

Fair Go Rates system – Applying for a higher cap

Guidance for councils 2021–22

December 2020



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About this document

This document details the requirements for Victorian councils applying for a higher rate cap for the 2021–22 rating year.

The Victorian Government's Fair Go Rates system establishes rate caps to limit the amount by which Victorian councils can increase rates in a year without seeking additional approval.¹ Appendix 1 provides an overview of the commission's role in administering the Fair Go Rates system.

Each year, the Minister for Local Government sets the average rate cap — that is, the maximum percentage increase in councils' average rates for the forthcoming financial year. The minister can set a cap for all councils, a group of councils or a single council. If any council considers the average rate cap increase to be insufficient for its needs, the council can apply to the Essential Services Commission for a higher percentage.

We are publishing this guidance to help councils plan for and make such applications. The Local Government Act 2020 came into operation in March 2020. It sets out new and changed requirements for community engagement, planning, procurement and other matters needed for higher cap applications. These new requirements take effect in stages, at dates up to July 2022; the legislation giving effect to rate capping remains, in Part 8A of the Local Government Act 1989.

To support an application and demonstrate that a higher cap is appropriate, we expect a council to produce records of its planning, financial and asset management, community engagement and so forth. Such activity was probably undertaken, and recorded, in 2020 or earlier to meet requirements of the 1989 Act then in force.

But we also recognise that a council may already have aligned some of its practices with the principles of the Local Government Act 2020, before preparing a higher cap application. Records and material produced in conformity with the new Act can also be used to support an application.

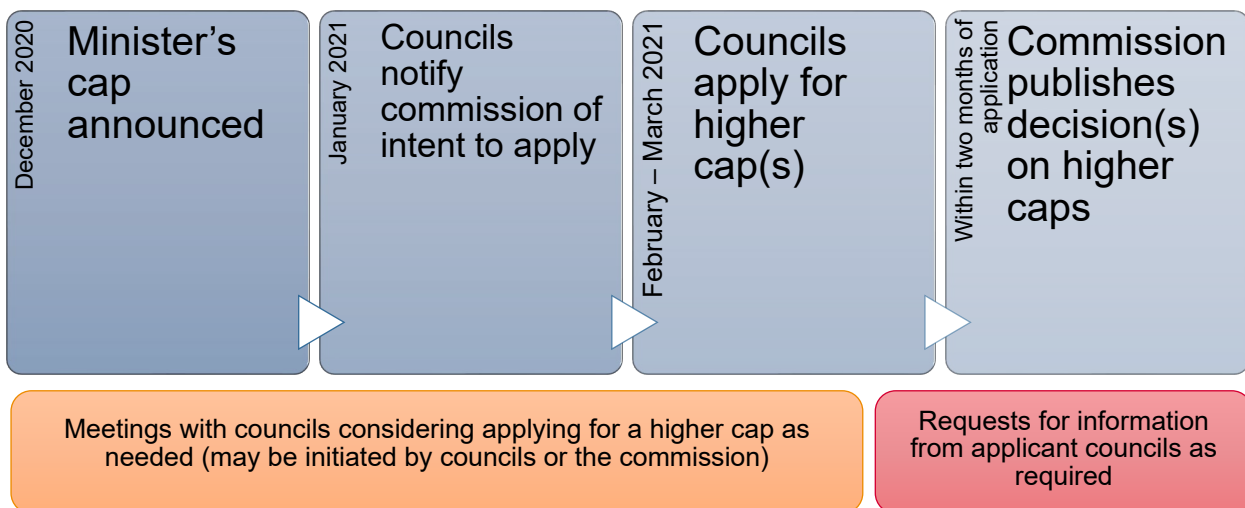
The current version of this guidance document reflects what we have learnt from assessing applications over the first four years, along with feedback from the sector, our technical working groups and ratepayers. The underlying principles and our approach to assessment are unchanged. To make it easier to refer to the guidance, some material may appear in more than one place.

¹ In references to capping in this document, unless otherwise stated, 'rates' should be understood to mean average rates including general rates and municipal charges and any other prescribed rates or charges on rateable properties. Also, see Footnote 3.

This document provides general advice or guidance only.² It aims to help councils understand how commission staff interpret relevant regulatory requirements. By following this advice or guidance, councils may be better able to present the information to support their applications. Separate guidance on councils' compliance and reporting requirements relating to the Fair Go Rates system is also available.³

However, councils should not read this document as a set of fixed rules that would secure the approval of an application in all circumstances. As the Fair Go Rates system matures, or as legislation changes, we will update and refine this guidance as necessary. Readers' feedback on the document will be most welcome and will help us to improve the guidance.

Key dates for the 2021–22 rating year



² This document is issued under s. 11 of the *Essential Service Commission Act 2001* in connection with the commission's functions under s. 10E of that Act and s. 185E(5)(c) of the *Local Government Act 1989*. This document is not intended to be a final statement. The commission may provide further directions, advice and guidance in relation to particular applications or issue guidelines under the *Local Government Act 1989*.

³ See 'Fair Go Rates system – compliance monitoring and reporting, guidance for councils 2020–21', which provides details on how to comply with the average rate cap set by the minister — or any higher cap approved by us — and how to report to us on their compliance. Updated guidance on councils' compliance relating to the 2021–22 rating year will be made available in early 2021 on our website www.esc.vic.gov.au/local-government/guidance-councils#tabs-container2.

Table 1 shows the key dates and timelines for the operation of the Fair Go Rates system for the 2021–22 rating year.

Table 1 Timelines for the 2021–22 rating year

Fair Go Rates system — key dates	Timeframe
Base year	1 July 2020 – 30 June 2021
The minister announces the rate cap	By 31 December 2020 ^a
A council seeking approval for a higher cap notifies the commission of intention to apply	By 31 January 2021
A council sends application for a higher cap, with budget baseline information	1 February – 31 March 2021
The commission assesses council applications	February – May 2021
The commission notifies councils of decisions	Within two months of receipt of application
Capped year	1 July 2021 – 30 June 2022
Councils formally adopt budget no later than	June 2021
All councils send annual compliance information	By 30 September 2021
The commission publishes compliance report	Late 2021

^a Unless an alternative date is determined by the minister and published in the Government Gazette.

Communicating with the commission

The local government team at the commission can be contacted via email: localgovernment@esc.vic.gov.au or telephone: 03 9032 1300 to respond to queries or requests for information.

All councils can expect to receive general information, enquiries and instructions from the commission about complying with the minister’s cap or an approved higher cap or applying for a higher cap.

We ask councils to nominate and maintain a key contact for these communications. We will also copy communications to the chief executive officer and the records area of each council.

1. Our expectations of higher cap applications

Higher cap applications should align with the purposes of the Fair Go Rates system and address the six legislative matters as outlined in the Local Government Act 1989.

The Fair Go Rates system allows Victorian councils to apply to us for higher caps (for up to four years) above the cap set by the minister.

1.1. Purposes of the Fair Go Rates system

An application should demonstrate to us that, by approving it, we will achieve our statutory objective, which is to promote the purposes of the Fair Go Rates system, as set out in Box 1.1.⁴

Box 1.1 The purposes of the Fair Go Rates system

The purposes of this Part are—

- (a) to promote the long-term interests of ratepayers and the community in relation to sustainable outcomes in the delivery of services and critical infrastructure; and
- (b) to ensure that a Council has the financial capacity to perform its duties and functions and exercise its powers.

Source: s. 185A, *Local Government Act 1989*.

1.2. Legislative matters

Section 185E of the 1989 Act sets out six legislative matters that an application must address. These largely reflect or reinforce existing council obligations (under the 1989 Act) to ensure effective planning, budgeting, financial management and community engagement. Compliance with these obligations, or with comparable obligations under the 2020 Act, should ensure councils are efficient and sustainable and provide good value for money to ratepayers for the services that councils deliver. The process for applying for higher caps provides additional independent scrutiny to ensure councils, when levying higher rates on their ratepayers, adhere to those statutory obligations. Box 1.2 sets out these legislative matters.

⁴ Section 10E(7) of the *Essential Services Commission Act 2001* states our objective is to promote these purposes in the *Local Government Act 1989*.

Box 1.2 Six matters an application for a higher cap must specify

An application under this section of the Act must specify —

- (a) a proposed higher cap for each specified financial year; and
- (b) the reasons for which the Council seeks the higher cap; and
- (c) how the views of ratepayers and the community have been taken into account in proposing the higher cap; and
- (d) how the higher cap is an efficient use of Council resources and represents value for money; and
- (e) whether consideration has been given to reprioritising proposed expenditure and alternative funding options and why those options are not adequate; and
- (f) that the assumptions and proposals in the application are consistent with the Council's long-term strategy and financial management policies set out in the Council's planning documents and annual budget.

Source: section 185E(3) *Local Government Act 1989*.

In assessing applications, we will have regard to each of these matters and any other relevant factors. We will assess each application on its merits and determine the appropriateness of a higher cap having regard to all relevant factors and the unique circumstances of the applicant council.

1.2.1. Applications should demonstrate a long-term funding need

As we interpret the purposes and legislative matters of the Fair Go Rates system, we should generally only approve higher caps when a council can demonstrate a long-term funding need that justifies a higher cap. Establishing a long-term funding need is particularly important because an approval can allow up to four annual higher caps in succession, each increasing the rate base permanently.

We define a long-term funding need as a situation in which, as projected, a council's adjusted long-term revenue is less than the adjusted long-term expenditure it will need to perform its duties and functions efficiently, including some capacity to accommodate unforeseen events. A council can best establish it has a long-term funding need through good long-term financial planning. Appendix 3 gives a more detailed description of such planning.

Conversely, a council that projects an adjusted underlying operating surplus has sufficient revenue to offset the cost of its current service provision.⁵ In this situation, residents paying rates and fees for service in any year are collectively ‘paying their way’. Revenue generated to cover depreciation expense should help ensure, on average and over time, the council generates sufficient net cash flow to cover its asset-renewal needs.

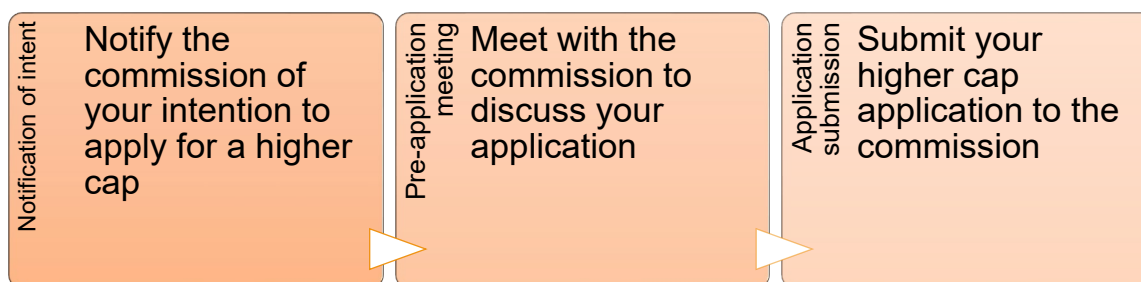
In summary, applications are expected to demonstrate that the council has done the following:

- It engaged effectively with ratepayers and communities about its services, infrastructure needs, rate levels, financial outcomes and trade-offs (see Appendix 3). It should also show how the outcomes of this engagement influenced its decision to apply for a higher cap
- It developed and applied rigorous and consistent internal policies, plans and processes to ensure efficiency and value for money
- It considered options to reduce or re-prioritise expenditure, and explored alternative funding, financing and revenue sources. If it rejected any options, it should demonstrate why those options were not adequate or appropriate.

We also have regard to a council’s record of compliance with any previous rate cap.

⁵ The adjusted underlying result, a financial indicator in the local government performance reporting framework, is defined as the surplus (or deficit) of *adjusted underlying revenue* less total expenditure, expressed as a percentage of *adjusted underlying revenue*, where this in turn is defined as total income other than non-recurrent capital grants for capital expenditure, non-monetary asset contributions and other contributions to capital expenditure.

2. How councils can apply for higher caps



2.1. Information sessions and informal meetings

Toward the end of each year, we conduct a series of information sessions or workshops across Victoria to remind councils of their obligations under the Fair Go Rates system and to inform councils about the higher cap application process and our activities relating to the local government sector. These sessions are a good opportunity to learn about the process and the legislative requirements, and to talk to us about a potential application. We also welcome the opportunity to meet with councils individually, if requested, during our visits to regional areas for the information sessions.

We encourage any council considering applying for a higher cap to contact us as early as possible to discuss the process and our requirements.

2.2. Notification of intent

Before applying to us for a higher cap, we ask that a council provide notification of its intention to do so. As in past years, we encourage councils to notify us **no later than 31 January** and include an estimated date of application. We can then estimate the resources we require to assess all applications properly in a timely manner.

To notify us, the council (or its chief executive officer) can send an email advising us of its intention and nominating a contact officer. We will confirm receipt of the notification and publish a list of councils that give notice. We will provide notifying councils with an embargoed copy of any media release before its publication.

The notification does not oblige a council to send an application. If a council subsequently decides not to apply, it should tell us (by email) of the change at the earliest possible time. We will publish this updated information on our website.

The notification of intent should specify the:

- indicative higher cap or caps that the council is seeking
- number of years (maximum of four financial years)
- indicative reasons for seeking a higher cap
- the date the council expects to submit the application
- details of the nominated contact for future communications.

2.3. Pre-application meeting

Once we receive a notification of intent, we will contact the council to arrange a time for a pre-application meeting. The meeting is a chance to discuss the application and to clarify as necessary the information that the council should provide.

2.4. Application submission

An application for a higher cap must be in writing, with the council's approval and sign-off, and sent to us electronically. We will discuss with each council as necessary the most appropriate format and delivery method for the application and supporting documentation. File size restrictions may mean a council has to divide attachments across a number of emails. In this case, the council should ensure each attachment is numbered and clearly listed on the application cover sheet. Councils should contact us if they have any difficulties completing the templates or submitting their application or supporting material.

When submitting an application, a council should clearly indicate any confidential information in its application (including in any attached supporting information). Councils should also ensure that their submissions, and any attachments, do not contain personal or sensitive information (such as ratepayer details).

We will confirm receipt of each application and place it on our website (excluding any confidential information).

We will publish a list of the councils that applied for a higher cap, with the size of the increases they seek and the number of years over which they would have effect. We will also provide applicant councils with an embargoed copy of any related media release.

Where to send notifications and applications:

Send electronic copies (required) to: localgovernment@esc.vic.gov.au

Send hard copies (at own discretion) to:

*The Local Government Team, Essential Services Commission,
Level 8, 570 Bourke Street, Melbourne, 3000.*

2.4.1. When should the council submit its application?

A council can send us its application for a higher cap at any time between 1 February 2021 and 31 March 2021.⁶ This application period provides councils with flexible timing to accommodate their different circumstances.

If a council cannot apply before 31 March, the minister may set a new application date in the Government Gazette.⁷ A council should not assume the minister will do so other than in exceptional circumstances.

A council can apply for higher caps to take effect over one to four financial years. Once we approve an application, we expect the council to manage budgetary fluctuations for the duration of the approved higher cap or caps. However, in the context of multi-year approvals, the council can apply for an alternative higher cap by sending a new application. The council should consider doing so only if it can demonstrate a significant change in circumstances that was unforeseeable at the time of the initial multi-year application.

⁶ Section 185E(2), *Local Government Act 1989*.

⁷ Section 185E(2)(b), *Local Government Act 1989*.

3. Higher cap application requirements

A higher cap application must include:

1. an application cover sheet (the cover sheet)
2. a statement addressing the six legislative matters (the statement).

These two documents must be supported by:

3. the budget baseline information
4. any other necessary supporting documentation including (but not limited to) records of engagement plans, tools and outcomes, key strategic planning and budgetary documents and relevant policies and procedures.

The following sections set out the basic data requirements and expected information in these elements of the application.

3.1. The cover sheet

Each application must include a completed application cover sheet. This template ([available on our website](#)) captures high-level information about the application. The cover sheet should include:

- the nominated contact for future communications
- the proposed higher cap or caps, in dollar and percentage terms
- the financial years (no more than four) in which a proposed higher cap or caps would have effect
- a brief summary of the reasons for the application
- a list of attachments that include the necessary evidence to support the application.

We expect these components to be consistent with the application statement, the budget baseline information and any other supporting documentation.

3.2. The statement

After the cover sheet, the second component of an application is a statement addressing the six legislative matters that the council is required to specify in seeking a higher cap (Box 1.2).

The statement forms the basis of the application for a higher cap. A council should use the statement, together with any supporting evidence, to demonstrate that it has a long-term funding need that justifies a higher cap, and that approval is in the interests of ratepayers and the community. In Section 4, we explain what we look for in the council's statement addressing each of

the legislative matters and how we assess whether what we find adequately demonstrates the fundamental features of good financial planning and management, and the need for a higher cap.

In addressing the six legislative matters satisfactorily, a council can show its community and the commission that a higher cap meets the purposes of the Fair Go Rates system, because:

- there is a long-term need for additional funding and,
- council took appropriate steps to ensure its plans were robust, efficient and reflected outcomes from community engagement.

A council should demonstrate publicly its adherence to best practice planning and budgetary processes before applying for a higher cap. The Best Value Principles and the principles of sound financial management are particularly relevant.⁸ The Best Value Principles require a council to engage with ratepayers and the community, and so develop their understanding of the trade-offs needed for strong financial outcomes, when planning service delivery. The conversation is not about what is wanted but about moving towards what is needed — and about ratepayers' willingness to pay for it.

But the Best Value Principles and the principles of sound financial management are not retained in their present form in the 2020 Act. However, a council that has already aligned its practices with the new legislation may meet our expectations by adopting the service performance principles and a Procurement Policy consistent with the new Act.⁹

If a council seeks a higher cap for more than one year, or for a percentage well above the minister's rate cap, we look for greater substantiation than for a minor increase for a single year. The greater the potential burden on ratepayers that a higher cap application represents, the greater is the effort we expect in preparing (and assessing) the application. A council is responsible for determining what it considers sufficient demonstration to support its application.

3.3. Budget baseline information

The third required component of any higher cap application is the completed budget baseline information template ([available on our website](#)). The data provided in this template gives us much of the information we require to assess the council's stated financial position, its calculation of the proposed higher cap, and its reasons for applying.

The budget baseline information is important for assessing a council's application for a higher cap or caps because it should identify the services and assets most affected by the outcome of the higher cap application, and the overall impact on a council's financial performance. It should also

⁸ Section 136 and ss. 208A – 208J of the *Local Government Act 1989*

⁹ Sections 106 and 108 of the *Local Government Act 2020*

show if circumstances have changed such that the council needs a higher cap, and identify the outcomes that the additional revenue would enable the council to achieve. The budget baseline information should also disclose and support the council's assumptions — for example, in forecasting grants and growth in rateable properties— and show whether they help to justify a proposed rate increase.

The budget baseline information template focuses on the outlook for the period of the proposed higher cap and the change relative to the base year. It requires a council to report on the forecast actuals in the base year and to present two scenarios for the years for which it seeks a higher cap. The first scenario assumes we approve the higher cap; the second assumes the council stays operating under the minister's cap. This comparison will display the impact of the proposed rate increase on services, assets and financial position, relative to the base year. Strategic Resource Plan information, including the proposed higher cap, is also required. Where the council has moved towards the requirements of the new Act, the equivalent in short-term detailed planning may be a Council Plan.

A council should provide information (income statements, balance sheets and capital works statements), for up to ten years, to complete the template. It should show both 'with' and 'without' higher cap scenarios, and do this for the budget year, three years of the short-term detailed plan, and as many years as are supported by the council's long-term Financial Plan.

Box 3.1 Why is long-term financial information important?

A council may cite underlying factors that will impact on its finances over the longer term as reasons for a higher cap. A four-year financial plan may not adequately capture these impacts. This is especially the case for a council applying for multi-year caps, where a four-year financial plan is unlikely to capture the long-term effects of the proposal and demonstrate the underlying financial need. A council submitting a four-year financial plan runs the risk of failing to demonstrate the need for a higher cap because of insufficient information. The same may be true where a council seeks a higher cap significantly above the minister's cap, with potential impact on its finances over an extended period.

Based on the short-term detailed plan and the long-term financial plan information provided, the budget baseline information template will automatically calculate relevant financial indicators, as used in the local government performance reporting framework.¹⁰ We will use these indicators (in addition to other information provided in the council's application) to assess a council's financial

¹⁰ The template calculates indicators of Liquidity (Working capital; Unrestricted cash), Obligations (Asset renewal; Loans and borrowings; Indebtedness) and Operating position (Adjusted underlying result).

capacity and long-term funding need. The council should also show the assumptions it has incorporated in its long-term financial plan.

A council is required to give forecasts of annualised supplementary general rate and municipal charge revenue and the growth in rateable properties over the course of the short-term detailed plan and long-term financial plan. These forecasts are important for calculating the required higher rates and the rate revenue that a council expects to receive in the following years with a higher cap. The onus is on councils to make the most reasonable forecasts of this growth, and to explain their assumptions in the budget baseline information template.

The budget baseline information template provides detailed instructions and definitions to help council staff complete it. The information is important for demonstrating the reasons for a higher cap. It captures whether the council's circumstances may have changed, affecting its financial position. The more detailed the information provided, the easier it will be for the council to demonstrate why it seeks the higher cap.

3.4. Supporting material

A clearly stated application can demonstrate these key matters with supporting material. For example, a discussion of a council's community engagement will be easier to understand and assess, if the application includes material such as:

- records of meetings and attendance
- the degree of involvement sought from participants
- samples of the information and material provided to participants or the public
- notes and analysis of participants' views.

We wish to minimise the need for a council to generate *new* accounting records, analyses and reports, purely to support an application. Rather, using *existing* detailed material can help to show the council identified a financial need through established and robust financial and planning processes. However, when attaching such material, a council should include cross-references in its statement (with relevant page numbers) and explain its significance in sufficient detail to support the application.

We expect councils to submit a long-term financial plan to support their applications. The outlook of the financial plan should capture the long-term effects of the proposal and demonstrate the underlying financial need. Where necessary, we may request a longer plan than the council has provided (or additional information) to assist us to better assess the underlying need. Failure to provide such financial information may limit our ability to be satisfied that a higher cap is appropriate.

Supporting documents prepared for different purposes at different dates may present different versions of what is essentially the same information. If a council is going to rely on these various

documents as supporting evidence for its application, it needs to consider how best to present the information to support its case and identify and explain any inconsistencies in the information provided.

When attaching supporting material to its application, council should ensure all personal or confidential information has been removed, or else draw the commission's attention to it to prevent sensitive information being uploaded on to our website.

3.5. Requests for further information

It takes considerable time to assess an application properly. We will use our best efforts to finish each assessment and publish the decision within two months of receiving an application. During this time, commission staff will be in touch with council contacts as necessary to clarify issues or seek additional information from the council, to understand its application better.

We will send a written request to the council as soon as possible: probably within two or three weeks of receiving the application. Other informal contacts for minor clarifications may continue as needed while we assess the application.

We will place the council's responses to our requests alongside the council's original application on our website. We will include any supporting documents provided, unless marked as confidential.

Ensuring appropriate supporting material is attached and relevant cross references to this material are included in an application will assist us meet this target time frame.

4. How we assess applications

4.1. What is our assessment approach?

We have an integrated approach to assessing higher cap applications which considers how councils have addressed the six legislative matters and our statutory objectives.

4.1.1. Integrating the six legislative matters and our statutory objectives

As the Fair Go Rates system requires, we examine each of the six legislative matters that a council addresses in its application. Further, the 1989 Act requires us to have regard to a council's record of compliance with previous years' caps.

Our assessment takes into account the statutory objectives and legislative matters that applications must address. This approach ensures that the assessment includes all relevant factors covered by the legislation that impact on whether the application demonstrates a long-term financial need that should be funded through a higher cap.

Our assessment approach is set out below.

4.1.2. Our integrated approach to assessing applications

The way in which a council establishes its long-term funding need, and the rigour with which it does so, are both important. Applications must address each of the six legislative matters listed in Box 1.2 and discussed in detail in Section 4.2. An application should demonstrate the magnitude of funds needed, the reasons for that need, and the actions that the council took to minimise the overall need. Our experience is that the more comprehensive and robust a council's long-term planning, and the better its engagement with the community, the simpler it will be for the council to demonstrate a long-term need for funds.

When assessing an application and determining whether a higher cap is appropriate, we depend largely on the information that the council provides in its application addressing the six legislative matters. However, data in the budget baseline information template also provides insights to guide our decision, as do key indicators in the local government performance-reporting framework. We examine the information provided in the whole application and seek to answer five basic questions.

1. What is the underlying financial position?

We look at the way the council has responded to the first two legislative matters: the *Proposed higher cap* and the *Reasons* for which it is required. They should be consistently stated and clearly explained throughout the application. We also look at the council's financial capacity, as shown by the current values and the past and forecast trends of financial indicators used in the local

government performance reporting framework. We focus on the adjusted underlying result (as well as other key financial indicators such as the working capital ratio, unrestricted cash position and asset renewal ratio). We also consider specific council characteristics such as road length, and trends such as population and dependence on grant revenue, to understand the financial pressures faced by the council.

2. What has been done to manage the underlying position?

We look at the council's response to the fourth and fifth legislative matters: *Efficiency and value for money*, and *Alternative funding and offsets*. We consider other supporting information the council provides and we look at indicators and trends in the local government performance reporting framework. We make comparisons with other councils, using unit costs of service delivery and similar benchmarks. We consider records of service reviews that are completed, and of planned and historical savings that the council can quantify. We consider processes for asset review and disposal. We look for any other cost saving initiatives the council has pursued or could pursue — within its own organisation and in cooperation with neighbouring councils.

We look at the council's management of cash including discretionary reserves, and its use of debt in the context of the council's policy on borrowing and the mandatory principles of sound financial management.

3. How were ratepayer and community views taken into account?

We look at the council's response to the third legislative matter, *Engagement*, and the content and the way it was undertaken. We expect that the council openly and actively discussed with ratepayers and the community all issues of substance covered in the other legislative matters. We consider measures of community satisfaction.

Beyond this, we also consider whether the council seeks views on how it can best conduct the engagement program. We assess whether the council monitors its success in reaching people and adjusts its program accordingly. We look for records showing the council considers participants' views and reflects them in its application. We consider how the council provides feedback to the community and addresses any unmet expectation.

4. Are the plans, policies and processes in place sufficient to demonstrate a long-term funding need?

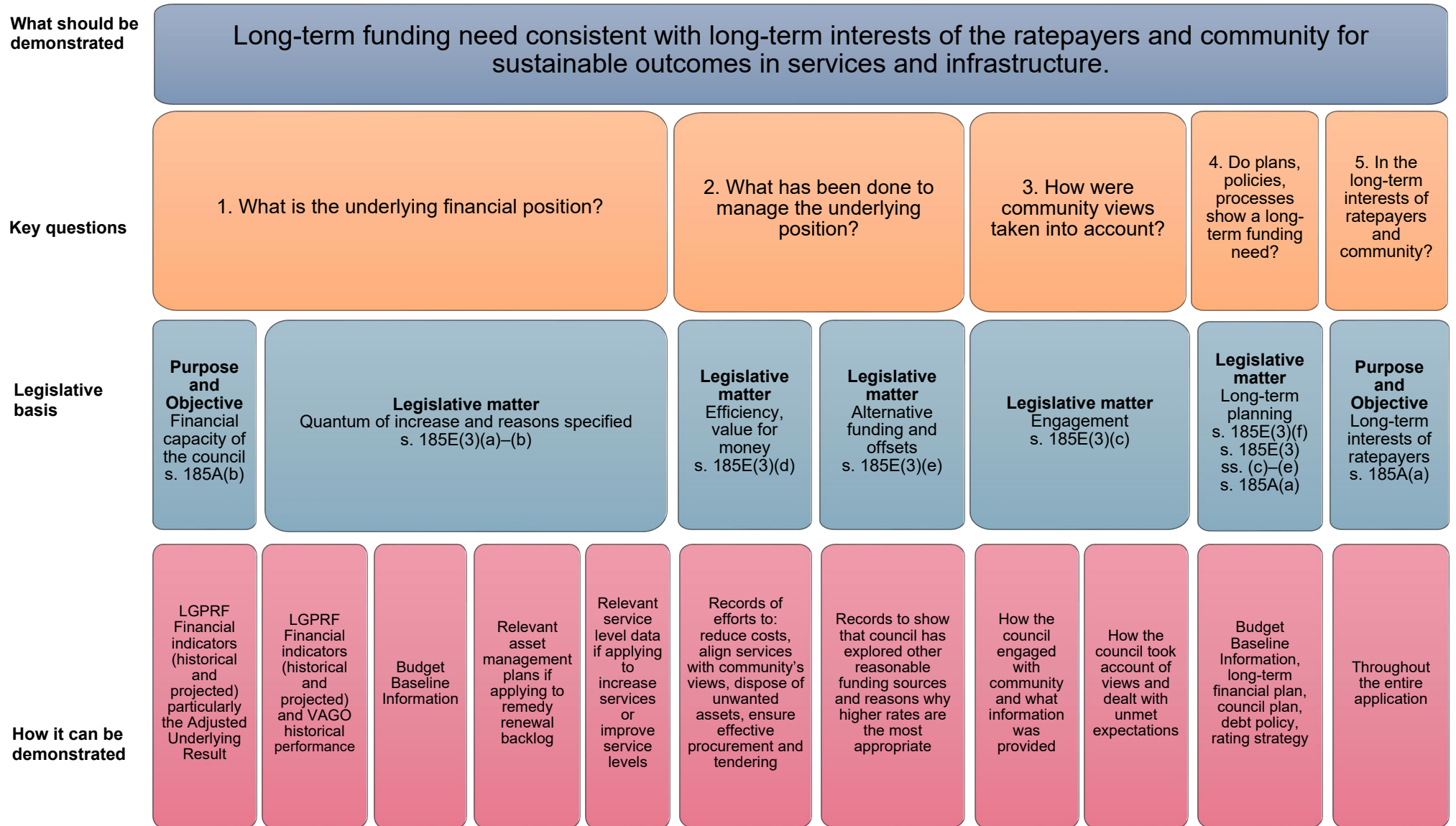
Our focus is on the sixth legislative matter, *Long-term planning*, and its integration with the other matters and its consistency with the supporting financial information. A council can establish its long-term funding need most clearly through good long-term financial planning. We consider the features outlined in Appendix 3 are fundamental to good financial planning and management, and we shall look for them in a council's higher cap application. These features help councils ensure they base their projected long-term revenue and expenditure trends on robust and timely

information. In this way, they can also identify long-term funding need with sufficient confidence for good decision-making.

5. Does the application demonstrate that it is in the long-term interests of ratepayers and the community?

To justify a permanent increase in the rate base and meet the statutory objectives, we must be satisfied that the application adequately demonstrates a long-term funding need. We must also be satisfied that a higher cap is consistent with the long-term interests of the council's ratepayers and community for sustainable outcomes in services delivery and critical infrastructure.

Figure 4.1 How our application assessment approach sits within the legislative framework



4.1.3. Other considerations

Need for greater demonstration for a multi-year cap

An application for a higher cap that will take effect over two to four years is not significantly different, in form and presentation, from a single-year cap. But if approved, it is different in one key respect: compared to a single year's higher cap, it can increase the council's revenue — and the community's rate burden — to a greater degree.

Because of this, we expect and require a multi-year application to show a higher standard of consistency and attention to detail. In documenting its plans, we would expect the council to demonstrate that it:

- considered whether trade-offs — such as different service, infrastructure and financial options that might not exist in the short term — may become available over two to four years
- models alternative scenarios (not limiting these to a single with/without higher cap comparison)
- outlined the key operating and financial assumptions in the long-term financial plan, ensuring these are consistently stated (or adequately reconciled) in the narrative statement, formal budgets and plans, and the budget baseline information template.

Engagement is particularly important for multi-year applications — and it must be clear how the views of ratepayers and the community informed the council's plans. We expect an application to show that the council engages effectively, securing adequate representation and involvement of its community. Its engagement program must make clear the options under consideration and the impact of a multi-year cap. The application must also show how the council responded to the views that it gathered through engagement, and dealt with unmet expectations.

Because circumstances may change significantly during the timespan of a multi-year cap, we expect a council to commit to continuing this engagement and reviewing its priorities, as part of its normal planning and budget processes, as stated in Sections 4.2.3 and 4.2.5.

The affordability of a higher cap

Affordability is an important consideration for a council when setting its rates. We encourage councils to take this into account when they make their decisions about whether to apply for a higher cap.

We do not assess affordability in councils' higher cap applications. The legislation does not require us to do so, nor is it appropriate.¹¹ Councils are best placed to determine their communities' capacity to pay after taking into account all major factors that may affect their communities. The

¹¹ Affordability is not one of the matters listed in the legislation that councils must address in their applications — section 185E(3).

decision on the appropriate trade-off between service impacts and the level of rates rightly sits within the council's jurisdiction.

Our role is limited to ensuring that the higher cap application process undertaken by councils is robust and transparent.

Long-term and short-term need

A council with a well-developed long-term financial plan should not have to resort to a higher cap simply to balance any net cash needs in its budget from year to year. It should be able to meet any short-term cash needs from available resources, including its existing unrestricted cash holdings. Seeking ongoing higher rates to fund year-to-year fluctuations in cash flow would be inconsistent with the long-term interests of ratepayers and communities.

Generally, we consider a higher cap is not appropriate when an application:

- does not demonstrate a long-term funding need
- proposes to apply the higher cap to fund short-term needs
- is not supported by adequate long-term financial planning
- does not demonstrate that the council accounted for the views of the community and ratepayers
- is inconsistent with the council's internal plans and policies, and conflicts with information provided to the community and the commission
- is not supported by our analysis of the council's financial capacity and overall flexibility to manage its short-term needs.

4.2. The six matters that must be addressed

When assessing how a council’s application has addressed each of the six legislative matters, we consider:

- **The purpose of each matter**
- **Guiding principles we consider for each matter**
- **How the application has met our general and specific expectations of each matter**
- **The supporting evidence.**

While we adopt an integrated approach to our assessments (as outlined in Section 4.1), all applications — whether for one year or for several — must cover the core subject matter. That is, they should consider the six legislative matters as the means by which they demonstrate a long-term funding need, established through robust financial planning and engagement with the community.

Sections 4.2.1 to 4.2.6 give further guidance on the information we consider will assist a council address the six legislative matters, namely:

1. Proposed higher cap
2. Reasons
3. Engagement
4. Efficiency and value for money
5. Alternative funding and offsets
6. Long-term planning

4.2.1. Proposed higher cap

*An application must specify a proposed higher cap for each specified financial year.*¹²

Purpose

The purpose of this legislative matter is to detail the magnitude of the rate increase(s) being sought and the year(s) in which the increase(s) will have effect.

Guiding principles

We will verify that the proposed higher cap is:

- correctly expressed as the total percentage increase above the base average rate, inclusive of the minister’s cap for 2021–22

¹² Section 185E(3)(a), *Local Government Act 1989*.

- consistently stated in the budget baseline information template and elsewhere in the application.

General and specific expectations

A council can address this matter by accurately completing the application cover sheet template (a Microsoft Word form) and the budget baseline information template (a Microsoft Excel spreadsheet that itself contains detailed instructions on how to enter the required data).¹³ These documents will cover:

- the higher cap or caps being sought
- the years to which the higher cap or caps will have effect (maximum of four years).

Appendix 2 outlines how the rate cap works and how the base average rate and capped average rate are calculated.

A council can apply to us for a higher cap for a period of up to four financial years.¹⁴

It can specify different higher caps each year for a multi-year application (for example 4 per cent to take effect in the first year, then 5 per cent and 3 per cent). However, to provide greater certainty to ratepayers and smooth the rate path, we encourage councils to adopt a uniform annual rate of increase (a rate that is equivalent to the average annual increase over the period specified). If a council chooses not to smooth the rate path, it will need to explain why a varying annual rate of increase is more appropriate.

The proposed higher cap should be expressed as the total percentage increase from the base average rate. Any approved cap is inclusive of the average rate cap that the minister sets. For multi-year applications, we recognise that the average rate cap will not be known for the years beyond the immediate budget year. Councils may want to use the Department of Treasury and Finance forecasts of the consumer price index for planning and budgeting.¹⁵ However, the increase the council seeks should reflect its long-term funding need and should be the outcome of rigorous long-term planning.

A council should ensure the application cover sheet, the statement and the budget baseline information template are consistent in stating both the amount of revenue applied for, and the corresponding percentage increase in average rates.

¹³ Both templates are available on our website at <https://www.esc.vic.gov.au/local-government/guidance-councils#tab-container2>.

¹⁴ Technically this would be a higher cap in each of (up to) four successive years. Each higher cap creates an ongoing permanent increase in the rate base.

¹⁵ See <http://www.dtf.vic.gov.au/Publications/Victoria-Economy-publications/Macroeconomic-indicators>

Supporting evidence

As above, a council must provide the completed application cover sheet template and budget baseline information template. The budget baseline information template requires the council to provide 'with higher cap' and 'without higher cap' forecasts of selected financial indicators in the local government performance-reporting framework.

As Section 3.3 explains, we expect the budget baseline information template to show results with and without a higher cap for the budget year and the three following years of the short-term detailed plan, and up to ten years of the long-term financial plan.

4.2.2. Reasons

*The reasons for which the council seeks the higher cap.*¹⁶

Purpose

The purpose here is to specify the immediate and underlying reasons for the application — reasons that the application and supporting documentation should consistently reflect throughout. This should explain whether the council is seeking a higher cap to address a material change in financial circumstances; a change to the services that the council provides; particular infrastructure needs; to ensure long-term financial sustainability; or some other factor or combination of factors.

Applications can specify more than one reason in one year — or in different years of a multi-year application. If different reasons are specified, then applications should demonstrate and quantify the funding requirements for each reason.

Guiding principles

The commission will consider whether the reasons for seeking the increased revenue are consistent with the long-term funding need of the council.

General and specific expectations

We expect councils to quantify the amount(s) that make up their funding need, and identify the purpose(s) for which the funding is required. Councils are generally expected to demonstrate a long-term funding need.

As part of its normal planning and budgeting process, a council is expected to model the services and service levels that it can provide in different revenue scenarios. We therefore expect that, before seeking a higher cap for 2021–22, the council prioritised the services and expenditures that made up its revenue requirement under the rate cap in the base year 2020–21.

¹⁶ Section 185E(3)(b), *Local Government Act 1989*.

If a council now seeks a higher cap to fund a service or expenditure that it previously funded from revenue in the base year, it needs to explain why it can no longer do so within the revenue generated by the average rate cap.

A council should also demonstrate the need for this funding change to its community. Further, it should include evidence of this community engagement in the application. Section 4.2.3 discusses this in detail.

Most reasons put forward by a council will likely fit into one or more of the following categories.

- The council faces sustained underlying operating deficits, possibly following a material change in revenue or costs. The deficits cannot be managed by trade-offs or alternative funding, such as internal savings, the use of other revenues, or by an operational change to minimise the impact in the short term. The application must make this point clear in the response to the fifth legislative matter. We expect a council to manage one-off or immaterial short-term variations in its liquidity through day-to-day financial management.¹⁷ When a council faces major increases in its long-term funding requirements it should give clearly identified and quantified reasons.
- The council, in consultation with its community, prioritised the provision of a new service or higher standard of service but does not have corresponding funding from other sources.
- The council is increasing its effort to address asset renewal requirements, consistent with its long-term strategy and asset-management plans.
- The council wants to fund significant investments in new infrastructure, which it prioritised in its plan and long-term strategy, developed through engagement with the community. The funding requirements (and corresponding revenue needs) should be calculated according to the whole-of-life cost of the project. A council should not seek higher caps to fund specific small, short-term capital projects that form part of its regular capital-works plan.

A higher cap represents a permanent increase in a council's rate base that will continue to compound every year thereafter. For this reason, we do not expect to receive applications that aim to fund short-term expenditure or cash-flow requirements. It is generally not in the interests of ratepayers and the community to approve higher caps on this basis.

There are no reasons that automatically ensure the approval of a higher cap.

Supporting evidence

We expect a council to provide documentation that supports the council's reasoning. The documentation should show how circumstances might have changed, or whether the council has an existing funding need, such as a renewal backlog or a long-term adjusted underlying deficit. This evidence may refer to previous financial statements, long-term financial plans, short-term

¹⁷ 'Liquidity' here meaning the council's ability to generate sufficient cash to pay its bills on time.

detailed plans or asset-management plans. If the increase is required to fund a specific action, such as repairing council-owned building infrastructure, then the council needs to explain how in future years it will use the higher revenue that will have been incorporated into the rate base.

We expect a council to explain clearly any material differences between past budget and actual expenditure (particularly underspends) for services or infrastructure. This explanation will give us confidence that funds budgeted will be appropriately spent in the interests of ratepayers.

The budget baseline information template (see Section 3.3) is an essential part of the evidence that demonstrates the council's reasons.

4.2.3. Engagement

*How the views of the ratepayers and the community have been taken into account in proposing the higher cap.*¹⁸

Purpose

The purpose of this legislative matter is to ensure a council demonstrates it considered the views of ratepayers and the community in relation to a higher cap.

Engagement on a higher cap should be part of a council's long-term planning. This front-end engagement could feed into the development of a four-year council plan, the annual budget, or be part of broader community engagement on key issues affecting the local government area.

The more a council integrates engagement on a higher cap into its formal planning process, including the consideration of key budget trade-offs, the easier it will be to address this legislative matter.

Guiding principles

The commission's consideration of this matter is guided by our key engagement principles (Box 4.1) and the Best Value Principles (e) and (f) on engagement (Box 4.2)¹⁹ in the 1989 Act.

¹⁸ Section 185E(3)(c), *Local Government Act 1989*.

¹⁹ Sections 208B (e) and 208B (f), *Local Government Act 1989* –and also see notes below on Best Value Principles, in [4.2.4. Efficiency and value for money - Guiding principles](#)

Box 4.1 Key engagement principles

Principle 1: The engagement program should contain clear, accessible and comprehensive information and follow a timely process to engender feedback from the community.

Principle 2: The engagement program should be ongoing and tailored to community needs.

Principle 3: The engagement program should prioritise matters of significance and impact.

Principle 4: The engagement program should lead to communities becoming more informed about council decision making.

Essential Services Commission 2015, A Blueprint for Change, pp. 69-70.

The community engagement principles above are broadly consistent with those set out in section 56 of the new Act. A council that has already aligned its practices with the new legislation may meet our expectations, having adopted the community engagement principles and a community engagement policy consistent with the new Act, by showing that it is following them as required for strategic planning around the proposed higher cap.²⁰

General expectations

As a minimum, a council's engagement on higher caps should meet our key engagement principles.

Councils will differ in how they engage with ratepayers and communities. We do not prescribe how councils should do this; such decisions sit with councils. But applications should clearly explain how the council engaged with its community and why it chose this approach, what information it provided to the community and how this was provided. Applications should also explain what the council learnt about the views of its ratepayers and the community, and how the council took these views into account in deciding to seek a higher cap.

We recognise that effective community engagement can be challenging. Whether or not a certain method is appropriate will depend on the demographic, geographic and financial characteristics of each council.

We expect that councils will increasingly integrate engagement on a higher cap application into their existing planning and budgetary processes. If records show that a council's engagement on its budget or long-term plan adequately covered its funding needs, service levels, trade-offs and the other Fair Go Rates system legislative matters, then we do not expect to see a separate engagement program for a higher cap application.

²⁰ Sections 55 and 56, and ss. 88–91, *Local Government Act 2020*

A council should show that it has engaged openly and effectively, and in ways that draw out community views. Community members and ratepayers should understand that the higher cap represents good value for money, that trade-offs have been considered, and that a higher cap fits into the council's long-term strategy. Over time, the community should become better informed of the trade-offs required for a council to achieve long-term financial stability.

An application should show the efforts that the council made to engage effectively with its ratepayers and community members to obtain a representative view. The council should actively seek the views of a sufficient number of people, reflecting diverse groups in the municipality.

Specific expectations

We expect the council to provide a narrative describing and demonstrating:

- what it did to engage with ratepayers and community members (outlining who was approached and in what way, when and where) and why the selected methods were chosen
- what information the council gave ratepayers and community members about issues such as:
 - the scale of the higher cap
 - whether the higher cap addresses a short-term or long-term need
 - details of the options, trade-offs and different rate-increase scenarios
- what the outcomes of the engagement program were (documentation and analysis of the responses of ratepayers and community members)
- how the council took into account the views of ratepayers and the community in seeking a higher cap. Although not bound to accept those views even if expressed by a majority, the council should explain how it weighed up and considered those views and how they influenced its decision, by describing:
 - what it learnt through the engagement process
 - how it is responding to the issues raised during the engagement and why it is responding that way
 - what the council is doing about unmet expectations arising from the engagement undertaken.

We note in particular that, based on the documentation provided by some councils in previous applications, it has not always been sufficiently clear:

- whether councils engaged with ratepayers and the community and presented adequate information to them, on trade-offs and the potential effects on rates, services and service levels
- how the council considered ratepayer and community views, and how it gave feedback on those views, particularly when it received mixed (or largely negative) responses to its engagement.

Supporting evidence

To support its narrative describing community engagement, the council must provide evidence. This should demonstrate the thinking at each stage of the engagement program — from planning through to evaluation. This evidence might include:

- an engagement plan
- agendas, material and information provided to community members during the engagement processes
- documents that capture and analyse the views expressed during the engagement processes (such as survey results, comments from community meetings or listening posts, or submissions)
- council analyses of community and ratepayer views
- council meeting reports, minutes or records of discussions where the council considered the outputs of the engagement process (i.e. the views of ratepayers and the community)
- material provided to community members reporting back and explaining how the engagement process informed the council's higher cap application.

Community engagement resources are available on our website

In consultation with the commission's engagement technical working group, we have developed resources to assist councils planning, undertaking and reporting on their engagement. These resources are available on our website.²¹

4.2.4. Efficiency and value for money

*How the higher cap is an efficient use of council resources and represents value for money.*²²

Purpose

The purpose of this legislative matter is to ensure an applicant council can demonstrate it has sufficient policies and processes in place (and has taken specific actions) to ensure the additional revenue raised would be used efficiently, and the outcomes being pursued represent value for money for ratepayers. In many ways, this matter represents a public demonstration of the council's adherence to the Best Value Principles that councils are obliged to meet in their service provision.²³

²¹ See <https://www.esc.vic.gov.au/local-government/resources-councils/community-engagement-resources>.

²² Section 185E(3)(d), *Local Government Act 1989*.

²³ Section 208B, *Local Government Act 1989*.

Guiding principles

The commission's consideration of this matter is consistent with the Best Value Principles (a)-(d) (Box 4.2).

Box 4.2 Best Value Principles

The Best Value Principles are —

- (a) all services provided by a Council must meet the quality and cost standards required by section 208D;
- (b) *[subject to sections 3C(2)(b) and 3C(2)(e),]* all services provided by a Council must be responsive to the needs of its community;
- (c) each service provided by a Council must be accessible to those members of the community for whom the service is intended;
- (d) a Council must achieve continuous improvement in the provision of services for its community;
- (e) a Council must develop a program of regular consultation with its community in relation to the services it provides;
- (f) a Council must report regularly to its community on its achievements in relation to the principles set out in paragraphs (a), (b), (c), (d) and (e).

Source: section 208B(a)–(e), *Local Government Act 1989*.

The Best Value Principles and the principles of sound financial management are not retained in their present form in the 2020 Act. However, a council that has already aligned its practices with the new legislation may meet our expectations by showing they have adopted the service performance principles and a Procurement Policy consistent with requirements of the new Act.²⁴ This includes requirements to develop quality and cost standards, provide value, and engage with the community in strategic planning and decision making.

A proviso in subclause (b) of the Best Value Principles referenced a section now repealed in the 1989 Act. In effect, this further required councils to have regard to efficiency, effectiveness, accessibility and equity, in providing services and facilities to meet community needs. Similar requirements are expressed in the service performance principles and strategic planning principles.²⁵

²⁴ Sections 106 and 108 of the *Local Government Act 2020*

²⁵ Section 89 of the *Local Government Act 2020*

We consider these principles cover expenditure that councils may not traditionally classify as a 'service', including capital works and expenditure that is not directly related to the *Reasons* for the application. This is because a council's failure to follow these principles in other areas of its operations will ultimately affect its capacity to deliver services. It will also affect ratepayers' value for money from the rates that are paid.

General and specific expectations

The application should show how the amount of any additional revenue the council proposes to receive through a higher cap represents a good value option for achieving the desired outcome.

We expect applications to demonstrate that the council has sound processes, policies and initiatives to ensure it uses resources efficiently, and that it followed these processes and policies in determining the need for a higher cap.

When proposing to fund the delivery of new or expanded services, or new infrastructure, a council should show it took appropriate steps to ensure the planned expenditure would represent value for money for ratepayers. This may include service reviews, business cases and/or cost benefit analyses (when appropriate), and consideration of whole of life project costs. A council should demonstrate the desired objectives and outcomes of the proposed changes to services or infrastructure, and the options considered for delivering those objectives and outcomes.

The council should quantify any efficiency savings gained and explain how forward expenditure projections reflect those savings.

Supporting evidence

To support its application, the council may refer to or describe relevant sections of internal policies and processes for ensuring efficiency and value for money. This evidence might include tendering or procurement policies; policies for reprioritising capital expenditure; service reviews and their outcomes; internal efficiency initiatives; business cases; cost benefit analyses (where appropriate); and assessment of alternative delivery options. The council should also explain how it has followed these policies/processes.

Further, if applicable, the council should provide the results of any benchmarking studies that compared the council's unit costs with its peers' unit costs. For example, information on the Know Your Council website can support an application effectively. This can be particularly helpful if the website shows performance measures related to the *Reasons* that the council identified in its application.

4.2.5. Alternative funding and offsets

*What consideration has been given to reprioritising proposed expenditures and pursuing alternative funding options and why those funding options are not adequate.*²⁶

Purpose

The purpose of this legislative matter is to ensure a council considered the prioritisation of services and different funding and financing options before seeking a higher cap. This matter requires the council to demonstrate that it considered other feasible options, and to explain why it judged those options inadequate. The application should show that the council's engagement program sought community views on the issues.

Guiding principles

The commission's assessment of this matter is based on evidence about whether:

- the council considered alternative budget scenarios, in conjunction with its ratepayers and community
- the council's decision to apply for a higher cap is the most appropriate funding option to meet the stated *Reasons*.

General and specific expectations

We expect a council to show how it came to prefer raising additional revenue through a higher cap to other options, and how it considered any trade-offs (see Box 4.3).

Councils should not simply resort to increasing their revenues through higher rates when faced with budget pressures. We expect a council to have also considered one or more of the following areas in addressing its funding need:

- scrutinising the full suite of its operations and its planned investments for opportunities to deliver outcomes more efficiently
- re-examining whether the range of services and service standards delivered align with the community's highest priorities
- assessing the possibility and merits of alternative funding or financing options for different activities and investments
- examining cash-flow options that are available to manage short-term funding needs, having regard to its long-term revenue and cost trends.

We do not advocate that the sector increase or reduce its debt level. Whether it is prudent or responsible to use debt finance depends on the circumstances of each municipality and the

²⁶ Section 185E(3)(e), *Local Government Act 1989*.

judgment of the council. But debt finance is an option available to councils as part of their financial toolkit and it can form a key element in a responsible long-term financial plan. In particular, debt finance can be useful when a council seeks to provide long-lived infrastructure that is likely to provide inter-generational benefits to the community.

We expect a council applying for a higher cap to show it has a well-considered debt policy (preferably consulted on with the community) that guides its decision whether to use debt to reduce the need for additional funding in the short-term through increased rate revenues. If the council adopts a debt position that is not consistent with its debt policy, then the application should clearly explain why. In other words, as required by the legislation, a council's application should demonstrate it considered the option of debt and the reasons for adopting or not adopting it.

The application needs to demonstrate that the council considered other suitable funding or financing options. It also needs to outline the decision reached (and reasoning for the decision) on those options, which could include different rate increase scenarios. In demonstrating the preferred option, the council should consider how a higher cap is in the long-term interests of the community and ratepayers. The council, in consultation with the community, must decide priorities and desired outcomes; this decision is not our role.

Box 4.3 Trade-offs

There will inevitably be 'trade-offs' between different options that a council can take into account to determine the most appropriate approach to meet its long-term funding need and the long-term interests of the community.

'Trade-offs' is a term that appears a number of times in this document, particularly in the context of choices presented in community engagement (Section 4.2.3), and when council is examining expenditure proposals or funding options (this Section 4.2.5). When an application describes the trade-offs that were considered, we expect a clear statement that compares the financial impacts, service impacts or infrastructure impacts that arise from the choice of pursuing different options.

A council's strategic approach to considering alternative options and their potential impacts on ratepayers and the community is a key element of sound long-term financial planning.

Supporting evidence

Where relevant, an application should show how the council considered reprioritising services and changing service levels. It should show that the council considered using alternative revenue sources such as its current financial reserves or debt financing for the proposed expenditure. The application has to describe the engagement undertaken to identify the community's service preferences, with council's consideration of these preferences. Where relevant, an application should provide asset-management plans that support the timing of proposed works and the whole-of-life project costs for capital projects.

Key supporting documents should include long-term financial plans, revenue and rating policies, and debt financing policies. The budget baseline information will also help provide evidence. In particular, it will show how service review and/or reprioritisation might have affected, or be likely to affect, the revenue and expenditure profiles of services.

4.2.6. Long-term planning

*That the assumptions and proposals in the application are consistent with those in the council's long-term strategy and financial management policies set out in the council's planning documents and annual budget.*²⁷

Purpose

The purpose of this legislative matter is to show the reasons for the application are consistent with the council's long-term strategy and financial management plans, policies and other key planning documents. Our assessment will follow the council's summary of its recent, current and projected financial position, its relevant policies and the way that the higher cap links to longer-term strategies. This information will frame and support the council's reasons for seeking a higher cap and help us understand the council's financial position.

Guiding principles

The commission's consideration of this matter is guided by the council's demonstration whether:

- its reasons for seeking a higher cap are consistent with and supported by the council's key financial management and other strategic and planning documents
- in seeking a higher cap, the council adhered to the principles of sound financial management required by s. 136 of the 1989 Act (Box 4.4).

²⁷ Section 185E(3)(f), *Local Government Act 1989*.

Box 4.4 Principles of sound financial management

- (1) A Council must implement the principles of sound financial management.
- (2) The principles of sound financial management are that a Council must—
 - (a) manage financial risks faced by the Council prudently, having regard to economic circumstances;
 - (b) pursue spending and rating policies that are consistent with a reasonable degree of stability in the level of the rates burden;
 - (c) ensure that decisions are made and actions are taken having regard to their financial effects on future generations;
 - (d) ensure full, accurate and timely disclosure of financial information relating to the Council.
- (3) The risks referred to in subsection (2)(a) include risks relating to—
 - (a) the level of Council debt;
 - (b) the commercial or entrepreneurial activities of the Council;
 - (c) the management and maintenance of assets;
 - (d) the management of current and future liabilities;
 - (e) changes in the structure of the rates and charges base.

Source: s. 136(1)-(3), *Local Government Act 1989*.

But a council that has already aligned its practices with the new legislation may meet our expectations by adopting the financial management principles of the 2020 Act (including the principle of achieving best outcomes for the community and future generations) and financial policies consistent with the requirements of the new Act.²⁸

General and specific expectations

We expect a council to demonstrate that the reasons for its application (and underlying need) are consistently represented in, and supported by, its relevant financial and planning policies and documentation. Accounting records and projections should be reconciled to operational programs and asset-management records.

The budget baseline information template described in Section 3.3 shows an appropriate level of detail. Box 3.1 explains the period that we would expect the long-term plans to cover. The council should use its proposed higher cap and the minister's cap to show and compare results with and without a higher cap for the budget year. It could use the Department of Treasury and Finance forecast of the consumer price index as a proxy for the minister's cap in future years to show

²⁸ Section 9(2) and ss. 101, 102 of the *Local Government Act 2020*

similar comparisons for the years of its short-term detailed plan. It should explain the basis of any critical assumptions it makes for the later years of the long-term financial plan.

In previous applications, not all councils have ensured their financial plans were clear and consistent with other supporting material such as corporate plans, financial strategies and policies, and asset-management plans. For instance, for a higher cap intended to close an asset-renewal gap, we would expect to see the purpose, monetary amounts and timescale reflected in an asset condition report and financial plans attached to the application.

We also expect an application to consider the council's major financial challenges systematically and reflect them in the financial plans. The plans should deal with major trade-offs, and model alternative scenarios that align with good policies and financial sustainability.

The council will have used certain assumptions to quantify the higher cap that it seeks. For example, these assumptions might relate to future costs, demand trends, changing community needs and appropriateness of funding source. All relevant planning documents should state these assumptions consistently; when this is not the case, the application should highlight and explain differences. We also expect a council to demonstrate that it reviews the assumptions underpinning its long-term financial plans annually, and to explain the reasons for changes to key assumptions in these plans.

We expect that the council adheres to the principles of sound financial management and that the application and supporting documentation reflect this.

Supporting evidence

As evidence, a council may provide its Council Plan, Strategic Resource plans and long-term financial plan, annual budgets, asset-management plans, revenue and rating policies, and debt policy. The budget baseline information should also provide supporting evidence. We expect a council's application to direct us to the relevant sections or pages of the plans and policies.

4.3. Expert advice

If appropriate, we may engage external expertise to assist our analysis and understanding of key aspects of higher cap applications. This expertise may include financial and accounting analysis, infrastructure maintenance and planning, corporate planning, and community engagement. Our use of this expertise does not represent an additional requirement or criterion, but simply helps us understand a council's application and the implications of our decisions. We will publish any external advice that is directly relevant to our assessment of an application, together with our decision report in response to that council's application.

4.4. How will councils receive our response?

We can approve, approve in part, or not approve, the higher cap proposed by the council. We may also approve an alternative higher cap, as long as this is not higher than the higher cap proposed by the council. In deciding on an application for a higher cap, we must have regard to:

- the purposes of the Fair Go Rates system
- whether the application satisfies the legislative matters
- whether the council has complied with directions, advice and guidance in relation to a particular application under s. 185E(5)
- the council's record of compliance with the rate cap.

We will publish a decision report that details the higher cap approved (or not approved), the year(s) for which it will have effect, and the reasons for our decision. We will also make all decisions publicly available on our website after notifying the relevant council of the decision. Further, any approved higher cap will appear in the Victorian Government Gazette.

We will provide a council with an embargoed copy of the decision report before its public release. We will also invite the council for a formal meeting to discuss the reasons for our decision.

Approved

Approval means a council can increase its capped average rate by no more than the percentage amount of the higher cap proposed in its application for the specified period.

Approved in part or approval of an alternative higher cap

Under s. 185E(6) of the 1989 Act, the commission has authority to set a lower rate cap than the one that the council proposed.

Approval in part may occur where the commission approves a higher cap proposed by the council, but does not approve all years of a multi-year application.

Approval of an alternative higher cap means a council can increase its capped average rate by more than the average rate cap set by the minister, but only by the percentage that we set. This will be lower than the percentage increase that the council applied for.

Not approved

A 'not approved' response means a council cannot increase its capped average rate by more than the average rate cap set by the minister.

4.5. How can a council contest a decision?

A council can seek a judicial review by the Supreme Court, on administrative law grounds, of a commission decision on an application for a higher cap. This means the court could set aside our decision if it finds that we did not give a council a fair hearing on its application or that we made an error of law. If the court finds a procedural or legal error, then we can be required to make a fresh decision on the application in a manner consistent with the court's guidance. The court could not substitute its own decision based on the facts before it.

5. Submissions

5.1. How do we respond to ratepayer and stakeholder submissions?

Throughout the process, we might receive submissions from the public or other stakeholders, particularly as ratepayers become aware that their council is considering a higher cap application. The Fair Go Rates system does not prescribe a process for the commission to respond to these submissions.

Concerned community members should contact their council directly with their concerns about a proposed higher cap. The council should then discuss those concerns in its application to the commission.

Concerned individuals or groups may wish to make a submission to us at any stage by email to localgovernment@esc.vic.gov.au. How we treat such a submission will depend on where we are in the application process.

5.1.1. Submissions received before a council submits an application

Any person or organisation making a submission on a possible higher cap will be referred to the relevant council. If that council later applies for a higher cap, we will assess how the council sought and responded to the views of ratepayers and the community, in proposing the higher cap.

5.1.2. Submissions received after a council has submitted an application

When we have an application from a council, we will consider a submission only if it is relevant to the purposes of the Fair Go Rates system and the six matters set out in s. 185E(3) of the 1989 Act (as shown in Box 1.2). If we receive submissions that are relevant, then we will consider those submissions, to the extent possible, depending on the stage that an application has reached. With the submitter's consent, we may forward the submission (or parts of it) to the relevant council for its response which we will consider as part of our assessment, but we cannot facilitate a dialogue between the submitter and the council. Submissions may be published with agreement from the submitter and if relevant to our decision.

Appendix 1: Background and role of the commission

The Fair Go Rates system

The Victorian Government established the Fair Go Rates system in December 2015. This legislative framework limits the annual increases in Victorian local government rates.

Our role in administering the Fair Go Rates system

In this system, Victorian councils cannot increase average rates by more than the **average rate cap** set for them by the Minister for Local Government, unless we approve their application for a **higher cap**.²⁹ In the past four years, the minister has set a single rate cap for all councils, but can set different rate caps for councils individually or by class. For simplicity, we refer to this as the minister's cap.

We also have a role in **monitoring and reporting**.³⁰ We report annually on councils' compliance with the rate cap (unless the context requires otherwise, this refers to their compliance with the minister's cap or a higher cap we approved). We also report on outcomes associated with the Fair Go Rates system every two years. Our first report on the outcomes of rate capping (2016-17 to 2017-18) was released in May 2019.³¹ Our next is due in the second quarter of 2021.

In performing our statutory responsibilities under the *Local Government Act 1989* (the 1989 Act), we have the following objectives:

- to promote the long-term interests of ratepayers and the community in relation to sustainable outcomes in the delivery of services and critical infrastructure
- to ensure that a council has the financial capacity to perform its duties and functions and exercise its powers.³²

Victoria's 79 councils reflect the very diverse geographic and socioeconomic circumstances of the people they represent. The reasons why councils seek higher caps are accordingly diverse. We are keen to help councils understand the system and its requirements which is why we publish this

²⁹ 'Average rates' refers to the rates paid by the notional average ratepayer. This is calculated by dividing total revenue required from rates by total number of rateable properties in each local government area.

³⁰ Section 10E, *Essential Services Commission Act 2001*.

³¹ See <https://www.esc.vic.gov.au/local-government/studies-and-reviews/local-council-outcomes-report-2019>.

³² Section 185A, *Local Government Act 1989*.

guidance for councils on an annual basis. To support this guidance, our website also contains reference information about community engagement.³³

Our role in assessing higher rate caps

Our role is to assess any application for a higher cap and to decide whether the proposed higher cap is appropriate.³⁴ We base our assessment of an application on all of the following:

- our statutory objectives to promote the purposes set out in s. 185A of the *Local Government Act 1989* (the 1989 Act) (see Box 1.1)
- the six matters specified in s. 185E(3) of the 1989 Act (see Box 1.2)
- the council's compliance history
- the council's compliance with any commission directions on the manner and form of an application.

When the assessment is finished, we publish our decision and reasons on our website and, if we approve a higher cap, we do so through a special Order published in the Government Gazette. The Order sets out the permissible percentage increase in average rates for the years specified.

³³ At <https://www.esc.vic.gov.au/local-government/resources-councils/community-engagement-resources>.

³⁴ Section 185E(6), *Local Government Act 1989*.

Appendix 2: How the rate cap works

The rate cap limits the maximum amount a council can increase its *average rates* in a rating year. The rate cap includes general rates and municipal charges only.³⁵ It does not include other charges and levies such as service rates and charges, special rates and charges, revenue in lieu of rates and the fire services levy.

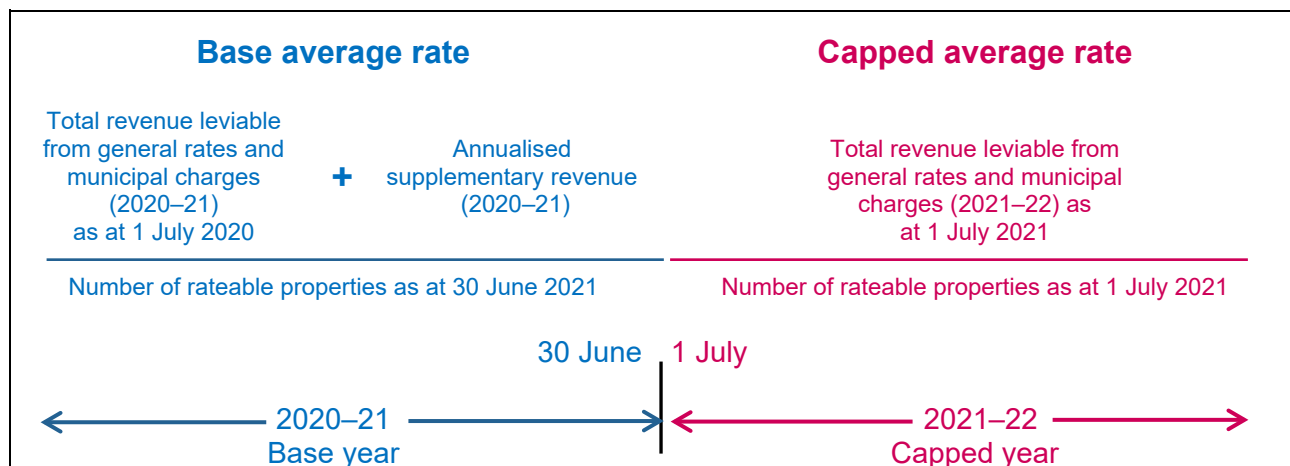
$$\text{Average rates} = \frac{\text{revenue from general rates and municipal charges}}{\text{number of rateable properties}}$$

Complying with the rate cap

A council must comply with the average rate cap set by general Order by the Minister for Local Government or a higher cap set by special Order by us (if applicable). To comply, the capped average rate must not exceed the base average rate by more than the average rate cap or higher cap.

Compliance with the rate cap in the capped year is calculated in relation to the base average rate in the preceding rating year. For the 2021–22 financial year, the base year is 2020–21 and the capped year is 2021–22. Figure 1 summarises the calculation of the base average rate and capped average rate for the 2021–22 financial year.

Figure 1 Summary of the base average rate and capped average rate



³⁵ The minister has the power to prescribe other rates and charges to be included in the rate cap.

How to calculate the base average rate

The base average rate is the total annualised revenue leviable from general rates and municipal charges as at 30 June in the base year divided by the number of rateable properties as at 30 June in the base year. This calculation is shown below.

$$\text{Base average rate} = \frac{\text{Rb}}{\text{L}}$$

Rb = total annualised revenue leviable from general rates and municipal charges on rateable properties as at 30 June in the base year

L = number of rateable properties as at 30 June in the base year

For the 2021–22 rating year:

total revenue leviable from general rates as at 1 July 2020
(excluding any allowance for supplementary general rates revenue)

+

total revenue leviable from municipal charges as at 1 July 2020
(excluding any allowance for supplementary municipal charges revenue)

Rb =

+

annualised supplementary general rates revenue as at 30 June 2021

+

annualised supplementary municipal charges revenue as at 30 June 2021

L = number of rateable properties as at 30 June 2021

Note: cultural and recreational land (as defined under the Cultural and Recreational Land Act 1963) is excluded from the calculation of base average rate.

How to calculate annualised supplementary revenue

Annualised supplementary general rates revenue

$$\begin{aligned} &= \text{(total value of land as at 30 June in the base year – total value of land as at 1 July in the base year)} \\ & \times \text{rate in the dollar} \\ &= \text{(total value of land as at 30 June 2021 – total value of land as at 1 July 2020)} \\ & \times \text{rate in the dollar (2020–21)} \end{aligned}$$

Annualised supplementary municipal charges revenue

$$\begin{aligned} &= \text{(number of rateable properties on which municipal charge is leviable as at 30 June in the base year – number of rateable properties on which municipal charge is leviable as at 1 July in the base year)} \\ & \times \text{municipal charge per property} \\ &= \text{(number of rateable properties on which municipal charge is leviable as at 30 June 2021 – number of rateable properties on which municipal charge is leviable as at 1 July 2020)} \\ & \times \text{municipal charge per property (2020–21)} \end{aligned}$$

How to calculate the capped average rate

The capped average rate is the total revenue leviable from general rates and municipal charges as at 1 July in the capped year divided by the number of rateable properties as at 1 July in the capped year. This calculation is shown below.

$$\text{Capped average rate} = \frac{Rc}{L}$$

Rc = total revenue leviable from general rates and municipal charges on rateable properties as at 1 July in the capped year

L = number of rateable properties as at 1 July in the capped year

For the 2021–22 rating year

total revenue leviable from general rates as at 1 July 2021
(excluding any estimate for supplementary general rates revenue)

Rc = +

total revenue leviable from municipal charges as at 1 July 2021
(excluding any estimate for supplementary municipal charges revenue)

L = number of rateable properties as at 1 July 2021

Note: cultural and recreational land (as defined under the Cultural and Recreational Land Act 1963) is excluded from the calculation of capped average rate.

Appendix 3: Features of good financial planning and considering 'trade-offs'

Good financial planning

Central to the Fair Go Rates system is the promotion of good long-term financial planning. Throughout this guidance, we have emphasised that applications for a higher cap are expected to demonstrate that the need for additional funds is based on and supported by rigorous and robust long-term financial planning.

A simple description of good long-term financial planning includes:

- Ensuring that the assumptions in a council's long-term plans and financial strategies are based on reasonable and reliable information, by having best-practice processes, plans and policies in place that include:
 - sound policies and practices to manage cash resources and debt
 - good asset-management plans, to identify cost-effective outlays based on properly considered and documented risk management
 - performance monitoring and reporting.
- Effectively managing areas within the council's control, to deliver services and fulfil its functions cost-effectively, through methods that include:
 - undertaking programs of continuous improvement and efficiency
 - considering options and trade-offs for different models of funding, finance and service delivery
 - seeking opportunities to collaborate with other councils in shared services, etc.
- Undertaking regular service reviews to plan and prioritise service delivery, using effective engagement practices to identify community preferences while maintaining financial sustainability.
- Providing a stable and predictable rating burden on ratepayers to avoid rate shocks.
- Updating financial plans regularly, to reflect best-available information.

Having these elements in place helps a council ensure it bases its projections of long-term revenue and expenditure on robust and timely information. Good long-term financial planning can also identify potential opportunities and constraints, to aid good decision-making.

Trade-offs

There will inevitably be ‘trade-offs’ between different options that a council can take into account to determine the most appropriate approach to meet its long-term funding need and the long-term interests of the community.

‘Trade-offs’ is a term that appears several times in this document, particularly in the context of choices presented in community engagement (Section 4.2.3), and when council is examining expenditure proposals or funding options (Section 4.2.5). When an application describes the trade-offs that were considered, we expect a clear statement that compares the financial impacts, service impacts and infrastructure impacts that arise from the choice of pursuing different options.

A council’s strategic approach to considering alternative options and their potential impacts on ratepayers and the community is a key element of sound long-term financial planning.