasonable timeframe;
- can demonstrate clear and transparent communication and consultation with their community in the development of their annual budget and/or 4 year SRP;
- AND: the Council is subject to outside of their control such as:
 - Government policy changes;
 - Recovery from emergency or other disaster;
 - Legacy asset management concerns;
 - Superannuation requirements.
 - Declining populations and economics.
- OR, where rate increases are in direct relationship to increased service.

Documentation required suggestions included: long-term financial plan, a business case for a major infrastructure, past history of council's rate increases supporting the justification for a variation

Some submissions stressed using existing information such as:

- Evidence of regular service reviews
- Evidence of compliance with other legislative and regulatory frameworks such as the LGA, including Performance Reporting.
- The variation framework should use the National Asset Management and Assessment Framework.

Additional suggestions included:

- A self-assessment approach should be considered to elements outside of Council control.
- Automatic approval for any rate increases caused by external factors. These should not require community consultation. For controllable costs councils should demonstrate community support for changes.

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TABLE E.15 (CONTINUED)

Peak Bodies
<p>There was broad agreement with the suggested factors with several suggestions and questions.</p> <p>One agreed in principle with the requirements wanted more clarity on the standards needed to fulfil them. It was interested in the specific processes and standards of proof required by councils to confirm they have fulfilled the requirements. It also believed the list should be applied to the larger rate increase, rather than more modest increases.</p> <p>One suggested that reference be made to a council's history of financial stewardship as measured by VAGO financial sustainability measures. Also, a history of improved position should be seen as a positive indicator in for a variation application.</p>
Other council groups
<p>There was broad agreement with the suggested factors with some questions and amendments.</p> <p>Use of the 'other' and 'extraordinary circumstances' categories are too broad and will not provide certainty to councils. It suggested additional categories including:</p> <ul style="list-style-type: none"> • Natural disasters, • Community wellbeing – for smaller communities to provide, • Population decline, • Significant economic downturn
Ratepayers / Ratepayers Association
Ratepayers and ratepayer associations highlighted the need for full justification of any changes.
Not-for-profit community groups
Community groups did not want the variation process to be too onerous and prevent justified increases to the cap.
Service Providers and Unions
Service providers and unions were concerned that the variation process might prevent justified rate increases.

TABLE E.16 QUESTION 15: WHAT DOES BEST PRACTICE IN COMMUNITY ENGAGEMENT, PROCESS AND INFORMATION LOOK LIKE? ARE THERE EXAMPLES THAT WE CAN DRAW FROM?

Many submissions stated that councils are already consulting with their communities in an adequate manner. Several were supportive of the framework providing guidance on best practice in engagement. Many submissions provided examples for the ESC to consider as good/best practice community engagement.

Councils

Refer to or support for existing legislative obligations regarding community consultation.

Opportunities to improve community engagement without being overly burdensome/strengthen existing engagement processes e.g. using LGPRF, improving standards of annual reports and planning documents, demonstrated engagement during development of SRP.

Support for existing examples of good engagement given around budget processes, social media, state government fire service property levy campaign, surveys, community events, storytelling through the arts, community panels, focus groups; the work of specific councils such as Melbourne, South Gippsland, Darebin, Wangaratta, ACELG Service Delivery Review June 2014.

Needs prior engagement to commencement of framework.

Support for ESC providing clear guidance on how it considers councils should engage.

Refer to IAP2 as a best practice model or used with some modifications.

Good engagement is: based on reasonable expectations, proportionate, relevant and suitable to needs of community, unique to each council, open, flexible, responsive, includes prioritisation, representative, multiple mechanisms, macro and micro levels, clear on the questions asked and the negotiables and non-negotiables and provides clear, accessible information, clearly .

Peak Bodies

Suggestions/comments from the peak body submissions include:

- Rate capping needs to be aligned better with community consultations.
- Framework should present best practice framework for community consultation to provide clarity and set expectations about requirements for variation applications.
- Look at the water industry processes that the ESC looks at regarding setting revenue levels.
- Majority of councils undertake community engagement on regular basis, within strategic framework – there are multiple opportunities for community members to shape council plans/strategies.
- Councils faced with competing demands on the budget - elected representatives are best placed to make these decisions; there is not a high level of interest from community regarding rates.
- Engagement occurs with development of every policy, strategy and plan which council prepares. Elected officials are accountable; community able to make submissions which are considered.
- Further information should be provided for discussion with the sector on the level and type of community engagement that would be sufficient.

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TABLE E.16 (CONTINUED)**Other council groups**

Key points from the submissions from other council groups include:

- Important the community has a good understanding of rate capping so they can provide informed feedback during consultation.
- A key pillar of the framework should be greater engagement with the community to prioritise requirements and rating policy.
- Additional community engagement requirement may come at a cost to residents.

Ratepayers / Ratepayers Associations

Individual ratepayer submissions provided quite a mixed response to this question ranging from stating that councils should focus on core responsibilities, focus on what the majority of people want, suggesting there is a lack of transparency to giving examples of where perceived good engagement is occurring across the sector. Comments from individual ratepayers include:

- Existing community knowledge of council services is poor.
- Supportive of strong/better engagement.
- Specific examples of types of perceived good engagement such as: 'council committees of management'; social media, face-to-face, surveys, focus groups; participatory budgeting, zero (activity) base budgeting.
- Transparency needs improvement: results from surveys need to be published; full disclosure of manager, director and CEO salaries and employment costs of other employees, leases, contractor costs, etc.; community engagement must be documented and conclusions independent; rates notices should include a breakdown of costs
- Best practice ensures the community has ample opportunity and time to engage with the process. This means having a variety of methodologies. It is also important to go to the community rather than only providing opportunities from the community to come to council. Also important to engage with breadth and depth of the community. Being effective can be costly and time consuming so there needs to be funds available.

Ratepayer associations and groups again ranged in their responses to this question from transparency and engagement needing improvement to providing examples of where consultation has recently improved or suggestions around what good consultation could look like such as use of surveys, IPART's guidelines, transparency in rates notices, IAP2 standards. One suggested including the new LGPRF measures to qualify and report councils' commitment and performance levels of community engagement.

Not-for-profit community groups

Importance of how engagement is incorporated into the service/cost nexus.

Council has well developed and inclusive community consultation and engagement mechanisms in place, these are also costly, especially when catering for such a diverse population.

Service Providers

Libraries already go through a variety of extensive consultation processes and types (surveys, focus groups, forums).

Unions

Councils already conduct extensive consultation with their communities.

TABLE E.17 QUESTION 16: HOW SHOULD THE FRAMEWORK BE DESIGNED TO PROVIDE COUNCILS WITH INCENTIVES TO PURSUE ONGOING EFFICIENCIES AND RESPOND TO COMMUNITY NEEDS? HOW COULD ANY UNINTENDED CONSEQUENCES BE MINIMISED?

The majority of council and peak body responses focused on the potentially negative impact of rate capping on council services and the likelihood of a deterioration in vital infrastructure, particularly if the cap is set too low (based on inappropriate cost index) or if the variation process is too burdensome. The framework, particularly the variation process, should account for the diversity of council positions, including past efforts to achieve efficiencies and invest in good planning (and encourage these practices). Implementation of the framework should be staged, in concert with the sector and encourage long-term planning and financial sustainability. A rushed framework will produce unintended consequences.

Other concerns in the submissions stressed the importance of:

- Proportionality in variation requirements.
- Training and support to councils to build capacity in financial and asset management and community engagement.
- Guidance on the requirements for applying for a variation, including templates.
- Close monitoring of the impact of the framework will be necessary.

Councils

Diminished service levels and insufficient investment in maintaining infrastructure (subsequent expansion of asset renewal gap) were identified by a majority of councils as likely consequences of the framework. Particularly if the rate cap is set too low based on the use of an inappropriate cost index or due to an excessively onerous variation process.

The rate capping and variation framework will restrict the capacity of councils to make their own judgements about services and infrastructure.

Councils will inevitably consider whether to continue delivering un(or under)-funded services on behalf of Commonwealth and State Governments.

The framework will result in an incentives system that benefits those who have a larger cash base or who have been inefficient in the past.

Language needs to shift to financial sustainability and value for money rather than an economic rationalist focus on efficiency.

The framework should improve council performance without compromising independence and democratic accountability.

Rate capping should not be seen as a punitive tool.

The level of regulatory oversight should be proportional to the demonstrated capability of each council re: financial management and community engagement. This will incentivise councils to improve capability.

A strong focus of efficiency of service delivery but arbitrary 'targets' should be avoided – particularly before a council's efficiency can be determined.

Cap should reward those who have managed their finances responsibly and invested in future through planning. The framework should reward good effort while strongly encouraging those who wish to improve their services and achieve greater efficiencies.

Unintended consequences can be minimised by ensuring a planned and staged introduction of the framework, in partnership with the sector. A rushed implementation will result in unintended consequences and reflect badly on both tiers of government.

Continued next page

TABLE E.17 (CONTINUED)

Councils (continued)

The framework should support long-term planning and be responsive to uneven asset maintenance and renewal.

Design of the cap and variation framework should consider the following:

- A narrow cap (rates and municipal charge) based on the 'right' cost index would best encourage councils to pursue new business models that lead to long-term sustainability.
- The framework should facilitate reasonable rate increases without a substantial diversion of resources to application process.
- Proving service efficiency should be part of variation application.
- Variation application requirements should be proportionate.
- Flexibility for multi-year variations to account for infrastructure projects.
- Variation process should make provision for councils that have already found efficiencies, this may be achieved by benchmarking some financial indicators
- Efficiency requires investment in new technology – this should be encouraged in variation process.

A number of councils identified the need to provide support for councils to build capacity, adapt to the framework and to clarify requirements (well-designed variation application templates)

ESC should set out best practice guidelines on what efficiency looks like – e.g. zero-based budgeting, continuous review of service standards; service planning; and community engagement.

The need for close monitoring of service levels, financial sustainability and asset renewal was also identified.

Integrate KPIs with LGPRF to assess effectiveness and efficiency. Use VAGO sustainability indicators but VAGO underlying result measure should reflect the 'real underlying result'.

Other responses from councils

Councils do not need incentives to respond to community needs - that is why they exist.

Councils are already efficient.

Rural councils face structural issues regarding size, remoteness that demand efficiency (cited Whelan report).

Financial incentives should be funded by the state.

Several councils cited the need for a risk assessment prior to implementation.

Provide additional untied government funding to offset reduced rate revenue.

Continued next page

TABLE E.17 (CONTINUED)

Peak Bodies
<p>Concerns regarding cutbacks to infrastructure investment and deteriorating services was cited as a potential outcome of the framework. The experience in NSW under rate pegging was cited as evidence. It was recommended that the ESC use VAGO indicators and direct information directly from councils to monitor.</p> <p>The framework should provide flexibility for funding up-front capital costs for projects that will deliver long-term efficiencies (e.g. IT systems or energy efficiency). The ESC should not be encouraging councils to take on more debt.</p> <p>Local Government Act already requires that council resources are used efficiently and effectively; services provided in accordance with Best Value principles. Does not support offering incentives to councils to respond to community needs; councils need to determine how they wish to balance efficiency against effectiveness and service quality having regard for community needs/level of subsidy provided.</p> <p>The key points of the framework should be the process of rate setting, promoting transparency, the use of good data and community engagement.</p> <p>The framework should promote financial sustainability and be responsive to community needs and encourage shared services implementation</p>
<i>Other responses from peak bodies</i>
<p>Unintended consequences can be minimised by measure community needs and feedback through funded surveys.</p>
Other council groups
<p>Potential for job losses, reduced social services and infrastructure.</p> <p>Councils are already downsizing and realising efficiencies. Further action with reduce services and jobs.</p>
Ratepayers / Ratepayers Associations
<p>Provide training to councils and councillors in financial management and budgeting.</p> <p>Council should not be able to subvert the cap by raising other fees and charges. Annual rate notices should itemise the special circumstances requiring a variation above cap.</p> <p>There should be a productivity factor applied to cap.</p> <p>Expenditure on administration is far too high. State government should mandate KPIs for effective implementation of efficiencies in administrative functions.</p> <p>Link CEO, councillor and executive performance appraisal with council efficiency and performance under rate capping.</p>
<i>Other responses from Ratepayers / Ratepayers Associations</i>
<p>The draft report should identify the unintended consequences and the solutions</p> <p>MAV LGCI could be used to measure efficiencies resulting from the rate capping and variation framework.</p> <p>Set up a common complaint system for all councils - benefit future policy setting.</p>

Continued next page

TABLE E.17 (CONTINUED)

Not-for-profit community groups

The cap may result in the loss of funding for community programs – negatively impacting on social harmony and mental health in communities.

Design a framework that takes into account the additional costs of councils such as Greater Dandenong that are in culturally diverse and socio-economically disadvantaged areas. Impact not only on direct services but also on community sector organisations.

Unions

Rate cap will lead to out-sourcing of jobs and services.

If councils waste money, they will be judged at next election.

TABLE E.18 QUESTION 17: A RATES CAPPING AND VARIATION PROCESS SHOULD ENSURE THERE IS ENOUGH TIME FOR COUNCILS TO CONSULT WITH THEIR RATEPAYERS AND FOR RATEPAYERS TO PROVIDE FEEDBACK, AND FOR US TO REVIEW COUNCILS' APPLICATIONS. TO ENSURE THE SMOOTH FUNCTIONING OF THE RATES CAPPING AND VARIATION FRAMEWORK, IT IS PARTICULARLY IMPORTANT THAT IT ALIGNS WITH COUNCILS' BUDGET PROCESSES. WE ARE INTERESTED IN STAKEHOLDERS' VIEWS ON HOW THIS CAN BE ACHIEVED.

Most councils support transitional implementation of the framework after the 2016 council elections and the 2016 revaluation year (commencing 2017/18). This would allow the framework to support with the development of new 4 year Council Plans and SRPs. Council focus should be long-term, rather than on the annual budgetary process.

- Timing of cap announcement and variation assessments and approvals should align with the current planning and budgetary cycle.
- There were quite mixed responses regarding timeframes for variation application submissions and assessment by the ESC – ranging from July in the year prior to May. Most councils requested either the end of February or the end of March as the date by which the ESC should decide on variation applications (this assumed that there are not changes to the current budgetary timelines and statutory obligations).
- No additional consultation requirements should be added or at the least should be integrated to current consultation processes.

Council

A majority of councils supported the announcement of the cap and 2-3 year forecast caps in October-December of the preceding financial year.

There was considerable divergence among councils about when variation applications should be submitted, assessed and approved. Most recommended that the applications be approved by or before 31 March.

As 2016/17 is an election and a revaluation year, the framework should not commence until 2017/18. If this is not possible, then the variation framework should be delayed until 2017/18 – one year after cap introduction.

Strong support for multi-year forecast caps and multi-year variation approvals as this supported long-term planning and better integration with Council Plans and SRPs.

Current Local Government Act requires consultation prior to adoption of budget by 30 of June. To accommodate this requirement, variations will need to be approved by the end of February, leaving March and April for budget preparation and adjustment. Submission may be in January, so a quick turnaround in assessment is critical.

Not enough time to implement all aspects of the framework by 2016/17 financial year.

Common emphasis on the need for as little burden as possible.

Process and timing issues will be mitigated setting the cap at a level that does not force most councils to seek a variation and a workable design with good supporting templates where rigour increases with thresholds and multi-year variations approved when supported by robust SRPs.

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TABLE E.18 (CONTINUED)**Council (continued)**

The community consultation process would need to occur between Sep and Nov, followed by the application process between Dec and Jan, a final submission in Feb and a decision the ESC by end of March. The cap should be communicated to councils by the end of November with a 3 year forecast.

The cap and variation process should cover a multi-year timeframe. This will reduce time pressures in budget cycle and promote more strategic planning rather than a year-by-year reactive approach.

Cap:

- A 4 year forecast would aid strategic budgeting.
- Cap should be applied through the SRP – which must be in place by December. Cap no later than December 31.
- Cap announced by mid-January.
- Budget processes commence seven months prior to adoption. Changes impacting council rating strategies need to be announced at least 12 months prior to implementation.

Variation

- The criteria for a variation should be fair across all councils using relevant and transparent information. The assessment should take place prior to the endorsement of the SRP each year.
- Council consultation processes on variation applications would need to be built into early phases of budget development (October–February). Applications would need to be assessed by no later than 31 March.
- Cap announcement before Oct, council engage with community in Oct, submit a variation in Nov and ESC to release decision in December.
- Authorisation of variations should be no later than 30 March to enable statutory consultation of 4 weeks during April/May, consideration of submissions and endorsement by 30 June.
- Additional consultation should not be added to the current budget/planning requirements.
- If a variation is required, a draft budget may have to be developed earlier than current practice.
- Submissions in January, variations approved by end of Feb – leaving March and April for budget development, May for consultation, June for consideration of ratepayer submissions and council adoption. Consideration over four years would make it easier for councils.
- Variation applications need to be approved by the end of Jan, with applications submitted in end of Dec.
- Variation approved by end of February.

Continued next page

TABLE E.18 (CONTINUED)

Other responses from councils

A number of councils provided processes under the current Local Government Act and under an amended Act – for example, Corangamite Shire:

No changes to Local Government Act =

- Nov - ESC determines cap
- Dec - Jan - Council offers draft budget incorporating proposed cap
- Feb - consultation
- March - submit application to ESC for variation and determination
- April - draft budget considered by council
- May - draft budget on public exhibition for consultation
- June - council adoption of budget and SRP

Amended Local Government Act =

- Nov - ESC sets cap
- Dec - Feb - Council offers draft budget incorporating cap
- March - draft budget considered by council
- April - draft on public exhibition for consultation
- May - submitted to ESC and determination
- June - adoption of budget and SRP.

The ESC should assess the four year SRPs on a rolling basis. Significant variations would require an amended assessment. The current election cycle prevents good strategic management. Councillors have limited time understand organisation, to assess new priorities and submit a variation application.

Added complexity created by council budgets being prepared in advance of State and Commonwealth budgets – which could impact on and cause the need for a variation. There needs to be a capacity to make up the impact of state and federal budget decisions in the following year through variation process.

Well considered and approved four year SRPs which councils have developed and updated over time and which propose levels of rates, charges and other income to match required service delivery and capital works and maintenance requirements should not be lightly dismissed due to rate capping.

There is not enough time to add another step in the budget process.

For 2016/17 - set base cap of 4-5 per cent if councils need to go above, then there is an ESC template that must be filled and returned to ESC.

If an emergency occurs (fires, floods, storms, etc.), alternative financial measures/increases/above cap rises should be allowed

Multi-year applications to be made any time, with response provided no later than April 30th for variations applying the following financial year.

Consultation process is on-going and doesn't revolve around budget process only.

Timing should be such that: council adopts budget and SRP in June 2015, from July - Dec 2015 ESC assess cap variations. The council can then set their next budget between Jan and June 2016.

Application to the Commission would be necessary in September each year to facilitate any adverse changes to budgets.

Use SRPs with corresponding exemptions as agreed, annual variations should be complete by 30 November to take effect for the following year

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TABLE E.18 (CONTINUED)**Peak Bodies**

The impact will be largely dependent on the time required by the ESC to assess variation applications. There are statutory processes already in place prior to approval of the budget by June 30. The framework will have to integrate with these processes and provide time for consultation.

The timing of the final report and the subsequent variation arrangements present particular challenges for year one that the ESC must consider.

Alignment with current budget cycle.

The current planning and reporting processes are sufficient for delivering the government's commitment. Emphasis should be placed on Council Plans, SRP, LGPRF, Best value principles and the role of VAGO. No additional layers of regulatory burden are necessary.

Variations approved no later than February. Proposed timeline: Consultation process on a proposed variation would need to take place in October each year with the expectation that a council would undertake community consultation in October; submit a variation to ESC in November; receive advice on the success or failure of the bid in December and proceed with the completion of the budget process.

Cap and forecast by December, variation approval by end of March.

Other council groups

Variations approved by 31 March.

Ratepayers / Ratepayers Associations

Participatory budgeting for annual budget and strategic plans (5 year outlook).

Sufficient time exists within the current system for councils to plan for and consult on special issues. Special issues could be dealt with through special rates. Emergency issues must be dealt with in conjunction with the state (cited Fire Service Levy).

Submission is very critical of current budgetary and financial reporting processes of Cardinia Shire Council. It is recommended that the legislation require councils to provide an electronic copy of the draft budget to Section 86 committees.

Cap should be set for four year SRP, council assesses need for variation and submits to ESC for decision – process could align with IPART.

The ESC will need an effective change management strategy to facilitate cultural change in sector.

Community engagement should be more traceable to and accountable by the levels of the IAP2 standard. Services and assets management plans need to be intertwined.

Establish a peak body for ratepayers.

Service Providers

Timing should align with council SRP process and annual budget.

Unions

Councils already consult with their communities. The RCVP will impose needless delays in budget process.

TABLE E.19 QUESTION 18: WHAT TRANSITIONAL ARRANGEMENTS ARE NECESSARY TO MOVE TO THE NEW RATES CAPPING AND VARIATION FRAMEWORK? IS THERE MERIT IN PHASING IN IMPLEMENTATION OVER A TWO YEAR PERIOD TO ALLOW FOR A SMOOTH TRANSITION?

There was strong and consistent support for transitional arrangements from the councils. Most councils argued for the full introduction of the framework, particularly the variation component in 2017/18 to allow for alignment with a new 4 year Council Plan and SRP following the elections and this also avoids the revaluation year.

The revaluation year presents public perception risks regarding the potential benefits of rate capping. Several councils advocated the need for a comprehensive communications campaign to help communities understand how the rate capping and variation framework will impact them, particularly in the context of property revaluation.

The implementation of the framework in 2016/17 does not provide councils with sufficient time to prepare a variation application and consult with their community.

The ratepayers generally rejected the idea of a phased or transitional introduction of the framework.

Council

Strong support for a phased or transitional implementation over two years.

As 2016/17 is an election year and a revaluation year the framework should not commence until 2017/18. If this is not possible, then the variation framework should be delayed until 2017/18 – one year after cap introduction. Also cited EBAs expiring in 2017.

Introduction in 2017/18 to allow full integration with new Council plans and SRPs and alignment with Council terms after elections. This would allow plans and SRPs that are consistent with the requirements of the framework and better quality variation applications.

Councils have already committed to funding in current SRPs for 2016/17. Insufficient time for councils to prepare variations and adjust to requirements of the framework for 2016/17.

Because 2016/17 is a revaluation year the potential benefit of the cap will be diluted in terms of public perception.

Consideration of the timing of variation applications and assessments is critical to business continuity. In particular, alignment with the council election process and budget cycle that would allow proper councillor input and stakeholder consultation.

Other responses from councils

One rural city council stated that it did not see the need for transitional arrangements.

Phasing in for rural councils if going to be CPI allows for detailed service review process with reductions to service levels identified before the next financial year's budget is finalised.

One rural council advocated a staged implementation based on grouping: Metro first, then regional, then remainder.

Small rural councils should be exempt from rate capping for at least four years to allow time to adapt.

A transitional approach will enable councils to consult and build capacity.

Continued next page

TABLE E.19 (CONTINUED)***Other responses from councils (continued)***

Where decisions are pending the council needs to be in a position to continue the delivery of quality services and infrastructure.

One council, while opposed to rate capping, did not want a transitional period due to the need for clarity of policy and surety of requirements.

Difficult to know what transitional arrangements might assist a smooth transition without knowing the details and impact of the policy.

Voluntary adoption of rate cap for first year of framework.

Peak Bodies

The timelines presented appear ambitious given close proximity of finalisation of report, variation and budget process in 2016. Also, 2016 is final year of 4y council plan. Major revisions so late in planning process could undermine long-term community and financial planning.

Fin-Pro advocated full integration with council plan and SRP, commencing from 2017/18. Cited elections and revaluation year. If introduced in 2016/17, then concessions should be granted for consultation for variation applications in year one.

Rate capping and variation framework should commence from 2017/18 to align with budget and planning processes, valuation year and council elections.

Other responses from peak bodies

No need for transitional implementation.

Other council groups

Transitional arrangements over two years.

Staged approach, with larger councils commencing in 2016/17 and smaller councils given an additional year to prepare. Any mistakes during the first year would be borne by the councils most able to afford it.

Ratepayers / Ratepayers Associations

A transitional period is undesirable given it would delay implementation. The shock of immediate introduction might be beneficial by shocking councils into introspection. A phased approach will allow councils to do a poor job then 'prove' the process isn't working.

Pareto rule (80/20) can be applied to a pilot implementation in 2015/16 LGV can select a small number of councils with healthy financial positions.

Other responses from Ratepayers / Ratepayers Associations

Transitional arrangements are probably necessary.

If a ratepayer peak body is established, selection of appropriate representatives and provision of training would need to occur immediately.

Service Providers

The framework should be phased in over two years.

The cap should apply from 2017/18.

Unions

Opposed to the cap so 'further comments... are irrelevant'.

TABLE E.20 QUESTION 19: WHAT ARE STAKEHOLDERS' VIEWS ON THE RESPECTIVE ROLES OF THE KEY PARTICIPANTS? SHOULD THE COMMISSION'S ASSESSMENT OF RATES VARIATIONS BE ADVISORY?

- **A majority of councils preferred the ESC to have an advisory role. However, it appears most councils saw themselves as holding the determinative power (because of council autonomy), instead of the Minister. Only two councils identified the Minister as having determinative powers.**
- **A number of councils supported the ESC having a determinative role.**
- **Strong support for the ESC having determinative powers from ratepayers.**

The ASU opposed the ESC having any role in budget/rate setting process.

Council

Strong support for the role of the ESC as an independent arbiter (as opposed to the responsibility for setting the cap and approving variations sitting with the minister). However, the majority of councils did not support the ESC having determinative powers.

A majority of councils favoured self-assessment, with the ESC's role as advisory. Most councils cited autonomy and the reason.

The ESC should:

Monitor the success of the implementation of the rate capping and variation framework and provide advice to the minister on any review, taking into account feedback from the sector; review council budgets and variation submissions; authorise rate increases where business case is sufficient; provide advice to the minister where business case is seen to be insufficient but where intervention may be required.

LGV should have a role in providing direct support to councils in reconsidering their financial strategies where a business-case is deemed to have insufficient merit.

Policy parameters should be integrated across VAGO, LGV and ESC to ensure maximum transparency. This should also be reflected in LGPRF.

Other responses from councils

A large minority of councils supported the ESC having a determinative role, most commonly citing the independence of the ESC and the need to avoid political interference.

A small number of councils advocated an advisory role with the Minister having determinative powers.

A number of councils advocated the need for an independent appeal process if the ESC does have determinative powers.

Peak Bodies

MAV supports an advisory role for the ESC in the assessment of variations. A determinative role will contradict with principles of council autonomy and democracy. An advisory role will still be a powerful driver for efficiency in the sector.

The ESC should have an advisory and monitoring role – with powers of determination sitting with Minister (consistent with the current governance arrangements).

Ratepayers / Ratepayers Associations

Consistent support for ESC having determinative powers.

Continued next page

TABLE E.19 (CONTINUED)

Service Providers

The ESC should have a determinative role in assessing applications.

Union

External agencies have no role in council budgets or setting rates. Democratically elected councils are best placed to set rates.

TABLE E.21 QUESTION 20: IS THERE A NEED FOR THE FRAMEWORK TO BE REVIEWED TO ASSESS ITS EFFECTIVENESS WITHIN THREE YEARS' TIME?

All of the submissions, bar one which stated that the framework should be abandoned as soon as possible, were in support of a review to assess the framework's effectiveness.

A majority of submissions explicitly agreed with the timeframe posed in the question – within three years' time; some supported a review within 2 years; a few commented that this review should occur prior to the next state election; a few stated that the review should be reassessed every year for the first 3-5 years; one stated that the framework should be reviewed every year for the first three years of implementation.

Once the framework is established, several submissions were in favour of a regular recurring review. Those which specified a frequency included a range from every 2 years, every 4 years, with every strategic council planning cycle which would be equivalent to every 4 years, with council election cycles every 4 years.

Council

- All council responses supported a review. Comments on the frequency of a review included: a review after the first three years and regular reviews thereafter.
- should occur every two years;
- should be reviewed within/after 2 years with one stating that it should then be reviewed regularly every 4 years thereafter.
- should be a review every four years in line with council election cycles;
- should be done prior to the next election
- should be reassessed every year for the first 3-5 years
- every year the review (and abolition) is delayed, it will take 5 years for community infrastructure to recover.
- framework should be the subject of an annual review with a particular focus on process. The framework fundamentals and principals can then be further reviewed on a three (3) year cycle.

Other comments as to what such a review should look at included:

- analysis of variation process and applications
- appropriateness of index
- impact of cap on, financial sustainability of councils; councils' asset renewal gaps; costs imposed on the sector; services
- consideration to sunset clause of rate capping
- feedback from the sector and ratepayers
- a baseline study to determine current level of economic activity and underlying sustainability of current council finances, infrastructure and services reviews would then examine any shifts in these factors across the study period as a result of the rate capping.
- principles of continuous improvement should apply

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TABLE E.21 (CONTINUED)

Peak Bodies
<p>All Peak Body responses supported a review.</p> <p>Comments on what the review should consider:</p> <ul style="list-style-type: none"> • feedback from sector, community, ratepayers • full economic assessment of impact on councils' financial sustainability and ability to meet asset renewal requirements pre/post rate capping • resident satisfaction survey results • sustainability of the index, volume and timing of applications received/granted • impact on service delivery and renewal gaps • process with ESC and associated legislative budget processes for councils • interaction with council EBAs
Other council groups
<p>The council group submission that responded to this question was in support of a review.</p>
Ratepayers / Ratepayers Associations
<p>The ratepayer associations or groups and individual ratepayers who responded to this question were in support of a review.</p> <p>Comments on the frequency and content of review include:</p> <ul style="list-style-type: none"> • should occur with every strategic council planning cycle. • councils' performance must be managed each year and annually reported • should be reviewed after 2 financial years to ensure all Victorian ratepayers benefit equally • Finance Minister should 'review the basis numbers of the calculation principle' 6 months prior to a local election. Finance minister should publish any decision 3 months prior to election. • important the review should go beyond asking "did it work or not" and whether problems encountered are systemic in nature. Where it did work, these should be analysed to see why and what 'best practice' stories can be shared.
Unions
<ul style="list-style-type: none"> • The union submission that responded to this question stated that the framework, if introduced, should be abandoned as soon as possible.

TABLE E.22 QUESTION 21: HOW SHOULD THE COSTS OF ADMINISTERING AN ONGOING FRAMEWORK BE RECOVERED?

The majority of the submissions responding this question were of the view that the Victorian State Government should bear the costs of administering an ongoing framework; A few submissions suggested that Councils should cover these costs. A few other submissions stated that councils should not have to cover these costs but did not suggest an alternative funding source.

Councils

Most of councils' submissions stated that the Victorian State Government should bear the costs of administering an ongoing framework. Comments in support of this position include:

- MAV should be consulted as well
- Would be perverse for councils to incur additional costs as part of a framework to reduce rates - further cost shifting
- Costs incurred by councils would place further financial burden on financially pressed councils and communities
- As it is a policy by the state, the state should bear the costs
- Anything other than state funding would be inappropriate, poor governance and unfair
- Costs can be minimised by ensuring the framework is not excessively bureaucratic
- Many councils are already experiencing the need to review service levels without adding additional costs of a variation process. If the cost is shifted to local councils then it would need to be included in the index calculation.
- Council costs of preparing submissions for cap variations including external expertise and community consultation could be included in the rate cap variation.

Other comments:

- ESC could set license fees and recover costs from councils.
- raised concerns about the cost to councils of the framework
- suggested that councils should not have to fund the framework but did not suggest where the funding should be found.

Peak Bodies

All submissions from peak bodies that responded to this question all stated that the costs should be borne by the Victorian State Government.

Further comments include:

- Applying these costs to councils would place additional pressure on financially pressed councils and communities.
- This policy is driven by state government policy therefore should be paid for by state government
- Cost of the framework should be entirely transparent and publicly available
- Should ESC costs be borne by councils these costs should be allowed as an automatic cost above the cap variation

Other council groups

The council groups that responded to this question both suggested that the cost of administering the framework should be borne by the Victorian State Government.

One noted that this should occur without reductions to local government programs and funding streams.

Continued next page

TABLE E.22 (CONTINUED)

Ratepayers / Ratepayers Associations

Individual ratepayers stated that the state government should bear the costs.

Submissions from ratepayer associations commented:

- that funding should be partially by councils and then from cost savings
- that if the budget process is undertaken properly then this framework should not add significant cost to council and stated that they could not comment on how costs for administering the framework could be recovered from government.
- that we should apply a fee to requests for above inflation rate setting and apply fines to Councils that do not meet Framework requirements.
- that funding could come partially from LGV's budget and incremental cost savings from the first few years of solution implementation.

Service Providers

The service provider submission that responded to this question suggested that the cost of administering the framework should be borne by the Victorian State Government.

Unions

The union submission that responded to this question suggested that the cost of administering the framework should be borne by the Victorian State Government as it was their policy.

TABLE E.23 QUESTION 22: OTHER MATTERS RAISED IN EARLIER CHAPTERS

We are interested in hearing from stakeholders on:

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

All stakeholders generally supported our principles.

Many stakeholders, especially councils, supported principle 3 – yet believed rate capping would inevitably result in a loss of autonomy.

Many councils and peak bodies were concerned with the burden of proof discussed in principle 4

Many councils and peak bodies were concerned with the expectations around community consultation mentioned through the principles.

Principle 1 — Local communities differ in their needs, priorities and resources

Council

Generally supported.

- The principle should consider population decline as well as growth.
- Rate capping will be a further state government impost on local government and their communities
- Small communities wishing to reverse and decline and encourage growth must be given opportunity to do so through variations.
- Due to diversity, a one size fits all framework will not work.
- Differing resource/admin capacity should be considered especially when applying for variations.
- Consultations with community on cap variations should be relative to the variation size.
- Clear guidance on engagement will be required.

Peak Bodies

Generally supported

- More information should be provided on expected community engagement and amount spent on engagement.
- The framework must help councils listen to the minorities in a region who depend on the services along with the majority of ratepayers and other community members who pay for the services.

Other council groups

Generally supported

Continued next page

TABLE E.23 (CONTINUED)

Principle 2 — Local communities and ratepayers are entitled to hold their councils to the highest standards of accountability and transparency in setting rates

Council

Generally supported

- It can be difficult for the community to understand rate increases and how they are set. The community is just as upset when a revaluation or a change in rating policy causes increased rates, as well as general rate increases.
- Local governments are more transparent to the community in regards to this principle compared to commonwealth and state government, as they are the only ones who consult the community on their budgets.
- The LGPRF indicators will give limited information to communities and must be viewed with caution. Councils are very diverse, some indicators aren't robust and favour certain council types compared to others.
- Councils are democratically elected and represent community views. Therefore the ESC should not have power to reject rate increase applications.
- Councils current budget consultations should remain be the benchmark for the ESC to assess community engagements.

Peak Bodies

Generally supported

Support in part. Councils already provide a sufficient amount of information to the community. The LGPRF will provide even more information soon too.

Other council groups

Generally supported

Ratepayers / Ratepayers Associations

Generally supported

This principle is a very high priority

Unions

This principle is undermined by principle 5 – which inhibits council power and their autonomy

Continued next page

TABLE E.23 (CONTINUED)

Principle 3 — The framework should support the autonomy of councils to make decisions in the long-term interest of their community and ratepayers

Council

Generally supported or strongly supported

- It is inevitable that councils will lose autonomy under rate capping
- Autonomy will only be maintained if ESC assumes a light touch or advisory role
- Local government already has a considerable amount of regulation to adhere to. Rate capping will add to this.
- Rate capping will mean council autonomy lies with the ESC
- State government already has broad control over local government autonomy

Peak Bodies

Generally supported

- It is inevitable that autonomy will fall

Other council groups

Generally supported

Ratepayers / Ratepayers Associations

Generally supported

- Some suggestions that local government autonomy is limited already – as a subsidiary to state government
- Local governments' subordination to state government.

Unions

This principle is undermined by principle 5 – which inhibits council power and their autonomy

Continued next page

TABLE E.23 (CONTINUED)

Principle 4 — Councils will need to satisfy the burden of proof outlined in the framework when seeking a variation above the cap

Council

Generally supported

- Councils currently under a large amount of regulatory burden and the community is sufficiently informed.
- LGPRF has been a large burden
- This principle/requirement is unnecessary as the community already scrutinises council plans/budgets
- There should be a staged approach to the introduction of the burden of proof
- The burden of proof should be relative to the size of the variation application
- It is important that renewal gap expenditure be a reason for variations
- Small councils experiencing declining population rates have diminishing economies of scale
- ESC needs to distinguish what a 'critical infrastructure gap' is relative to a normal one
- The principle implies rate capping will not cause services to be cut - it is inevitable.
- Councils should not have to do anymore consultation than they are already doing

Peak Bodies

Generally supported

- Burden of proof should be relative to size of variation application
- Concern with what constitutes burden of proof. It shouldn't be too burdensome.
- The burden of proof will need clear guidelines.

Other council groups

- Concerned the burden of proof shouldn't be too much of an administrative burden and shouldn't require consultants.
- ESC should have a flying squad to help councils prepare applications.

Ratepayers / Ratepayers Associations

Generally supported

Continued next page

TABLE E.23 (CONTINUED)

Principle 5 — Rate increases should be considered only after all other viable options have been explored.

Council

Generally supported

- This principle is complex to apply in practice
- Council's already consider all other options first before increasing rates
- Strongly disagree with this principle
- Rates should not be income of last resort. They are an equitable, progressive tax and favour poorer people in the community to the better off.
- The principle should be re-worded to 'increases in rates should be moderate' or that 'growth in rates at CPI should be acceptable'. No growth in rates would be unacceptable.
- 'Viable' options should be considered within broader social and economic considerations - not just financial. What constitutes 'all viable options' needs clarification from the ESC e.g. does this include debt?

Peak Bodies

Generally supported

- The principle should be reworded to say rate increases at CPI are okay. As it is, it implies any rate increase (even below CPI) is not okay (2 submissions).
- MAV would like further discussion on this principle with the ESC. This principle disregards council autonomy.
- Many other council revenues are limited, thus principle 5 is limited
- The principle is at odds with the recommendations of the tax reform agenda. That land taxes should be grown

Other council groups

Many councils and small councils have improved efficiencies over the years. Rate capping will not find many more in these councils without cutting staff numbers.

This principle is at odds with the recommendations of the Australia's future tax system (2009). Council's should focus on finding efficiencies, but in general this principle clashes with council autonomy

Ratepayers / Ratepayers Associations

Generally supported

Unions

Very critical of this principle. Rate capping undermines local democracy and thus undermines principles 2 and 3

This principle promotes an outsourcing agenda

Continued next page

TABLE E.23 (CONTINUED)**Principle 6 — The framework should support best practice planning, management systems and information sharing to uphold council decision-making****Council**

Generally supported

- This principle is complex to apply in practice
- Residents, not just ratepayers should be involved in consultations.
- Council planning/reporting systems are already strong and sufficiently consulted on
- Councils already do this. Councils should not have variation proposals knocked back based on this principle.
- Councils already undertake significant consultation. Other levels of government do not undertake this level/type of consultation
- 'Effective engagement' needs clarification by the ESC. If the ESC wants more community engagement it should clarify what this looks like
- Rural councils need to be supported to enable their complying with best value principles

Peak Bodies

Generally supported

- MAV looks wishes to further discuss council consultations and the ESC's expectations.

Other council groups

Generally supported

- The community already receives a significant amount of information. Any more provided may be costly to the community

Ratepayers / Ratepayers Associations

Generally supported

- ESC needs to comply with COAG best practice regulation, so councils do not unfairly influence the development of the framework

Continued next page

TABLE E.23 (CONTINUED)

Principle 7 — The framework should be flexible and adaptable	
Council	
Generally agree	
<ul style="list-style-type: none"> The design of the rate capping framework will need to be driven by a considerable amount of evidence. Widespread agreement that the framework should be adaptable and be phased in over 12 months. The period of time councils can apply for variations to the cap should align with the timing of long-term plans e.g. 10 year plan. If councils have robust and integrated long-term plans, they should not have to submit any other information for rate cap variations. State government should cover council rate capping admin costs. Applications or variations should be relative to their size and the councils resource capacity. 	
Peak Bodies	
Generally supported	
<ul style="list-style-type: none"> Another point should be added to this principle: that the framework will not require any unnecessary levels of bureaucracy or administrative burden. Planning for cap variations need to be integrated with SRPs. It should not be too burdensome though. 	
Other council groups	
Generally supported.	
<ul style="list-style-type: none"> There should be a transitional period. Large councils should be capped a year earlier than smaller councils. 	
Ratepayers / Ratepayers Associations	
Generally supported	

Continued next page

TABLE E.23 (CONTINUED)

Principle 8 — There should be few surprises for ratepayers and councils in the implementation of the framework

Council

Generally supported.

- The design of the rate capping framework will need to be driven by a considerable amount of evidence.
- There should be clear guidance and expectations to support the flexibility.
- The framework should not disadvantage smaller councils.

Peak Bodies

Generally supported.

Ratepayers / Ratepayers Associations

Generally supported.

Continued next page

TABLE E.23 (CONTINUED)

Other Issues
<p>Whilst mostly listed in the consultation paper, considerations for the framework and principles raised in submissions were:</p> <ul style="list-style-type: none"> • To consider cost shifting onto local government. • State government set fees (planning fees) that have not escalated overtime. • Frozen grant funding. • Population growth and service and infrastructure demand. • The disparity between councils rate rises over recent years, and those who have kept to moderate rate rises being disadvantaged. • General concerns that pressure will be put on service levels to reduce and for renewal gaps to widen. • Concern over the administrative burden rate capping may cause for councils. • The revenue, resourcing and cost pressures faced by rural councils compared. • Some peak bodies and ratepayer associations proposed differing principles and potential rate capping systems. • A large number of stakeholders made comments on other considerations for our review
Council
<p>Majority of considerations</p> <ul style="list-style-type: none"> • Cost shifting needs to be considered (many submissions). • A general concern services and renewal gaps are likely to deteriorate which should be considered in the framework (many submissions). • Growth in population and services and infrastructure demand should be considered (many submissions). • Commonwealth and state funding cuts and grant freezing needs to be considered (many submissions). • Commonwealth and state regulatory burdens placed on councils need to be considered (many submissions). • There should be no new administrative burden created for councils without extra resourcing provided (many submissions). • The burden and volatility of defined benefits super contributions needs considering. (a few submissions). • State governments set fees that have not escalated over time need considering (many submissions). • State government should grow their funding to councils at CPI (a few submissions). • The costs of complying with the LGPRF should be considered, including the admin and audit costs (a few submissions). • Councils should be able to do an online self-assessment on an ESC web portal for variation applications (a few submissions). • Clarity with the FSLP needs to be considered (a few submissions). • Rural councils should be favoured. They have fewer resources, high costs, more assets to manage and less own source income. (some submissions). • The consultation paper does not address the unfair stating point council rate bases will be at. Councils who have increased rates for a long time will be benefited (a few submissions). • The economic and social impacts of the rate cap framework must be transparently investigated and understood before implementation (a few submissions). • Principles do not consider intergenerational cost shifting (a few submissions). • Country road and bridge funding has decreased too (a few submissions).

Continued next page

TABLE E.23 (CONTINUED)

Other Issues (continued)
Council (continued)
<p>Other Considerations</p> <ul style="list-style-type: none"> • Information requirements/community consultations for applications for variations should be relative to proposed rate rise. • The system should be simple. • The framework should promote better and more transparent state govt to council financial relations. • State government departments could fill out RISs assessing impacts on local government. • Council expresses future intent on rate/variation cap exemption. • Local government expenditure has a big state/national economic impact. • The framework should consider the community's ability to pay. • Community service demands fluctuate overtime. • Infrastructure provision should be timely, not lagging (as it is currently). • Demographic change (ageing population) and impact on services should be considered. • State government should identify/put out guidance on alternative/suitable funding sources. • ESC should consider whether a cap is the best answer e.g. will it address renewal gaps? If not, change the rate collecting funding system for local government: don't impose a limitation. • Clear guidelines and fact sheets will be imperative. • The impact of rate capping must be monitored transparently and independently. • A good outcome of rate capping will be a better understanding of local government financial sustainability, and a review of local government funding models. • Cost shifting/changed legislative. Obligations (super call up) should pass for reasons for automatic variation approval. • There are problems with some LGPRF indicators e.g. rate effort indicator unfairly favours high value metros. • The rate capping implementation should be monitored by community satisfaction with rates and services outcomes. • If any new taxes or levies are introduced, the impact on local government should be considered. • Rate capping cannot be viewed in isolation; there are many other issues in local government to consider. • EBA negotiations are complex and need to be considered. • Local government is the tier of government closest to the community. • Business decline should be considered. • ESC should consider the impact of rate capping as it will be imposed during a council election year, and plans and SRPs will be newly developed. This will be a large work load for councils. • Local government are the biggest stewards of community assets as there are no other viable keepers of the assets (2 submissions). • The principles do not consider whether the imposition of rate capping will be financially sustainable for councils through the future. • Determinative rate caps by the ESC may conflict with councils' obligations under the Local Government Act.

Continued next page

TABLE E.23 (CONTINUED)

Other Issues (continued)
Council (continued)
Other Considerations (continued) <ul style="list-style-type: none"> • Councils collect three per cent of Australia's tax but manage 30 per cent of assets held by governments. • Sector wide issues should be addressed in the framework so variations can occur for exceptional circumstances, rather than common reasons amongst councils. • Councils set their rates in many ways which will have to be considered. All councils and their rating set ups should be impacted on equally. • Experienced rate setters/modellers at councils should be consulted. • It is noted that the ESC has consulted widely. • The framework should be risk based and adaptive to council circumstance rather than one-size fits all. VAGO could advise ESC on sustainability risks. • Local government will be reluctant under rate capping to take on any future new services. • Multicultural diversity must be considered in the framework - expensive to manage. • Community engagement is important but to gain community support on all council decisions is impossible. • Higher rate increases are not a significant cost of living pressure e.g. if rates = \$1500, a 4% rate increase instead of a 2.5% increase costs the ratepayer \$0.23 a week more. • State government should focus more on working with and better managing their relationship with Local Government to align common visions and direction. • Councils are democratically elected representations of communities; therefore they should have complete control. • Rate capping will stifle innovation, new programs and assets. • Job losses are likely. Pay and work conditions are likely to erode. • LGPRF should entwine with rate capping. • Ensuring sustainable and stable revenue streams for Local Government are important. • The principles reflect diversities and difficulties there will be in developing rate capping. • It is necessary that sufficient time and planning supports the introduction of rate capping. • The sector must be included in the development of guidelines, fact sheets and other material which forms the framework.
Peak Bodies
Majority of Considerations <ul style="list-style-type: none"> • A general concern services and renewal gaps are likely to deteriorate which should be considered in the framework (a few submissions). • Cost shifting needs to be considered (a few submissions). • Lack of growth in state government set fees collected by local governments needs to be considered (a few submissions). • Changing commonwealth and state government policy positions which flow onto local governments having to increase charges in excess of CPI (a few submissions).

Continued next page

TABLE E.23 (CONTINUED)

Other Issues (continued)
Peak Bodies (continued)
<p>Other Considerations</p> <ul style="list-style-type: none"> • Councils have scope to be less debt-averse (they have a capacity to borrow). • Performance compliance and reporting and auditing should occur on councils taking on rate capping to assess fulfilment of rate capping objectives and its impacts. • Extra resourcing requirements in future should be a reason for a variation. • Recommendations for a light touch monitoring role for ESC, rather than implementing rate capping. • Councils and especially rural councils need sustainability and stability of revenue streams to be improved. • The focus on rates capping should not just be on costs. There should be communication that service costs to community will be more expensive. • Rate capping implementation and impact should be monitored carefully. • Important that all stakeholders understand the methodology and benefits of the framework. • Councils' contribution to communities' quality of life is not properly addressed in CPI. • The impact on local industry due to capital program scale backs need to be considered. • It is not fair that local governments have to comply with defined benefit superannuation liabilities but Commonwealth and State Governments do not. • The framework needs to consider growth. • Defined benefit super schemes unfairly affects local governments and not Commonwealth and State Governments. • Information requirements supporting the criteria to assess variation applications should be relative to proposed rate rises. • Community asset stewardship (including lack of viable alternatives) needs to be considered. • The proportion of rate base that is exempt from rates needs to be considered. • Natural disasters need to be considered. • Lack of own source income needs to be considered. • A further principle should be added saying there will be no unnecessary admin burden.
<p>Other council groups</p> <p>Rate capping should be developed to support the current tax reform agenda. Structured tax reform on land is needed, not just targeting council rates. Land taxes should be grown</p> <p>A financial model should be developed to assess impact of rate capping, grant freezing and capacity to absorb other future costs.</p> <p>The ESC should be transparent in their assessment of variation applications.</p> <p>Better engagement with communities to prioritise services and infrastructure is a key pillar of the new framework.</p> <p>Where the ESC is able to identify/provide alternate forms of financing solutions for LG, RCV offer their assistance and help in doing so.</p> <p>Rural councils should be favoured. They have less resources, high costs, more assets to manage and less own source income</p>

Comment [AP1]: Reworded?

Continued next page

TABLE E.23 (CONTINUED)

Other Issues (continued)
Ratepayers / Ratepayers Associations
<ul style="list-style-type: none"> • Visitors to council areas should be charged more for council services. • Councils need to embrace new budget systems. • Cost shifting needs consideration (a few submissions). • The framework should mandate best value principles. • The Minister should set rates. • Council costs have been rising but not relative to the amount of output. • The CEO has full staffing and costing power, not councillors. • Solar photovoltaics may be used by councils as another potential revenue stream and support cleaner energy. Rates could be set to incentivise solar panel investment, which would incentivise development and clean energy usage. • Councils already aim for low rates. • Councils with asset renewal problems will need help. • More amalgamations are required. • There are better systems to learn from than NSW. • Councils who cut back on services and critical infrastructure spending, based on political decisions to counter rate capping from MAV and VLGA, may be disciplined as VLGA and MAV are subject to the trade practices act. • There should be a peak ratepayers body. • Councils have diverse infrastructure responsibilities and problems. • Applications for variations should not be too administratively burdensome or require consultants. • Councils who exceed the cap should not be too penalised, as this may exacerbate financial problems at the council. • Organisations like private schools, which are like businesses, are given concessions in their rates, which is unfair. • Council engagement with the community at present is futile. Councils do not consider or listen to individuals views. • Councils spend unnecessarily on non-core services e.g. spending on an electronic football scoreboard instead of cheaper manual scoreboards (2 submissions). • Important infrastructure should be managed by Commonwealth and State Government. • The community should have more power/input into planning decisions. • Rate notices should give a breakdown of costs. • An article is cited, questioning rates as an "Australian tax" for the purposes of Division 81 of the GST Act (OCTOBER 22.2012 BY CHRIS SEIVERS). The ESC should clarify. • Rates are so high they should come back down (negative growth). • Councils need to stop spending on noncore services.

Continued next page

TABLE E.23 (CONTINUED)

Other Issues (continued)
Not-for-profit community groups
<ul style="list-style-type: none"> • Best practice engagement is important for councils but is costly. Important to get the correct and worthwhile balance. • Many large societal factors should be considered such as online technology, alternate energy sources, necessity of clean water and growing use of recycled water, preservation of our biodiversity assets, local foods, the unique logistical strengths of our road, rail, sea and air, growing immigration and population, reduced amount of people with unions. • The sharing of adjacent council and state government assets and facilities should be considered. • Councils need to plan their services and programs more, rather than being reactionary. • General concern services will be cut and more specifically, non-core social services (a few submissions). • The framework should mandate the Minister's ability to set rates and mandate compliance with best practice principles. • There should be incentives for councils to continue to support important health services and programs.
Service Providers
<ul style="list-style-type: none"> • The cap should consider long-term councils commitments, e.g. EBAs, super contributions. • Higher land values unfairly distribute rate costs amongst the community.'
Unions
<ul style="list-style-type: none"> • Consultation paper did not address the impact on local government job losses and repercussions for services (likely to happen). • Cost shifting needs to be considered. • Rate capping is contrary to Fair Work Act objectives. It undermines good faith bargaining and locks negotiations at CPI; giving no regard for productivity or concessions made through bargaining. • Rate capping undermines local democracy. • Councils consult excessively and are close to the community. • ESC accountability and mandate questioned. • Rate capping shifts responsibilities and service shortcomings to the state government. • General concern service levels and renewal gaps will deteriorate. • False to assume the cap will correct local government inefficiencies and wastage. It will not drive behavioural change and simply restricts revenue. • The framework should align with the best value principles (NB best value does not equal least cost)

APPENDIX F — INTERSTATE COMPARISONS AND RATE CAPPING IN OTHER JURISDICTIONS

This appendix summarises some of the background research undertaken by the Commission in relation to inter-state comparisons of local government in Australia and the lessons from rate capping in other jurisdictions, including in NSW and internationally.

F.1 INTERSTATE COMPARISONS

F.1.1 EXPENDITURE

Table F.1 shows average local government operating expenditure per person by state between 2008 and 2012. Operating expenditure is not drawn from rates revenue only.

TABLE F.1 LOCAL GOVERNMENT OPERATING EXPENDITURE PER PERSON (\$)
2008 to 2012

State	2008	2009	2010	2011	2012	Growth in expenses over the period (per cent)
NSW	1 019	1 085	1 083	1 190	1 223	20
VIC	972	1 018	1 081	1 168	1 197	23
QLD	1 475	1 599	1 628	1 602	1 721	17
SA	803	858	900	950	977	22
WA	996	1 088	1 123	1 184	1 200	20
TAS	1 320	1 356	1 142	1 146	1 216	-8

Data source: ABS 2012-13, Government Finance, Australia, Statistics cat. no. 5512.

The different responsibilities placed on local government across Australia (for example, in both NSW and Queensland councils provide water and sewerage services) partially explains the different levels of expenditure.

For the period shown, average growth in local government expenditure per person was approximately 20 per cent. Victoria experienced the highest growth of 23 per cent. Tasmania experienced a decline in expenditure after 2010, most likely due to water sector reform when water and sewerage assets, liabilities and staff were transferred to water corporations.¹⁰⁸ Victoria's total operating expenditure per person is comparatively low compared to other states (second only to South Australia).

F.1.2 REVENUE

Compared to other states, Victoria has the highest level of rate revenue per person (see table F.2). However, it should be noted that other states, particularly NSW and Queensland generate a much higher proportion of their total revenue through the sale of goods and services (for example, water).

TABLE F.2 LOCAL GOVERNMENT RATE REVENUE PER PERSON (\$)
2008 to 2012

State	2009	2010	2011	2012	Growth over the period (per cent)
NSW	428	443	456	471	10
VIC	545	577	617	650	19
QLD	558	584	624	643	15
SA	545	573	609	645	18
WA	534	569	607	638	19
TAS	521	542	583	619	19

Data source: ABS 2012-13, Government Finance, Australia, Statistics cat. no. 5512.

Victoria collected approximately \$650 in rate and municipal charges per person in 2012, compared to \$471 per person in NSW and \$643 per person in Queensland. Victoria experienced 19 per cent growth in rate revenue per person over the period, as

¹⁰⁸ Tasmanian Audit Office 2011, *Report of the Auditor-General*, June, p.10.

did Western Australia and Tasmania. NSW experienced the lowest growth in rate revenue per person over the period at 10 per cent.

F.1.3 LOCAL GOVERNMENT DEBT

Table F.3 shows the average debt level (total council liabilities divided by total council assets) of local government in each state between 2009-10 and 2013-14.¹⁰⁹

TABLE F.3 COUNCIL DEBT LEVELS

Per cent					
State	2010	2011	2012	2013	2014
NSW	4.2	4.3	4.4	4.4	4.4
QLD	6.5	7.2	7.9	8.1	8.4
SA	3.8	3.8	3.8	3.9	5.0
TAS	2.8	2.9	3.0	2.9	2.9
VIC	3.0	3.3	3.9	3.6	3.7
WA	5.6	5.6	5.5	5.3	4.3

Data source: ABS 2012-13, Government Finance, Australia, Statistics cat. no. 5512.

Debt levels ranged between 2.8 per cent and 8.4 per cent over the five year period shown. Over that period, Victoria's local government debt level varied from 3 per cent to 3.7 per cent. Victoria's local government sector has the second lowest debt levels behind Tasmania, at 3.7 per cent.

¹⁰⁹ The debt ratio is determined by dividing total liabilities by total assets.

F.2. SUMMARY OF RATE CAPPING EXPERIENCE IN NSW AND ELSEWHERE AROUND THE WORLD

The Commission has been able to draw on both domestic and international experiences in designing its rates capping and variation framework. Aside from NSW, rates capping has been implemented in other countries including New Zealand, the UK and the USA.

F.2.1 NEW SOUTH WALES

The terms of reference for this review asks us to have regard to *any relevant insights* from the experience of rate pegging in New South Wales, including any reviews and evaluations that can suggest ways to minimise any unintended consequences. In meeting this requirement, the Commission consulted extensively with the Independent Pricing and Regulatory Tribunal (IPART) about their experience with rate pegging; held meetings with NSW councils; and reviewed key reports into the sustainability and performance of the local government sector in NSW.

Each year IPART sets a 'rate peg' that determines how much the 152 local councils in NSW can increase their general rates income. The rate peg is based on an index of councils' costs and includes a productivity factor. If a council wishes to increase its general rates income above the peg, they are required to submit an application for a Special Rate Variation to IPART for assessment.

Many submissions from councils and council peak bodies cited the performance of councils in NSW under rate-pegging as evidence of the potentially negative impact rate capping in Victoria could have on infrastructure investment and financial sustainability. A number of recent reports have also identified significant financial sustainability challenges in local government in NSW, principally related to persistent operating deficits and the size of the infrastructure renewal gap and backlog.¹¹⁰ In particular, the final report by the Independent Local Government Review Panel, *Revitalising Local Government*, found that rate pegging had led to four main unintended consequences for the sector:

¹¹⁰ NSW Treasury Corporation 2013, *Financial Sustainability of the New South Wales Local Government Sector*, April; Independent Local Government Review Panel 2013, *Revitalising Local Government: Final Report of the Independent Local Government Review Panel*, October.

- unrealistic community expectations about the rate of increase in council rates
- excessive cuts in expenditure on infrastructure maintenance and renewal, leading to a large backlog
- under-utilisation of borrowing (in part because of uncertainty about future approval of rates needed to repay loans)
- reluctance to apply for Special Rate Variations even when they are clearly necessary because exceeding the rate peg is considered politically risky, or the process of applying is perceived to be too onerous relative to benefits.¹¹¹

While the NSW experience highlights some challenges for rate capping in Victoria, it is worth noting that the infrastructure and financial sustainability problems in the NSW local government sector have accumulated over a long period of time and have been influenced by a number of other factors such as: the number of councils, governance and decision-making, poor asset management practices, and reluctance of some councils to incur debt. The lessons from NSW highlight the importance of ongoing monitoring of the service and performance outcomes and financial sustainability of councils in Victoria following the implementation of the rates capping framework.

F.2.2 NEW ZEALAND

New Zealand does not have an overt system of rates capping, but rather limitations on rates increases have been developed into council planning requirements. *The Local Government Act 2002* (LGA) that governs New Zealand's local governments requires councils to publish long-term plans (LTPs), containing information on projects, financial strategies and rates limitations. LTPs involve extensive citizen consultation in council decision-making, as councils are required to hold referenda on any proposed changes to LTPs, including rates increases.

A commonly cited example is the Wanganui District Council, which undertakes annual referenda on key components of their LTP. The 2009 Wanganui referendum included a question on three rating scenarios (low, medium or high) with corresponding levels of service and infrastructure maintenance.¹¹² This gave the community more power to

¹¹¹ Independent Local Government Review Panel 2013, *Revitalising Local Government: Final Report of the Independent Local Government Review Panel*, October, p.42.

¹¹² New Zealand Institute of Economic Research (NZIER) 2009, 'Rates Capping: A Study of the International Literature and Experience', p. 16.

influence rates levels for the year and also increased voter turnout for the referenda from previous years (the four year average increased from approximately 50 per cent to 61 per cent).¹¹³

F.2.3 THE UNITED KINGDOM

The United Kingdom has a long history of centralised oversight of how local governments' raise revenue. A set of principles defined by the Secretary of State of the Department for Communities and Local Government is used to determine whether the amount to be raised by local government is excessive. Councils are required to hold a referendum if they wish to raise council taxes to a level deemed excessive by the Secretary of State. Currently, this threshold is set at two per cent. Council rate increases have been further discouraged with the introduction of more grant funding for councils, where councils were offered a greater portion of grant funding as a substitute for seeking rate increases.¹¹⁴

F.2.4 THE UNITED STATES OF AMERICA

The US has a system of containing both state and local government revenue and expenditure. These are broadly known as tax and expenditure limits (TELs). Rate limitation occurs in approximately 38 states, enforced by state legislation. Tax (rates) limits take several forms, the most common of which are property rates and assessment limits. Property rate limits are designed to limit payments to a certain percentage of the property's market value. California and Washington, for example, limit property rates to 1 per cent of market value. Assessment limits restrict how much property values may increase in a year for tax purposes. Similar to variation methods in New Zealand and the UK, councils that seek to increase TELs above their assigned levels are required to hold a referendum for their proposed variation. Colorado, for example, instituted TELs in 1992 through a constitutional amendment called the 'Taxpayers Bill of Rights' (TABOR).¹¹⁵ This limited council revenue to the previous

¹¹³ Ibid.

¹¹⁴ Department for Communities and Local Government 2015, *2010 to 2015 government policy: Council Tax reform*, London, <https://www.gov.uk/government/publications/2010-to-2015-government-policy-council-tax-reform/2010-to-2015-government-policy-council-tax-reform>, Accessed 15 August 2015.

¹¹⁵ Whilst TABOR is defined in state legislation, its formation was citizen-initiated.

year's level plus inflation and a net percentage increase in market value of all property within the jurisdiction.

GLOSSARY

Annual budget	Sets out the services and initiatives to be funded for the financial year and how these will contribute to achieving the strategic objectives specified in the council plan.
Annual report	Contains report of operations, performance and financial statements (including rating outcomes).
Asset renewal expenditure	Expenditure on an existing asset or on replacing an existing asset that returns the service capability of the asset to its original capability.
Capital Improved Value	The total market value of the land plus buildings and other improvements. Most councils in Victoria use the CIV valuation in setting rates.
Cost shifting	<p>A term used by the sector to describe situations where other levels of government shift service responsibility onto local government without a commensurate level of funding support.</p> <p>The major areas of cost shifting cited by councils include:</p> <ul style="list-style-type: none">• the withdrawal or reduction of financial support once a program is established, therefore leaving local government with the choice of continuing a program or ceasing

service provision;

- the transfer of assets without appropriate funding support;
- the requirement to provide concessions and rebates without appropriate funding;
- increased regulatory and compliance requirements; and
- failure to provide for indexation of fees and charges for services prescribed under state legislation or regulation.

Council Plan/Community Plan

Sets out the medium-term strategic objectives, strategies, strategic indicators and resources reflecting the vision and aspirations of the community for the next four years.

Council election

A general election of Councillors for all Councils held every fourth Saturday in the fourth year after the last general election of Councillors for all Councils was held.

The next election for all Victorian councils will be held in the fourth Saturday in October 2016.

Cultural and recreation land rates

Rates paid on recreational and cultural lands as defined under the Cultural and Recreation Land Act 1963. They are based on services provided to the land and the community benefits derived from the land.

Developer contributions

Payments or works-in-kind towards the provision of infrastructure made by the proponent of a new development. The Planning and Environment Act 1987 allows for development contributions to be provided through the:

- planning scheme amendment process
- planning permit process, or
- building permit process.

Development contributions are one of a number of options for funding infrastructure available to local and State government.

Differential rate

A different rate in the dollar is set for different categories of rateable land. For example, a council might have differential rates for farm land, various categories of residential property or commercial/industrial properties — each paying a higher or lower rate in the dollar.

Differential rating can only be used by councils using the Capital Improved Value system of valuing land.

There is no limit on the number or type of differential rates that can be levied, but the highest differential rate can be no more than four times the lowest differential rate.

Financial assistance grants

General purpose and road grants from the Commonwealth Government allocated to Victorian councils. Both grants are untied, which means that the Commonwealth Government cannot direct how they are spent by councils.

Financial sustainability

The Victorian Auditor-General defines financial sustainability as being able to meet current and future expenditure as it falls due. Councils also need sufficient capacity to absorb certain risks and changes that may materialise without significant change to their revenue or expenditure policies.

A council will be financially sustainable over the long-term when it is able to generate sufficient funds to provide the levels of service

and infrastructure agreed with its community.

Freeze of Federal Assistance Grants

The national funding pool (for Federal Assistance Grants) is indexed annually in line with population growth and inflation forecasts. This indexation is 'paused' for three years (from 2014-15 to 2016-17).

General rates

Applied as a percentage of each property's valuation; either a uniform rate, or a number of different rates for different property classes, such as residential, farms, commercial and industrial enterprises.

General revaluation

State legislation requires that all properties in every municipality are revalued every two years. Changes in property values will vary across a municipality. A general revaluation may result in the rates for some properties going up while others go down. If a property's value increases by less than the average increase across the municipality, the rates for that property will be relatively lower. Rates will be relatively higher if a property's value increases by more than the average increase in valuation.

Councils do not collect extra revenue as a result of the revaluation process. Valuations are simply used as an apportioning tool to assess the rates payable for each individual property.

Green wedge

The non-urban areas of metropolitan Melbourne that lie outside the urban growth boundary are known as green wedges. There are 12 designated green wedge areas, spanning 17 municipalities, which collectively

form a ring around the city.

Land in each green wedge area is unique in terms of its use and appearance ranging from the coastal landscape of Mornington Peninsula to the open basalt plains of the west and to the highly scenic landscapes in the Yarra Valley.

These areas contain a mix of agriculture and low-density activities, including major infrastructure that supports urban areas, such as Melbourne and Moorabbin airports and the western and eastern water treatment facilities. They include major quarries used in the building industry, cultural heritage sites, biodiversity conservation areas and water catchments that provide clean drinking water for a growing population.

Infrastructure

Infrastructure comprises the assets needed to provide people with access to economic and social facilities and services. For councils, examples of infrastructure may include: roads and bridges; facilities for arts and culture, early childhood and family support, education, health, justice and emergency services and sport and recreation.

Interface/growth councils

The Interface Councils lie at the interface of metropolitan Melbourne and rural Victoria, sharing aspects of both urban and rural communities. Characteristically, the population dispersion across the municipalities is concentrated around urban areas, with significant numbers of people living in rural townships. In all of the municipalities, approximately 70 per cent of the population live in about 30 per cent of the area. The

interface councils are Cardinia Shire Council, City of Casey, Hume City Council, Melton City Council, Mitchell Shire Council, Mornington Peninsula Shire Council, Nillumbik Shire Council, City of Whittlesea, Wyndham City Council and Yarra Ranges Council.

Local Government Act 1989 (the Act)

Governs the operation of local government in Victoria. It outlines councils' purpose as: to provide for a democratic, efficient and effective system of local government in Victoria, to give councils powers which will enable councils to meet the needs of their communities, to provide for an accountable system of local government and reform the law relating to local government in Victoria.

Key service areas

The nine key service areas covered in the Department of Energy, Land, Water and Planning's Annual Local Government Community Satisfaction Survey.

Survey respondents rate council performance on the following nine key service areas: local roads and footpaths, health and human services, recreational facilities, appearance of public areas, waste management, economic development, traffic management and parking facilities, enforcement of local laws and town planning policy and approvals.

Matching grants

When the State or councils designate funds to go to particular types of projects. Various groups within the community can then develop project proposals and apply for the grant. If accepted, the council will match the community contribution to the project.

Municipal charges

To cover some of council's administrative costs. (Administrative costs are not defined in the Act.)

The legislation requires that revenue from the municipal charge can be no more than 20 per cent of the total revenue raised from the combination of the municipal charge and the general rates.

Net Annual Value

The current value of a property's net annual rent, i.e. gross annual rental less all outgoings — such as land tax, building insurance and maintenance costs etc.

By law, the Net Annual Value must be at least 5 per cent of the Capital Improved Value for commercial property and exactly 5 per cent of Capital Improved Value for residential property.

Peri-urban councils

Councils on the urban-rural fringe experiencing rapid growth relative to the existing population base. These include the shires of Bass Coast, Baw Baw, Golden Plains, Macedon Ranges, Moorabool, Murrindindi and Surf Coast.

Property valuation

Property values affect the amount paid in municipal rates. Property values are determined by independent valuers appointed by a council or the Victorian Valuer-General. These valuers assess the market value of each property in line with guidelines issued by the Valuer-General. Properties are valued either on the basis of Net Annual Value, Site Value or Capital Improved Value.

Rate in the dollar

Used to calculate a property's rates. Rate in the dollar is multiplied with the value of a

ratepayer's property to calculate the property's rates. For a council using only a general rate, the rate in the dollar is calculated as:

If council plans to raise the total rate revenue of \$10 million, and the total Capital Improved Value of all rateable properties in the municipality is \$2,380 billion, then the rate in the dollar is calculated by dividing \$10 million by \$2,380 billion = 0.0042.

Rateable land

All land is rateable except those listed in section 154(2) of the Act.

Rating policy

A council's rating policy outlines how its rates will be applied and calculated.

Revenue and rating strategy

A revenue and rating strategy may comprise a number of components and may include documents on: council rationale and objectives including a discussion about its pricing policy and core components of its rating structure; related research and background discussion on the municipality and past practices; comprehensive rates, fees and charges impact modelling on the municipality; explanatory material and opportunity for public review/consultation.

Renewal gap

The difference between the funding that councils need to renew their existing assets and the money they actually allocate for this purpose. Can be measured using a number of methodologies.

Currently, the Victorian Auditor-General's Office, the Municipal Association of Victoria and the Local Government Victoria measure the renewal gap using different methodologies.

Revenue in lieu of rates	Payments received by councils on unrateable lands such as railway land, Commonwealth and State Government buildings, mining land, power stations, airports and windfarms.
Service charges/rates (garbage)	For services to properties such as waste management. Can be levied as either a rate (i.e. based on property valuation) or a charge (i.e. per unit) or some combination. A different amount may be charged for different property categories or for different sized bins.
Site Value	The market value of the land only.
Special rates/charges	Are levied on ratepayers specifically benefitting from a service or investment such as footpaths; kerbs and channels; and arrangements for providing services like promotion, marketing or economic development (such as for commercial businesses).
Strategic Resource Plan	Sets out the financial and non-financial resources for the next 4 years to achieve strategic objectives (including rating strategies).
Supplementary rates/charges	Rates assessed/adjusted during the year as a result of supplementary valuations. Reasons for a supplementary valuation include: development of vacant land, new subdivisions, renovations and extensions, sale of non-rateable properties and consolidation of properties.
Tied grants	Specific purpose monetary grants tied to certain activities/outcomes (often legislative) that the recipient must deliver in order to

receive the grant.

Uniform rate

All rateable land in a municipality are charged based on the same rate in the dollar.

Untied grants

General purpose monetary grants which are not tied to certain activities/outcomes. Providers of untied grants are unable to direct councils as to how the funds allocated are to be spent.

Victorian Auditor-General

The Auditor-General is an independent officer of the Victorian Parliament, appointed to examine the management of resources within the public sector (including local councils) on behalf of Parliament and Victorians. The Auditor-General conducts and reports on financial and performance audits.

Victorian Grant Commission

Allocate grants provided by the Commonwealth Government for councils in Victoria according to the *Local Government (Financial Assistance) Act 1995* and a set of national distribution principles. All funds provided by the Commonwealth are distributed to councils.

Whelan report

The Whelan Report examines the financial sustainability of Victorian councils using a statistically based measurement system created for the purpose (the Whelan Model).

Its aim is to provide an objective, reliable basis for determining the relative sustainable capacity of Victorian councils by identifying, quantifying and applying the geographic, demographic and financial characteristics impacting on this capacity.

ABBREVIATIONS

ABS	Australian Bureau of Statistics
ANMF	Australian Nurses & Midwifery Federation
ASU	Australian Services Union
CIV	Capital Improved Value
CPI	Consumer Price Index
CPN	Corporate Planners Network
DELWP	Department of Environment, Land, Water and Planning
DTF	Department of Treasury and Finance
ESC	Essential Services Commission
FINPRO	Local Government Finance Professionals
ICG	Interface Councils Group
IPART	Independent Pricing and Regulatory Tribunal (NSW)
LGCi	Local Government Cost Index
LGPRF	Local Government Performance Reporting Framework
LGPRo	Local Government Professionals

LGV	Local Government Victoria
NAV	Net Annual Value
MAV	Municipal Association of Victoria
OLG	Office of Local Government (NSW)
PPI	Producer Price Index
RBA	Reserve Bank of Australia
RCV	Regional Cities Victoria
RCV	Rural Councils Victoria
RMA	Revenue Management Association
RV	Ratepayers Victoria
SRP	Strategic Resource Plan
VAGO	Victorian Auditor-General's Office
VFF	Victorian Farmers Federation
VGC	Victoria Grants Commission
VLGA	Victorian Local Governance Association
WPI	Wage Price Index