



## **Appendix F: Local Government Financial Assistance Grants<sup>1</sup>**

The Commonwealth has been providing untied financial assistance to local government since 1974-75. Until the Territories achieved self-government, these grants did not cover the ACT or the Northern Territory. Grants for local government bodies in the Northern Territory began in 1979-80 and a grant to the ACT for municipal purposes began in 1988-89. Local roads grants were added to the financial assistance grants in 1991-92.

In 2002-03, it is estimated that the Federal Government will provide \$1.449 billion nationally – equivalent to about \$74 per capita – in financial assistance to local government.

These financial assistance grants are paid as tied grants through the States and have two components – general purpose grants and identified local road grants.

The objective of general purpose assistance from the Federal Government to local government is to strengthen local government to enable it to provide a wider range of services and to promote equity between councils and certainty of funding. These grants are untied in the hands of the receiving council. This means that councils are able to spend the grant according to the priorities of their communities.

The general purpose grants commenced in 1974-75 with allocations in the 1974 and 1975 Budgets distributed according to Commonwealth Grants Commission recommendations. This was followed, over the next two decades, by development in legislative arrangements for providing financial

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<sup>1</sup> Extract from DOTARS Submission No. 103, Appendix 2, pp. 73-82.

assistance to local government. In mid-1984 the Federal Government commissioned an Inquiry into local government (the Self Inquiry) which reported in October 1985. The Self Inquiry led to the *Local Government (Financial Assistance) Act 1986*. From July 1991, as a result of a decision at the 1990 Special Premiers' Conference, local roads grants to local government were provided under the 1986 Act (as amended). These grants are intended to help councils with the cost of maintaining their local roads but, as they are also untied, councils are not required to spend them on local roads.

The 1986 Act was reviewed in 1994 and the *Local Government (Financial Assistance) Act 1995*, under which grants are currently provided, came into effect from July 1995.

In 2000–01, the Commonwealth Grants Commission (CGC) undertook a review of the operation of the 1995 Act.

A more detailed history of Commonwealth untied financial assistance to local government is found in Chapter 6 of the CGC Review Working Papers.

## Objects of the Act

Section 3 of the Act explains the objects of the Parliament in enacting the *Local Government (Financial Assistance) Act 1995*:

(2) The Parliament wishes to provide financial assistance to the States for the purposes of improving:

- The financial capacity of local governing bodies;
- The capacity of local governing bodies to provide their residents with an equitable level of services;
- The certainty of funding for local governing bodies;
- The efficiency and effectiveness of local governing bodies; and
- The provision by local governing bodies of services to Aboriginal and Torres Strait Islander communities.

## Overview of Current Arrangements

In determining the distribution of grants to councils, the current arrangements are:

At the beginning of each financial year, the Federal Government determines the quantum of general purpose and local roads grants estimated to be available for local government nationally. This is equal to the quantum of the grants received nationally in the previous financial year adjusted by an estimated escalation factor.

The estimated quantum of general purpose and local roads grants for each State is then calculated according to requirements of the *Local Government (Financial Assistance) Act 1995* and these amounts are advised to States.

Local government grants commissions in each State determine the allocation of general purpose and local roads grants among local governing bodies in their State.

The Local Government Grants Commission recommendations are then sent, by the State Minister, to the Federal Minister for approval.

Once these grants have been approved by the Federal Minister, quarterly payments are made by the Federal Government to the States and, without undue delay, these are passed on by the States to local governing bodies as untied grants.

Toward the end of the financial year, the escalation factor is revised and the final quantum of the grants for the financial year is recalculated.

An adjustment to the allocations to local governing bodies is made and their payments in the following year adjusted.

#### Determining the Quantum of the Grant

Section 8 of the Act specifies the formula to be applied by the Federal Treasurer each year to determine the increase in the level of local government financial assistance grants. Up to and including 1999–2000, the annual increase in local government grants was based on the increase in financial assistance grants and special revenue assistance to the States.

From 1994–95 to 30 June 2000, the grants were increased annually in line with population and consumer price index movements (N.B. in 1997–98, local government grants were increased for inflation, but not population growth).

Following the introduction of the new tax system in July 2000, increases in financial assistance grants to the states are no longer related to the consumer price index and population. This link was abolished from 1 July 2000 under the terms of the *Intergovernmental Agreement on the Reform of Commonwealth–State Financial Relations*. The States now receive the goods and services tax (GST) revenue.

In June 2000, the *Local Government (Financial Assistance) Act 1995* was amended to remove the nexus between movements in the local government financial assistance grants and States' financial assistance grants. The escalation factor for local government financial assistance is now on a real per capita basis similar to that previously operating for the State grants.

The amendments provided the Treasurer with discretion to increase or decrease the escalation factor in special circumstances. In applying his or her discretion, the Treasurer is required to have regard to the objects of the Act and any other matters he or she thinks relevant. The same escalation factor is applied to both the general purpose and local roads components of the grant.

#### **Determining Actual State Entitlements and Estimated Entitlements**

For each State and for both components of the grants, actual entitlements for the previous year and estimated entitlements for the forward year are calculated using the respective final factor and estimated factor, which are determined in accordance with the Act.

#### **Calculation of Grants**

Each year, the quantum of the grant to local government is determined at the start of the financial year, using a formula based on estimates of the consumer price index and population increases for the year. Councils are usually advised in August of the grant to be paid that financial year.

At the end of each year the estimated grant for local government is adjusted to an 'actual' entitlement, calculated using the actual consumer price index and population figures. Inevitably there is a difference between the estimated and actual grant entitlements. This difference is added to or subtracted from the grant paid to the State in the following year. Therefore for each year there is an estimated grant entitlement, an actual grant entitlement and an actual grant paid.

#### **Interstate Distribution**

Table A 2.1 shows the allocation of funds amongst the States for 2002–03. The Act specifies that the national allocation of the general purpose component of the grant is to be divided amongst the States on a per capita basis. This uses the Australian Bureau of Statistics' estimate of each State's population and the estimated population of all States as at 31 December of the previous year.

In contrast, the State shares of the local roads component of the grant are fixed. The distribution is determined on the basis of shares inherited from the former, tied grant arrangements. Therefore, each State's share of the local roads component is obtained by multiplying the previous year's funding by the escalation factor determined by the Treasurer.

**Table A 2.1: General Purpose and Local Roads Grants, Allocation amongst States, 2002–03**

State	General Purpose Grant			Local Roads Grant			Total Grant		
	\$m	% of total	\$ per capita	\$m	% of total	\$ per capita	\$m	% of total	\$ per capita
NSW	340.2	33.89	51.21	129.2	29.01	19.45	469.4	32.39	70.66
Vic	248.6	24.76	51.21	91.8	20.62	18.92	340.4	23.49	70.12
Qld	188.0	18.73	51.21	83.4	18.74	22.73	271.4	18.73	73.94
WA	98.3	9.79	51.21	68.1	15.29	35.49	166.4	11.48	86.70
SA	77.8	7.75	51.21	24.5	5.50	16.11	102.3	7.06	67.32
Tas	24.2	2.41	51.21	23.6	5.30	49.87	47.8	3.30	101.08
NT	10.2	1.02	51.21	10.4	2.34	52.20	20.7	1.43	103.41
ACT	16.5	1.65	51.21	14.3	3.21	44.26	30.8	2.13	95.47
<b>Total<sup>a</sup></b>	<b>1003.7</b>	<b>100.00</b>	<b>51.21</b>	<b>445.4</b>	<b>100.00</b>	<b>22.72</b>	<b>1,449.1</b>	<b>100.00</b>	<b>73.93</b>

<sup>a</sup> all variations due to rounding adjustments.

The interstate distribution of local government financial assistance grants has been a contentious issue between States for some time.

### Principles for Determining Distribution of Grants within States

The 1995 Act requires National Principles to be formulated in consultation with State Ministers and a body or bodies representative of local government. The National Principles came into effect from 1996–97 and apply to both grant components. The National Principles applying to the general purpose component provide additional criteria to the objectives of full horizontal equalisation and the minimum grant which are established in the Act.

#### *The Horizontal Equalisation Principle*

The Commonwealth pursues a policy of horizontal equalisation when it distributes general purpose funding for State Governments. Horizontal equalisation would be achieved if every council in a State, by means of reasonable revenue-raising effort, were able to afford to provide a similar range and quality of services. Horizontal equalisation within States aims to bring all councils in that State up to the same fiscal level.

More formally, section 6(3) of the Act defines horizontal equalisation as being an allocation of funds that:

- a) ensures each local governing body in a State is able to function, by reasonable effort, at a standard not lower than the average standard of other local governing bodies in the State; and
- b) takes account of differences in the expenditure required to be incurred by local governing bodies in the performance of their functions and in their capacity to raise revenue.

Horizontal equalisation distribution of grants is determined by estimating the cost each council would incur in providing a normal range and standard of services, and by also estimating the revenue each council could obtain through the normal range and standard of rates and charges. The grant is then allocated to compensate for these variations in expenditure and revenue and (ideally) bring all councils up to the same level of financial capacity.

This means councils that would incur higher costs in providing normal services, for example, in remote areas (where transport costs are higher), or areas with a higher proportion of elderly or pre-school aged people (where there will be more demand for specific services) will receive additional grant monies. Similarly, councils with a strong rate base (highly valued residential properties, high proportion of industrial and/or commercial property) will tend to receive less grant monies.

For the general purpose grant, the most important Principle is that the grants are distributed so as to contribute to achieving horizontal equalisation. Horizontal equalisation is achieved if each council in a State is able to provide the average range, level and quality of services by reasonable effort, taking account of differences in their capacities to raise revenue and in their expenditure needed to provide average services.

#### *The Minimum Grant Principle*

The Minimum Grant Principle ensures that each council receives at least a minimum level of general purpose assistance as required by the Act. This minimum is set at 30 per cent of a council's per capita share of general purpose grants.

Section 6(2)(b) of the Act requires the Minister to ensure that:

No local governing body in a State will be allocated an amount under section 9 (the general purpose component of the grant) in a year that is less than the amount that would be allocated to the body if 30 per cent of the amount to which the State is entitled under that section in

respect of the year were allocated among local governing bodies in the State on a per capita basis.

#### *The Effort Neutrality Principle*

The Effort Neutrality Principle requires that a council's grant be independent of its policies. This means the grant to a particular council is not influenced by that council's actual rates charged, its actual expenditure on particular functions or the extent of its reserves or debt. This process allows a council to decide its own spending priorities and revenue-raising policies without The Other Grant Support Principle

The Other Grant Support Principle requires other grants provided to a council by another sphere of Government to be regarded like any other source of revenue and taken into account when assessing the overall financial capacity of each council. In the assessment of each council's financial capacity, local roads grants provided under this Act should be included as well as any other grants that relate to the provision of local government services that are within the scope of services covered by the grant allocation process.

#### *The Aboriginal Peoples and Torres Strait Islanders Principle*

The Aboriginal Peoples and Torres Strait Islanders Principle seeks to address the specific needs of Aboriginal and Torres Strait Islander peoples in the provision of council services. The Principle requires that the level of grants received by councils should reflect the Aboriginal and Torres Strait Islander population within council boundaries. This means that calculation of the grant for councils should reflect differences in the demand for services by Indigenous people, the cost of providing services to them and the capacity to raise revenue from them.

#### *The Roads Principle*

There is one National Principle applying to the Identified Road Component. It requires distribution of this component on the basis of road expenditure needs, including consideration of factors such as length, type and use of roads.

#### **Transitional Modifications**

Section 26 of the Act allows the Federal Minister to approve transitional modifications of the National Principles for individual States for specified years. Queensland, Victoria and Tasmania requested, and were granted, such modifications which allowed phased introduction of changes resulting from implementing the National Principles. Queensland has been granted transitional modifications each year since the 1996–97 grant year.

### Determining the Distribution of Grants within States

Local government grants commissions, established within each State and the Northern Territory (not the Australian Capital Territory), determine individual council allocations in accordance with the National Principles. In the Australian Capital Territory, local government is integrated with the Territory government and there is no role for a Commission.

Local government grants commissions are State authorities required by the Federal Government under the *Local Government (Financial Assistance) Act 1995* as a condition of the State receiving local government financial assistance grants. The State provides the resources for the grants commission.

### Local Government Grants Commissions

Section 6 of the Act specifies the criteria a body must satisfy to be eligible to be recognised as a Local Government Grants Commission for a State. These criteria are:

- The body is established by a law of the State;
- The principal function of the body is to make recommendations to the State Government about the provision of financial assistance to local governing bodies in the State; and
- The Commonwealth Minister is satisfied that the body includes at least two people who are or have been associated with local government in the State, whether as members of a local governing body or otherwise.

Sections 11 and 14 of the Act require local government grants commissions to:

- Hold public meetings in connection with the recommendations;
- Permit local governing bodies to make submissions to the Commission in relation to the recommendations; and
- Make their recommendations in accordance with the National Principles and any agreed State-specific principles.

After the local government grants commission has determined the grant distribution, the State Minister recommends the allocation to the Commonwealth Minister for approval. One of the conditions for approval is that the Commonwealth Minister is satisfied the State has adopted the recommendations of its Grants Commission.

The Commonwealth pays grants to each State Governments as a tied grant to be passed on to councils in accordance with the approved distribution.



Although a tied grant to the States, the grants are untied in the hands of local government, to give councils discretion regarding local priorities.

Section 15 of the Act requires, as a condition on the payment to local government from the States, that they are paid by the State without undue delay and without conditions. Further, each State Treasurer must give the Federal Minister, as soon as practicable after 30 June each year, a statement detailing payments made to councils during the previous financial year as well as the date the payments were made. The State Auditor-General must certify the statement.

The grants are paid to the States in equal instalments in the middle of each quarter. The first payment for a financial year is paid as soon as statutory conditions are met. One of the requirements of the Act is that the first payment can not be made before 15 August.

### Bodies Eligible to Receive Financial Assistance Grants

Only local governing bodies are entitled to receive financial assistance grants. All councils constituted under State local government Acts are automatically local governing bodies. In addition, Section 4(2) of the Act provides for 'a body declared by the Minister, on the advice of the relevant State Minister, by notice published in the Gazette, to be a local governing body for the purposes of this Act'.

In total, 723 councils will receive grants in 2002–03. Included in this figure are 39 declared local governing bodies made eligible under this provision. Table A 2.2 shows the distribution of declared bodies by State.

**Table A 2.2: Distribution of Local Governing Bodies by Type by State at June 2002**

Type	NSW	Vic	Qld	WA	SA	Tas	NT <sup>2</sup>	Total
Councils established by legislation <sup>1</sup>	173	78	157	142	68	29	37	<b>684</b>
Declared	2	1	0	0	6	0	30	<b>39</b>
<b>Total</b>	<b>175</b>	<b>79</b>	<b>157</b>	<b>142</b>	<b>74</b>	<b>29</b>	<b>67</b>	<b>723</b>

Notes:

- 1 Local governing bodies eligible under section 4(2) of the Act as they are constituted under State local government Acts.
- 2 includes Northern Territory Road Trust Fund

### Local Government Grants Commissions Methods

The State Grants Commissions are required to determine the distribution of grants in accordance with the National Principles and to take into account local circumstances.

To determine the allocation of general purpose grants within a State, the respective Grants Commission assesses the amount each council would need to be able to provide a standard range and quality of services, while raising revenue from a standard range of rates and other income sources. The Commission then develops recommendations for grant distribution by allocating the available grant to councils taking account of their assessed grant need, and the minimum grant requirement. Distribution of the local roads component is determined based on assessments of councils' road expenditure need.

These are difficult tasks, requiring considerable experience and judgement. Grants Commissions need to accurately and quantitatively assess the unique circumstances of a large number of councils in their jurisdictions in terms of providing a variety of services and raising a number of revenues.

Grants Commissions use a variety of assessment methods to quantify a council's level of advantage or disadvantage across each area of expenditure and revenue. A detailed description of the methods used by each grants commission is contained in the Commonwealth's National Report, Appendix B. The Commissions also publish information about their methods in annual reports and occasional publications.

### National Grant Allocation

The level of general purpose grants since the Commonwealth commenced general purpose assistance to local government in 1974–75 together with untied local road grants since 1991–92 is detailed in Table A 2.3.

**Table A 2.3: National Financial Assistance Grant Allocation, 1974–75 to 2002–03 (\$)**

Year	General purpose	Local roads	Total
1974–75	56,345,000	n/a	56,345,000
1975–76	79,978,000	n/a	79,978,000
1976–77	140,070,131	n/a	140,070,131
1977–78	165,327,608	n/a	165,327,608
1978–79	179,426,870	n/a	179,426,870
1979–80 <sup>1</sup>	222,801,191	n/a	222,801,191
1980–81	302,226,347	n/a	302,226,347

1981–82	352,544,573	n/a	352,544,573
1982–83	426,518,330	n/a	426,518,330
1983–84	461,531,180	n/a	461,531,180
1984–85	488,831,365	n/a	488,831,365
1985–86	538,532,042	n/a	538,532,042
1986–87	590,427,808	n/a	590,427,808
1987–88	636,717,377	n/a	636,717,377
1988–89	652,500,000	n/a	652,500,000
1989–90	677,739,860	n/a	677,739,860
1990–91	699,291,988	n/a	699,291,988
1991–92 <sup>2</sup>	714,969,488	303,174,734	1,018,144,222
1992–93 <sup>3</sup>	730,122,049	318,971,350	1,049,093,399
1993–94	737,203,496	322,065,373	1,059,268,869
1994–95	756,446,019	330,471,283	1,086,917,302
1995–96 <sup>4</sup>	806,748,051	357,977,851	1,164,725,902
1996–97	833,693,434	369,934,312	1,203,627,746
1997–98	832,859,742	369,564,377	1,202,424,119
1998–99	854,180,951	379,025,226	1,233,206,177
1999–2000	880,575,142	390,737,104	1,271,312,246
2000–01	919,848,793	408,163,979	1,328,012,772
2001–02	965,841,233	428,572,178	1,394,413,411
2002–03 <sup>5</sup>	1,003,702,209	445,372,208	1,449,074,417

## Notes:

- 1 Grants to the Northern Territory under the Act commenced in 1979–80, the initial allocation being \$1,061,733.
- 2 Prior to 1991–92 local roads grants were provided as tied grants under a different Act.
- 3 In 1992–93 part of the local roads grant entitlement of the Tasmanian and Northern Territory Governments was reallocated to local government in the respective State.
- 4 Grants to the Australian Capital Territory under the Act commenced in 1995–96, the initial allocation being general purpose (\$13,572,165) and local roads (\$11,478,714).
- 5 For 2002–03 the national grant allocation is the estimated entitlement.

The grant entitlements for States from 1998–99 to 2002–03 are provided in Table A 2.4.

**Table A 2.4: Grant Entitlements for all States by Type of Grant, 1998–99 to 2002–03 (\$m)**

State	Type of Grant	1998–99	1999–00	2000–01	2001–02	2002–03
NSW	GP	289,122,909	297,893,674	310,670,281	327,747,092	340,161,401
	LR	109,967,111	113,365,094	118,421,178	124,342,237	129,216,452
	Total	399,090,020	411,258,768	429,091,459	452,089,328	469,377,853
Vic	GP	212,348,975	218,827,409	228,730,976	239,054,282	248,565,220
	LR	78,141,293	80,555,859	84,148,650	88,356,082	91,819,641
	Total	290,490,268	299,383,268	312,879,626	327,410,365	340,384,861
Qld	GP	157,152,792	162,692,473	170,764,707	179,769,293	187,952,916
	LR	71,015,440	73,209,818	76,474,975	80,298,724	83,446,434
	Total	228,168,232	235,902,291	247,239,682	260,068,017	271,399,350
WA	GP	83,128,999	86,223,641	90,349,594	94,473,299	98,256,102
	LR	57,953,514	59,744,277	62,408,872	65,529,316	68,098,065
	Total	141,082,513	145,967,918	152,758,466	160,002,614	166,354,167
SA	GP	68,005,311	69,591,120	72,250,229	75,398,572	77,776,866
	LR	20,830,002	21,473,649	22,431,374	23,552,943	24,476,218
	Total	88,835,313	91,064,769	94,681,603	98,951,515	102,253,084
Tas	GP	21,683,676	22,002,166	22,731,964	23,564,215	24,233,779
	LR	20,085,659	20,706,306	21,629,807	22,711,297	23,601,580
	Total	41,769,335	42,708,472	44,361,771	46,275,512	47,835,359
NT	GP	8,636,642	8,938,475	9,382,393	9,903,259	10,234,625
	LR	8,878,600	9,152,948	9,561,170	10,039,228	10,432,766
	Total	17,515,242	18,091,423	18,943,563	19,942,487	20,667,391
ACT	GP	14,101,647	14,406,184	14,968,649	15,931,221	16,521,300
	LR	12,153,607	12,529,153	13,087,954	13,742,351	14,281,052
	Total	26,255,254	26,935,337	28,056,603	29,673,572	30,802,352
National total	GP	854,180,951	880,575,142	919,848,793	965,841,233	1,003,702,209
	LR	379,025,226	390,737,104	408,163,979	428,572,178	445,372,208
Total		1,233,206,177	1,271,312,246	1,328,012,773	1,394,413,411	1,449,074,417

Notes: all years are actual entitlement except 2002–03 which is an estimated entitlement. All variations are due to rounding adjustments.

GP = General Purpose

LR = Local Roads