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## 2 Local government in Australia

### Key points

- The Australian local government sector is characterised by a high degree of diversity in terms of its functions, characteristics and revenue sources.
- Local governments are increasingly providing services beyond their traditional role of services to property, to include greater involvement in human services, planning and regulatory functions.
  - Local government spending is predominantly in the areas of property-related services, roads, recreation, health and welfare services.
- Property rates and revenue from fees and charges account for most of local government own-source revenue. The shares of these revenue components as a proportion of total revenue have decreased slightly in recent times.
- At a national level, rates revenue is a small share of total taxation revenue collected by all levels of government. The ratio of own-source revenue, including rates, to gross domestic product is also small.
- The evidence suggests that both the ratio of rates revenue to GDP and household disposable income, at a national level, decreased between 1990-91 and 2005-06.
- Between 1998-99 and 2005-06, the decline in the ratio of local government rates revenue to gross state product occurred exclusively in New South Wales, Queensland, Western Australia, Tasmania and the Northern Territory.
- The levels and shares of local government revenue sources vary considerably at the state level, reflecting a multitude of factors including differences in legislative frameworks, the functions of local government in different jurisdictions and patterns of demography and regional development.

Local governments play an important role in Australian society through their delivery of goods and services, and their regulation and planning activities. They exhibit considerable diversity in relation to their functions, inherent characteristics and revenue sources, both within and between the States. In this chapter, an overview is provided of local government in Australia, both at a national and state level. An introduction to the institutional arrangements under which local governments operate and a brief profile of local governments across Australia are provided in section 2.1. The roles and functions of local governments and trends in local government expenditure are examined in section 2.2, including how these

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have changed over time. The sources of revenue collected by local governments are described in section 2.3. Recent trends in revenue raising by local governments are described to provide an indication of the aggregate level of revenue-raising effort in the sector.

## 2.1 An introduction to local government

An introduction to the local government sector in Australia is set out in this section, including institutional arrangements, local government powers to raise revenue from various sources and the diversity that exists within the sector.

### Institutional arrangements

The Commonwealth Constitution does not establish or recognise local government in Australia. Most local governments in Australia are statutory bodies created under State legislation to provide good governance and a range of services to their communities. It is the Constitution Acts of the States that provide for systems of local government.<sup>1</sup> The Constitution Acts are statutes of the State Parliaments and permit the State Governments, by resolutions of varying forms, to create or abolish a system of local government, dismiss councillors and appoint administrators, change council boundaries and abolish individual municipalities (DOTARS 2006).

It is principally the Local Government Acts that provide the legal and regulatory frameworks within which local governments carry out their functions. In addition, there are many other pieces of legislation that affect them; for example, planning and development legislation. These frameworks determine the functions and revenue-raising powers of the local government sector. Local governments typically possess a governing board (council) elected from and by its constituents, which is headed by a chairperson (usually the mayor) and an executive arm (which might include the general manager or chief executive officer).

Although most local governments are established under State local government acts, these are not the only entities recognised as constituting local governing bodies. In particular, a number of other bodies established under other State legislation, or 'declared' to be local governing bodies by the Commonwealth Minister, are eligible

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<sup>1</sup> Although the Northern Territory does not have a Constitution Act, a system of local government is provided for by the *Northern Territory (Self-Government) Act 1978* and the *Local Government Act 1993*. The Commonwealth Parliament also legislated self government in the Australian Capital Territory, which has responsibility for both state and local government functions.

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to receive financial assistance from the Australian Government under the *Local Government (Financial Assistance) Act 1995*.<sup>2</sup> These include two village committees within the unincorporated areas of New South Wales, the Lord Howe Island Board, the Outback Areas Community Development Trust in South Australia, the Roads Trust in the Northern Territory and some Indigenous community councils.

Although not formally recognised in the Commonwealth Constitution, over the past decade the local government sector has become a regular participant in national forums. The Australian Local Government Association (ALGA), recognised as the peak national representative body for local governments in Australia, is a member of:

- the Council of Australian Governments (made up of the Commonwealth and State heads of Government and the president of ALGA)
- the Local Government and Planning Ministers' Council
- other ministerial councils including the Regional Development Council.

In 2006, an Intergovernmental Agreement on Establishing Principles Guiding Inter-Governmental Relations on Local Government Matters was signed by ALGA, the Australian and State Governments. The objective of the Agreement is to obtain greater consultation and financial transparency between the three spheres of government in relation to local government services and functions.

At the state level, there are a variety of arrangements and forums through which state-based local government associations (LGAs) interact with State Governments, both formally through partnership agreements and informally. The LGAs represent the interests of their member local governments by providing a leadership and service role. They seek to promote good practice in the sector by providing assistance in a wide range of areas including:

- financial management
- procurement services
- risk management (including workers compensation and professional and public liability insurance)
- industrial and workplace relations

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<sup>2</sup> There were 663 local governments and 37 declared bodies in 2005-06 (DOTARS 2007). The number of local governing bodies has decreased over time due to amalgamations of some councils in some states, mostly recently in Queensland. Proposed amalgamations in the Northern Territory will significantly reduce the number of councils during 2008.

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- occupational health and safety
  - education and training.

In addition, there are a number of professional bodies in which state or local government officials participate; for example, the Australian Chief Executive Officers Group and Local Government Managers Australia.

Local governments sometimes establish cooperative bodies, such as Regional Organisations of Councils (ROCs) and county councils to collaborate on functions, services and issues of common interest. ROCs are voluntary associations of councils with nominated representatives, an agreed constitution and a formal set of objectives. Their activities can include coordinated research, regional strategies, resource sharing, advocacy and implementation of programs of other levels of government. There are currently 64 ROCs in Australia (ALGA 2007).

Somewhat similar to ROCs, county councils comprise a number of constituent councils which are located within an operating area and have a governing body elected by the constituent councils. Most county councils are formed to facilitate joint responsibility for management and provision of particular services or infrastructure. An example is the Richmond River County Council, which comprises three councils, is responsible for management of flood control infrastructure. The Riverina Water County Council supplies water to a number of local government areas in southern New South Wales.

The ACT is a self-governing territory under the *Australian Capital Territory (Self-Government) Act 1988* (Cwlth). The Act does not provide for a separate local government entity in the ACT (ACT Government, sub. 59). The ACT Government undertakes those functions that would otherwise be performed at the council level, including collection of property rates. It is not possible to separate its Territory functions from its local government functions. Therefore, the ACT Government is omitted from the analysis of local government functions and revenue sources reported in this chapter and elsewhere in this study.

### **Diversity in local government**

In 2005-06, there were 701 local governing bodies (including the ACT) eligible to receive financial assistance grants from the Australian Government (DOTARS 2007). Of these, 37 were declared local governing bodies.<sup>3</sup> Together, they directly employ around 168 000 people and are responsible for management of

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<sup>3</sup> See appendix B for an explanation of local governing bodies.

an estimated \$183 billion of non-financial assets and infrastructure (ALGA unpublished). The ratio of local government revenue (including grants) to GDP in 2005-06 was approximately 2.5 per cent.

Local governments differ in many ways, including the scope and scale of their functions, as well as their size, economic, geographic, environmental and social characteristics. Some dimensions of their diversity are illustrated in table 2.1.

**Table 2.1 Selected characteristics of local governing bodies by jurisdiction**  
1 July 2006<sup>a</sup>

<i>Jurisdiction</i>	<i>NSW</i>	<i>Vic</i>	<i>Qld</i>	<i>SA</i>	<i>WA</i>	<i>Tas</i>	<i>NT</i>
Number of LGBs	155	80	157	74	142	29	64
Area (sq km)							
Minimum	–	3	–	–	2	80	–
Median	2 689	1 532	2 422	984	2 000	1 158	5
Average	4 568	2 841	11 153	2 102	17 515	2 379	1 453
Maximum	53 511	22 087	117 084	8 860	378 533	9 750	28 700
<b>Total</b>	<b>708 067</b>	<b>227 316</b>	<b>1 751 096</b>	<b>155 581</b>	<b>2 487 130</b>	<b>68 982</b>	<b>92 989</b>
Population (no)							
Minimum	57	3 191	57	67	150	877	–
Median	20 357	39 744	3 558	8 282	2 743	11 454	530
Average	41 339	62 774	25 234	20 838	14 156	16 733	3 016
Maximum	283 458	217 349	971 757	154 514	182 047	65 021	69 262
<b>Total</b>	<b>6 773 615</b>	<b>5 021 886</b>	<b>3 961 698</b>	<b>1 542 033</b>	<b>2 010 113</b>	<b>485 263</b>	<b>193 035</b>
Road length (km)							
Minimum	–	7	2	–	9	154	5
Median	881	1 293	834	941	738	437	145
Average	895	1 615	904	1 018	866	485	220
Maximum	3 245	5 168	5 562	3 882	4 147	980	2 145
<b>Total</b>	<b>143 782</b>	<b>129 171</b>	<b>174 522</b>	<b>75 310</b>	<b>122 993</b>	<b>14 079</b>	<b>14 108</b>

<sup>a</sup> LGBs are local governing bodies. – Nil or zero. Some LGBs have no population, such as the Northern Territory Roads Trust. Similarly, some LGBs have no incorporated area and road lengths.

Source: DOTARS (2007).

The area of local governing bodies in 2006 ranged from 2 square kilometres for Peppermint Grove in Perth to 378 533 square kilometres for East Pilbara Shire in northern Western Australia. Some local governing bodies in New South Wales, Queensland, South Australia and the Northern Territory have no defined area. Either their boundaries are not legislatively defined (such as some Indigenous community councils) or they are not responsible for providing property-related services within a particular area of land (such as the Outback Areas Community Development Trust in South Australia and the village committees in New South Wales).

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Median population per local governing body in 2006 ranged from 530 in the Northern Territory to 39 744 in Victoria. Brisbane City Council currently has a population of over 970 000 and Ugar Island (Queensland) has a population of only 57 people.

The length of roads for which local governing bodies were responsible in Australia in 2006 ranged from 2 kilometres for Ugar Island to 5562 kilometres for the Brisbane City Council. The median length of roads ranged from 145 kilometres in the Northern Territory to 1293 kilometres in Victoria. Some local governing bodies in New South Wales and South Australia do not have local road responsibilities (DOTARS 2007).<sup>4</sup>

Local governments are also diverse in terms of a number of other features, including:

- the State legislative framework within which they operate
- the extent and nature of economic activity in their areas
- functions
- per person incomes
- the demography of their populations
- the extent of population growth or decline
- the management capacity and skill base of their councillors and staff
- the attitudes and aspirations of their local communities
- the significance of grants as a source of revenue.

The Commonwealth Grants Commission (CGC) (2001), in its review of the operation of the *Local Government (Financial Assistance Act) 1995* (Cwlth), noted that there are major differences in form, governance and responsibilities between States. These include differences in the methods for calculating rates, the extent of local government involvement in providing water and sewerage services, and the proportion of State land that is governed by local governments (incorporated land).

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<sup>4</sup> This includes the Lord Howe Island Board and the Silverton and Tibooburra village committees in NSW.

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## 2.2 Roles and functions of local governments

Local governments across Australia have a variety of roles and functions and deliver a wide range of services. Under State legislation, they have the authority to provide for ‘good governance’ through powers of general competence conferred on them. That is, they are able to take on roles not precluded by other legislation (DOTARS 2007). In addition, local governments are designated as responsible authorities for the purpose of undertaking functions and providing services on behalf of other levels of government. The main roles of local governments include:

- governance and advocacy
- planning and community development
- regulation
- provision of infrastructure
- service delivery.

Local governments have legislative and regulatory functions defined in statutes that enable them to make and enforce local laws within their jurisdiction. They are also responsible for undertaking land-use and environmental planning decisions and for approving development applications.

Major functions of local governments involve providing goods and services that are *public* goods or have natural monopoly or externality characteristics. This includes certain physical infrastructure such as local roads, bridges, water drainage and some health services. If left to private sector markets alone, it is likely that there would be under-provision of these goods and services (box 2.1). As a result, it is likely to be necessary and desirable for local government to provide such services. It is generally not feasible to impose user charges to finance provision of infrastructure services such as local roads. Therefore, local governments use rates, grants, or forms of indirect charging to provide these types of infrastructure services.

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### Box 2.1 Roles of local government

Some reasons for local governments to provide services include:

- *Public goods* — services that, over a defined geographic area, are non-rival (consumption by one person will not diminish the consumption by another) and non-excludible (once provided, no one can be excluded from consumption of them whether or not they offer to pay). Such goods would be under-provided by private markets. Public good characteristics can be found in goods and services such as local roads, environmental management (such as catchments management, parklands and gardens), and planning and development approval processes.
- *Externalities* — services for which production or consumption decisions by one party have *spillover* effects (positive or negative) for those not party to the decision and for which the decision-maker has no incentive to take into account. If left to unregulated private markets, such services would be under- or over-provided. In the case of local governments, spillover benefits are *internalised* through, for example, subsidies (paid from rates) that ideally reflect the nature and size of the spillovers. Such services include public health programs, such as immunisation services at community health centres, libraries and waste collection services.
- *Natural monopolies* — infrastructure with substantial economies of scale (decreasing average costs as the scale of provision increases) which, as a result, can be provided at least-cost by a single provider. These include local roads, bridges, footpaths, freshwater and sewerage networks, stormwater drainage and waste collection services.

*Source:* Based on Productivity Commission (2001).

Generally, local governments have the legal ability to provide a range of services within their local government areas, charge for their services and enter into contractual arrangements. Local governments determine the services they provide according to local needs and the requirements of legislation. In practice, the range of services provided by local government varies widely across Australia, reflecting differences in legislation, population and geography, as well as history, community preferences, and the willingness of communities to pay for the services. A broad set of examples of services provided by local governments is given in table 2.2. Some functions and services are undertaken jointly by local governments and other spheres of government, notably health and social services.

**Table 2.2 Local government functions and services**

<i>Function/service category</i>	<i>Service examples</i>
Engineering and infrastructure	Public works design, construction and maintenance of roads, bridges, footpaths, drainage, cleaning, waste collection and management.
Property-related	Domestic waste management including solid waste and recycling services, water and sewerage. <sup>a</sup>
Administration, regulation and planning	Land use and town planning (including heritage), development approvals, building inspection, <sup>b</sup> licensing, certification and enforcement, administrative functions related to aerodromes, quarries, cemeteries, parking stations and street parking.
Environmental and health	Catchments management, parks and gardens, tree removal, pest and weed control, water sampling, food sampling, immunisation, toilets, noise control, meat inspection and animal control.
Community and social	Aged care and child care services, health clinics, youth centres, community housing refuges and facilities, counselling and welfare services.
Recreation, cultural and education	Swimming pools, recreation centres, community halls, sports facilities, lifeguards, camping grounds, community festivals, libraries, art galleries, theatres and museums.
Other	Bus services, abattoirs, sale-yards, markets and group purchasing schemes.

<sup>a</sup> Provided by some local governments in New South Wales, Queensland and Tasmania only. Some local governments in South Australia are involved in the operation of effluent drainage schemes. <sup>b</sup> Local governments in the Northern Territory do not have development planning and building regulation functions.

Source: DOTARS (2007; sub. 38); PwC (2006); IIFS (2006).

## International comparisons with Australian local government

The roles and functions of local governments, and correspondingly their significance as a sphere of government, differ significantly across countries. Most local governments in Australia have a relatively small role compared with other developed countries. Comparisons with countries with *unitary* systems of government, such as the United Kingdom, are less relevant. This is because local governments in such countries are often used as administrative arms of the central government to deliver services (such as health and education) which, in federations would reside with autonomous intermediate (State, Provincial or Lander) governments. However, even when compared with other federal countries (such as the United States, Canada and Germany), local governments in Australia have very limited functions, lower expenditure shares, and lower tax sources available to them. Local government revenue constituted less than 3 per cent of total taxation revenue in Australia in 2004 compared with almost 15 per cent in the United States and about 8 per cent in Canada and Germany (OECD 2006).

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The Canadian federal system consists of multiple levels of government like Australia. These include a federal government, provincial governments and local governments. Canadian local governments consists of municipal governments and smaller specific-purpose local authorities, which are mostly school boards (Shah 2006). The authority of Canadian local governments is derived from provincial governments. Municipal services include transportation (roads), emergency services, property-related services, land-use planning and social and health services. Local government's share of total government spending in Canada has decreased largely because expenditure by provincial governments has increased, mainly in social service areas, particularly health (Shah 2006).

Germany's federation consists of the central government, 16 States (Lander) and almost 14 000 municipalities which form part of 323 rural districts. Municipalities are responsible for expenditure on education, fire departments and sporting and cultural facilities. Most municipalities own and operate special-purpose associations for waste management, electricity and water supply. Accountability for some areas of expenditure is not clearly defined between spheres of government in Germany; for example, the distribution of social welfare grants (Shah 2006).

New Zealand has a unitary system within which the local government sector consists of both regional and territorial councils (which include district and city councils). The main functions of territorial councils are similar to those of Australian councils. However, regional councils undertake a number of functions that are outside the scope of Australian local governments, such as civil defence preparedness, harbour navigation and safety, marine pollution and some water management (PwC 2006). Similar to Australia, New Zealand local government has undertaken a number of reforms, including amalgamations, and has moved beyond delivery of traditional core services.

## **How have the roles of local governments been changing?**

The scope of local government functions and service provision has changed significantly over time. Local government in Australia developed largely during the late nineteenth and early twentieth centuries. Local governments evolved as local governing authorities which initially provided basic municipal services and local roads within communities. Local government roles, responsibilities and service provision have evolved in response to demographic changes, local preferences and settlement trends. This has included increased urbanisation, growth of major regional centres, declining rural populations and the ageing population (ALGA unpublished). Development of individual local governments has varied between and

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within states, depending on historical events and enthusiasm for local government (Dollery, Crase and Johnson 2006).

At the time of federation, Australian local governments were largely responsible for delivering physical services to property (*roads* and *rubbish*). After World War II, local governments extended their services beyond traditional services to include town planning, building and health standards and, later, welfare and recreation services. Local government also intensified its role in road provision, particularly in rural areas. Over time, some local governments have ceased control of a number of services due to their inability to achieve scale efficiencies and coordinate service delivery across council boundaries. This includes electricity, gas, public transport and, in some areas, water and sewerage (Dollery, Crase and Johnson 2006).

There has been a particularly notable transition of local government roles, from being essentially providers of property-related services to increasing involvement in the provision of social services, including health and welfare services, community housing and recreation and sporting facilities. Provision of a broader range of services and increased service standards have occurred in many council areas. Local governments have also been actively promoting economic development in their areas (SCEFPA 2003).

The CGC (2001, pp. 52–3) identified the main reasons for increases in local government service provision and expenditure to include:

- (i) *Devolution* — where another sphere of government gives local government responsibility for new functions.
- (ii) *Raising the bar* — where another sphere of government, through legislative or other changes, increases the complexity or standard at which a local government service must be provided, which increases its cost of service.
- (iii) *Cost shifting* — where there were two types of behaviour. The first is where local government agrees to provide a service on behalf of another sphere of government but funding is subsequently reduced or stopped, and local government is unable to withdraw because of community demand for the service. The second is where another sphere of government ceases to provide a service and local governments voluntarily decide to provide the service.
- (iv) *Increased community expectations* — where the community demands improvements in existing local government services.
- (v) *Policy choice* — where individual LGBs [local governing bodies] choose to expand their service provision. (CGC 2001, pp. 52–3)

A number of cost shifting issues raised by the CGC were examined in a report by the Hawker Committee (House of Representatives SCEFPA 2003), *Rates and Taxes: A Fair Share for Responsible Local Government*. One of the key recommendations of the report was the development of an inter-governmental

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agreement to identify local government roles and address cost shifting. Subsequently, the Intergovernmental Agreement on Establishing Principles Guiding Inter-Governmental Relations on Local Government Matters was signed in 2006. The agreement provides a framework for the delivery and funding of services and functions to the community at the local level on behalf of other levels of government. It will be reviewed, and compliance with it assessed, within five years. Disputes can be considered by the Local Government and Planning Ministers' Council.

## **Local government expenditure**

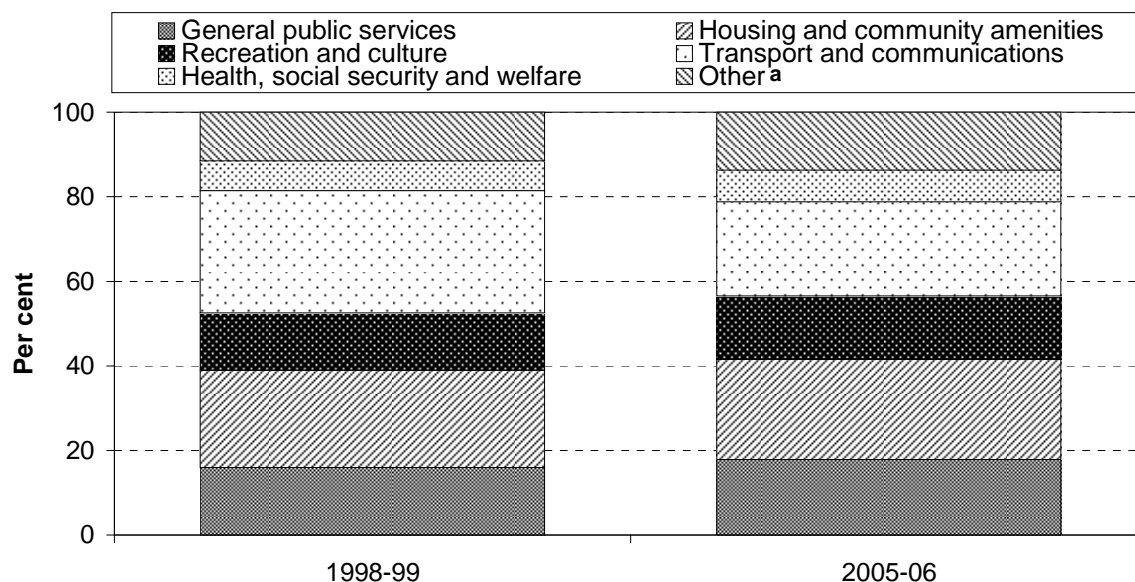
A national picture of local government expenditure by function and service is presented in figure 2.1.

The four largest shares of local government expenditure are in the following areas:

- transport and communication (including road construction and maintenance, parking, rail and air transport, community transport and communication technology)
- housing and community amenities (including housing and community development, water supply, household garbage and sanitation, sewerage and street lighting)
- general public services (including administrative functions such as executive, legislative and financial affairs and expenditure not classified elsewhere)
- recreation and culture (including public halls, swimming pools, national parks and wildlife, libraries, museums and art galleries).

The share of total expenditure on housing and community amenities and general public services has remained fairly constant in recent years. The share of transport (roads) and communications spending decreased from 29 per cent of total expenditure in 1998-99 to 22 per cent in 2005-06. The shares of other categories have increased slightly, including general public services, recreation and culture, and other expenditure.

Figure 2.1 **Local government expenditure by function**  
Shares, selected years



<sup>a</sup> Other includes public order and safety; education; fuel and energy; agriculture, forestry and fishing; mining, manufacturing and construction; other economic affairs; and other purposes.

Source: ABS (2007g); Productivity Commission calculations.

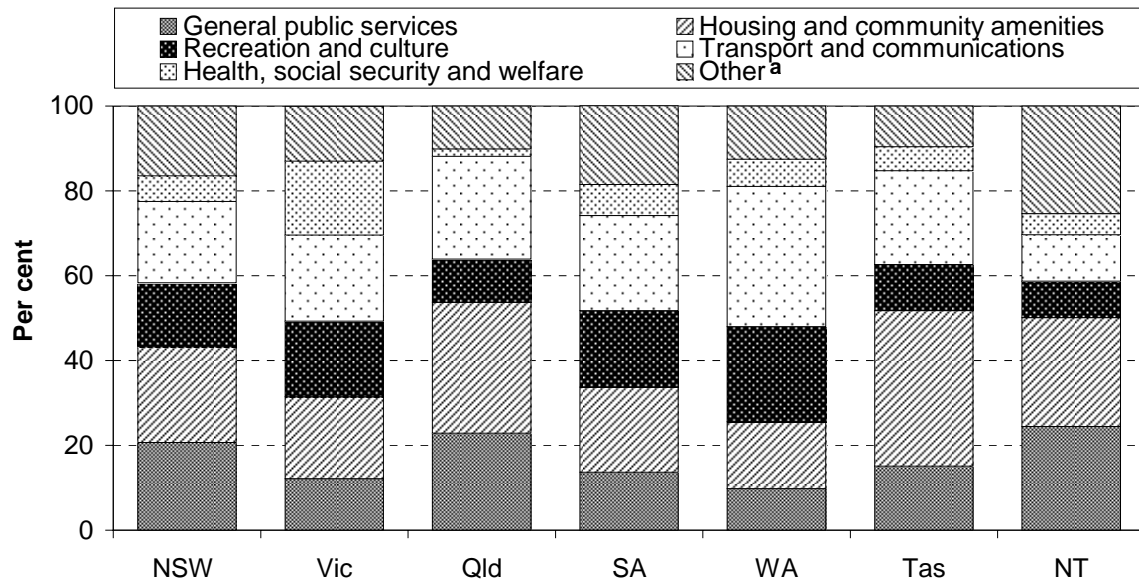
The shares of local government expenditure by State are illustrated in figure 2.2. There is considerable variability between jurisdictions, reflecting a range of factors, some of which include:

- Queensland, Tasmanian and some New South Wales councils provide sewerage and water supply services
- a large proportion of councils in Victoria provide some health and community services on behalf of the Australian and the Victorian Governments<sup>5</sup>
- councils in Western Australia and Queensland are required to maintain a larger network of local roads
- the Brisbane City Council provides urban public transport services.

<sup>5</sup> Victorian local governments deliver 80 per cent of Home and Community Care (HACC) services in the State. Comparatively, the local government sectors in other states are 'minor' providers of the HACC program (MAV 2007).

Figure 2.2 **Local government expenditure by State**

Shares, 2005-06



<sup>a</sup> Other includes public order and safety; education; fuel and energy; agriculture, forestry and fishing; mining, manufacturing and construction; other economic affairs; and other purposes.

Source: ABS (2007g); Productivity Commission calculations.

## 2.3 Revenue sources of local government

The revenue-raising powers and the sources of local government revenue are discussed in this section.

### Local government revenue-raising powers

Australian local governments are empowered through State legislation to raise revenue through:<sup>6</sup>

- council rates and charges on property
- user fees and charges
- interest

<sup>6</sup> Local governments are local governing bodies established under State legislation. Local governing bodies also includes *declared bodies*, which are provided with financial assistance grants and treated as councils for the purposes of grant allocations (DOTARS 2007). However, they may have different legislative requirements than councils, as explained in appendix B.

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- fines and other penalties
  - developer charges and contributions.

Rates levied on property are the only source of tax revenue available to local governments. Within limits, local governments can alter the level and composition of rates revenue by altering the percentage rate in the dollar applied to the rateable value of property, the structure of rates, the categorisation of land and the valuation method applied to each land category (in some jurisdictions). Local governments are generally permitted to differentiate the rates levied according to the nature and use of property (for example, residential or commercial use). The ability of local governments to raise rates revenue can be subject to regulatory limits, such as rate pegging, provisions relating to the method for land valuation assessments, and rate exemptions and concessions. In some States, categorisation of land is explicitly specified in legislation, while in others, more flexible rating regimes are allowed. Rates levied on property owners often include a minimum amount or a fixed charge in addition to an *ad valorem* amount of a rate levied on the value of land.

The legislative and regulatory frameworks in each jurisdiction generally permit local governments to collect a wide range of fees and charges, including service and utility charges, regulatory fees and other fees for service. The levels of some charges are statutorily set, however, most are discretionary. Generally, legislation provides for local governments to impose charges in addition to, or in combination with, rates. This includes the application of service and special charges to recover the costs of providing a particular service (for example, rubbish collection, water and sewerage) or funding an activity that benefits land holders in a specific area (for example, environmental programs). Local governments are generally empowered, through planning and development legislation, to raise revenue from developer charges and contributions for economic and social infrastructure.

In addition to State legislative frameworks, the requirements of National Competition Policy (NCP) can impact on the revenue-raising powers of local governments. This may occur where fees and charges for significant business activities are required to be set on the basis of recovering full cost (competitive neutrality) or where prices are subject to prices monitoring (NCC 2000).

Local governments also earn interest income from cash investments, securities and other financial assets. Local governments are typically permitted to invest in Commonwealth or State government securities, or a financial institution that is approved or guaranteed by the State.

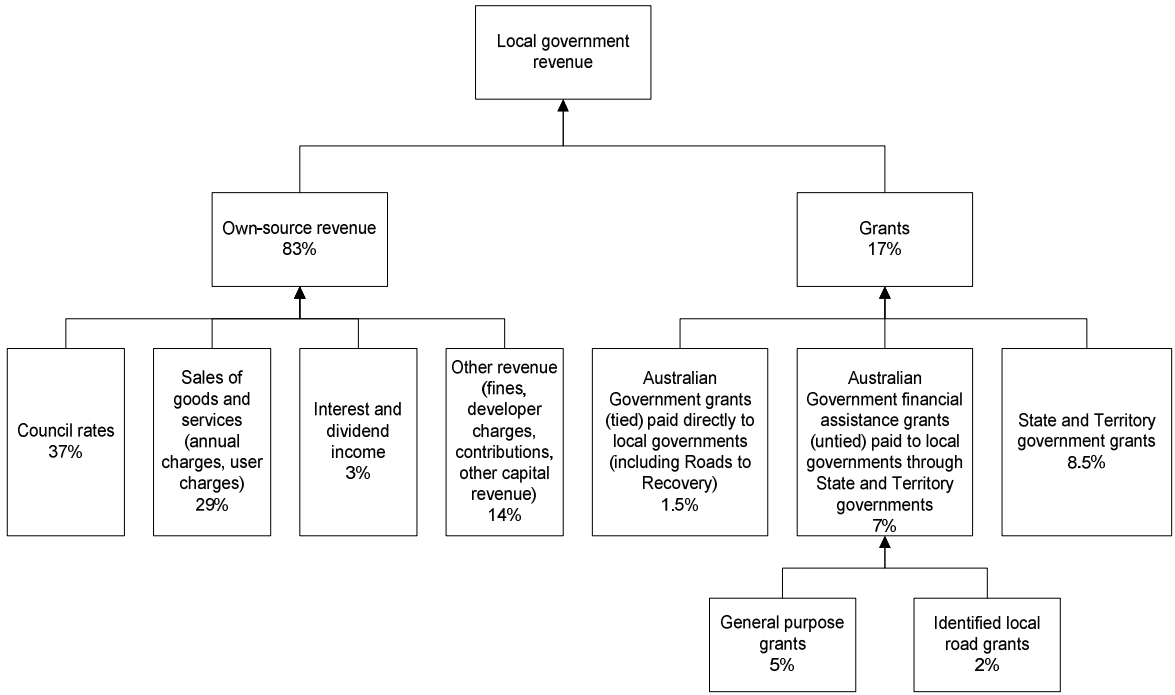
In addition to their revenue-raising powers, local governments may source finance through borrowings. State governments, depending on the jurisdiction, impose

restrictions on the level of borrowings or the purpose or the source of borrowings. Local governments in most States are required to seek ministerial approval prior to entering into contractual arrangements to borrow. Borrowing by local governments is often arranged through State government treasury corporations or departments.

The powers of local governments in each jurisdiction to raise various sources of revenue, as prescribed in State legislation and regulations, are discussed in detail in chapter 6 and appendix B.

Local government revenue sources can be defined as own-source revenue and grants and subsidies from other levels of government (figure 2.3). Own-source revenue consists of council rates, revenue from the sale of goods and services, interest income and other revenue. The remaining revenue source available to local governments is grants and subsidies distributed by the Australian and State Governments.

**Figure 2.3 Sources of local government revenue in Australia**  
2005-06



Source: ABS unpublished; Australian Government (2006); Productivity Commission calculations.

Council rates are taxes collected from land owners on the basis of property value. They often include a minimum charge or fixed charge, above which an *ad valorem* component may be applied. Rates may consist of general rates, separate or special rates.

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Sales of goods and services includes any revenue derived from the direct provision of goods and services. This category includes user fees and charges (for example, for parking or using sporting and recreational facilities), water and sewerage charges, fees for regulatory services, rental income, and revenue for acting as an agent on behalf of other levels of government.

Interest and dividend income includes revenue derived from owning financial assets, such as interest on bank account balances and government securities.

Other income includes all revenue which is not in the other three categories. This includes fines, contributions and donations (including developer contributions and non-financial assets acquired free or at a price below fair value).

Grants and subsidies revenue includes current and capital grants from the Australian and State Governments. The Australian Government provides funding to local government in the form of annual untied financial assistance grants (which are paid in quarterly instalments through the States) and (tied) specific purpose payments direct to local governments. The financial assistance grants consist of two components:

- general purpose grants, distributed among the States on an equal per person basis
- identified local road grants, distributed among the States on the basis of historical shares (although identified as road grants, they are untied).

The State governments allocate both components of the financial assistance grants to local governments in their respective jurisdictions according to the recommendations of the State grants commissions in each State and the Northern Territory. In determining grant allocations, the State grants commissions are required to make their recommendations in line with National Principles under the *Local Government (Financial Assistance) Act 1995* (box 2.2).

The application of the horizontal equalisation principles leads to larger general purpose grants per person for councils with relatively smaller rates bases and those that are disadvantaged in terms of the relative cost of delivering services. However, the total general purpose grants pool in each State is not sufficient to achieve full fiscal equalisation.<sup>7</sup>

The Australian Government also makes specific purpose payments direct to local governments to fund local roads and infrastructure (for example, *Roads to Recovery*

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<sup>7</sup> The balance of the general purpose grants pool (after allocating minimum grants) is distributed to each local governing body in proportion to its relative need as assessed by the State grants commissions. However, the grants pool is insufficient to meet the full amount of the assessed need.

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grants), child care programs, and disability and other services administered by local governments.

**Box 2.2 National principles for allocation of financial assistance grants**

The State grants commissions are required to observe the National Principles relating to grants allocation under the *Local Government (Financial Assistance) Act 1995* (Cwth):

- *Horizontal equalisation* — this principle requires that each local governing body in a jurisdiction is able to function, by reasonable effort, at a standard not lower than the average standard of other local governing bodies in that State. Further, it takes account of differences in the expenditure requirement and revenue-raising capacity of local governing bodies.
- *Effort neutrality* — the revenue and expenditure policies of individual local governing bodies shall not, as far as practicable, affect grant determination through the assessment of revenue-raising capacity and expenditure requirements.
- *Minimum grant* — the minimum general purpose grant allocation for a local governing body is to be no less than 30 per cent of its per person share of the total amount of general purpose grants available for allocation among local governing bodies in the States or Territory.
- *Other grant support* — this principle requires recognition of other relevant grant support to local governing bodies to meet any expenditure needs.
- *Aboriginal peoples and Torres Strait Islanders* — financial assistance shall be allocated to councils in a way which recognises the needs of Aboriginal peoples and Torres Strait Islanders within their boundaries.
- *Council amalgamation* — where two or more local governing bodies are amalgamated into a single body, the general purpose grant provided to the new body for each of the four years following amalgamation should be the total of the amounts that would have been provided to the former bodies in each of those years if they had remained separate entities.
- *Identified road component* — the identified road component of the financial assistance grant should be allocated on the basis of the relative needs of local governing bodies for road expenditure. Relative needs should be determined based on length, type, and usage of roads in each local governing area.

Source: DOTARS (2007); CGC (2001).

The State governments provide grants to local governments for specific purposes or services. A component of State government grants are reimbursements for rate concessions provided by local governments on behalf of State governments. State government grants are distinguished from total grants paid to local government in

table 2.3. State governments also provide contract payments to councils to carry out some State functions.

**Table 2.3 Grants to local government by function**  
2004-05, (\$) millions<sup>a</sup>

<i>Function/grant</i>	<i>NSW</i>	<i>Vic</i>	<i>Qld</i>	<i>SA</i>	<i>WA</i>	<i>Tas</i>	<i>NT</i>	<i>Total</i>
Grants from Australian and State Governments								
General public services	15	17	69	1	8	1	38	149
Health, social security and welfare	122	316	31	24	50	15	15	573
Housing and community amenity	86	40	118	13	9	8	71	345
Recreation and culture	52	72	48	17	27	13	7	236
Transport and communications	281	230	232	54	204	36	13	1 050
Other	500	311	221	96	125	28	10	1 291
<b>Total</b>	<b>1 056</b>	<b>986</b>	<b>719</b>	<b>205</b>	<b>423</b>	<b>101</b>	<b>154</b>	<b>3 644</b>
Australian Government financial assistance grants								
General purpose grants	358	263	205	82	105	26	11	1 050
Identified local road grants <sup>b</sup>	137	98	89	26	72	25	11	458
SPP direct grants	90	78	54	22	43	10	7	305
Australian Government grants (\$)/person	87	87	87	84	109	126	142	90
State government grants	471	547	371	75	203	40	125	1 831
State grants (\$)/person	70	108	93	48	101	81	604	91

<sup>a</sup> Estimates may differ from other sources. Includes current and capital grants. <sup>b</sup> Local roads grants for South Australia include supplementary local road funding of \$4 million.

Source: DOTARS (sub. 38); Australian Government (2005); ABS (2007h); Productivity Commission calculations.

## Local government revenue in Australia

The total revenue received by all Australian local governments has been steadily increasing, in real terms, in recent years (table 2.4). Between 1998-99 and 2005-06, total revenue in real terms increased from over \$18 billion to nearly \$24 billion, representing an average annual growth of 3.4 per cent. Real per person revenue has similarly increased during this period, growing from \$985 to \$1174 per person, representing average annual growth of 2.2 per cent. Rates revenue as a share of total revenue has declined over time. The shares of sales of goods and services revenue and grants revenue fluctuated during the same period, but was largely unchanged in 2005-06 from the 1998-99 share. The share of other revenue increased from 12 to 14 per cent of total revenue.

**Table 2.4 National trends in real local government revenue**

Shares, 1998-99 to 2005-06<sup>a</sup>

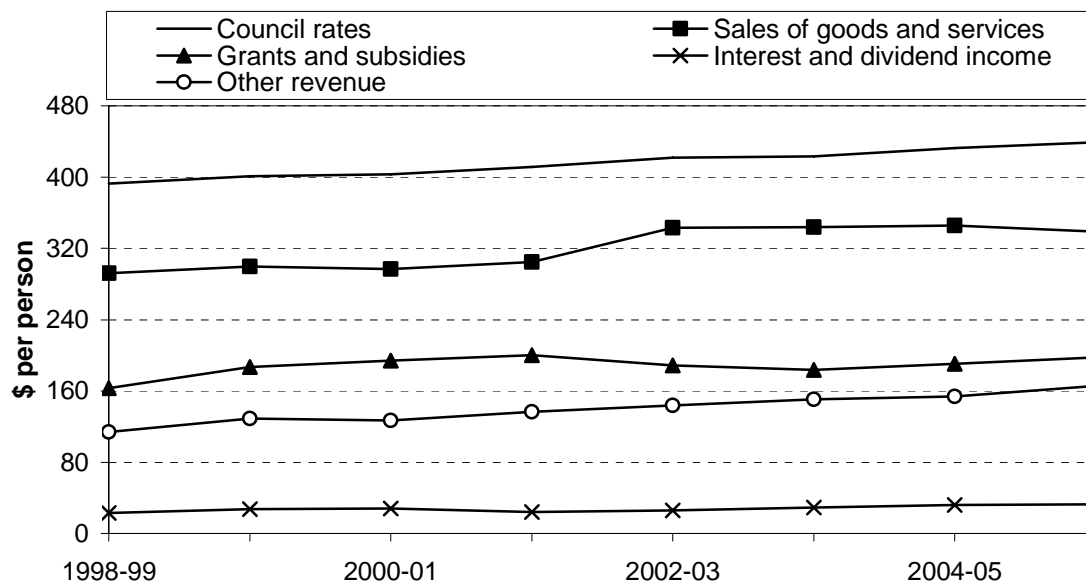
Year	Council rates	Sales of goods and services	Grants and subsidies <sup>b</sup>	Interest and dividend income	Other revenue <sup>c</sup>	Real total revenue <sup>d</sup>	Per person real total revenue
	%	%	%	%	%	\$m	\$/person
1998-99	40	30	17	2	12	18 331	985
1999-2000	38	29	18	3	12	19 661	1 044
2000-01	38	28	19	3	12	20 018	1 049
2001-02	38	28	19	2	13	20 814	1 077
2002-03	38	31	17	2	13	21 980	1 123
2003-04	37	30	16	3	13	22 395	1 131
2004-05	37	30	17	3	13	23 177	1 155
2005-06	37	29	17	3	14	23 915	1 174

<sup>a</sup> Estimates may differ from other ABS sources. <sup>b</sup> Grants and subsidies includes both capital and current grants from Australian and State Governments, and reimbursements of rate concessions. <sup>c</sup> Other revenue includes fines, developer charges and contributions and other current and capital revenue. <sup>d</sup> Data are adjusted to 2005-06 dollars using the ABS non-farm GDP deflator.

Source: ABS unpublished; Australian Government various; Productivity Commission calculations.

**Figure 2.4 National trends in real local government revenue**

Real revenue per person, 1998-99 to 2005-06<sup>a</sup>



<sup>a</sup> Data are adjusted to 2005-06 dollars using the ABS non-farm GDP deflator.

Source: ABS unpublished; Australian Government various; Productivity Commission calculations.

In real terms, there was an increase in all components of revenue per person at the national level over the same period, with the exception of interest and dividend income which remained relatively constant (figure 2.4).

Although local government rates revenue has increased steadily in recent years, its share of the total taxation revenue collected by all levels of government in Australia has decreased significantly over the long term. As illustrated in figure 2.5, local government rates decreased from 18 per cent of total taxation revenue in 1901-02 to 3 per cent in 2005-06. This is largely due to substantial increases in the level of income tax revenue collected by other levels of government. More recently, the share of *other taxes* has risen significantly with the introduction of the goods and services tax.

Local government rates increased from about 1.2 per cent of GDP in 1901-02 to about 2 per cent in 1929-30. They decreased to 1.2 per cent of GDP in 1980-81 and had fallen further to about 0.9 per cent by 2005-06 (Groenewegen 1990, ABS 2007d and 2007i).

**Figure 2.5 Australian taxation revenue, all levels of government**  
Shares of total taxation revenue, selected years<sup>a</sup>



<sup>a</sup> Income taxes includes taxes on persons and companies. Customs and excise duties in 2005-06 includes excises and levies and taxes on international trade. Other tax revenue in 2005-06 includes goods and services tax.

Source: Groenewegen (1990); ABS (2007i); Productivity Commission calculations.

Between 1990-91 and 2005-06, the ratio of local government taxation (rates) revenue to GDP decreased from 1.03 to 0.92 per cent (table 2.5). Over the same

period, combined Australian and State government taxation revenue as a ratio to GDP increased.

The rates revenue collected by local governments, at a national level, is a small proportion of the income of all residents, largely because local governments raise a relatively small amount of revenue on a per person basis. This can be illustrated by expressing local government revenue as a ratio of household disposable income (table 2.5).

**Table 2.5 Revenue, GDP and personal income, all levels of government**  
Shares and ratios, selected years, per cent<sup>a</sup>

<i>Year</i>	<i>All local governments</i>	<i>All State Governments</i>	<i>Australian Government</i>
<b>Share of total taxation revenue<sup>b</sup></b>			
1990-91	3.54	17.79	78.67
1997-98	3.35	19.26	77.39
2005-06	2.99	14.70	82.30
<b>Ratio of taxation revenue to GDP</b>			
1990-91	1.03	5.17	22.85
1997-98	0.98	5.60	22.51
2005-06	0.92	4.53	25.35
<b>Ratio of taxation revenue to HDI<sup>c</sup></b>			
1990-91	1.50	7.54	33.35
1997-98	1.48	8.47	34.05
2005-06	1.48	7.28	40.74

<sup>a</sup> Ratios have been multiplied by 100 to express them in percentage terms. <sup>b</sup> Tax revenue refers to the ABS taxation revenue measure. Goods and services tax is reported as Australian Government taxation revenue. <sup>c</sup> Household disposable income (HDI) refers to gross household income plus imputed rent to owner-occupiers less income tax payable, other current taxes on income and wealth, interest on dwellings and consumer debt, interest payable by unincorporated enterprises, health insurance premiums and other current transfers payable by households.

Source: ABS (2007a, 2007i); Productivity Commission calculations.

#### FINDING 2.1

*At the national level, the ratio of local government rates revenue to GDP decreased over the period 1990-91 to 2005-06.*

### Local government revenue across jurisdictions

Analysis at the aggregate Australian level masks differences in the level and proportion of revenue components across jurisdictions. The jurisdictional variation is due to, among other things, legislative differences (for example, rate pegging in

New South Wales) and variation in the functions of local governments (for example, water and sewerage services provided by local governments in New South Wales, Queensland and Tasmania).

The majority of local government revenue is derived from its own sources, that is, all revenue other than grants received from other levels of government (table 2.6). In 2005-06, own-source revenue was lowest in the Northern Territory at 48 per cent of total revenue and highest in Queensland, where it accounted for 88 per cent. The component shares of own-source revenue, as well as the grants and subsidies revenue shares, similarly exhibit variation across jurisdictions.

**Table 2.6 Trends in own-source revenue**

Own-source revenue as a share of total revenue, 1998-99 to 2005-06<sup>a</sup>

Year	NSW	Vic <sup>b</sup>	Qld	SA	WA	Tas	NT	Australia
1998-99	85	81	85	84	78	83	na	83
1999-2000	87	81	79	84	78	82	51	82
2000-01	87	78	80	83	76	82	45	81
2001-02	86	76	83	82	78	82	48	81
2002-03	88	77	86	83	79	81	46	83
2003-04	87	79	88	83	78	83	48	84
2004-05	85	80	88	84	80	83	51	83
2005-06	84	80	88	82	80	82	48	83

<sup>a</sup> Own-source revenue is total revenue less revenue from grants and subsidies <sup>b</sup> Grants data for Victoria were sourced from the Victorian Grants Commission to overcome data limitations. **na** Not available.

Source: ABS unpublished; Victorian Grants Commission unpublished; Australian Government various; Productivity Commission calculations.

### *Component shares of total revenue*

There are significant differences in the level of local government revenue, when compared across States. In 2005-06, total revenue ranged from \$361 million in the Northern Territory to \$7388 million in New South Wales, largely reflecting differences in population size. On a per person basis, total revenue was highest in the Northern Territory at \$1712 per person and lowest in South Australia at \$846 per person (table 2.7).

Just as the aggregate and per person levels of total revenue across jurisdictions are quite varied, so is the composition of total revenue. In 2005-06:

- the revenue per person from council rates ranged from \$294 in the Northern Territory to \$501 in South Australia<sup>8</sup>

<sup>8</sup> Some local governments in the Northern Territory collect 'poll tax' for services in relation to land. This is classified by the ABS as part of sales of goods and services.

- the revenue per person from sales of goods and services ranged from \$138 in South Australia to \$629 in Queensland<sup>9</sup>
- grants and subsidies revenue per person ranged from \$149 in South Australia to \$883 in the Northern Territory
- interest and dividend income per person ranged from \$10 in South Australia to \$51 in Tasmania
- other revenue per person ranged from \$48 in South Australia to \$311 in Queensland.

**Table 2.7 Local government revenue sources by State**  
2005-06

	<i>Council rates</i>	<i>Sales of goods and services</i>	<i>Grants and subsidies</i>	<i>Interest and dividend income</i>	<i>Other revenue</i>	<i>Total revenue</i>	<i>Total revenue</i>
	\$/person	\$/person	\$/person	\$/person	\$/person	\$/person	\$m
NSW	387	347	173	47	130	1 084	7 388
Vic	491	184	208	13	133	1 029	5 279
Qld	442	629	192	38	311	1 612	6 594
SA	501	138	149	10	48	846	1 326
WA	451	232	226	36	176	1 121	2 308
Tas	422	524	237	51	112	1 345	659
NT	294	283	883	32	220	1 712	361
Australia	439	339	198	33	166	1 174	23 915

Source: ABS unpublished; Australian Government (2006); Productivity Commission calculations.

Local government ratios of own-source and rates revenue to gross state product and household disposable income for each State are presented in table 2.8. The highest ratios were in Queensland and Tasmania, in part, reflecting high own-source revenues from the provision of water and sewerage services (table 2.7).

<sup>9</sup> Sales of goods and services revenue raised by Queensland local governments includes charges for water and sewerage services.

**Table 2.8 Local government revenue, state output, and personal income**  
Ratios at the state level, selected years, per cent<sup>a</sup>

<i>Year</i>	<i>NSW</i>	<i>Vic</i>	<i>Qld</i>	<i>SA</i>	<i>WA</i>	<i>Tas</i>	<i>NT</i>
<b>Ratio of own-source revenue to GSP<sup>b</sup></b>							
1998-99	2.13	1.48	2.93	1.62	1.74	2.82	0.92
2001-02	2.13	1.58	2.84	1.60	1.58	2.89	1.48
2003-04	2.03	1.66	3.31	1.63	1.60	2.76	1.39
2005-06	1.97	1.78	3.25	1.68	1.53	2.88	1.38
<b>Ratio of rates revenue to GSP</b>							
1998-99	0.95	0.85	1.13	1.11	0.91	1.19	0.63
2001-02	0.89	0.89	1.11	1.12	0.87	1.20	0.53
2003-04	0.85	0.93	1.06	1.15	0.86	1.12	0.52
2005-06	0.84	1.07	1.01	1.20	0.77	1.10	0.49
<b>Ratio of own-source revenue to HDI<sup>c</sup></b>							
1998-99	3.10	2.33	4.44	2.38	3.00	4.57	1.60
2001-02	3.08	2.49	4.41	2.33	2.85	4.42	2.96
2003-04	3.12	2.68	5.33	2.53	2.83	4.40	2.82
2005-06	3.02	2.76	5.40	2.55	3.09	4.46	2.79
<b>Ratio of rates revenue to HDI</b>							
1998-99	1.39	1.33	1.71	1.63	1.57	1.93	1.09
2001-02	1.30	1.39	1.73	1.62	1.57	1.84	1.05
2003-04	1.31	1.50	1.71	1.79	1.52	1.78	1.05
2005-06	1.28	1.65	1.68	1.83	1.56	1.70	0.99

<sup>a</sup> Ratios have been multiplied by 100 to express them in percentage terms. <sup>b</sup> Own-source revenue is equal to total revenue less grants revenue. <sup>c</sup> Household disposable income (HDI) refers to gross household income plus imputed rent to owner-occupiers less income tax payable, other current taxes on income and wealth, interest on dwellings and consumer debt, interest payable by unincorporated enterprises, health insurance premiums and other current transfers payable by households.

Source: ABS unpublished; ABS (2007a, 2007d); Australian Government various; Productivity Commission calculations.

#### FINDING 2.2

*At the state level, the ratio of own-source revenue to gross state product varies across jurisdictions due to a large number of factors, including differences in the functions of local governments, such as provision of water and sewerage services in some States but not others.*

The trends in local government revenue at the state level are influenced by the underlying diversity of individual local governments within jurisdictions. The characteristics of different types of councils and the factors driving their revenue requirements and capacity to raise revenue are discussed in chapters 3 and 5.