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27 August 2015

**Essential Services Commission
Level 7, 32 Lonsdale Street
MELBOURNE VIC 3000**

By email: localgovernment@esc.vic.gov.au

To whom it may concern,

RE: Submission on Local Government Rates Capping and Variation Framework Review

At its meeting of 26 August 2015, Baw Baw Shire Council resolved that:

Council endorse the submission to the Essential Services Commission on Local Government Rates Capping and Variation Framework Review.

I herewith provide attached, Baw Baw Shire Council's submission on Local Government Rates Capping and Variation Framework Review.

Yours sincerely,

A handwritten signature in black ink, appearing to read "Helen Anstis", written over a circular stamp or seal.

**Helen Anstis
Chief Executive Officer**

Response - Local Government Rates Capping & Variation Framework Review

A The Variation Process

The Commission have advised that each Council is expected to address the following options prior to seeking a variation to the cap.

1. Consider delivering services and projects more efficiently – Baw Baw Shire Council (BBSC) believe that a service based approach to reporting will more adequately satisfy the Commission's intent to monitor Council performance in service delivery. The service based approach is discussed later in this submission. Council also believes that the Commission reports should consider the impact of efficiency gains already built into the base line cost structure. BBSC have returned \$1.5 million in salary cost savings effective from the commencement of the current 2015/16 year with minimal scope to generate further efficiencies without impacting current service levels or service standards.
2. Ensuring the services delivered are based on community priorities – while BBSC continually deliver services according to community expectations, Council is concerned as to how the Commission proposes to assess this measure. This is particularly important given the Commission has advised that the assessment of variations will include both prescriptive and discretionary elements and that the Commission proposes to give either a 'pass' or 'fail' regarding each variation request. It is recommended that the Commission therefore provide robust feedback to Councils with regard to the more discretionary elements of the variation assessment.
3. Identifying alternate funding sources – We believe that further feedback is required regards how the Commission proposes to assess the extent that each Council has satisfied, or should satisfy, the ESC criteria for alternate funding. For example, each Council will have a different view as to their appetite for debt as a funding alternate per their respective Borrowing Policy. Non approval of a variation due to a Council's reluctance to take on additional debt may be counterproductive to the long term sustainability and a Council's view of loan borrowing. It is important that Councils do not raise additional debt for inappropriate purposes and simply as a means to satisfy the Commission's assessment criteria.

With regard to discretionary fees and charges, BBSC is scheduled to implement a more commercial based focus to user fees that is likely to identify additional funding alternatives. It is important for the Commission to articulate its expectations with regard to alternate funding particularly in light of pre-existing Council debt, each Council's appetite for new debt as well as each Council's capacity to generate other forms of revenue.

Council has identified the following concerns in response to the Commission's five matters that require consideration when seeking a variation.

1. The reason for a rate increase greater than the cap – quantification of amounts, movement in costs, variations to assets and change in service levels for every Council service are expected to require significant staff time to research, analyse, collate and report. It is important for the Commission to recognise this impost to Council resources when providing guidance and assessment to the variation process.

2. The application takes account of ratepayers' and communities' views – Council continues to engage the community with regard to the delivery of new projects and how services are delivered. A community consultation framework that includes alternate options for meeting Councils funding needs, including the ability to identify trade- offs and project prioritisation, will also require significant resources and staff commitment to develop. Council recommends that the Commission provide guidance with regard the expected engagement process to enable Councils to better utilise their limited resources in order to satisfy ESC evaluation criteria.

3. The variation represents good value-for-money and is an efficient response to the need.
While Council is able to submit business cases or cost-benefit analyses to justify the need for a variation to the cap, it is also important for the Commission to acknowledge the potential impact to services and or project delivery. Baw Baw Shire Council has implemented an organisation restructure resulting in employee cost savings in the order of \$1.5 million in response to the demands for more efficient service delivery. This initiative has enabled Council to undertake an increased capital works program. The impact of the rate cap is expected to result in Council reducing its future capital program and delaying the expected timeline to close the infrastructure gap.

4. Service priorities and funding options have been considered. The capacity to demonstrate that Council have considered reprioritising funding from other areas of expenditure, including the reasons for not proceeding with reprioritisation, will require a significant body of work to review and assess for every Council service. Such an exercise will require significant resources in order to conduct appropriate analyse, review including the need for community engagement on a service by service basis. As previously noted, the resource requirement to complete this body of work will be counterproductive to Councils capacity to generate further efficiencies in day to day operations.

5. The proposal is integrated into the council's long-term strategy. Council has a robust strategic reporting framework including community consultation and adoption of key documents including the Long Term Financial Strategy, Long Term Infrastructure Plan, Rating Strategy in addition to the statutory Council Plan and Budget reports. It is requested that the Commission provide guidance regards their expectation for integration to Council strategy documents.

Council also recommends that the variation process give consideration to the increased burden of asset management responsibilities that apply to rural Councils. The limitations of a single rate cap, based on a one size fits all approach, can be partly alleviated by the Commissions recognition of the higher rural demands for maintenance and replacement of infrastructure assets.

B The Efficiency Factor and Measurement Process

The indicative forecasts for the annual rate cap include efficiency factors of 0.05 percent and 0.10 percent for the financial years 2017/18 and 2018/19 respectively.

It is understood that the intent of the efficiency factor is to require Councils to pursue efficiencies in their operations, and that this 'benefit' be returned to ratepayers by way of a further rate cap reduction – in this case a reduction to the weighted cap calculation (60% Department of Treasury and Finance CPI and 40% Wage Price Index).

Council is concerned that the efficiency factor is now included to the rate cap as it was not identified within the original terms of reference for the rate capping review.

Subject to the completion of a robust productivity analysis we believe that the inclusion of an arbitrary efficiency factor is immature and does not reflect the efficiencies gained by Baw Baw Shire Council, as a result of reduced operating costs, that resulted in the moderate rate increases and an improved capital works program.

Introduction of an efficiency factor presupposes that the weighted average rate cap reflects the actual cost increase of local government projects and services. While Council acknowledges the Commissions inclusion of the wage price index, cost drivers are also impacted by price movements in the areas of construction, asset maintenance, waste & landfill management, utilities and fleet. Such cost drivers generally exceed the rate of increase of the consumer price index that is reflected within the rate cap.

The recently implemented organisation restructure at Baw Baw Shire Council resulting in employee cost savings in the order of \$1.5 million that reduced Council's ongoing cost base and demonstrated a significant increase in efficiency. This initiative has enabled Council to expand its capital works program while continuing to deliver essentially the same level of services. The impact of the Commissions introduction of escalating efficiency factors, that unless supported by a productively analysis, would fail to recognise the employee cost efficiencies built into the 2015/16 Budget and future financial years.

In order for the Commission to satisfy its objectives of reporting service delivery, asset management and financial performance it is important that the monitoring framework includes:

- A service based approach to the review and operating costs and
- Monitoring of capital expenditure and particularly the level of investment in capital infrastructure both before and after the rate cap.

It is understood that the Commission will only communicate if a Council has either met or not met the requirements for a variation and that the variation request will either be accepted or rejected in full. While it is accepted that it is not the Commissions role to provide an alternative variation, it is important for Councils to receive feedback regards how their requests were assessed and how future submissions may be improved particularly with regard to unsuccessful submissions.

Structured feedback to Council variations will not only support more robust future variation requests but also enable Councils to satisfy the Commission objectives for Councils to

consider delivering services and projects more efficiently, ensuring the services delivered are based on community priorities and support the identification of alternate funding sources.

The Commission has advised that guidance material will be detailed and prescriptive in some areas however will be principles-based and provide Councils with discretion in other areas of the variation process.

Community engagement model – It is important that Councils receive structured feedback particularly as the Commission has advised that it intends to be less prescriptive with regard to how the proposed community engagement principles can be operationalised. If a Council was unsuccessful in their request for a rate variation, feedback by the Commission is important in order to improve their community consultation process as well as more appropriately meet the ESC expectation both with regard to efficient service delivery and the submission of more robust variations to support the future needs of their communities.

C Reporting and Monitoring

The 'Blueprint for Change – Local Government Rates Capping & Variation Framework Review' Section 2.6, and specifically Table 2.4, sets out the indicative information for compliance with the cap and compliance with approved variations.

The Commission have identified that a working group, comprising Council sector representatives, be formed to develop the specific information to support the proposed rates capping framework.

While Council supports this approach it is important that, where possible, the Commission utilises pre-existing reporting mechanisms in order to minimise the expected additional burden on Council staff to create additional reporting requirements.

Currently Council's reporting requirements include, but are not limited to:

- Annual Financial Statements; and
- Annual Budget process that for Council includes the Council Plan, Budget, Long Term Financial Strategy / Plan, Long Term Infrastructure Plan and Rating Strategy; and
- Annual Performance Reporting Framework; and
- Victorian Grants Commission; and
- Annual acquittals for Federal and State grant funding and;
- MAV surveys – including rates survey and STEP asset management program.

Council therefore supports the Commission approach to utilise existing reporting mechanisms to limit the additional burden for Council administration.

Notwithstanding this approach, Council is concerned that the Commission's new framework will result in an increased reporting burden to local government that can only be counterproductive to the ESC expectation for Councils to demonstrate future efficiencies as expected by the introduction of the rate cap efficiency factor. Additional performance reporting, outside the already extensive reporting requirements required by local government, would also be counterproductive to the best value principles as articulated in the Local Government Act.

The proposed timelines for the 2016/17 year are extremely tight and limits the budget public exhibition period to the month of May in order to achieve statutory budget adoption by the end of June. It should be noted that some Councils preference to conduct public exhibition of their draft budget prior to the month of May will now not be possible.

The Commission has indicated that their costs in administering the cap framework may be recoverable from local government. Council strongly opposes this suggestion as the rating cap is a State Government initiative and should therefore be borne by this tier of government. To burden local government with costs of monitoring a state government function would only add to the already increased burden of cost shifting that is evident by a range of state funded services now the responsibility of local government.

D Services Based Approach

Council understands that the Commission is proposing to provide guidance regards the baseline information and evidence to enable Councils to submit variations to the rates cap.

Council believes that a service based approach to financial reporting would better support the intent of the Commission to both monitor Council performance and provide justification for an increase above the cap.

For Councils to adequately demonstrate the impact of rate capping to services, Baw Baw Shire Council believe this can be more robustly assessed by a review of the current and proposed future services costs in a rate capping environment.

Baw Baw Shire Council, as a member of the pilot Councils working group, submitted its baseline data (operating revenue and operating expenditure) according to Council's service delivery framework. Baw Baw understands that some Councils, who are members of the pilot working group, are not in favour of the service based approach. However, in order to demonstrate the impact of rate capping to services, a service based approach to the review process is necessary. While the structure and format of chart of accounts may differ from Council to Council, BBSC believe that the majority of services are common across each Council and the sector should progress towards a standard approach to the measure and costing of services.

Baw Baw Shire Council therefore concurs with the Commissions view to standardise the recording of Council inputs and outputs across the sector from a service based perspective.