Department of **Local Government and Regional Development**
Government of **Western Australia**

Submission

Productivity Commission Draft Report - Assessing Local Government Revenue Raising Capacity

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Department of Local Government & Regional Development

2 Havelock Street, WEST PERTH WA 6005

Telephone (08) 9217 1500   Facsimile: (08) 9217 1555

Website: www.dlgrd.wa.gov.au

Introduction

This submission has been prepared by the Department of Local Government and Regional Development in response to the Productivity Commission's Draft Research Report (the Report) *Assessing Local Government Revenue Raising Capacity*. The Department would like to express its appreciation for the opportunity to comment on the Draft Report.

The purpose of this submission is twofold. Firstly, in observation of the data displayed in Table 5.3 and Table 5.5 and 5.6, the Department seeks further clarification the capacity for local governments with exceptionally high incidences of rates to increase their own source revenue.

Secondly, the Department requests that the Productivity Commission, in preparation of its final report, examine Commonwealth Financial Assistant Grants (FAGs) in the context of a relaxation model for the minimum grant principle. The Department is of the view that this may provide some opportunity to address the sustainability concerns of rural and remote local governments.

Financial Assistance Grants

The revenue raising efforts (own source revenue divided by fiscal capacity) of local governments analysed in the Report indicate that rural and remote councils have the highest level of revenue raising effort among the ACLG categories. This result confirms the findings of several other recent studies on the financial sustainability of local government in WA and nationally.

The Report also confirms that rural and remote communities incur a higher incidence of rates (total rates paid the community divided by the aggregate income of that community) and higher levels of rates per capita than their urban counterparts.

In addition, the Productivity Commission has found that a significant increase (10%) in own source revenue would still leave 73% of rural and 91% of remote local governments dependant on grant funding[1]**.**

The revenue raising effort for rural and remote local governments is, in some cases, well in excess of the level of effort for other ACLG categories. Table 5.3 in the Report indicates that the median revenue raising effort for rural and remote councils is 8.0 and 17.6 respectively, well above the median effort of between 3.1 and 6.8 for the other ACLG categories[2]. This suggests that there is little scope for remote local governments to increase their revenue raising effort.

However, this is not the inference that is drawn from Table 5.5 and 5.6 of the Report which highlights the potential of local government ACLG categories to increase their own source revenue and total revenue. The median estimated indices of relative

[1] Productivity Commission, 2007.

[2] Productivity Commission, 2007.

potential to increase own source revenue (Table 5.5) suggests that urban local governments and rural and remote local governments have similar capacity to increase own source revenue.

The Department's experience is that the position of rural and remote local governments is reflected more accurately in Table 5.3. With the highest level of revenue raising effort, the highest incidence of rates and limited opportunity to develop sources of non-rate revenue the Department considers that the capacity for rural and remote communities to increase their own source revenue is severely constrained. Opportunities to improve rural and remote financial sustainability in Western Australia are largely confined to measures that promote economies of scale such as voluntary amalgamation and resource sharing.

Further, as rural and remote local governments generally incur the highest per capita rate incidence relative to urban local governments and, on average, have the lowest level of fiscal capacity, any increase in revenue raising is likely to lead to a disproportionate impact on individuals in these communities.

Broadly speaking, local governments raise revenue to fund activities required by their roles and functions and to deliver a wide range of services to their community. Own source revenue is a major source of such funds but not the only source of funding. This Department is of the view that consideration of local government own source revenue must be placed within a total budgetary context, irrespective of whether within an annual or longer budgetary cycle. In particular, it is important to note how the different components of a local government's budget interact and impact upon each other.

One such example is Commonwealth Financial Assistance Grants (FAGs). Through the budgetary process, FAGs impact upon revenue raising effort and rate incidence in different classes of local government. As this issue is closely related to the capacity of local governments to raise revenue to match their budgetary requirements, consideration of the impact of FAG allocation appears to be consistent with the Commission's Terms of Reference.

The Department is of the view that a review of the methodology employed for the allocation of FAGs may provide an opportunity to reduce the pressures on rural and remote local governments without significantly impacting upon rating effort or rates incidence in urban and larger local governments. As such, the Department would like to see the Productivity Commission undertake further quantitative work and analysis on the impact of the removal of the minimum grant condition in FAG allocation. The minimum grant condition, including a relaxation model for WA, is discussed in further detail below.

Minimum Grant Condition

The minimum grant condition (which requires a minimum payment to all local governments of not less than 30% of what they would receive if grants were allocated on a per capita basis) results in many local governments receiving more than an equalisation entitlement of revenue. This is at the cost of other local governments having their grant revenue factored back[3], with the greatest impact falling onto rural and remote local governments.

There is also evidence to suggest that the impact of the minimum grant has grown significantly in recent years. Table 1 is taken from the 2005-06 Local Government National Report and shows the number of local governments on the minimum grant[4] 1996-97 to 2006-07.

Table 1: Number of Local Governments on Minimum Grant 1996-97 to 2006-07

	NSW	Vic	Qld	WA	SA	Tas	NT	Total
1996-97								
Number of Local Governments	21	5	0	14	4	1	0	45
% of population	22	10	0	43	10	10	0	15
2006-07								
Number of local governments	21	10	2	30	22	1	1	87
% of population	25	18	37	75	55	10	36	33

(Source: DOTARS, 2007)

Research undertaken by DOTARS[5] indicates that from 1995-96 to 2005-06 the per capita funding for rural and regional local governments increased by 38 per cent, compared to 8 per cent for local governments in major cities. However, it was also stated that:

"…continuation of this trend will be increasingly constrained as the number of urban local governments on the minimum grant increase and there becomes less potential for these local governments to incur any further reduction in grants."[6]

Extensive modelling was conducted by the Western Australian Local Government Grants Commission (WALGGC) to ascertain the impact of a decline in the minimum grant entitlement from 30% (current minimum grant entitlement) to 0% (complete removal), including the amount of revenue available for redistribution in WA. The results are available in Table 1 below:

[3] In Western Australia, the factoring back ratio was 91% in 2005-06, using relatively conservative WALGGC methodology.

[4] Note: the methodology for determining minimum grant payment differs between States.

[5] DOTARS, 2006.

[6] DOTARS, 2006.

Table 2- Minimum Grant Relaxation and Redistributed Funds WA 2006-07

Minimum Grant	Total Received By Minimum Grant LGs	Total Redistributed Funds	Minimum Grant LGs
30%	$25,946,506	$0	31
25%	$20,085,284	$5,861,222	30
20%	$15,479,930	$10,466,576	29
15%	$10,815,905	$15,130,601	28
10%	$7,028,077	$18,918,429	27
5%	$3,447,000	$22,499,506	26
0%	$0	$25,946,506	0

(Source: WALGGC, 2007)

As expected, the results show that a decrease in the minimum grant entitlement would lead to a higher allocation of funding for non minimum grant councils[7], with a further $25,946,506 available for redistribution. It is noted that the number of local governments on the minimum grant entitlement declines with a reduction in the minimum grant.

Table 3 below is also taken from the WALGGC data and illustrates the impact on two local governments- Stirling, a minimum grant council, and Halls Creek, a rural remote council, of a decrease in the minimum grant entitlement. The complete removal of the minimum grant entitlement results in an increase in FAG funding by almost 25% for this rural remote local government.

Table 3 Minimum Grant Relaxation Model for Stirling and Halls Creek 2006-07

Halls Creek				Stirling			
2006/07 Grant	Per Capita Amount	% increase	% of Total Revenue	2006/07 Grant	Per Capita Amount	% increase	% of Total Revenue
2,790,805	30%	0.0%	31.5%	3,128,346	30%	0.0%	2.58%
2,926,233	25%	4.9%	33.0%	2,606,955	25%	-6.6%	2.15%
3,049,432	20%	9.3%	34.4%	2,085,564	20%	-25.3%	1.72%
3,165,270	15%	13.4%	35.7%	1,564,173	15%	-44.0%	1.29%
3,273,690	10%	17.3%	36.9%	1,042,782	10%	-62.6%	0.86%
3,379,283	5%	21.1%	38.1%	521,391	5%	-81.3%	0.43%
3,483,571	0%	24.8%	39.3%	0	0%	-100.0%	0.00%

(Source: WALGGC, 2007)

[7] Analysis assumes the removal of the maximum drop principle.

It is further evident from Table 3 that a decrease in the minimum grant has a varying level of impact between the two councils. A decrease in the minimum grant would see only a 2.58% drop in revenue for Stirling; however, the redistribution of funds would see an increase in the percentage of revenue from 31.5% to 39.3% for the Shire of Halls Creek.

Given that local government sustainability can be considered in the context of total revenue- own source revenue and grant funding- an increase in revenue of this capacity represents a significant boost to the sustainability levels of rural and remote local governments. Further, in consideration of the impact of the relationship between grant funding and own source revenue, the removal of the minimum grant may result in a more equitable incidence of rates between the ACLG categories.

Appendix One

Table 1 shows large variations in regional shares of Commonwealth financial assistance grants in Western Australia.

Table 1: Regional Shares of Commonwealth Financial Assistance Grants in Western Australia 2006-07

Region	**Share of Population %**	**Share of Grants %**	**Average Grants per capita**
Gascoyne	0.5	4.8	$559
Goldfields-Esperance	2.7	7.2	$156
Great Southern	2.7	5.2	$112
Kimberley	1.8	9.8	$316
Metropolitan	72.9	24.1	$19
Mid West	2.5	11.5	$266
Peel	4.6	3.6	$45
Pilbara	2.0	7.2	$213
South West	7.0	7.2	$59
Wheatbelt	3.5	19.4	$321
Total	**100.0**	**100.00**	**$58**

(Source*:* WALGGC, 2006)

Reference

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