SUBMISSION TO THE
Essential Services Commission
Local Government -
Rates Capping & Variation Framework

The Form of the Cap

1. **While a cap based on CPI is simple to understand and apply, are there any issues that we should be aware of?**

Mitchell Shire Council relies heavily on Rate Revenue. In 2015/16 the forecast Rate Revenue is 55% of all revenue and 67% when capital grants and contributions are excluded. Rates Revenue is heavily relied upon to fund the increasing cost of delivering existing services as well as the need for increased demand for service delivery and infrastructure development in the growth areas.

In some circumstances Council is currently tied to existing contracts, including an Enterprise Bargaining Agreement which provides for a 3% per annum increase, this is combined with an expectation that Councils allow a 1% increase in wages for the progression and promotion of staff through levels within a band.

Mitchell Shire Council is unique in that we are;

- one of the largest geographic municipalities in Victoria,
- an Interface council,
- the 3rd fastest growing municipality,
- a Growth Council within Melbourne's designated growth boundary,
- catering to a mix of urban and rural communities,
- on the nationally significant transport corridor between Melbourne and Sydney, and
- supporting socially and economically disadvantaged communities

Mitchell Shire's 2015 population is identified as 39,911 and is expected to grow to 89,214 by 2036. A 123.53% growth forecast. Council comprises five major towns and we are striving to balance the need to maintain services and infrastructure for our existing communities and address inadequate and aging infrastructure, as well as expand and build new infrastructure for our growth areas and new communities. Council has funded and will need to continue to fund, Capital Works with borrowings to ensure that we provide the required new infrastructure within our growth areas and to fund other new assets for existing communities that have intergenerational benefit, such as the planning, acquisition and construction of the Seymour Flood Levee. The borrowing costs then decrease the amount available for service provision.

As with other Interface Councils we have a higher proportion of local road infrastructure when compared to inner / middle metropolitan councils where a greater proportion of the road network consists of state funded arterial roads. Council maintains 652km of Sealed Roads and 915km of unsealed roads. This higher proportion of local infrastructure places an additional burden on our budgets compared to those other Councils. We rely on grant funding to adequately renew this road infrastructure. Recently these previously recurrent grant sources have been cut or stopped altogether (Roads to Recovery and Country Roads and Bridges Infrastructure).

Annual rate increases at Consumer Price Index (CPI) level will not address the current issues facing Mitchell Shire Council. In Council's long term modelling which proposes rate increases of 4.5% annually from 2016/17, key VAGO indicators move between medium and high risk. This will result in Council needing to consider service reduction or cessation of services in order to ensure sustainability, in particular to maintain and balance spending on services and infrastructure. Even at this higher than CPI rate Council only expects to achieve an asset renewal ratio of between 30-40% without additional funding in grants and contributions.

Council's previous SRP outlined rate increases of 8.5% for three years in order to return Council to financial sustainability while providing current service levels into the future. Significant cost containment work has been carried out in an effort to minimise this increase.

At 4.5% we have assumed that this will result in the requirement to apply for a variation to the capping which will require funds to be redirected for extensive community consultation within a short time frame.

Significant progress has been made to reduce the operating costs of Council over the past two budget cycles including a restructure in 2014/15 that reduced annual employee costs by $1M (4% of the total employee budget) without reducing services to the community. Mitchell Shire Council's average rates, municipal and garbage charge were in the middle of the range when compared to other similar Councils in a 2014/15 survey.

2. What are some ways to refine the cap (for example, alternative indices), in line with the Government's objectives?

Council would support a proposal to develop an independent local government cost index that could be implemented over a number of years to allow a transition period for any instances where Councils are currently locked into existing contracts and arrangements that could potentially exceed a rate cap. This index could include recognition of State and Commonwealth Grants being reduced and in some instances, even removed, the impact of cost shifting as well as the impact from statutory fees not increasing at an appropriate level each year in line with the costs of delivering those service.

We would support different caps for different Council groupings, i.e. metropolitan, growth, rural, interface, etc. The ability to raise non-rate revenue differs in councils, such as parking fees and fines, etc. and councils in rural and remote areas, especially those that may have large geographical areas, face higher costs in delivering works and services compared to metropolitan areas.

Alternatively a set percentage above the rate cap could apply to councils that meet set categories and groupings, i.e. Growth and Interface. This would reduce the need for costly variation applications and administration.

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?

Mitchell Shire Councils believes that the cap should be confirmed annually with future indicative caps to support the preparation of the 4 year Strategic Resource Plan at a minimum as well as allowing time for sufficient planning and preparation for any variation processes that Council identifies.

4. Should the cap be based on historical movements or forecasts of CPI?

The cap should take into account historic movements in addition to local government known challenges, including the risk of future defined benefit calls, reduced and removed Federal and State grants, inability to increase non-rate revenue, and other known or forecast cost shifting impacts. To restate Mitchell Shire's position, Council does not believe the use of CPI as one standard indicator is appropriate.

5. Should a single cap apply equally to all councils?

A single cap could be applied as a base. Referring to discussions in point 1 above, an above cap percentage could apply to Councils outside the metropolitan area facing different and additional challenges.

Alternatively multiple caps could be developed for Councils that are inner / middle metropolitan, interface, growth, regional, rural, etc.

We would support a tiered model where rate increases below a base cap would not need review, a certain % above the base to have a light review and a more rigorous review for higher % increases.

THE BASE TO WHICH THE CAP APPLIES

6. What base should the cap apply to? Does it include rates revenue, service rates/charges, municipal charges and special rates/charges?

The cap should only apply to general rates and the municipal charge where applicable. Service charges such as waste should be based on a cost recovery basis as these are directly linked to specific services or infrastructure projects.

The cap should be calculated on the rate revenue of the prior year and adjusted for supplementary revenue (growth).

7. Should the cap apply to total revenue arising from these categories or on average rates and charges per assessment?

The cap should apply to the total general rate and municipal charge revenue adjusted for growth.

If we understand per assessment correctly our concern around applying a cap per assessment is that it may restrict the ability of Council to alter rating strategies around municipal charges and differential rates. We would seek to clarify if this would require a separate validation/approval process.

8. How should we treat supplementary rates? How do they vary from council to council?

Supplementary rates should be excluded from the rate cap, they are driven by growth and impact councils through additional services and infrastructure required. Additional revenue is required to deliver to a growing community.

Supplementary rates would become part of the base for the following financial year.

9. What are the challenges arising from the re-valuation of properties every 2 years?

A property re-evaluation requires additional engagement and education, rate payers will generally not receive a straight % increase due to valuation movements up and down.

The rate in the dollar would adjust up or down to ensure the rate capping value is not exceeded due to the changes.

The valuation changes will mean that some rate payers will experience an increase above the published cap, whereas others may experience a decrease, this is difficult to explain to the community, however occurring every two years will make it easier to understand as opposed to it occurring less frequently.

An annual re-valuation would result in unnecessary additional costs.

10. What should the Base Year be?

If the rate capping commences for the 2016/17 financial year, then 2015/16 should be the base year.

THE VARIATION PROCESS

11. How should the variation process work?

It is important that the variation process is simple and not costly for councils. Some councils, and in particular small rural councils, may struggle to provide the resources required to ensure a successful variation application where necessary and should receive external support.

Variation / Exemption guidelines should be developed that clearly detail the requirements of a successful application. Variation options should be available, for example, an application could be for 1 year or more, illustrated as follows,

- rate cap + 2% for 1 year, or
- rate cap + 2% for a set number of years, or
- rate cap + 4% in year 1, rate cap +3% in year 2 and 3, etc.

The level of information in support of the application should correlate back to the length of time the application covers and / or the increase amount.

A standard template should be established and annual information sessions should be held to educate councils on common challenges, how to guides and the like.

Financial Assessment of both the current sustainability status versus the change the variation will have on Council in the long term. Detailed information and demonstration of the following would be required;

- Realistic and sustainable policies and procedures are adopted;
- Council has a robust 10 year Long Term Financial Plan and 4 year Strategic Resourcing Plan in place;
- It can be demonstrated that Council decisions are made referencing the long term implications;
- Clear and transparent communication and consultation has occurred within the community in the development of annual budgets and mid to long term plans, including the plan to apply for capping variation or exemption; and
- Clearly defined impacts and implications of external factors including cost shifting, State and Commonwealth funding and policy changes, natural disaster recovery, etc.

12. Under what circumstances should councils be able to seek a variation?

Councils should be able to seek a variation where their financial circumstances warrant the need for an increase above the cap or where a new service or infrastructure is planned for and community consultation has been undertaken and can support the decision. Councils must be able to show that sound decision making has led to the application.

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?

Yes, councils that are already faced with financial challenges, including insufficient asset renewal and capital spend, that were addressing these concerns through planned increases over the coming years, in addition to circumstances where;

- State and Federal Government cuts to grants where the services will continue;
- Cost shifting by other statutory agencies;
- Service increases and expansions in consultation with the community;
- To compensate for inadequate statutory fee increases; and
- Where a community requires an increase in service to address a substantial community disadvantage and / or challenge.

14. What should councils need to demonstrate to get a variation approved? What baseline information should be required for councils to request a variation? A possible set of requirements could include:

- **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.**

We would like stakeholders' views on whether the above requirements are adequate.

Council would support the five possible requirements outlined above if the concerns outlined in 1 above have been taken into account when developing the cap. Guidelines would be required to clearly define the meaning of, 'effectively', 'reasonable' and 'legitimate'.

COMMUNITY ENGAGEMENT

15. What does best practice in community engagement, process and information look like? Are there examples that we can draw from?

Community engagement must ensure that the community has time and opportunity to engage with Council using a variety of methods. Methods include community panels, written submissions, public hearings, social media, face to face meetings, surveys, polls, focus groups, reference to Community Plans and the like. There must be preparedness to go to the community to ensure feedback is representative of the whole community, i.e. visit train stations, supermarkets, banks, etc.

INCENTIVES

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?

Incentives would include ensuring that the variation process was designed to meet the type of variation, simple processes for small variations and more substantive and complex for larger, longer variations as well as working with the sector to define the guidelines and capping methodology and to ensure that the implementation dates are achievable and allow enough planning and guidance for those councils who may need a variation in year 1.

Unintended consequences could include;

- Councils lacking resources and needing a variation unable to prepare a successful application impacting on their long term sustainability;
- reduced services and infrastructure that is not maintained at current standards;
- increases to the asset renewal gap;
- increases to fees and charges and thereby removing subsidies that are currently for the community benefit; and
- increased borrowings that may be unmanageable in the long term.

In order to minimise the consequences above a reasonable indexation should be applied as discussed in previous points in addition to a simple and efficient variation process. Where required professional support and guidance in the variation process should be available.

TIMING AND PROCESS

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.

Council recommends that the commencement year be moved to 2017/18 for the reasons that, one, many councils will have completed their existing EBA's, two, many Councils' existing contracts will have concluded allowing for possible increase restrictions being based on the indicative rate capping for future years and thirdly because it will allow councils sufficient time to prepare and plan for the change or the need to apply for a variation.

The cap should be published by 1 November each year with applications for variations closing around mid December. Utilising future indicative cap rates councils could commence a variance application earlier than the cap announcement. Notifications of the variation outcome should be by 1st February to allow adequate time to feed into the budget process and make changes where necessary.

TRANSITIONAL ARRANGEMENTS

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?

Council recommends that the implementation year be moved to 2017/18. The Framework could be implemented and the rate cap commenced with voluntary adoption until 2017/18. Councils will not be able to ensure adequate consultation and engagement when the framework or process is yet to be announced. This would provide for a smooth transition and education of all parties.

ROLES

19. What are stakeholders' views on the respective roles of the key participants? Should the Commission's assessment of rates variations be advisory or determinative?

The Essential Services Commission (ESC) as an independent participant should review all variation submissions and advise the Minister of Local Government for determination.

The ESC would review the variations based on merit against pre-established criteria and detailed findings by the ESC should be reported to the Minister for Local Government for a final determination. The final decision and findings should be reported back to the Council.

OTHER MATTERS

20. Is there a need for the framework to be reviewed to assess its effectiveness within three-year's time?

Yes. The principles of continuous improvement should apply. The review should take into consideration feedback from all stakeholders, including any related changes to services and standards, as well as a review of the impact on councils' financial sustainability and in particular a pre and post review of,

- the VAGO sustainability indicators, and
- an asset renewal gap analysis to assess deterioration impacts.

It is recommended that the review not be undertaken in an election year to ensure independence from political settings.

21. How should the costs of administrating an ongoing framework be recovered?

The State Government should cover the costs of administration as the policy owner and driver. 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.

OTHER MATTERS RAISED IN EARLIER CHAPTERS

22. 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.**

Refer to section 1 for context around Mitchell Shire Council and our unique challenges.

Prior to the announcement of the introduction of rate capping Mitchell Shire Council had planned rate increases of 5-7%. In preparation for rate capping Council has adopted an SRP of 4.5% each year assuming a rate capping variation would be required. This reduction in the long term impacts Mitchell Shire Council with a potential loss of $23M in rates revenue which will impact on the ability to renew infrastructure. Council's asset renewal ratio is forecast between 30-40% over the coming 10 years which gravely impacts on Council's ability to maintain even basic community infrastructure already in place. Furthermore it leaves no funding available for the development of much needed new infrastructure across the municipality to support our new and existing communities.

If Council was not able to achieve a rate increase of 4.5% p.a. and instead was capped at an assumed rate of 2.5% this would further reduce rate revenue over the 10 years by $35M, thus requiring significant service reduction and / or cessations.