INSURANCE COUNCIL
OF AUSTRALIA

Local Government Study
Productivity Commission
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6 July, 2007

Dear Productivity Commission

Productivity Commission Study into Local Government Revenue Capacity

The Insurance Council of Australia is pleased to provide the following submission into the commissioned study on local government revenue capacity.

Statutory Funding of Fire Services

The Productivity Commission Issues Paper seeks submissions on how existing statutory constraints on local government impact on the performance of local government. The Insurance Council particularly wants to draw to the attention of the Commission the impact of the fire service funding models in NSW and Victoria and in particular how these models serve to constrain local government financial capacity. [1]

The relevant legislation with respect to fire services funding that impacts on local government in New South Wales and Victoria is as follows:

New South Wales

- Division 2, Section 50 of the *NSW Fire Brigades Act 1989* wherein local government is required to meet 12.3% of the NSW Fire Brigade budget
- Division 5, Section 109 of the *NSW Rural Fires Act 1997* wherein local government is required to meet 13.3% of the NSW Rural Fire Services budget

Victoria

- Section 37 of the *Metropolitan Fire Brigades Act 1958* wherein local government is required to meet 12.5% of the Victorian Metropolitan Fire Brigade budget.

[1] NB: The insurance industry currently contributes 73.7% of the funding for the NSW fire services (Metropolitan and Rural); 75% of the funding in Metropolitan Victoria and 77.5% of the funding for the Victorian Country Fire Authority. The Insurance Council has previously submitted to government and decision makers in NSW and Victoria that funding of the fire services is in need of reform including ensuring that the funding of the fire services is placed on a more efficient, equitable and transparent basis. For further information see The Insurance Council of Australia: "*The Non Insured: Who, Why and Trends*" (May, 2007)

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Statutory fire contributions imposed by legislation serve to leave a significant impost on local authorities, which is in turn exacerbated at a time of escalating budgets within the fire brigades. The table overleaf outlines the extent to which the NSW Fire Authorities have seen their budgets increase over the past ten years.

NSW Fire Authority Outlays

	NSW Fire Brigade Outlays ($m)	% change	NSW Rural Fire Service Outlays ($m)	% change
Yr Ending June				
2007	496.0	5.5	256.7	45.0
2006	470.3	4.6	177.0	22.2
2005	449.6	8.7	144.8	4.2
2004	413.5	10.1	139.1	-37.5
2003	375.7	6.2	222.5	16.0
2002	353.6	6.8	191.9	107.3
2001	331.1	4.8	92.6	10.9
2000	316.0	6.5	83.5	4.9
1999	296.9	9.0	79.6	-10.2
1998	272.4		88.6	
Average % change		***6.9***		***18.1***

Source: NSW Budget Papers, Various

As the table demonstrates, funding for the NSW fire authorities in total has doubled between 1998 and 2007. As a result, the statutory fire contributions from NSW Councils has increased from $45.3 million in 1997/98 to $95.1 million in 2006/07 - an average annual growth rate of 9%.

The Insurance Council submits that the statutory contribution model adopted by the NSW and Victorian governments to fund the fire authorities is conducive to poor budget oversight and fiscal supervision of the fire authorities. In particular, in NSW and Victoria where the fire authorities are able to fund the bulk of their operations "offline"[2], the expenditure review that arises from competing and contestable resource requirements within State government is necessarily diminished. Fire authorities are able to secure enhancements to both operating and capital conditions without reference to overall State fiscal circumstances and accordingly, the natural rationing process that may arise for other State government outlays does not present itself for the fire authorities.

[2] NSW and Victorian fire authorities fund the majority of their operations from statutory contributions from licensed insurers and local government.

Under the current statutory contribution system, incentive for effective budgetary management is reduced. Fire authorities are able to make enhancements to their operations (both recurrent and capital) and effectively shift the cost burden of these enhancements to other exogenous statutory funders – namely local government and insurers. Funding of the entity is ultimately disconnected from both the fire brigade management and the owners of the fire brigades themselves (ie the respective State governments). Diseconomies are further exacerbated by the inability of the statutory funders to exercise any control or supervision over the outlays themselves - leaving them to effectively fund the enhancements without an ability to review, control or ration their appropriateness.

The fire funding systems in Victoria and NSW were subject to review in 2003 and 2004 respectively.[3] However, in the case of the Victorian review the statutory contributions from local government was not considered as part of the review.[4] The NSW Public Accounts Review highlighted the inequity of the local government contributions. [5]

The Insurance Council submits that the statutory contribution model for funding the fire services is outdated and in need of urgent reform. In particular, the Insurance Council submits it would improve local government capacity fundamentally if the burden of having to fund statutory fire contributions was to be removed as part of an overall fire funding reform. The Insurance Council also believes that there are present more appropriate models under which the fire brigades can be funded, namely the approach adopted in Western Australia.The Insurance Council recommends to the Productivity Commission that it consider the overall funding models of the NSW and Victorian fire authorities as part of the constraint on local authorities in these jurisdictions.

Risk Mitigation in Local Government

The Insurance Council is of the view that local government is an important partner in managing risk with the insurance sector. In particular, the Insurance Council submits that the capacity for local government to fund and support capital expenditures in risk mitigation works is essential. For example, the ability of local government to improve the conditions of roads is important in mitigating the risk of personal injury and property damage arising out of motor vehicle incidents. Similarly, the ability of local government to support risk mitigation works such as flood levies is important in combating the risk of property damage for businesses and households.

The Insurance Council is keen to ensure that solid capacity exists within local government to fund and undertake mitigation works. To this extent, the need to ensure that local government budgets are primarily geared towards capital outlays as opposed to recurrent outlays is supported. To the extent that the limited resources of local government are being utilised to support recurrent spending at the cost of a capital program, the task of effective risk mitigation is diluted.

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[3] See NSW Public Accounts Committee (2004) "*Review of Fire Services Funding*" & Victorian Department of Treasury & Finance (2003) "*A Review of Victorian Fire Service Funding Arrangements*".
[4] See Victorian Department of Treasury & Finance (2003), *ibid*, at page 20
[5] See NSW Public Accounts Committee (2004),*op cit*, at page 61

The Insurance Council notes that local government has available to it funding under the National Disaster Mitigation Program for the purposes of supporting risk mitigation works. According to the Commonwealth Budget Papers, funding under this program amounted to $22.5 m in 2006/07 and is estimated to be $43.6 m in 07/08, after which the program is to be reviewed. [6] The program funds mitigation works on the basis of a 1/3, 1/3, 1/3 formula between Federal, State and Local Government.

The Insurance Council would like to see the program maintained but also improved to allow works in local government jurisdictions which may lack the capacity to fund their component of the works. This particularly applies to those regional and rural areas where local government funding capacity is restricted. However, the Insurance Council believes that where local government capital capacity is compromised because of an emphasis on recurrent outlays, shortfalls in funding should not be met by either the State or Commonwealth in such instances.

Conclusion

Local government and the insurance industry share a common objective in reforming the contributions model of fire services funding in NSW and Victoria. The Insurance Council contends that the Productivity Commission would be well placed in recommending that NSW and Victoria review their fire services contribution model as it applies to both the local government and insurance sectors.

Furthermore, both local government and the insurance sector share an interest in ensuring that appropriate capital expenditure is available for the purposes of risk mitigation. The Insurance Council believes it is appropriate that in its deliberations, the Productivity Commission consider the balance of capital versus recurrent outlays in local government so as to ensure that resources are available for investments in local risk mitigation.

The Insurance Council submission draws these issues to the attention of the Commission. If the Commission requires any further elaboration on the matters raised in this submission, please do not hesitate to contact me on (02) 9253 5130 or email asanchez@insurancecouncil.com.au.

Yours sincerely

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[6] See Commonwealth Budget Paper No 3 "*Federal Financial Relations 2007/08*" at pages 64 and 76.