



GREATER  
DANDENONG  
*City of Opportunity*

# Rate Capping and Variation Framework Submission

28 August 2015

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## 1. Introduction

The City of Greater Dandenong thanks the Essential Services Commission for the opportunity to submit a response to the 'blueprint for change' rate capping and variation framework issued by the ESC on Friday 31 July, 2015.

At the outset, Council wishes to note that there are several aspects of the draft framework where it would appear that the ESC has listened to the feedback provided by this Council and others and have made prudent recommendations in this respect.

There remains however a number of features of the proposed framework where Council has strong concerns and this submission will highlight these points.

Council looks forward to the ESC continuing to review all submissions lodged with an open mind towards further refining the draft framework.

**Mayor Sean O'Reilly**

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## 2. The Rate Cap

Council makes the following comments and observations about Section 2 of the draft rate capping and variation framework.

### 2.1 One cap or many?

The City of Greater Dandenong supports the view that there should be a single cap that is uniformly applied to local government rather than a wide range of different caps which are set at different levels for different Councils.

This position is however, completely reliant on the variation framework being flexible enough to take account of the uniqueness of each Council and its circumstances. In the initial round of consultation on the framework, the City of Greater Dandenong stated quite strongly that its ethnic diversity and socio-economic position were such factors that would need to be considered by the ESC and at this point it is not obvious that this has been accounted for in the draft variation framework.

### 2.2 Which revenues come under the cap?

Council supports the position adopted by the ESC where service rates and charges will be excluded from the rate cap. Using the 2015-16 financial year as the base year, Council accepts the future requirements to evidence that any increase in service rates and charges are matched by an equal increase in the costs associated in the provision of these services.

The exclusion of supplementary rates in the year in which they occur is also strongly supported. It is equally important that the supplementary rates be 'annualised' and added to the base for the purposes of calculating the new rate cap. It is not clear from the draft framework that this is fully understood by the ESC and a worked example of this is provided in the following section.

### 2.3 Applying the cap to Total Rate Revenue or Rates per assessment?

On the basis that supplementary rate revenue is correctly treated, Council does not see any significant difference between either using Total Rate Revenue or Rates per assessment as the basis for applying the rate cap. It is however pivotal in terms of the recognition of supplementary rate revenue.

The example below outlines the understanding of the City of Greater Dandenong of how supplementary rates should be treated under this framework.

At the commencement of the 2015-16 financial year, the below table summarises the various rates and charges that comprise the line item “Rates and Charges” in Councils Income Statement contained within the Annual Budget.

| Rating Type                                       | Assessments<br>1/7/2015 | 2015/16 Rates<br>Declared |
|---|-------------------------|---------------------------|
| General   | 51,908                  | \$ 47,251,136             |
| Commercial  | 3,201                   | \$ 11,688,214             |
| Industrial  | 5,712                   | \$ 41,994,574             |
| Vacant Residential                                | 940                     | \$ 1,227,887              |
| Farm  | 61                      | \$ 471,785                |
| <b>Total rates within the cap</b>                 | <b>61,822</b>           | <b>\$ 102,633,596</b>     |
| <b>Rates &amp; Charges outside the cap</b>        |                         |                           |
| Service Charge (Waste)                            |                         | \$ 14,738,000             |
| Supplementary Rates                               |                         | \$ 950,000                |
| Keysborough Maintenance Levy                      |                         | \$ 1,015,000              |
| Rates Abandoned                                   | -\$                     | 100,000                   |
| <b>Total Rates and charges (Income Statement)</b> |                         | <b>\$ 119,236,596</b>     |

The commencing “Rates per assessment” would then be calculated as being the 2015-16 Total rates amount of \$102.633 million divided by 61,822 assessments – equaling a figure of \$1,660.15 per assessment.

During 2015-16, Council will undertake approximately seven individual supplementary rate returns for varying portions of the year. The first supplementary return in August for example will be backdated to commence on 1 July and be for the full financial year. The final supplementary valuation return in March 2016 however, is likely to be only for the final four months of the year.

In the event that Council raises \$950,000 in revenue from all supplementary rate returns, this is likely to equate to approximately \$1.3 million should all of the supplementary changes to valuation have been applied for the full rating period.

The following example highlights how the cap should then be applied.

| Rating Type                             | Assessments<br>1/7/2015 | 2015/16 Rates<br>Declared | Rates per<br>assessment |
|---|-------------------------|---------------------------|-------------------------|
| <b>Total rates within the cap</b>       | <b>61,822</b>           | <b>\$ 102,633,596</b>     | <b>\$ 1,660.15</b>      |
| Supplementary Rates Raised              |                         | \$ 950,000                |                         |
| Supplementary Rates Annualised          |                         | \$ 1,300,000              |                         |
| <b>Total Rates and Annualised Supps</b> | <b>62,800</b>           | <b>\$ 103,933,596</b>     | <b>\$ 1,654.99</b>      |

*NB: the estimate of 62,800 for assessments at 30 June 2016 is simply a projection*

The example notes that during 2015-16, the annualised amount of the supplementary rates raised should be added to the base amount declared in the Annual Budget. The rates per assessment must be further amended to take account of any increase in the number of assessments to arrive at the amended rates per assessment figure. It is on this newly calculated base from 2015-16 that the rate cap percentage is then applied for 2016-17.

Council seeks confirmation that the above example mirrors the interpretation that the ESC is seeking to apply to supplementary rate revenue.

## 2.4 How should the rate cap be calculated?

The City of Greater Dandenong remains firmly of the view that CPI is not an appropriate indicator of local government costs but does note that the ESC are restricted by the terms of reference provided to it by the State Government.

Whilst it remains preferable for an agreed local government cost index to be determined, Council agrees that where CPI must be utilised, the application of a forecast, underlying CPI figure as estimated by DTF is the best option.

Council further supports the concept of including a percentage allocation of the rate cap to be calculated reflecting the significance of employee costs in driving overall local government expenditure increases. However, Council submits that the 40% proposed allocation to this is too low and doesn't accurately reflect the proportion of employee costs in local government.

Based on the 2013-14 Annual Financial Statement released by the 30 Melbourne metropolitan Councils (excluding City of the Melbourne), the overall share of employee costs as a percentage of cash operating costs was 46%. For the City of Greater Dandenong that percentage is 53%.

| All Melbourne Metropolitan Councils 2013/14 |                  |
|---|------------------|
|   | Amount           |
| Total Operating Costs                       | \$ 4,304,915,000 |
| Less Depreciation                           | \$ 327,774,000   |
| Less Asset Adjustments (non cash)           | \$ 19,184,000    |
| Total Adjusted Operating Costs              | \$ 3,957,957,000 |
| Total Employee Costs                        | \$ 1,803,466,000 |
| <b>% Employee Costs</b>                     | <b>46%</b>       |

Source: 2013/14 Annual Financial Statements

The second major concern with what has been proposed by the ESC is the use of the WPI as the indicator of local government wages. This Council strongly advocates that the index that should be used instead is a weighted average of the Enterprise Agreements of the 79 Victorian Councils.

Many Councils are already locked into three-year Enterprise Agreements and will have no ability to influence wage outcomes until well into the rate capping framework.

It is further acknowledged the ESC will have concerns that by utilising the Enterprise Agreement framework within Local Government may reduce the level of efficiencies sought by the industry. To counter that, the negotiation of an industry wide Agreement dealing with the quantum of any increase, should be part of the industry reform with Councils retaining individual powers negotiate only the associated conditions

The final concern with this section of the framework is the proposed application of an efficiency factor.

What the current report fails to acknowledge at any point is how the application of the current Local Government Interim Award impacts on Councils wage costs.

At present, there are two sources of wage cost increases that Council has to fund. The first is the cost from the annual percentage increases that apply to all Council staff as negotiated in the various Enterprise Agreements. The second relates to the banding structure under the Local Government Interim Award.

The vast majority of Council staff are banded within an 8 level band structure – and then within these bands are generally three or four levels (A,B,C,D). Employees progress along the band levels each year until they reach the end of the band. This structure adds approximately 0.5-0.7% to Councils total annual labour costs increases, which are in addition to those contained in the Enterprise Agreement.

A 3.0% Enterprise Agreement will therefore cost Council 3.5% per year as an increase in total employee costs.

These costs –which stem from the structure of the Interim Award – should either be a) recognised in the wage element of the how the cap is calculated or at worst b) should represent any efficiency factor and negate the need for the ESC to escalate an artificial percentage which Councils cannot meet.

## 2.5 What is the base year for setting the cap

Council agrees that 2015-16 financial year should form the base year for the rate cap subject to its comments presented in Section 2.3.

## 2.6 What information will be required each year?

There are no concerns expressed with meeting the information requirements outlined in Section 2.6 other than to again note that the supplementary rates should be based on an annualised rather than actual basis.

### 3. The variation process

The City of Greater Dandenong makes the following observations on the proposed variation process as outlined in Section 3 of the draft framework

#### 3.1 Why is a variation process needed?

Council is in agreement with points made in this section with two important departures.

The draft framework continues to stress that all other avenues for funding must be explored prior to Council seeking a rate variation. Council disagrees with this assertion in that raising rates may just be the most equitable means of securing additional funding.

At present Council utilises a significant differential rating structure in order to minimise the rating impact on its relatively poor residential sector. Whilst Council's overall rates per assessment are slightly above average, Council's residential rates per assessment are well below average which is reflective of this outcome.

It should further be noted that this rating structure is encapsulated in Councils documented Rating Strategy which is placed out to the community for public comment every two years.

There may well be scenarios where Council could be required to double fees and charges in order to meet the ESC criteria of exploring all other avenues for funding – yet doing this is likely to penalise an already low socio-economic residential sector that will then be unable to afford to utilise many services.

As noted in Councils previous submission to the ESC, many of Councils facilities and services have utilisation rates well in excess of other municipalities due to the community need for these services and the inability of many residents to access or afford these services from other sources.

Council accepts that all other options may be considered but does not accept an outcome where all other options need to be actively pursued prior to the ESC openly considering an application for a variation to the cap.

Council's final point in this section is to ensure the ESC has a realistic understanding of the significance of the total revenue received from fees and charges over which Council has control of the pricing level. As indicated in baseline financial data recently supplied to the ESC, discretionary fees and charges make up just 6.5% of Council's total cash revenue.

In situations where the City of Greater Dandenong seeks a rating variation, quite simply an increase in the discretionary fees and charges revenue will not make any significant impact.

#### 3.2 When can Councils seek a variation

Council notes the preference of the ESC to not outline in any detail what it perceives to be the triggers that would qualify for a variation to the cap. Council accepts that by doing this, the ESC also notes that there are no circumstances under which Councils should be prohibited from seeking a variation but remains concerned whether the ESC will genuinely take account of the special needs of the Greater Dandenong community.

### 3.3 How would a Council demonstrate the need for a variation?

The City of Greater Dandenong supports most of the content contained in this section and in particular the need to evidence the reason for a rate increase greater than the cap, the need to demonstrate the application is an efficient response to the need and the incorporation of the proposal into Council's long-term strategy.

Council does however, hold significant concerns regarding what would appear to be the current ESC position in terms of community consultation prior to a variation application proceeding.

In particular two comments from the “*Questions, Actions and Evidence for a Variation Application*” are highlighted:

- “Is a rate increase the preferred option of the community/ documented evidence of the community satisfaction with the proposed variation”
- “Community survey results showing preference for rate increases /relative to service reductions”

Both of these requirements set the community consultation bar beyond what can realistically be achieved, bearing in mind that Council rates are a property tax and have no direct correlation to the services an individual consumes.

It would be entirely reasonable to expect Council to conduct community consultation for a proposed variation and the reasons as to why Council is seeking the variation. It is unreasonable however for the outcome of the variation application to hinge on a Vaux pop outcome of community views. Irrespective of how much a variation may be needed for the overall community wellbeing, it is very unlikely to receive popular support from a majority of the community.

An example was recently provided to the ESC of much needed community infrastructure in one section of Council – which is likely to be supported by that section of the community, but unlikely to win much support from the balance of residents who will not access these facilities.

The current approach put forward by the ESC fails to pay regard to the fact that Councillors are elected under the Local Government Act (1989) to make decisions based on the good governance of the entire Council, and in the best interests of the community. The proposed rate capping and variation framework should not act to fetter these responsibilities.

### 3.4 Who decides whether a variation is approved?

Council agrees with the view contained in the draft framework that the ESC be the responsible body for assessing and determining the response to all applications.

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### 3.5 What decisions should be made in response to an application?

The draft framework highlights the ESC position that applications for a variation will either be rejected or accepted in full with no negotiation over any potential middle ground. Whilst it is understood why the ESC has recommended this outcome, this lack of any flexibility is likely to ultimately work against the efficient functioning of the rate capping and variation model.

For Council to make a case for a rate increase of 5% and for the ESC to be 80% convinced the case has been made (but without the ability to approve a slightly lesser outcome) will mean this same Council being restricted to the rate cap for a further twelve months.

This is neither a common sense nor pragmatic outcome for any of the parties involved.

### 3.6 How difficult will it be to have a variation approved?

Council notes the views expressed by the ESC that 'we do not expect a large number of applications each year' and is concerned by the position that this comment portrays to the industry – being one of discouraging applications.

Council further notes the comments contained in the section regarding the ESC seeking to not routinely become involved in Councils' rating decisions and not wishing to intrude on the autonomy of Councils.

For the many reasons already outlined in this submission, whether this occurs in the early years of this rate capping and variation framework or takes several years to manifest itself – ultimately virtually every Council will at some point need to pursue a rate variation or alternatively risk running services and facilities into the ground.

## 4. Monitoring and reporting

The City of Greater Dandenong provides the following responses to this section of the draft framework.

### 4.1 Why is a monitoring regime important?

Council readily accepts the need for a strong monitoring regime where Council can provide detailed base line data annually to the ESC. It is the view of Council that this information will readily show the endeavours Council has made over time to save expenditures.

Council notes the comment made by the ESC about the data supporting comparisons between Councils, however the composition of the respective communities and structures of the various organisations will always render direct comparisons as slightly ineffective and dangerous to be relied upon.

### 4.2 What makes a good monitoring regime?

Council agrees with the view expressed that the ESC should make use of data already provided by Council where possible and minimise the additional reporting burden.

### 4.3 How adherence with the cap be monitored?

Council notes the proposed actions to be taken by the ESC in the event it is considered a Council has breached the rate cap. Council would expect in any such investigation that individual Councils would be fully consulted with and involved in any investigation to enable them to show cause why a breach has not occurred.

### 4.4 Monitoring overall outcomes for the community?

The City of Greater Dandenong has been involved with the trial exercise to establish base line financial data to be submitted to the ESC and is satisfied with the outcomes of that trial. Council notes the concerns from the NSW experience where the most significant adverse outcomes came from Councils not pursuing a rate cap variation.

Where these adverse impacts are noted by the ESC over a trend period in Victoria, it is essential they be acted upon with haste rather than for a community to reach a point where any improvement would require a significant rating shock. To this end, Council suggests the ESC has a proactive role in encouraging rate variation applications rather than simply reporting outcomes to the Minister.

### 4.5 Public reporting

Council notes the proposed reporting framework. Council has strong concerns in regard to the annual timetable which is discussed in the following section.

## 5. Implementing the framework

The City of Greater Dandenong provides the following responses to this section of the draft framework.

### 5.1 What will be the timelines for the capping and variation process?

In the first year of implementation of the rate capping and variation process, it is understood that timelines will be somewhat compromised due to the legislation to enact rate capping not being finalised until December, 2015. This will then lead to a compressed time period for the first year in terms of making applications for a variation and the consideration of these application by the ESC.

In future years however, this should not be the case yet the draft framework does not provide for a more strategic approach in the years that follow.

For the 2016-17 year, the timetable for the 2015-16 Annual Budget is copied below for the information of the ESC.

| Date   | Activity   |
|--|--|
| Wednesday 8 April 2015<br>Wednesday 15 April 2015  | Council briefings on the draft Budget.   |
| Thursday 23 April 2015                             | Proposed Budget document completed and distributed to Council.                       |
| Monday 27 April 2015                               | Proposed Budget submitted to Council for approval at an Ordinary Meeting of Council. |
| Wednesday 29 April 2015                            | Public notice advising intention to adopt budget.                                    |
| Wednesday 29 April 2015 –<br>Wednesday 27 May 2015 | Public submission process undertaken.  |
| Wednesday 27 May 2015                              | Closing date for submissions on the Proposed Budget.                                 |
| Thursday 11 June 2015<br>(to be confirmed)         | Submissions considered by Council/Committee.   |
| Monday 22 June 2015                                | Budget and submissions presented to Council for adoption.                            |

Ideally Council should be in a position by the end of March, 2016 to know it either has an approved variation to the rate cap or alternatively must prepare a 2016-17 Annual Budget on the basis of rate cap. The timetable produced by the ESC will mean that Council will

have to work on the basis that a variation will not be approved with the ability to then add key infrastructure projects at the eleventh hour should that not be the case.

In future years, without the restriction of enabling legislation and other matters, this above outcome can easily be avoided by bringing forward the process.

The City of Greater Dandenong believes the following timelines would make more sense:

- The ESC announce an interim cap for the following year in July of each financial year based on the May forecast provided by DTF;
- Councils prepare their long-term financial models during September and October and consult with the community on various community priorities and needs;
- Council's who wish to submit a variation application do so by early December (6 ½ months prior to the start of the next financial year);
- The ESC provides an update in December of the rate cap forecast from DTF. (Note it is the view of this Council that movements of up to 0.5% in this forecast will have zero impact on any decisions to apply for a variation. Variation applications almost universally will be for a higher rate increase than this over the cap.)
- The ESC consider applications received and provide an answer on all applications not later than 28 February;
- Councils can then run the remainder of their budget processes in full knowledge of the rate increase to be applied.

Council does not support the notion contained in the draft framework for the later adoption of Budgets (e.g. August).

## 5.2 Are special transitional arrangements required?

Based on the above information, the City of Greater Dandenong would continue to argue that a transition arrangement for year one would be preferable.

Council has previously noted in this submission its opposition to the efficiency factor and this being set at zero for year one has no bearing on Council's potential need to seek a variation application.

Council has a well established process for strategic planning and community consultation but the timelines for 2016-17 will most certainly be onerous and require decisions to be made that do not accord with the best interests of full and detailed community consultation.

The ESC has commented that its expectations of the rigour of applications in the first year will be different from the expectations it will hold after a few years of experience with the framework. The prudent exercise of this judgement will be essential in the first year.

## 5.3 What about the costs of administering the framework?

Council strongly objects to the cost of administering the rate capping and variation framework being passed on to local government in any form.

## 6. Over the longer term

The City of Greater Dandenong provides the following responses to this section of the draft framework.

### 6.1 When should a comprehensive review be undertaken?

The City of Greater Dandenong believes that a review following the initial two years of operation would be preferred, with future reviews after this occurring every four years. For a period of four years to elapse with no review over something that has the potential to have a very detrimental impact on local government is too long in the initial phase of introduction.

### 6.2 What is still required to drive efficiency?

The implementation of rate capping with a base of CPI combined with a WPI factor will in itself ensure that the rate cap is set well below the annual cost of providing local government services.

As previously highlighted in this submission, Councils are locked in to Enterprise Agreements and beyond this must pay a loading of approximately 0.5-0.7% per annum in wages due to the structure of the Interim Award. This coupled with the fact that the vast majority of other products that Council purchases do not align with CPI –the very starting basis of this model will mean that Councils will quickly be forced into reducing some services and critically evaluating whether it continues to participate in others.

Most Councils' can today identify the resources used to produce different outputs and generate unit costs for the outputs they produce. The commentary in the section however continues to pursue a 'standardisation' of Councils which fails to recognise the very differing nature of Councils from each other.

The City of Greater Dandenong disagrees with the recommended directions within the report which seeks standardised recording of inputs and outputs including standardised definitions and measures.

It is the view of this Council that the ESC should be more concerned about the changes that occur within unique Councils over a trend period rather than efforts to turn all Councils into the same basic service model that does not fit the very different needs of diverse communities.

### 6.3 Should Councils be given any guidance on their financing options?

In its submission to stage 1 of the rate capping and variation process, the City of Greater Dandenong highlighted to the ESC that it has not been averse to prudently using debt funding as a source of funding to achieve key infrastructure objectives. This Council is however now reached its maximum responsible debt level and the future use of debt funding will be restricted from this point. Council trusts that this factor will be considered by the ESC in future variation applications.

#### 6.4 Should there be greater cost reflectivity in some rates and charges?

Council agrees that service rates and charges should not exceed the respective *direct and indirect* costs of providing these services. Using the 2015/16 financial year as the baseline data, Council would be happy to provide financial expenditure data that would verify any movement in these charges are reflected by an equal increase in Council costs.

Council further supports that statutory fees should be subject to far more regular review and indexation – and that failure for this to occur should form a valid ground for future applications for rate variations.

## 7. Recommendations

Throughout this submission, detailed comment has been made on the recommendations made by the ESC for the rate capping and variation framework. Rather than repeat this information, the below points highlight this Council's recommended *changes* to the draft framework released by the ESC.

- Whilst Council supports the concept of introducing a percentage of the cap to be linked to a wage index, this index should be the weighted average of local government enterprise agreements for the forthcoming financial year;
- Noting the perception that this may not drive local government efficiency, it is recommended that industry reform be implemented leading to a single enterprise agreement for local government to be negotiated at State level rather than all 79 municipalities negotiating their own agreement;
- The proportion of the labour index (as a % of the calculation) should be increased to a minimum of 45% to reflect the real cost of wages as a percentage of cash expenditures;
- The framework needs to recognise that in addition to enterprise agreement percentage increases, the Interim Award banding structure adds between 0.5 and 0.7% per annum in addition to this cost. This either needs to be added on to the wage index or alternatively any notion of an efficiency factor needs to be abandoned.
- Council disagrees with the viewpoint that all other avenues for funding need be explored prior to lodging an application for a variation. For very good equity reasons, raising the funding gap via rates may result in a far better community outcome than by increasing fees and charges.
- The framework suggests in a number of places that for a variation application to be successful, it must show that a rate increase beyond the rate cap has community support. Council is accepting of the need for community consultation but setting the bar at a level where an increase in taxation must attract broad community support is beyond the levels imposed on any Commonwealth or State Government taxation. The framework should simply require Council to evidence it has undertaken broad community engagement;
- Whilst Council can understand the reluctance of the ESC to approve in 'part' some variation applications, the adoption of a complete 'black or white' outcome lacks flexibility and may act to the serious detriment of communities who will be forced to wait a further twelve months for the next round and deal with a worsening financial situation;
- Council has concerns over the ESC's desire to 'standardise' Councils which it believes fails to recognise the inherent unique characteristics and communities that are served by each Council;
- Council acknowledges the difficulties with timing in the first year of operation of rate capping and variations. Council has submitted a draft timetable for future years that would alleviate this and provide a much greater strategic window for community consultation to occur and for existing Budget timetables to be maintained;

- Council continues to support a transition period in 2016-17, particularly in light of this being both a revaluation year and an election year;
- Council strongly objects to the cost of administering the rate capping and variation framework being passed back to local government;
- Following the initial introduction of the rate capping and variation framework, an initial review after two years of operation is considered to be more ideal. Review periods can lengthen after this but it remains critical to address any concerns regarding the implementation at the earliest possible point;