



**South Australian
Local Government Grants Commission**

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Mr David Hawker MP
Chair
Standing Committee on Economics, Finance
and Public Administration
House of Representatives
Parliament House
CANBERRA ACT 2600

Dear Mr Hawker

The South Australian Local Government Grants Commission submits the attached submission in relation to the *Commonwealth Inquiry Into Local Government and Cost Shifting*.

Yours sincerely

Malcolm Germein
CHAIRMAN

This submission is part of a joint presentation by the New South Wales, Victorian and South Australian Local Government Grants Commissions (LGGC) and supports the written response from the Victorian LGGC.

The SA Local Government Grants Commission strongly supports the Victorian Local Government Grants Commission's written response to the inquiries discussion paper "AT THE CROSSROADS".

The main issues commented on by the Victorian Commission included:-

- The central distribution of the grant funds.
- A perceived lack of understanding by the committee of the grant process.
- The suggested alternative methodology for determining Councils grants.
- The value to Councils of the grants remaining untied.
- Local Governments concern that the quantum of funds cannot achieve the objectives of the financial assistance program.

The SA Commission supports the views expressed in the Victoria discussion paper and we thank the committee for the opportunity to add our own comments.

These comments will concentrate on 4 issues:

1. The appropriateness of the current Horizontal Fiscal Equalization (HFE) principals and how they are interpreted
2. The suggested central distribution compared to the current situation
3. The value to good local governance of the untied nature of the grants.
4. The concern expressed by some at the perceived difference in grant outcome for similar Councils in different States.

1. HFE and why we interpret it as we do.

The principal of **Horizontal Fiscal Equalisation** (HFE) has been the foundation principal of the program since its introduction in the 1970's. This distribution principal is recognised internationally as being a fundamental principal to apply to any needs based grant program, which is designed to give assistance to an individual or organisation, which is disadvantaged compared to others and to measure the level of that disadvantage.

The discussion paper doesn't question the validity of using the **HFE** principal as the main driver in the **General Purpose Grants** and so we assume the committee accepts it should continue as the driver of the grant process.

The State based Commissions have taken their lead in developing their methodologies from the pre-eminent authority on **HFE** methodologies the Commonwealth Grants Commission. This Commission, a Commonwealth authority, is recognised world wide as a leader in the equitable distribution of

funds using this principal and has been of considerable assistance to the SA LGGC as we have refined our methodology over time.

The Victorian submission gives some detail of how the methodology works in practice. All States use a similar methodology.

As part of the SA Commissions process of review and refinement of our methodology we recently conducted a major review of the way we measure Councils capacity to raise revenue. As part of that review we investigated the appropriateness of including measures of community wealth (capacity to pay) not currently used by us. Among the alternatives considered we investigated the ABS SEIFA index.

This is an index produced by the ABS after the 1986, 1991, and 1996 Censuses and is a set of five Socio-Economic Indexes based on Census data that measures different aspects of socio-economic conditions by geographic areas.

Section 3.44 of your "At the Crossroads" discussion paper suggests: -
 "Other equalization formula based on evidence of needs could also be considered, for example, the SES model used by the Department of Education, Science and Training to fund the non-government school sector."

We understand this formula is derived from elements of the ABS SEIFA index.

Our investigations lead us to conclude that there are considerable problems with using this index to measure Councils capacity to raise revenue.

These problems include: -

- These indexes only provide **ordinal measures** and not **interval measures** of the socio-economic relationship between areas. That is the indexes only rank areas in order from least to most disadvantaged and gives no measure of the relative difference between areas.
- These measures are only a snapshot of the situation at the time the Census was taken and is not updated until the next 5 year Census. Given that the results from the 2001 Census will not become available until later this year the current index is derived from information that is seven years old.

The SA LGGC will look at the new SEIFA index when it is released later this year and further consider its suitability then. However it is clear that at best it will only have limited application in accessing Councils ability to raise revenue but has no application in measuring Councils expenditure needs.

2. Direct Distribution by the Federal Government.

This matter is well covered in the Victoria Commission submission and we support their comments.

The assumption by your Discussion Paper in paragraph 4.8, that central distribution can lead to a simpler distribution formula and therefore reduced administrative and compliance costs needs further investigation before it is accepted.

The diversity of functional responsibility and geographic location of incorporated Councils across Australia is acknowledged in the report and was recognised by the Deputy Chair Ms Anne Burke MP in her comment to the Annual Conference of the Local Government Managers Association in Adelaide recently.

Added to that is the need to access assistance levels to local government type bodies in unincorporated areas.

These communities' organisational structures and funding arrangements are extremely diverse and cannot be adequately reflected in a distribution formula. The funding committee needs to have a direct knowledge of these communities to make an appropriate judgment of what is an equitable level of funding for them.

This requires regular contact with and visits to the communities.

We believe a central body would find it impossible to adequately reflect this diversity in individual Local Governments and their service delivery responsibilities across Australia.

3. The importance of untied grants.

The discussion paper discusses the significant shortfall in funds, which Local Government in particular, is experiencing as it relates to infrastructure provision. There is no doubt that there are urgent projects needing Council attention and funding as there are for both the Federal and State Governments.

However Councils constantly impress on my Commission the vital importance to them of the untied nature of the **General Purpose Grants (GPG)**.

My Commission is convinced that the loss of the discretion to reflect local community priorities in the expenditure of the **GPG** by Councils would be a major weakening of the local democratic authority of Councils and should be avoided.

The significant differences in Council circumstances and needs simply cannot be adequately reflected if the grants are tied to some other priorities. This

applies particularly to regional and remote communities whose needs are often specific to their own situation.

The **Identified Local Road Funds**, although technically untied, are generally assumed to be for roads and are accepted as being for that purpose. These funds were tied to road expenditure until 1991 when the State LGGC's were given responsibility to distribute these funds.

In SA a significant part of the success of this program stems from its being applied in a way that enables the SA LGGC to make recommendations on the allocation of a **special local roads component**, to secure regional coordination in relation to roads of regional significance.

A similar component of the Road to Recovery program is applied in a similar way to regional priorities.

The particular SA arrangements for these funds has enabled the State and Local Government sectors to foster a coordinated strategic approach to using the road funds in the most efficient and effective way.

4. Perceived difference in grant outcome.

The perceived difference of grant outcome for Councils particularly across State borders has been discussed for as long as the program has existed. The Commonwealth has attempted to address this issue in recent years by the introduction of the National Report and by insisting State LGGC's methodologies are more consistent.

However as the discussion paper recognises, paragraph 3.43 to 3.48 and question 11 & 12, the issue of the current interstate distribution of both the general-purpose pool and the local roads component is the major cause of the inequity in grant outcome for similar Councils in different States. The report suggests that while the grants go to the States for distribution to Councils, it will be very difficult to change this situation.

This has proven to be the case now for 30 years.

We believe this lack of equity in the interstate distribution is a major failing of the current program and does demand to be resolved by this inquiry.

The discussion paper, paragraph 3.34, discusses the possibility of the Commonwealth Grants Commission being involved in determining the interstate distribution of the **General-Purpose** funds. This suggestion has considerable merit in our view and should receive further consideration by the inquiry.

We suggest two alternatives for the involvement of the Commonwealth Grants Commission in determining the interstate distribution of the general-purpose grants: -

1. Using the relativities established for distribution of the GST to the States. This has limited direct relationship to Local Governments revenue and expenditure needs and may not properly reflect the needs of Local government within each State.
2. Asking the Commonwealth Grants Commission to develop a formula, which reflects the differences between Local Government in each State, for the interstate distribution of the general-purpose funds.

The Commonwealth Grants Commission, due to the work previously done by them in this area is well placed to do this.

The interstate distribution of the road element also demands review. The current inequities in interstate distribution are recognised and partially corrected in the distribution of the Road to Recovery Program.

The committee as a matter of urgency should investigate a new road needs formula. Advice could be sought from either the Commonwealth Grants Commission or the Dept of Transport to assist your committee with this.

We suggest your committee commission work on a more equitable interstate distribution of both the general purpose and the road elements of the program to be done by the Commonwealth Grants Commission in conjunction with the Dept of Transport

This would give your committee sound information to assist in making an informed judgment on the effect of any changes to the current arrangements.

The current State based LGGC's should remain to assist in recommending distribution within each State boundary. They could do this as an agent of the CGC funded by the Commonwealth or continue as a State funded Commission to acknowledge the responsibility of the States for Local Government within their boundaries.

This would ensure that the local knowledge of the State LGGC's would continue to be available in the grant process. Additionally the regular visits to individual Councils to explain the reason for their grant outcome would continue and could be extended to include assisting Councilors to understand the value to their community of this important Commonwealth Government program.

Thank you again for the opportunity to make a further submission to this inquiry.

Financial Assistance Grants (2003-04)

SA Share = \$105.8 mill (7.03%)



General Purpose Grants

SA Share = \$ 80.4 mill (7.71%)

(based on population share and distributed on HFE principles)

Identified Local Road Grants

SA Share = \$ 25.4 mill (5.5%)

(based on a historical share and distributed on a needs basis)



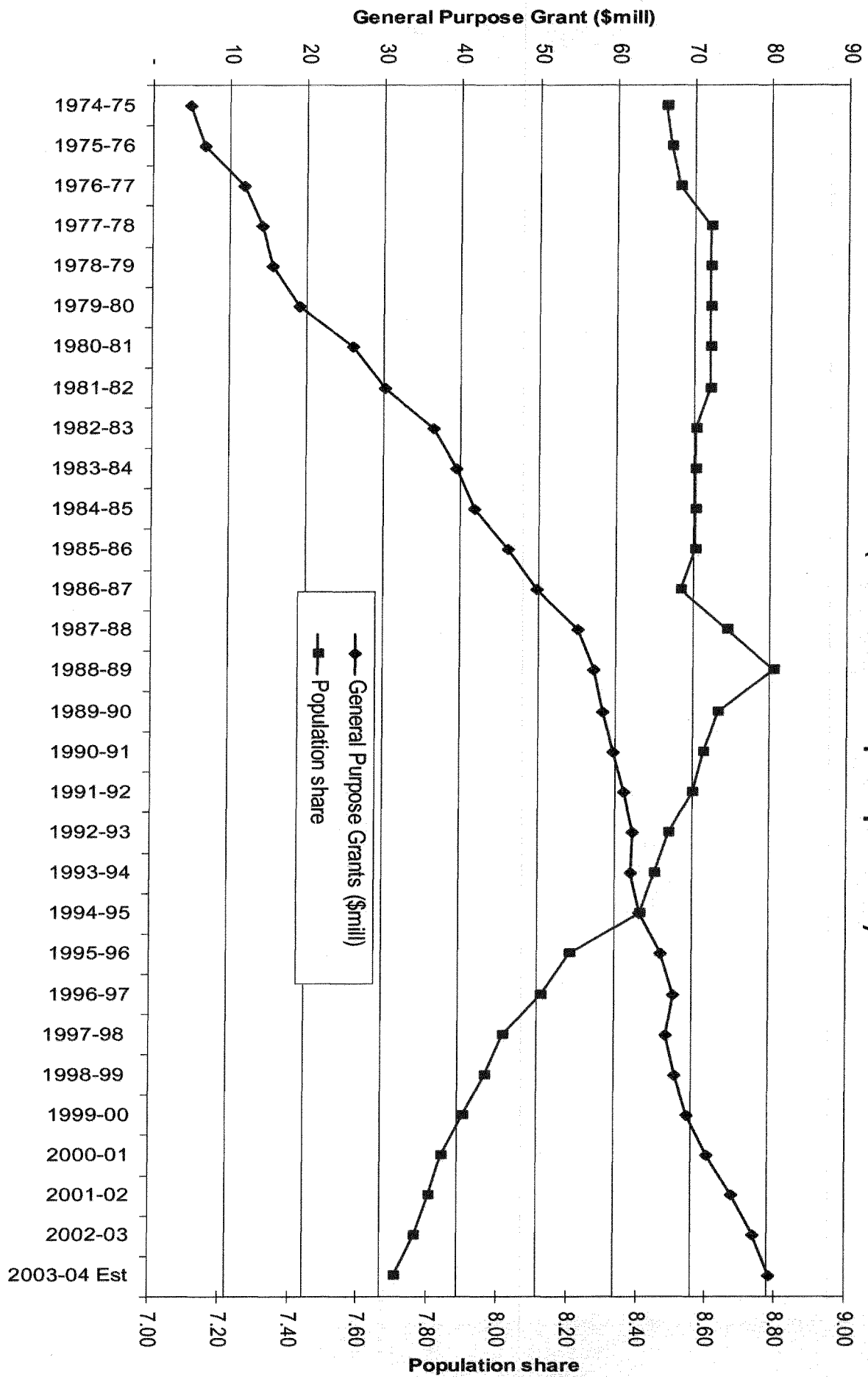
Formula Grants (85%)

= \$21.6 mill

Special Local Road Grants (15%)

= \$ 3.8 mill

South Australia's share of Commonwealth General Purpose Grants over time (1974-75 to 2003-04)
 (distributed on a per capita basis)



**General Purpose Grants
(alternative model)**



Commonwealth Grants Commission
Interstate distribution on principles of
Horizontal Fiscal Equalisation (HFE)



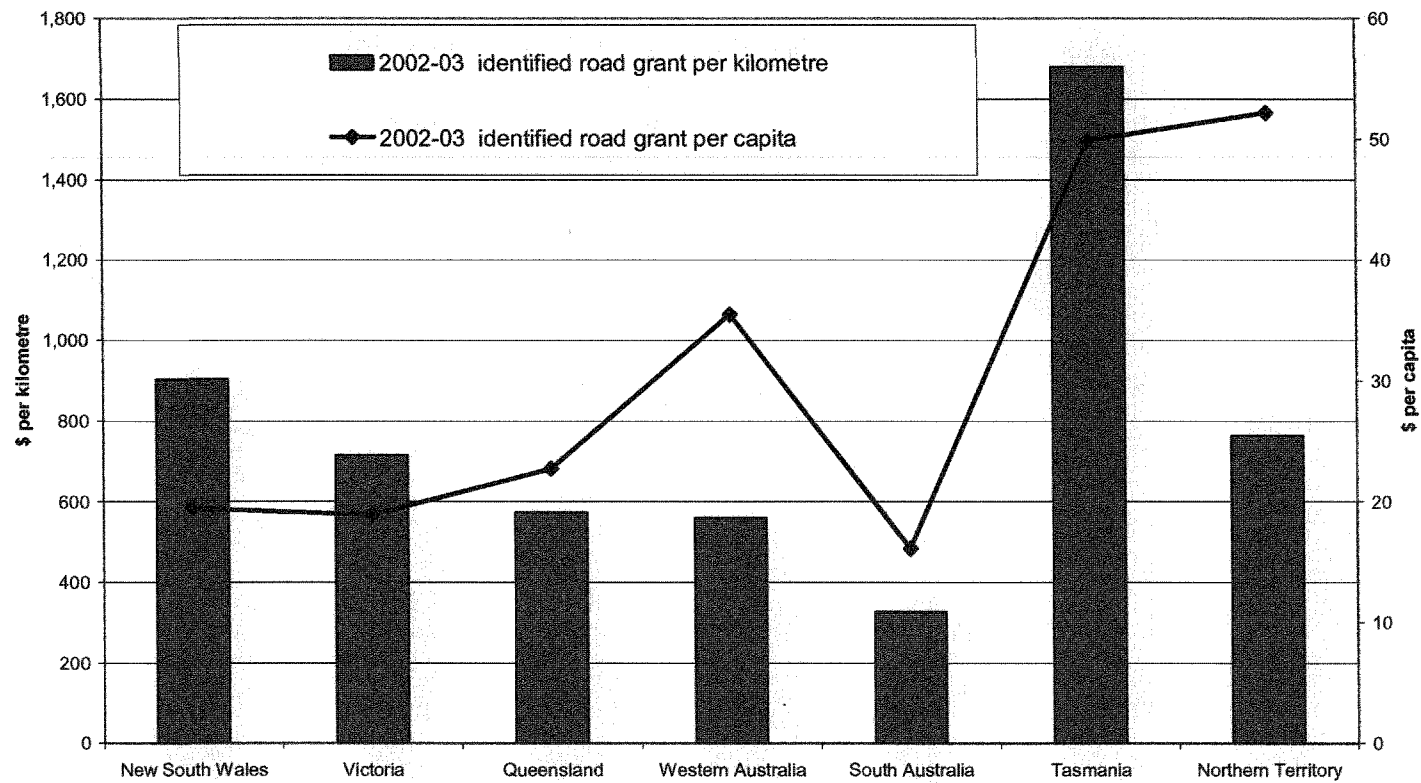
States Grants Commissions
(distribution on HFE principles)



Councils

Commonwealth road funding by State and Territory (excluding ACT)

2002-03 Identified Local Road Grants



**Identified Local Roads Grants
(alternative model)**



**Commonwealth Grants Commission
supported by Department of Transport
Distribution on road needs principles**



**States Grants Commissions
(distribution on roads needs principles and
provision for regional road program)**



Councils

TABLE 1

**Total Commonwealth Financial Assistance Grants for Local Government
Current distribution and on a per capita basis**

State	Current Proportion (%)	2002-03 Actual (\$mill)	Per capita share (%)	Revised Allocation (Estimate) (\$mill)	Difference (\$mill)
New South Wales	32.24	469.83	33.72	489.66	19.83
Victoria	23.60	341.07	24.78	359.82	18.75
Queensland	18.76	272.32	18.95	275.10	2.77
Western Australia	11.53	166.80	9.81	142.51	-24.29
South Australia	7.04	102.59	7.71	111.92	9.33
Tasmania	3.30	47.96	2.40	34.79	-13.17
Northern Territory	1.43	20.63	1.00	14.47	-6.16
Australian Capital Territory	2.10	30.80	1.64	23.74	-7.06
TOTAL	100.00	1,452.00	100.00	1,452.00	0.00

TABLE 2

**Commonwealth General Purpose Financial Assistance Grants
Current distribution (per capita) and on GST principles**

State	Current Proportion (%)	2002-03 Actual (\$mill)	% GST revenue (%)	Revised Allocation (Estimate) (\$mill)	Difference (\$mill)
New South Wales	33.89	340.35	30.50	306.75	-33.60
Victoria	24.76	249.06	21.70	218.24	-30.82
Queensland	18.73	188.71	19.10	192.09	3.39
Western Australia	9.79	98.56	9.60	96.55	-2.01
South Australia	7.75	78.06	9.20	92.53	14.47
Tasmania	2.41	24.31	3.70	37.21	12.90
Northern Territory	1.02	10.18	4.30	43.25	33.07
Australian Capital Territory	1.65	16.49	1.90	19.11	2.61
TOTAL	100.00	1,005.73	100.00	1,005.73	0.00

NB % GST revenue sourced from page 21 "At the Crossroads"

TABLE 3

**Commonwealth Identified Local Road Grants for Local Government
Current distribution (historical) and on equal weighting of road length and population**

State	Current Proportion (%)	2002-03 Actual (\$mill)	Share based on road length and population (%)	Revised Allocation (Estimate) (\$mill)	Difference (\$mill)
New South Wales	29.01	129.48	28.04	125.13	-4.34
Victoria	20.62	92.01	22.35	99.74	7.74
Queensland	18.74	83.62	20.67	92.24	8.63
Western Australia	15.29	68.24	14.33	63.95	-4.28
South Australia	5.50	24.53	9.71	43.33	18.81
Tasmania	5.30	23.65	2.30	10.26	-13.39
Northern Territory	2.34	10.45	1.57	7.01	-3.45
Australian Capital Territory	3.21	14.31	1.03	4.60	-9.71
TOTAL	100.00	446.27	100.00	446.27	0.00

TABLE 4

Total Commonwealth Financial Assistance Grants for Local Government
Distribution based on GST principles for the General Purpose Grants and
on an equal weighting of road length and population for the Identified Local Road Grants

State	Current Proportion (%)	2002-03 Actual (\$mill)	% GST revenue (%)	Revised Allocation (Estimate) (\$mill)	Share based on road length and population (%)	Revised Allocation (Estimate) (\$mill)	Revised proportion (%)	Combined allocation (\$mill)	Difference (\$mill)
New South Wales	32.39	469.83	30.50	306.75	28.04	125.13	29.74	431.88	-37.95
Victoria	23.49	341.07	21.70	218.24	22.35	99.74	21.90	317.99	-23.08
Queensland	18.73	272.32	19.10	192.09	20.67	92.24	19.58	284.34	12.01
Western Australia	11.48	166.80	9.60	96.55	14.33	63.95	11.05	160.50	-6.30
South Australia	7.06	102.59	9.20	92.53	9.71	43.33	9.36	135.86	33.27
Tasmania	3.30	47.96	3.70	37.21	2.30	10.26	3.27	47.48	-0.49
Northern Territory	1.43	20.63	4.30	43.25	1.57	7.01	3.46	50.25	29.62
Australian Capital Territory	2.13	30.80	1.90	19.11	1.03	4.60	1.63	23.71	-7.10
TOTAL	100.00	1,452.00	100.00	1,005.73	100.00	446.27	100.00	1,452.00	0.00