

Campbelltown City Council

Submission

**Parliamentary Inquiry into
Cost Shifting By The States
To Local Government**

Executive Summary

Local Government has existed since 1840 and anchors the Australian system of government at the community level. It is committed to the overarching principles of local democracy, peace, social and economic justice and ecologically sustainable development.

Australia currently has 698 local governing bodies representing local communities. Local Government serves its community as:

- A local representative government providing a voice for community aspirations and concerns
- A policy maker setting local agendas and priorities
- An advocate representing local communities to other spheres of government and various community based agencies
- A regulator in areas such as building controls, public health and the environment
- A planner overseeing the development of local planning frameworks
- A coordinator ensuring integrated, effective and efficient service delivery
- A service deliverer providing social and physical infrastructure
- An agent providing services to the community on behalf of other spheres of government
- An information broker between suppliers and consumers, across all spheres of government, business, community organizations and local residents

However within our federal system two elements are required in order for it to function effectively. First, accountability between spheres of government must be clear and unambiguous. Second, fiscal equality is essential to ensure each sphere of government possesses the resources to fund relevant actions across its own domain of responsibility.

The functionality of Australia's federal system is impacted by

- Limited recognition of Local Government as an integral part of the federation
- Vertical fiscal imbalance and inequitable financial arrangements between the spheres of government
- Unclear delineation of the roles and responsibilities of the spheres of government; and

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- Ineffective mechanisms for cooperation and consultation between governments

Both Commonwealth and State/Territory Governments have tax bases that currently exhibit high levels of real growth. This may be expected to continue into the future. Stable revenue bases exhibiting real levels of growth, are critical to the efficient and effective operation of any sphere of government.

Financial relations between the Commonwealth and Local Government are characterised by the significant difference between the revenue raising and expenditure responsibilities of the two spheres of government. This mismatch of spending and taxing powers results in a vertical fiscal imbalance (VFI).

As Local Government taxes do not grow at the rate of Commonwealth and State taxation regimes the VFI between Local Government and the Commonwealth continues to grow. To compensate for the imbalance the Commonwealth distributes surplus revenues in the form of General Purpose payments. Their primary objective is to reverse the VFI and strengthen Local Government, enabling the provision of a wider range of services while promoting both financial equity between councils and certainty of funding.

The Local Government General Purpose Payments are indexed annually on the basis of changes in the level of inflation and population changes in each state. Therefore these payments grow at a rate substantially less than that of GDP or Commonwealth and State taxation revenue. This methodology is both an unfair and discriminatory mechanism for sharing the nation's tax resources.

In the absence of an equitable methodology a serious VFI gap is emerging. This widening gap is already undermining the financial viability of Local Government. Financing the gap is problematic for Local Government which has few alternatives, none of which is desirable:

- Declining unfunded mandates imposed by the Commonwealth and States, although some of these may be difficult as they are legislated and difficult to neutralize.
- Increasing property rates
- Increasing user charges
- Increasing local government debt

Setting the General Purpose Payments to an appropriate percentage of total Commonwealth Taxation Revenue would stabilise the VFI gap and offset the need for less desirable financing alternatives. The extra funding provided by such a methodology will enable Councils to:

- Improve the capacity to provide standard levels of service to communities

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- Improve the delivery of service
- Maintain and improve the quality of social and physical infrastructure.
- Assist in the repair of environmental degradation; and

Further enhancing Local Government's contribution towards the achievement of State and community objectives cannot be achieved without an adequate revenue base. Linked to a broad agreement on the role of Local Government, and processes to examine specific areas of responsibility both state-wide and at the local and regional level, a number of options to consolidate and enhance Local Government's financial capacity warrant detailed consideration.

The system of rate pegging in New South Wales should be reviewed with the aim of removing unwarranted limits on revenue. The tendency of the current system to depress increases in Local Government revenues below those of other spheres and hence deprive the public sector overall of much needed resources, seems wholly counter-productive. Nor is it clearly evident that the system any longer produces significant political gains for the State Government.

Consideration also needs to be given to the inter-relationship between Council rates and State Land Tax. The growing incidence of land tax could effectively eat into the rating base by reducing capacity to pay and/or increasing political resistance to payment of rates.

It is important that there are no arbitrary limits on the fees and charges Councils are permitted to levy for various services, licences and approvals. Circumstances vary substantially from one local area to another, and the case for State –wide uniformity is also debatable. A better system is for Councils to justify their charges in terms of detailed analysis of costs and against a set of guiding principles.

On the other side of the ledger, State imposts on Local Government in areas such as waste management and fire services should also be properly justified or reduced. Local Government should not be used as a proxy collector of State taxes.

Under the Implementation Agreement for National Competition Policy (NCP) the NSW Government received nearly \$140m in 1999-2000 and a similar amount in 2000-2001. Payments are scheduled to increase to over \$200m per annum by 2005-2006. Among the factors to be taken into account in the allocation of these payments is the performance of Local Government in implementing competition policy reforms.

To date, the NSW Government has refused to discuss sharing competition payments with Local government. This is despite the significant business reforms being implemented by

Councils. As well, Councils are facing additional costs due to the application of competitive neutrality principles by State utilities.

Terms of Reference

1. Local Government's current roles and responsibilities.

Local Government throughout Australia and particularly in New South Wales has developed strongly in the latter part of the 20th Century. Its functions have expanded enormously to embrace now routine activities such as local and regional planning, environmental health, pollution control, natural resource management, community services and economic development.

Fundamental changes were made to the way Councils do business, internal restructuring, strategic and corporate planning, financial management, benchmarking and performance indicators and application of competition principles have all impacted on the industry over the past decade.

The Local Government Act introduced in 1993 provides a framework to manage ongoing change and improvement. But it needs to be complemented by a shared vision, shared primarily by Local and State Governments, but also involving the Commonwealth, of how Local Government should continue to develop in this new century. Central to ensuring the achievement of community goals is the development and implementation of financial and other intergovernmental arrangements to bring about desired outcomes.

The 1993 Act listed other legislation under which Councils have functions including:

- Community Land Development Act
- Conveyancing Act
- Environmental Planning and Assessment Act
- Fire Brigades Act
- Public Water Supplies Act
- Food Act
- Impounding Act
- Library Act
- Public Health Act
- Recreation Vehicles Act
- Roads Act
- State Emergency Services Act
- Strata Schemes Act
- Swimming Pools Act

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Since 1993 there have been some important additions, notably the Waste Minimisation and Management Act, The Protection of the Environment Operations Act, The Rural Fires Act and the Companion Animals Act. At the same time, further or more complex responsibilities have been inserted into existing legislation, such as the Environmental Planning and Assessment Act and the Local Government Act itself.

The corporate planning and reporting requirements of the 1993 Act were themselves a very significant extra function for many Councils, and for all Councils the requirement to prepare State of Environment reports was completely new. To these have been added in more recent years responsibilities for the preparation of Social Plans, and to incorporate special provisions relating to ecologically sustainable development and access and equity into Council's management plans.

It seems clear that NSW State agencies will continue to respond to pressures on their own resources, and to community demands for action on issues of concern, by devolving responsibilities to Local Government. The key issue for Councils is whether this trend will proceed ad hoc or through a coordinated, consultative process. In particular, there is a pressing need to address the cost implications for Councils when functions are transferred without corresponding financial support or revenue mechanisms.

2. Current funding arrangements for local government, including allocation of funding from other levels of government and utilisation of alternative funding sources by local government.

Local Government finances are under increasing stress. Local Governments capacity to deliver services and to develop and maintain infrastructure are under genuine threat. This is the combined result of restricted revenue raising capacity, increasing responsibilities and rising community expectations.

Rating is the only taxation measure available to Local Government and accounts for approximately 50% of total revenue. This narrow taxation base places a severe restriction on a Councils capacity to raise revenue generally. Further, the rating base varies significantly between Local Government areas, an aspect only partially addressed by the Horizontal Fiscal Equalisation principles of the Local Government grants process. Unlike the Commonwealth and State Governments, Local Government does not have the flexibility to spread its taxation effort over a suite of taxation tools. The situation is further exacerbated by the rate pegging system in New South Wales.

The restricted taxation base has led to a growing reliance on fees and charges but this recourse is reaching its limitations. User charges are the second largest source of revenue and already represent 27% of Local Government operating expenditure in New South Wales. Through the application of user fees and charges Local Government already achieves a much higher cost recovery ratio than other spheres of government. On a national basis, the cost recovery ratio for Local Government is 36.8% compared to ratios of 4.3% for the Commonwealth and 12.2% for the States.

This partly reflects the type of services provided by Local Government. However, it also suggests that Local Government is already maximising its use of user fees and charges and that there may be limits to the extent that Local Government is already maximising its use of user fees and charges and that there may be limits to the extent that Local Government can increase its cost recovery efforts. Apart from general community resistance to ever increasing fees and charges there are important equity and governance considerations. Many Council services by their very nature cannot be provided on a cost recovery basis. Further, the opportunity to raise revenue in this way varies significantly between Councils. For example parking meters are an option restricted to high density commercial and tourist areas.

Grants are the third major source of revenue for Local Government, with Commonwealth Financial Assistance Grants representing 8.6% of total operating revenue for Councils in New South Wales.

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Grants to Local Government have continued to decline as a share of GDP over the past 20 years and currently represent around only 0.4% of GDP. Financial Assistance Grants are currently being maintained in real terms per capita with no foreseeable prospect of an increase. The current Commonwealth Government is more likely to argue that State Governments should meet the additional needs of Local Government, particularly considering the revised Commonwealth/State funding arrangements since the introduction of the GST.

State Government grants to Councils in New South Wales have fallen significantly over the past two decades. Until 1982 the State Government distributed some \$15 million per annum to Council's in general purpose grants through the Local Government Assistance Fund. However this was terminated on the grounds that the Federal Government had accepted responsibility for general purpose assistance.

The level of special purpose grants has also declined, notably in key areas such as roads, water supply and sewerage. Also of concern is that arrangements for pensioner rebates have not been reviewed since 1989, despite the growing cost to Councils resulting from an ageing population. Furthermore, unlike its counterparts in Queensland and Victoria, the NSW Government has not passed on to Councils a share of the National Competition Policy payments it receives from the Commonwealth, even though Local Government reforms are an integral part of the justification for these payments.

The cost of compulsory pensioner rate concessions is placing an increasing strain on Local Government finances and is threatening the level and range of services that Councils are able to provide. While the level of the compulsory concession has remained unchanged since 1989, an ageing population has ensured that the cost has escalated substantially, rising from \$41 million in 1992-93 to over \$75 million in 2000-2001. The cost to larger councils such as Campbelltown is typically in the range of \$1-2 million per annum.

Pensioner rate concessions are in essence a form of welfare payment and given the limited tax base of Local Government, it can be argued that such schemes are more appropriately fully financed by State or Commonwealth Governments.

3. The capacity of local government to meet existing obligations and to take on an enhanced role in developing opportunities at a regional level including opportunities for councils to work with other councils and pool funding to achieve regional outcomes.

Local Government in New South Wales can demonstrate that there have been improvements in management, functions and structures in recent years. But, as part of the public sector Local Government cannot escape the changes in performance and accountability being demanded at the state, national and indeed international levels.

If Local Government is to not just maintain but increase its relevance in the political, economic and social development of the State Councils must work together to recognise the need for improving their performance, to identify the means by which this can be achieved and to take the initiative themselves.

Local Councils and local communities must achieve lasting benefits from current and prospective public sector reforms. The critical issue is to ensure Councils collectively are providing services and facilities which are relevant to users and provided in a cost effective manner.

The expanded range and increased complexity of the tasks required of Local Government means that Councils need to have greater technical expertise to adequately perform. There may also be the opportunity to generate savings through economies of scale and greater utilisation of plant and equipment.

Through resource sharing on a regional basis Councils can improve the efficiency, effectiveness and quality of services and functions. Importantly, they provide the opportunity for Councils to maintain but also to improve service delivery to their communities in response to increasing external pressure resulting from other levels of government and to increasing regulatory, compliance and reporting requirements imposed on them.

Resource sharing can be implemented in a number of ways including:

- Resource sharing through service agreements where Councils as a group agree to allocate functions between themselves – one Council does a function on behalf of the group. Here a Council outsources a function to another Council.
- Resource sharing through a joint enterprise where Councils form a joint business to achieve economies of scale across a functional area of core business.
- Merger/amalgamation where Councils join together voluntarily

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There are other variations of resource sharing through service agreements. These include agency agreements, where one Council performs operations on behalf of other Councils as their agent. As well there could be a range of formal and informal arrangements to jointly fund, operate or provide services and share staff, facilities and assets. Examples of these include the sharing of building inspectors and joint library services.

There are opportunities to rationalise and achieve better utilisation of major operational assets such as plant and equipment, depots, workshops, administration centres and office technology, such as IT systems. Specialised items of plant which may have relatively low utilisation levels can be better utilised.

To achieve a successful outcome from the process of resource sharing it is essential that the process is designed to enable a range of options to be considered and informed decisions made only when the strengths and weaknesses of the options are determined.

4. Local government expenditure and the impact on local government's financial capacity as a result of changes in powers, functions and responsibilities between state and local governments.

Of particular concern to Local Government are the growing financial pressures on Councils resulting from a combination of factors.

- Expanded responsibilities without adequate corresponding access to increased revenues – the problem of unfunded mandates.
- Increased and additional State charges on Councils
- Restrictions on Council revenue raising

Within the constrained financial environment Local Government has had to cope with new and increased responsibilities. The Commonwealth Grants Commission has also acknowledged this fact in its review of the Local government Financial assistance Act. ABS Government Finance Statistics data supports the conclusion clearly demonstrating a shift in the composition and by inference, an expansion in the range of services provided by Local Government over the past 25 years.

In that time there has been a growth in expenditure on human services, with increases in education, welfare and public safety services. There has also been an increase in the relative importance of recreation and culture and housing and community amenities. While not highlighted as a separate category in the Government Finance Statistics, it is also clear that Local Government activities in the areas of the environment and planning have expanded substantially, particularly in recent years. Expenditure on roads remains as a major category and continues to grow in real terms, but has declined as a proportion of overall expenditure.

The growth in responsibilities has largely resulted from:

- Devolution – new responsibilities imposed by other spheres of government
- “Raising the Bar” – where increased standards or complexity of service provision are imposed by other spheres of government or the community itself.
- Cost Shifting – where Local Government agrees to provide a service on behalf of another sphere of government but funding is subsequently reduced or withdrawn with Local Government having to maintain the service because of community expectations or where another sphere of government ceases to provide a service and Local Government is obliged to step in.

- Increasing community expectations

The fact that Local Government has met these increasing responsibilities while subject to severe financial constraints is evidence of a sustained increase in productivity in Local Government over the past 25 years.

Few of the additional responsibilities conferred on Local Government over the past few decades have been matched by adequate, ongoing funding or new sources of revenue.

An excellent example of this is the requirements of the Local government act itself. The requirements to prepare management plans, social plans and state of the environment reports impose a very considerable burden and can divert resources from other community priorities. Similarly the Protection of the Environment Operations Act has greatly expanded Councils roles in environmental regulation. In the area of stormwater Council is now required under the direction of the Environmental Protection Authority to prepare management plans, at significant cost to Council.

Environmental planning and development and building control are another case in point. Again, these are now accepted as essential Local Government activities, but over the years have become very demanding of Council resources. Council's ability to charge application fees and levy developer contributions has been constrained by the State Government at the same time as the complexities of the planning and approvals system have compounded. Private certification of building approvals threatens a significant reduction in Council revenues. Moreover, Councils are now expected to play a much greater role in strategic planning with virtually no financial assistance.

Councils are often encouraged to enter new areas of activity by State and Commonwealth agencies through the provision of short term financial assistance or one-off capital grants. This has been particularly evident in the field of community development and some specific community services such as childrens services and aged care. Responding positively to community wishes Councils have accepted such grants and allocated matching expenditure only to find themselves locked into ongoing commitments when after a few years funding support is withdrawn or substantially reduced.

When funding is denied from Federal and State Governments, representations are made to Local Government to fund the shortfall. This has occurred in relation to education and transport. In particular community expectation is cost shifted to Local Government in areas where Council has no funding streams. The consequences of central agencies promoting expanded functions for Councils in this way should be considered in the broader policy context of Local Government finances.

Local Government is increasingly required to pay substantial charges to State agencies to meet cost of services provided to communities or for other purposes. These have been increasing at rates well above inflation and the rate-pegging limit imposed on Councils. In some cases the charges clearly subsidise agencies basic operating costs, which ought to be a State responsibility.

The levies for landfill disposal of garbage collected under the Waste Minimisation and management Act have increased by nearly 50% in recent years and now amount to some \$60 million per annum. More than half is channelled to State Treasury as general revenue rather than being allocated for waste management and recycling. In effect Councils are collecting a tax for the NSW State Government.

The NSW Fire Brigades levy is now approaching \$50 million per annum and the recent introduction of load based licensing for sewerage operations will cost Councils in New South Wales an extra \$3.7 million per annum once fully implemented.

Insurance premiums are rising dramatically at the present time and indications are that further increases will occur. The HIH collapse, international events and natural disasters have exacerbated insurance premium increases. Councils are facing insurance premium increases of over 100%.

These charges impact heavily on Councils capacity to allocate funds for other purposes, including other priorities of State and Commonwealth governments.

Campbelltown Council together with the NSW Local Government Association have argued that the current system of rate pegging is inefficient and inappropriate as it deprives Councils of the ability to respond to the needs of their respective communities and the increasing demands being placed on Local Government by other spheres of Government. Amendments need to be made that would improve the operation of rate pegging in terms of Council performance, financial capacity to meet obligations and ability to satisfy community needs.

Under the current system of rate pegging, there is evidence that the approved percentage increase frequently does not even match CPI increases. The approved increase for 2001/2002 was 2.8%. Local Government salary increases in the last year were between 4% - 5%. It should be noted that wages and salaries comprise a substantial amount of Local Government operating costs.

Like many developed urban areas Campbelltown is going through a period where a large number of assets (primarily roads, drainage and other major physical infrastructure) are reaching an age and /or a state which requires significant injection of resources. Funding

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substantial repairs or replacement of these ageing assets is becoming a major issue for Councils while trying to manage long-term sustainability and financial performance.

Rate pegging in New South Wales has forced Councils to utilise Financial Assistance Grants as a means to prop-up operational expenditure, which also tends to mask the adequacy of Council's rating revenue base and its coverage in managing core services and asset replacement programs.

5. The scope for achieving a rationalisation of roles and responsibilities between the levels of government, better use of resources and better quality services to local communities.

Currently there is no consistent basis for determining whether a particular function is best carried out by Local Government or a State agency. Nor is there an adequate policy framework to ensure productive working relationships between Councils and State agencies where functions are shared. Coordination amongst State agencies necessary to implement efficient and effective service delivery at the local and regional level is also lacking. From a Local Government and community perspective, the results can be highly unsatisfactory.

Many recent discussions of the future of Local Government focus on the concept of subsidiarity. This has been given particular emphasis in Europe, where it is a key element in both the political underpinning of the European Union and the reintroduction of democracy to Eastern Europe.

Subsidiarity is defined in the European Charter of Local Self Government in the following terms:

Public responsibilities shall generally be exercised, in preference, by those authorities which are closest to the citizen. Allocation of the task to another authority should weigh up the extent and nature of the task and the requirements of efficiency and economy.

This highlights a critical point. Subsidiarity is about achieving the most appropriate distribution of functions amongst different spheres of government. It is a principle which invokes a partnership approach to intergovernmental relations, and can only be applied effectively in a context of mutual respect. Negotiation must be a central element.

In a situation of overlapping roles and responsibilities amongst governments, such as exists in Australia, it is necessary to consider not only the effectiveness of Local Government itself but also the inter-relationships between its activities and those of other agencies operating at a local level. Those inter-relationships have to be managed in a way which is responsive to the particular circumstances and needs of different communities, and which will secure the best possible outcomes between different governments or agencies. The principle of subsidiarity needs to be applied within such a broader intergovernmental framework.

Such concerns underpinned the concept of Integrated Local Area Planning which promoted the potential for rationalisation of some Local, State and Commonwealth Government functions. ILAP identified problems in service delivery associated with poorly defined, overlapping responsibilities; complex and fragmented administrations; ineffective

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intergovernmental consultation; and hence the failure to address appropriately the particular and varying needs of different local areas.

Similar ideas can be seen at work in recent moves in Tasmania for the negotiation of State-Local Government partnership agreements. These involve joint identification by teams of State agency and Council officials of key issues in a local area requiring cooperative action, and then formal agreement amongst the parties concerned on the action to be taken to address priority tasks.

The stated purpose of the agreements is to facilitate the role of Local Government in a strategic way which will in turn, drive their local economies and communities. They are seen as an opportunity to examine service delivery arrangements and jointly identify measures to improve their design and delivery

6. The findings of the Commonwealth Grants Commission Review of the Local Government (Financial Assistance) Act 1995 of June 2001, taking into account the views of interested parties as sought by the Committee.

The Local Government (Financial Assistance) Act 1995 is the principal mechanism through which the Commonwealth attempts to achieve its objectives for Local Government. These objectives include the promotion of fiscal equity and performance improvement in Local Government and the facilitation of Local Government's contribution to national economic, social and environmental performance.

The central theme underpinning the provision of financial assistance grants to Local government has been improving the equity of grant outcomes to councils. That is, as far as practicable, bringing all Councils in a State up to the same fiscal level. The other requirement of the Act, that all Councils receive at least a minimum grant, conflicts directly with this equity objective. This requires State and Territory Grants Commissions to achieve a balance between the equity principle and the certainty of funding to all Local Councils through a minimum grant.

The review of the Act undertaken by the Commonwealth Grants Commission in 2001 has highlighted a number of areas of major concern for Local Government generally. The anomalies that have existed for the past 25 years in the methodology for the distribution of Federal Assistance Grants need to be addressed as a matter of urgency.

- The continual real decline in Financial Assistance Grants to Local Government. The Vertical Fiscal Imbalance between tax powers and expenditure responsibilities of the Commonwealth and Local Government has worsened and will continue to do so.
- Horizontal Fiscal Equalisation is a primary objective of the Act. Sufficient funds need to be provided to achieve this objective and urgent consideration should be given to increasing the total pool of funding.
- The present formula of 30% of distribution of Federal Assistance Grants based on population is inequitable as it does not recognise efficiency, self sustainability and does not follow the philosophy of effective income tax redistribution