



3/12/2020

RM/20/22314

The Hon Shaun Leane MP
Minister for Local Government
Level 16, 121 Exhibition Street
Melbourne VIC 3000

By email: OfficeMinLeane@ecodev.vic.gov.au

Dear Minister,

Essential Services Commission advice on the rate cap for 2021–22

The Essential Services Commission is responsible for administering the Fair Go Rates system and providing advice to the Minister for Local Government on the average rate cap for councils. On 29 October 2020, you requested the commission's advice on setting the average rate cap for councils for 2021–22, under section 185D(3)(a) of the *Local Government Act 1989* (the Act).

In response to that request, we provide this advice under section 185D(4) of the Act.

We recommend the average rate cap be set equal to 1.50 per cent for 2021–22. Our reasoning is set out in Attachment A. We note that the Department of Treasury and Finance's latest Consumer Price Index (CPI) forecast (November 2020) for 2021–22 is 1.50 per cent.

We also recommend that a uniform cap continue to apply for all councils in 2021–22. We consider that the higher cap application process remains an efficient, transparent, and participative mechanism to deal with the varying financial circumstances of individual councils.

Under the Act, our advice on the rate cap must be provided as a recommendation for any adjustments to the forecast CPI that is published as part of the December Budget Update. As the December Budget Update has not yet been released, we have included a table that shows our recommended adjustments for various potential CPI forecast figures.

For example, if the CPI forecast in the December Budget Update is 1.75 per cent, we recommend an adjustment of negative 0.25 per cent, resulting in the average rate cap of 1.50 per cent. Should the CPI forecast remain at 1.50 per cent, we recommend no adjustment, resulting in the average rate cap of 1.50 per cent.

Adjustment to December Budget Update CPI forecast – rate cap for all 79 councils (%)

December Budget Update CPI forecast	Adjustment to the CPI forecast	Recommended average rate cap
0.75	+ 0.75	1.50
1.00	+ 0.50	1.50
1.25	+ 0.25	1.50
1.50	No adjustment	1.50
1.75	- 0.25	1.50
2.00	- 0.50	1.50
2.25	- 0.75	1.50

A 1.50 per cent rate cap reflects the long-term average of CPI from 2016–17 to 2021–22. We are recommending a specific rate cap in response to the uncertainty created by the coronavirus. In our view, setting the average rate cap at this level will provide stability and balance the needs of ratepayers and the community with the long-term sustainability of councils.

It is important to consider the role the rate cap and financial hardship policies have in addressing the affordability concerns highlighted by the coronavirus. While lower rate caps can decrease the overall rate burden on a community, this must also be balanced against the long-term sustainability of councils. This must be complemented by well-functioning financial hardship policies and programs, which are more effective in targeting the affordability issues that vulnerable ratepayers are facing.

We provide this advice on the rate cap, noting that the Minister for Local Government has the ability to set rate caps that differ from our advice.

This advice will be published on our website following your announcement of the rate cap for 2021–22.

If you have any questions regarding this advice, please do not hesitate to contact Angelina Garces, Senior Regulatory Manager Local Government, on 03 9032 1337.



Kate Symons
Chairperson

Attachment A – rate cap rationale

On 29 October 2020, you requested the commission's advice on setting the average rate cap for councils for 2021–22, under section 185D(3)(a) of the *Local Government Act 1989* (the Act):

- A recommendation for any adjustment(s) to be applied to Consumer Price Index (CPI) in setting the cap for all 79 local councils, a grouping of councils or any individual council.
- The rationale for any such adjustment(s) and the quantum of such adjustment(s).
- Should more than one option be recommended, indicate which is the preferred option.

We are of the view that a rate increase within the range of 1.50 per cent to 2.25 per cent would meet the objectives of the Fair Go Rates system. The range is based on various historical measures of CPI. The lower bound of the range (1.50 per cent) is the rounded average of DTF's published CPI figures from 2017–18 to 2021–22. The upper bound of the range (2.25 per cent) is an average of the rate caps set by the Minister of Local Government since 2016–17.

In our view, this range strikes a balance between the long-term interests of ratepayers and the community with the long-term financial need of councils. If the December Budget Update forecast CPI falls within this range, it is reasonable to set the rate cap to that forecast CPI figure.

However, our preferred approach is for the rate cap to be set at the lower end of the range (1.50 per cent). Given the current uncertainty around economic forecasts, the historical downward trend in actual CPI and increased financial pressure on household budgets, setting the rate cap to the lower end of the range would best reflect a reasonable rate increase for the average ratepayer.

Councils that cannot maintain financial capacity to perform their duties and achieve sustainable outcomes in the delivery of services and infrastructure may choose to apply for a higher cap. We are required to assess higher cap applications in consideration of the legislative matters and generally only approve higher caps when a council can demonstrate a long-term funding need.

A rate cap that is lower than 1.50 per cent may be preferable if the financial constraints on households are a concern. However, a lower rate cap could deepen the financial sustainability issues in the sector which, in the long run, would ultimately be borne on ratepayers and the community. Further, the effect annual revaluations have on individual rate increases means that setting lower average rate increases is not a substitute for well-targeted financial hardship policies and programs.

A maximum average rate increase of 1.50 per cent will provide a safeguard for ratepayers by keeping rate increases at a reasonable level. Councils will maintain the ability to further respond to issues around affordability in their own communities by adopting a lower average rate increase or offering other support (such as rebates or waivers)