

18 February 2008

Mr John Salerian
Assistant Commissioner
Local Government Revenue Raising Study
Productivity Commission
LB2 Collins Street East
MELBOURNE VIC 8003

By email: localgov@pc.gov.au

Dear Sir

Re: Draft Report – Assessing Local Government Revenue Raising Capacity

The Australian Local Government Association (ALGA) welcomes the opportunity to comment on the draft report of the Commission's Study into Local Government Revenue Raising Capacity.

Individual councils may be providing comment on the details of the draft report and state local government associations will also be providing comment on the report.

ALGA has already provided a submission to the Commission and our comments on the draft report will be limited to its broad findings.

ALGA views the report as a valuable contribution to the understanding of all spheres of government about the revenue environment facing local councils and we are pleased that the report acknowledges the diversity of local government bodies and the substantial variation in reliance on different sources of revenue. ALGA has long made the point that rural and remote councils are for the most part reliant on government grants, particularly the Commonwealth's Financial Assistance Grants (FAGs).

Quality of Data

ALGA continues to have concerns about the quality of some of the underlying data about local government revenue in particular although we note that this is an area which has not been commented on nor does it appear to be of concern to the Commission. ALGA's concerns reflect the difficulty we had in obtaining data from the Australian Bureau of Statistics (ABS) and the clear errors which occurred in some ABS data tables, such as those relating to the amount of state government funding provided to local government. There were instances of double counting where Federal funding to local government was provided through the states.

ALGA has raised these concerns with Commonwealth and State Officials and directly with ABS officers and there is currently work underway to try to improve local government data collected by ABS. ALGA is surprised that the Commission appears not to have confronted similar issues.

Conclusions about Rates as a proportion of GDP

The Commission concludes that Local Government Revenue is around 2% of GDP. ALGA accepts that the proportion is in the order of 2.5% and has been relatively stable at that level over recent years, certainly since 1999-2000 (ABS Cat 5206.0 and DOTARS Local Government National Report, various years).

The Commission finds that the ratio of rates revenue to GDP decreased from 1.1% to 0.9% between 1990-91 and 2005-06 and appears to imply this has been a lost revenue opportunity. The Commission notes that had the ratio remained at 1.1% national revenue from rates would have been 20% higher – an extra \$1.7b.

ALGA does not believe that the issue is that clear. The National Inquiry into Local Government Finance in 1985 (the Self Report) estimated local government rate revenue in 1980-81 to be \$1,498.4 million and revenue from fees and charges to be \$156.3 million out of total revenue of \$3,107.4 million. Rate revenue accounted for 48.2% of total revenue and revenue from fees and charges accounted for just over 5%. The combined revenue from the two sources was about \$1,655 million or just over 53% of total local government revenue.

In 2005-06, revenue from Rates and fees and charges (sale of goods and services) accounted for an estimated 69% of local government revenue. It would appear that while rates have declined in relative terms as a source of revenue, local government's revenue raising effort has been maintained through the substitution of sale of goods and services (cost recovery). The draft report implies that the Commission may be treating rates as the "base level" of funding for local government with fees and charges levied to provide additional services. If so, then ALGA has some difficulties with such an assumption.

The trend has been towards cost recovery where appropriate and it is reasonable to expect that there would have been a reduction in the relative importance of rates as goods and services, such as the cost of permits and entry to local government owned facilities such as swimming pools and caravan parks, moved to cost recovery instead of being funded by general rate revenue. ALGA does not agree that this indicates a failure of local government to exploit revenue sources and sees this as a useful area for further work by the Commission.

ALGA does not dispute the usefulness of using GDP as a frame of reference against which to measure local governments overall revenue sources although it should be noted that rates are a property tax, reflecting property values & GDP is an income measure. ALGA has long been concerned about the declining level of Financial Assistance Grants although the frame of reference we have used is FAGs as a proportion of Commonwealth revenue. Taxation revenue may perhaps be seen as a reasonable proxy for GDP. FAGs, as a proportion of Commonwealth revenue, declined from 1.01% in 1995-96 to just 0.71% in 2008-09. This is a far steeper decline than the

decline in rates identified by the Commission. ALGA has called for the restoration of FAGs as a proportion of Commonwealth taxation revenue (excluding GST) If FAGs were restored to the level of 1% of Commonwealth Taxation revenue (excluding GST) in 2008-09. Local government would receive an additional \$620 million.

Fiscal Capacity

The Commission asserts that, on average councils, are raising about 90% of their hypothetical benchmarks in own source revenue. To ALGA this seems a relatively high level of exploitation of revenue. ALGA notes that the Commission stresses that the scope for raising additional revenue should not be taken to imply that local government's should increase the revenue they raise.

ALGA would argue that the services government provides to the community need to be considered as a whole as do the taxes and charges for government services paid by communities.

Over the period 2000-01 to 2005-06, ABS figures (Cat 5506) show that total taxation revenue increased by 39.05%. Commonwealth income taxation revenue increased by 41.4% over that period but local government rate revenue increased at a higher rate - 41.5% - over the same period, from about \$6.3b to \$8.9b. ALGA argues that this demonstrates an appropriate level of exploitation of taxation opportunities by local government. In addition, over the same period, local government fess and charges, according to the Commission, increased from about \$5.6 billion to more than \$6.9 billion in real terms – an increase in revenue of \$1.3 billion.

As with other levels of government, the Productivity Commission does conclude that the major constraint on local government raising additional taxation revenue appears to be the democratic process. ALGA agrees with that point, noting that local communities do not generally distinguish between different spheres of government in terms of services and infrastructure provided, and nor do they distinguish between the spheres of government in terms of taxation paid. It is difficult for local government to argue that rates need to increase to pay for government services at the local level when the Federal Government runs a surplus in excess of \$10 billion per annum.

Legislative Restrictions on Revenue Raising

The ALGA supports the Commission's conclusions that a wide variety of legislative and regulatory restrictions are imposed by jurisdictions on the raising of own source revenue although the Commission concludes that only in NSW do the rate pegging and concessions appear to be significant impediments. ALGA is concerned about the decision of the Northern Territory to introduce rate pegging which will have a significant impact on local government revenue.

ALGA questions the Productivity Commission's conclusion that while rate exemptions and concessions limit revenue from particular groups, this impost is, at least partially, offset by reciprocal tax arrangements and reimbursements. Further there is scope for raising higher revenue from remaining taxpayers.

While there is a reciprocal taxation agreement in place in Tasmania, other jurisdictions decided not to pursue that course in response to a recommendation in the Hawker Report which favoured reciprocity. ALGA and state and territory local government associations were also not in favour of reciprocity. The additional suggestion of the Commission that other rate payers be charged more does not seem an appropriate suggestion.

This approach of qualifying or excusing the seriousness of the problem for local government is also evident in the finding that while statutory fee setting and other constraints limit the ability of councils to raise revenue from the sale of some specific goods and services, this is likely to be somewhat offset by flexible fee setting arrangements for many other goods and services, as well as from rates revenue. ALGA does not accept that the solution to the problem is to ignore it and try to charge other users or rate payers more than would otherwise be the case.

Principles for Improved Financial Management

The Australian Local Government Association supports an improved framework for financial management in local government and has supported work through the Local Government and Planning Ministers Council to improve the financial and asset management frameworks applying to local councils.

ALGA looks forward to the finalisation of the Productivity Commission's Report and to the further discussion of broader issues of local government funding at a future meeting of the Council of Australian Governments.

Yours sincerely

Adrian Beresford-Wylie
Chief Executive