Productivity Commission Study on Local Government Own Source Revenue

Joint Submission by the Department of Treasury and Finance and the Department of Local Government and Regional Development

1. Introduction

This submission to the Productivity Commission Study into Local Government Own Source Revenue has been prepared by the Department of Local Government and Regional Development in collaboration with the Department of Treasury and Finance.

The submission will provide detail on the legislative context of WA local government revenue raising ability and the regulatory constraints placed on local governments under the *Local Government Act 1995*.

2. Financial Capacity of the Local Government Sector

While there is much variation between local governments, there is no clear evidence of greater stress for the local government sector as a whole than for the State Government sector, based on the Government Finance Statistics (GFS) published by the ABS. Commonwealth finances are in better shape than those of the State/local sector.

In this regard, the table below summarises selected financial aggregates for the Commonwealth, State and Local General Government sectors.

Table 1: Commonwealth, State and Local Government Operating Statements

	1998/99	**1999/00**	**2000/01**	**2001/02**	**2002/03**	**2003/04**	**2004/05**	**2005/06**	**Average**
GFS Total Revenue Growth									
Commonwealth	-	8.7%	11.3%	2.4%	8.7%	7.4%	9.0%	7.7%	**7.9%**
State Governments	-	3.4%	6.6%	5.3%	6.6%	9.0%	6.4%	8.1%	**6.5%**
Local Governments	-	9.2%	4.1%	6.4%	4.7%	6.6%	9.0%	6.1%	**6.6%**
GFS Net Lending(+)/Borrowing(-) (i.e. net operating balance less net acquisition of non-financial assets) **(Relative to Total Revenue)**									
Commonwealth	3.1%	7.1%	3.1%	-1.8%	3.1%	3.1%	4.9%	6.4%	**3.6%**
State Governments	1.0%	1.5%	-1.3%	-0.5%	1.6%	3.2%	3.0%	2.4%	**1.4%**
Local Governments	2.4%	1.7%	1.2%	1.4%	0.1%	-1.5%	-1.0%	0.8%	**0.6%**

(Source: *ABS Catalogue No. 5512.0*)

Since 1998-99 (when accrual accounting was introduced) local government revenue has on average grown at the same rate as State government revenue, but more than 1% per annum less than the Commonwealth's revenue growth.

The Commonwealth has recorded consistently higher net lending outcomes (as a percentage of revenue) than State or local governments.

The 2004-05 Local Government National Report, page 36, notes that "At 30 June 2004, local government nationally appeared to be in a strong financial position with total cash, deposits and lending exceeding gross debt. This continues the trend since 30 June 2000 of a negative net debt (a net surplus) position for local governments nationally." (DOTARS, 2006)

2.1 Vertical Fiscal Imbalance

As a whole, the local government sector has greater control over its finances than the States (which are heavily dependent on Commonwealth grants).

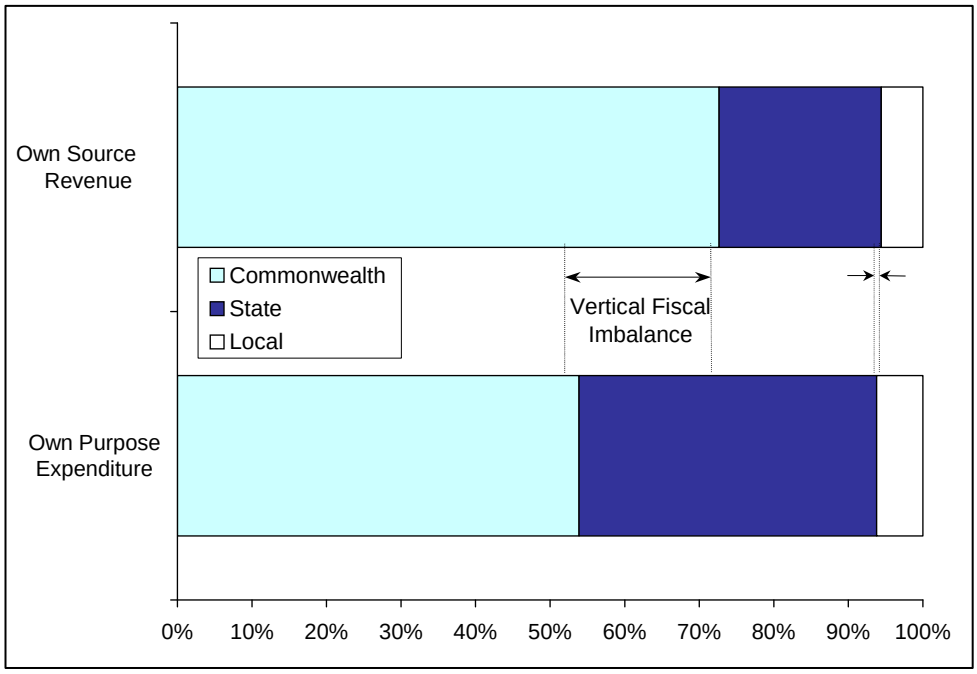
The dependence of one level of government on another to fund its expenditure responsibilities is referred to as vertical fiscal imbalance (VFI).

VFI in Australia is high compared with other federations, with Australian States relying on Federal grants to fund approximately 60% of their expenditures.

In comparison the total local government sector has a far lower level of VFI (funding about 90% of their expenditures from own source revenues).

Overall, the revenue raising capacity powers and expenditure responsibilities of local governments are fairly evenly matched, contrasting with the substantial mismatches for the Commonwealth and State levels of government (see Figure 1).

Figure 1: Vertical Fiscal Imbalance Across Levels of Government



(Sources: *ABS Catalogue No 5512* and *Commonwealth of Australia*, *2006*)

However, VFI varies widely across individual local governments, being very high in remote areas.

The 2004-05 Local Government National Report, page 25, notes “there is wide disparity in the ability of individual councils to raise revenue due largely to differences between urban, rural and remote councils, in population size, rating base and the ability or willingness of councils to levy user charges.” (DOTARS, 2006)

3. Western Australian Local Government

Local government in Western Australia is a significant industry. There are currently 140 local governments covering all land in Western Australia (except Kings Park).

In 2006, local government in Western Australia held a net asset value in excess of $12.4 billion and achieved a total operating revenue in excess of $2 billion. More than 12,500 people are employed by the sector (LGAB, 2006).

Table 2 below provides Estimated Resident Population (ERP) and Total Operating Revenue (TOR) for WA local governments sorted according to the Australian Classification of Local Government (ACLG) Categories.

Table 2: Total Operating Revenue (TOR) and ERP (Estimated Residential Population) for Western Australian ACLG Categories

*ACLG Category	TOR 2005-06	**ERP June 2006p
Urban Regional (UR)	306,017	245919
Urban Fringe (UF)	716,159	797148
Urban Metropolitan Developed (UD)	592,341	696421
Urban Capitol City (UCC)	109,832	12549
Rural Remote (RT)	151,364	58889
Rural Significant Growth (RSG)	97,718	93545
Rural Agricultural (RA)	354,144	154574

(Sources: *DLGRD, 2007*; *DOTARS, 2002-2003* and *ABS* Cat. No. 3218.0 & 3235.0)

* See Appendix 1 for full ACLG classification
**Estimated Resident Population, June, 2006, preliminary.
***Cue, Mukinbudin and Nedlands did not supply information for 2005/06

4. Local Government Sustainability

Recently, there have been a number of studies concerning the sustainability of local governments in Western Australia. These include:

- *Ensuring the Future Sustainability of Communities*, April 2006, WA Local Government Advisory Board; and
- In Your Hands - Shaping the Future of Local Government in Western Australia – Systemic Sustainability Study, December 2006, West Australian Local Government Association.

Findings from these reports have indicated various degrees of sustainability throughout the Western Australian local government sector, with some local governments considered unsustainable, some considered marginally sustainable and some considered currently sustainable.

The Local Government Advisory Board stated in its 2006 report “some local governments are not generating enough revenue to meet their operating demands and are likely to have difficulty in meeting long-term infrastructure needs.”

The *Systemic Sustainability Study* used the revenue base of local governments, exclusive of capital grants, to determine the financial sustainability of local governments for WA. Under this analysis, given that a number of local governments in WA are reliant on grant revenue, 83 local governments, mainly in regional areas, were considered financially unsustainable (WALGA, 2006).

However, the WALGA report appears to overstate the number of unsustainable local governments due to:

- inconsistency in the treatment of capital grants and capital expenses; and
- the comparison of operating deficits to own-source revenues rather than all revenues, implying that local governments that are not financially self sufficient are less likely to be sustainable in the broader sense.

While the finances of many regional and remote local governments may appear unsustainable under existing revenue and expenditure policy settings, it is less clear how many of these councils could be sustainable with appropriate financial management and policy settings (including carefully prioritising the provision of services and infrastructure, managing community expectations and using resources more efficiently through amalgamation or resource sharing).

In Western Australia, most local governments (although representing a minority of the population) are heavily dependent on grants. The majority of local governments receive more than 40% of their revenues from grants, and 45 local governments (all in rural and remote areas) receive more than 50% of their revenues from grants.

5. Grants to Local Government in Western Australia

Table 3, below, illustrates the breakdown between State and Commonwealth grant funding for Western Australian local governments in 2005-06.

Table 3: Grants to Local Government in Western Australia

	2005-06 Actual $m	2006-07 Estimated Actual $m	2007-08 Budget Estimate $m
STATE GRANTS			
Main Roads	109	100	101
Fire and Emergence Services	15	18	18
Sport and Recreation	7	8	20
Planning and Infrastructure	7	-	-
Treasury and Finance	4	6	-
Local Government and Regional Development	3	2	11
Industry and Resources	1	4	6
Other	9	11	9
Total	**154**	**149**	**166**
COMMONWEALTH GRANTS			
Financial Assistance Grants			
General Purpose Funding	111	116	122
Untied Local Roads Funding	76	80	83
Specific Purpose Payments			
Children's Services	4	3	3
Regulation Incentive Fund	1	1	-
Roads to Recovery Program	40	59	75
Total	**231**	**259**	**283**

(Source: *DTF, 2007a*)

5.1State Grants

State grants for local government mainly comprise funding for roads.

The State Road Funds to Local Government Agreement 2005-06 to 2009-10 provides local government with a 27% share of vehicle license fees. Latest estimates of vehicle licence fees indicate that local government will receive $564 million over five years (DTF, p801, 2007b) $104 million more than originally estimated in 2005.

The State Black Spot Program has an annual allocation of $20 million, of which 50% is allocated to address specific road safety issues on local roads.

The Fire and Emergency Services Authority provides grants for local government emergency services (DTF, p436, 2007b).

Funding for bush fire brigades and SES units is allocated via a grants process where local governments apply for an operating grant and a capital grant for each service. Operating grants fund essential costs such as running vehicles and buildings, protective equipment, volunteer insurance and operational consumables. Capital grants include new fire fighting appliances, vehicles and buildings.

The Department of Sport and Recreation's Community Sporting and Recreation Facilities Fund (CSRFF) provide financial assistance to local government authorities to develop basic infrastructure for sport and recreation.

5.2 Commonwealth Grants

A detailed analysis of the impact of Commonwealth Financial Assistance Grants is provided in Appendix 2.

6. Western Australian Local Government Own Source Revenue

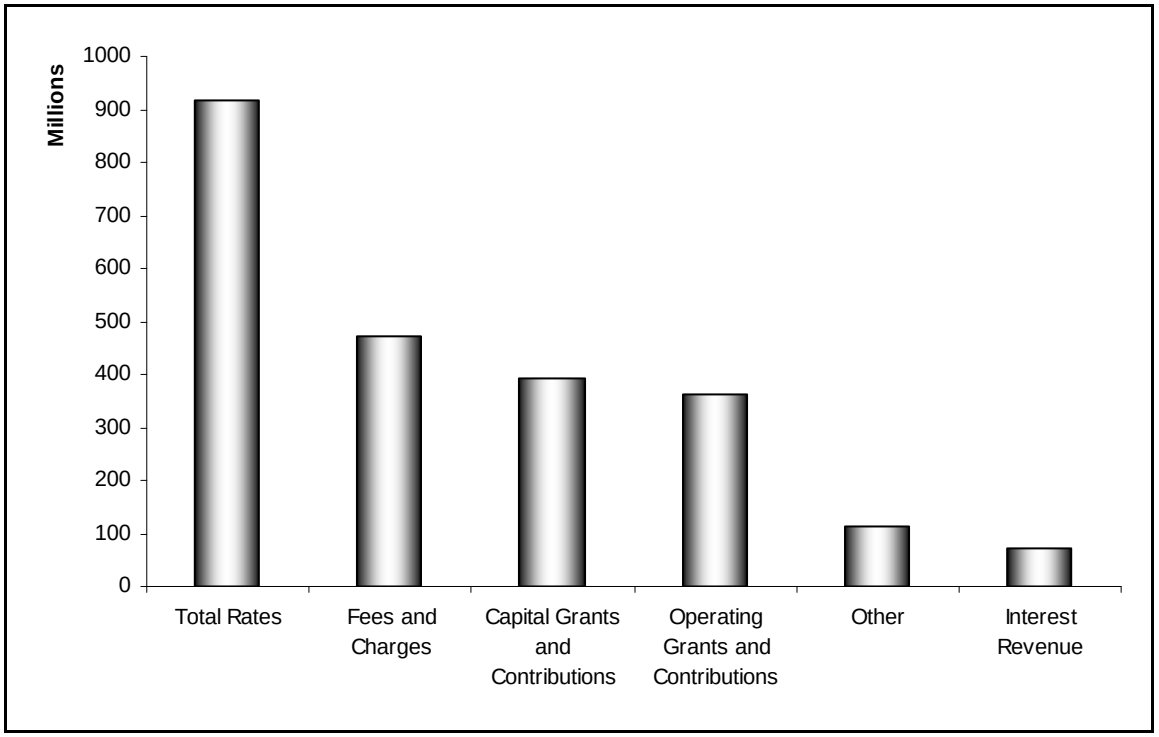
The provisions under which local government in Western Australia are able to raise own source revenue are outlined in the *Local Government Act 1995* (the Act).

Western Australian local governments may, under section 6.15 of the Act, receive revenue from the following sources:

- rates;
- service charges;
- fees and charges;
- borrowings;
- investments;
- dealings in property; and
- grants or gifts.

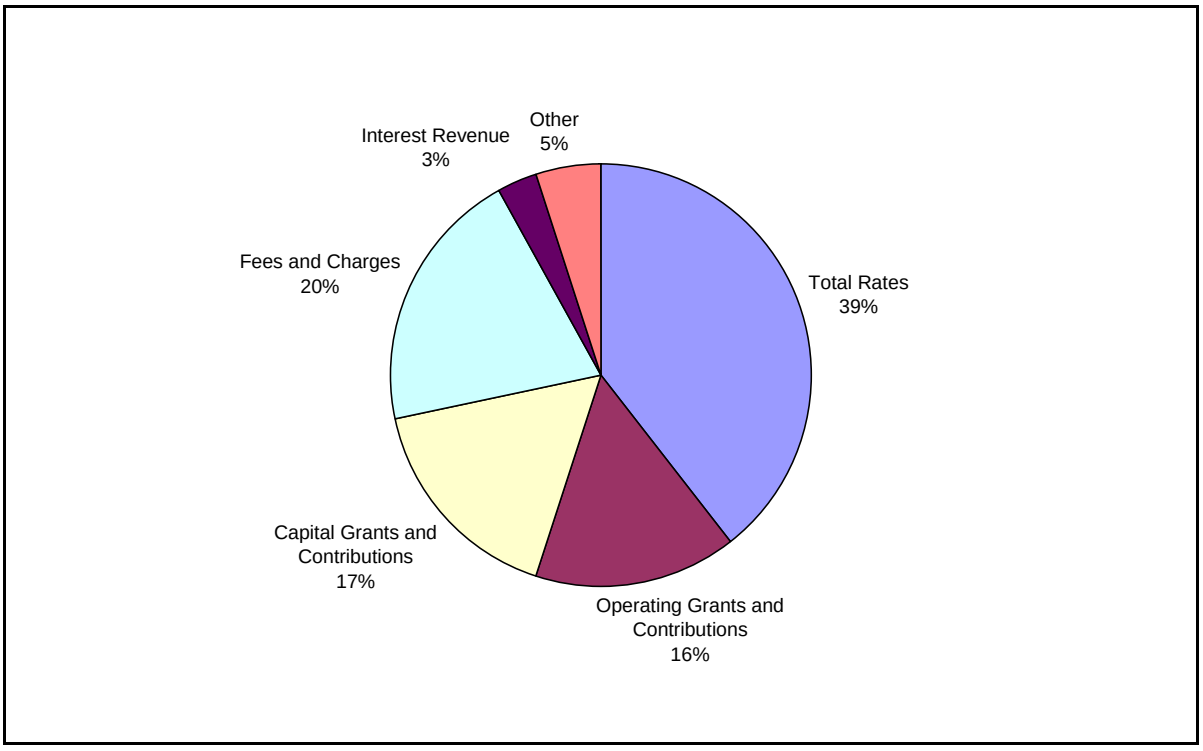
Figures 2 and 3 illustrate the components of WA local government Operating Revenue for 2005-06.

Figure 2- Components of WA Local Government Operating Revenue, 2005-06



(Source: *WALGGC, 2001-01 -2005-06*)
*Cue, Mukinbudin and Nedlands did not supply information for 2005/06

Figure 3- Components of WA Local Government Operating Revenue, 2005-06



(Source: *WALGGC, 2001-01 -2005-06*)
*Cue, Mukinbudin and Nedlands did not supply information for 2005/06

6.1 Rates and Service Charges

Rates and service charges are the major streams of own source revenue for local governments in Western Australia (see Figure 2).

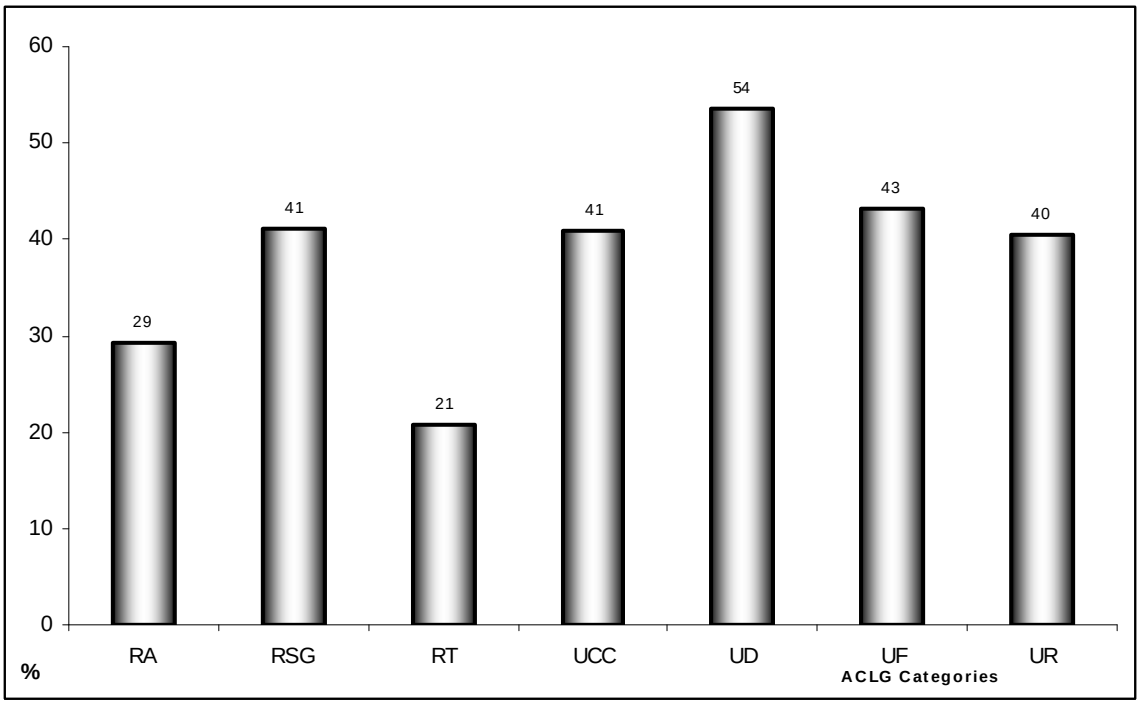
The Act provides for local governments to impose a general rate on all rateable land in its district. Section 6.32 of the Act establishes that local government may impose rates and services charges as:

- a general rate which is applied either uniformly or differentially;
- a specified area rate;
- a minimum rate; or
- a service charge on land within its district.

The Act requires local governments to set a rate which is expressed as a rate in the dollar of either the Gross Rental Value (GRV) or the Unimproved Value (UV).

Figure 4 outlines the percentage of total operating revenue raised by rates in WA, 2005-06, for the ACLG categories.

Figure 4- Rates as a Percentage of Total Operating Revenue for Western Australia, 2005-06



(Source: *WALGGC, 2001-01 -2005-06*)
*Cue, Mukinbudin and Nedlands did not supply information for 2005/06

Proposition 1
Many of the rural or remote local governments in WA face declining populations leading to stagnant or declining housing and land values and lower levels of commercial activity. As indicated by Figure 4, in 2005-06, local governments categorised Rural Remote (RT) received only 20% of their revenue from rates, while local government categorised Urban Developed (UD) received 53% of their revenue from rates.

The number of households, the value of housing stock, land values and the level of commercial or industrial activity are all influences on the level of revenue that local government is able to extract from its rating base. There is significant disparity between individual local governments' capacity to rely on this stream of own source revenue to meet their budget needs.

6.1.2 General Rates

Under section 6.28 of the Act, the Minister, in determining the method of valuation for land in a district, is to have regard to the general principle that the basis for a rate on any land is to be:

- where the land is used predominantly for rural purposes, the UV of the land; and
- where the land is used predominantly for non-rural purposes, the GRV of the land.

In discharging their responsibilities, successive Ministers have chosen to respond to applications from local governments for changes to valuation methods (as opposed to directing local governments to make such changes). This approach recognises that local governments are best placed to identify where changes may be needed to the method of valuation of land within their districts. Local governments are also encouraged to adopt a valuation that attracts the highest income from the land within their district

The introduction of the Goods and Services Tax (GST) has impacted on the determination of GRV. Where property rental payments are subject to GST they represent a tax payable by the property owner and as such must be included in the GRV.

Where an annual rental cannot reasonably be determined (i.e. vacant land), then the GRV becomes the assessed value. ‘Assessed value’ is defined in the *Valuation of Land Act 1978* as a set percentage of capital value, currently fixed by regulation at 5%.

Proposition 2
The scope for local governments in WA to rate properties is influenced by the market value of property. Variation of property and land values according to geographical location – that is, inter alia, inner metro property values as opposed to outer metro values or rural GRV values – will invariably impact upon an individual local government’s capacity to increase own source revenue.

6.1.3 Differential General Rates

Local governments, under Section 6.33 of the Act, have the power to implement differential rating in order to take into account certain characteristics of rateable land. These characteristics include:

- the purpose for which the land is zoned under a town planning scheme in force under the *Town Planning and Development Act 1928*;
- E.g. Residential, Commercial, Industrial
- the predominant purpose for which the land is held or used as determined by the local government; and
- whether or not the land is vacant.

Differential rates may be applied according to any, or a combination of the above characteristics. However, local governments are constrained in the range of differential rates that they may impose. That is, a local government may not impose a differential rate which is more than twice the lowest differential rate applied by that local government unless approval from the Minister is sought.

Proposition 3

Local governments may implement rating practices that incorporate the characteristics of the land in their district. Specifically, this leaves flexibility for local governments to determine the composition of their rates to increase and decrease the incidence of the rate burden on different segments of the community. For example, there is scope for local governments to rate more heavily commercial or industrial activity for the purposes of adjusting the incidence of tax to reflect community values.

6.1.4 Minimum Rate Payment

Section 6.35 of the Act provides for local government to impose on any rateable land in its district, a minimum payment which is greater than the general rate which would otherwise be payable on that land. The minimum payment is not to be imposed on more than:

- 50% of the total number of separately rated properties in the district; or
- 50% of the number of properties in the following categories:
    - land rated on GRV;
    - land rated on UV; and
    - differential rate categories.

Proposition 4

Local government has the capacity to increase rate revenue by setting a minimum rate to encompass a higher level of revenue than would have otherwise been attainable.

6.1.5 Specified Area Rates

Local governments have the power, under Section 6.37 of the Act, to impose specified area rates for the purpose of meeting the cost of a specific work, service or facility on a specified area of its district.

A local government may impose a specified area rate if it considers that ratepayers:

- have or will benefit from;

- have access or will have access to;
- have contributed or will contribute to the need for a work, service or facility.

Local governments are required to use the money from a specified area rate for the purpose for which the rate is imposed in the financial year it was introduced, or place it in a reserve account. A local government may only use money raised to meet the cost of providing that service or to repay money borrowed to meet the cost of the service.

If a local government receives more than it requires from a specified area rate, it must either refund or credit individuals proportionate to the contribution received.

Proposition 5
The capacity of local government to differentiate between ratepayers with particular or additional service needs in a geographical area provides local government with flexibility in implementing its rating regime. Ratepayers who benefit from a particular service or amenity can be levied with a higher incidence of tax accordingly.

Nevertheless, the ability to increase revenue is constrained by the purpose for which that revenue may be used. Specified area rates can be regarded as a form of recovery of long run costs for facilities or amenities that are enjoyed by an identifiable segment of the community.

6.1.6 Multiple Rating

Under the *Mining Act 1978*, the *Petroleum Act 1967* and the section 6.27 of the *Local Government Act 1995*, land held in respect to a mining tenement, petroleum production licence or exploration licence may be subject to multiple rating.

For example, land held under both pastoral lease and mining tenement may be rated separately on each holding, establishing multiple rating on the same land.

Land held under mining tenement, the *Conservation and Land Management Act 1984* or leases under the *Land Administration Act 1997* for the purpose of grazing may be rated with a statutory valuation calculation for UV based on formula, for example a fixed rate per hectare or a multiple of the annual rent. However, this does not apply to land used for accommodation of permanent residents, or land that holds commercial infrastructure.

Proposition 6
Local governments are not restricted, in the above cases, to singular rating on land held under both mining tenement and pastoral lease. However, local government is restricted to rating land held under mining tenement, petroleum production licence or exploration permit, without regard to multiple rating, as UV. Whilst this does not apply for land used for accommodation of permanent residents, it does apply for land used for accommodation of construction workers, and thus, State Agreement Acts, have impacted upon local government ability to raise own source revenue. However, the net impact of State Agreements Acts on local government finances is unclear.

6.1.7 Service Charges

Service charges differ from user fees and charges. Along with rates, local government, under Section 6.38 of the Act, has the power to impose service charges on owners or occupiers of land to meet the cost of providing a prescribed service. Regulation 54 of the *Local Government Financial Management Regulations 1996* prescribes the types of services that a service charge can be levied for. These are as follows:

(a) television and radio rebroadcasting;
(b) volunteer bush fire brigades;
(c) underground electricity;
(d) property surveillance and security; and
(e) water.

All money raised is required to be used to meet the cost of providing the prescribed service and a local government must refund or credit any additional funding received to a person in proportion to the amount payed by that person.

Proposition 7

Local government may raise revenue to cover the costs of operation. However, utilising this as a revenue maximising opportunity is prohibited by legislation that restricts any money raised for use only to cover the cost of providing the service. This constraint is considered an appropriate control on the cost of essential services to the community.

6.2 Fees and Charges

User fees and charges are the second largest component of own source revenue for WA local governments. Section 6.16 of the Act provides for local government to impose fees or charges, for any good or service they provide (except for a service which a service charge is imposed).

Fees or charges may be imposed on any of the following:

- providing use or admission to any facility owned or maintained by local government;
- supplying a service or carrying out work at the request of a person;
- providing information from local government records;
- receiving an application for approval, granting an approval, making an inspection and issuing a licence, permit, authorisation or certificate
- supplying goods; or
- any other services as prescribed by the *Local Government Act 1995.*

6.2.1Setting the Level of Fees and Charges

In determining the amount of a fee or charge for a service or good local governments are required, by Section 6.17 of the Act, to take into account the following factors:

- the cost to the local government of providing the good or service;
- the importance of the service or good to the community; and
- the price at which the service of good could be provided by an alternate provider.

A higher fee or charge may be imposed if the good or service is to be provided urgently.

National Competition Policy requires that local government ensure that its fees, charges and services are set so as to not create an unfair competitive advantage over the private sector. If requested, allegations made by the private sector that local governments have adopted an uncompetitive pricing regime can be examined by the Department of Local Government and Regional Development.

Section 6.17 (3) of the Act requires that the fee or charge for the following goods and service be limited to the cost of providing these goods or services:

- receiving an application for approval, granting an approval, making an inspection and issuing a licence, permit, authorisation or certificate;
- copies of a range of local government information that the public is entitled to inspect as listed in Division 7 of Part 5 of the Act;

There is a range of legislation that local governments are required to administer which requires them to undertake approval, licensing, enforcement and inspection functions. This includes the following Acts:

- *Caravan Parks and Camping Grounds Act 1995*
- *Dog Act 1976*
- *Health Act 1911*
- *Liquor Control Act 1988*
- *Local Government (Miscellaneous Provisions) Act 1960*
- *Planning and Development Act 2005.*

In many cases, the fees that local governments are able to levy for it to undertake its responsibilities may not enable them to recover the costs that they incur when undertaking the various functions required.

Other goods and services, including those that a local government has the right or ownership to deliver, may be rated on a revenue raising basis. For these goods and services the Act provides that the basis for determining a fee or charge for a good of this kind is not to be limited to the cost of providing the service or good. Examples include hire charges for halls, community rooms and recreation centres and lease fees for property where a formal agreement to lease, contract to lease or license to occupy is in place.

Proposition 8

For certain goods and services, revenue is capped to reflect a cost recovery rating basis and restrictions apply on how local governments can impose fees and charges. However, for a large number of good and service provisions, local government has the capacity to impose rating on a revenue raising basis, without regard to the cost of the provision of the good or service.

Fees and charges are required to be set out in a local government's budget and are hence also subject to community scrutiny.

7. Restrictions on Revenue from Rates and Service Charges

7.1 Rating Exemptions

Section 6.26 of the Act also establishes exemptions on local government ability to rate certain land, including:

- land which is the property of the Crown;
- land owned by and used for local government;
- land owned by and used for regional local government;
- land used or held exclusively by a religious body as a place of public worship, a place of residence of a minister of religion or occupied exclusively by a religious brotherhood or sisterhood;
- land used exclusively as a school for the religious instruction of children;
- land used exclusively as a non-government school;
- land used exclusively for charitable purposes;
- land vested in trustees for agricultural or horticultural show purposes;
- land owned by Co-operative Bulk Handling Limited or leased from the Crown by a company for the storage of grain and has agreed to make a contribution to the local government; and
- land declared by the minister to be excluded.

Land may still be classified suitable for exclusion even if it is used occasionally for other purposes, provided the purpose is of a charitable, benevolent, religious or public nature.

7.1.1 Rating exemption for land used for charitable purposes

The WA Local Government Advisory Board inquired into the operation and application of section 6.26 (2) (g) of the *Local Government Act 1995* in 2005. A major focus of the inquiry was in relation to whether or not it was appropriate for local governments to rate independent living units in retirement villages operated by the not-for-profit sector.

In undertaking its study, the Board found that the rate revenue foregone by local governments to provide a rating exemption for retirement village and supported accommodation was around $6.5 million per annum (LGAB, 2005).

The Inquiry also noted that, in contrast, pensioner and senior concessions provided by other entities such as the Water Corporation and Western Power are considered a ‘Community Service Obligation’ and foregone revenue is reimbursed by the State Government. While State Government compensation for local governments that provide rating exemptions is not provided, the State does fund the local government rates concession scheme. The value of this scheme was $52 million in 2007-08 (LGAB, 2005).

Another key finding in the report is that there is a disproportionate distribution charitable land exemptions across the State. An example of this is the City of Stirling, which, with the highest number of independent living units of any local government within WA, has forgone revenue of approximately $500,000 annually, while many

local governments do not have any land used for charitable purposes located in their districts (LGAB, 2005).

Proposition 9
Land and property exempt from rates still contribute to infrastructure and service provision costs, while simultaneously meaning a decrease in revenue for local government. Combined with the uneven distribution of land and property exempt from rating, this often means a further and unequal increase in financial pressure on some local governments in light of restrictions on revenue raising ability.

7.1.2 Rating Exemptions - State Agreement Acts

State Agreements are negotiated legal instruments or contracts, primarily made between the State and proponents of major resources projects. They bind both the State and developers to specific rights and responsibilities.

Historically many State Agreements had clauses that limited the capacity of local government to levy rates on projects covered by these agreements. There are 51 State Agreements that include rating restrictions.

Rates clauses in most State Agreements limit the valuation of project lands to unimproved value. This limitation does not apply to residential accommodation associated with the project or commercial premises not directly related to the project (which can be rated at gross rental value).

Most rating restrictions were included in State Agreements ratified by Parliament in the 1960s and 1970s, reflecting the position at the time that the locations of many projects were remote, and that often companies built the towns and community infrastructure and made little or no demands on local government services or facilities.

In 2004 the Government decided that future State Agreements would not automatically impose rating restrictions on local government authorities, and the State would not generally seek to include such provisions.

The State Government in association with the resources industry and local government is conducting a study into the effects of State Agreement rating clauses on local government revenue. The study will provide information on:

- rates currently paid by the selected State Agreement projects;
- rates payable if it were not for the ratings clauses in the State Agreement Acts; and
- details of voluntary payments and current contributions made by the selected companies to local governments, community programs and community infrastructure.

The study commenced in 2005 and should be completed later this year. The main cause of delay has been an inability to get valuers given competing demands related to the economic boom.

Proposition 10
There is currently no reliable data on which to quantify the impacts of State Agreements on local government rates.

7.1.3 Rating of Government Enterprises and Crown Land

Rates cannot be levied on Government owned land. However, where State and Commonwealth Government instrumentalities are engaged in commercial trading activities such as ports, water, electricity provision and so on, to ensure these bodies act in a competitively neutral manner, tax and rate equivalents are generally made to the relevant Government.

Under the current arrangements, each level of government generally retains tax and rate equivalent payments made by its business enterprises. That is, State Government Trading Enterprises pay tax equivalents for local and Commonwealth Government taxes to the State Government. Similarly, local and many Commonwealth Government business enterprises are not required to pay State taxes, or their equivalents, to the State Government.

In 2006-07 rate equivalent payments from all WA State Government corporations amounted to $11.9 million and are projected to be $13.2 million in 2007-08 and to rise to $14.8 million by 2010-2011.

The State is not aware of any study of the financial impacts on State and local government of current rating arrangements in regard to crown land and government trading enterprises on individual local governments or the local government sector throughout the State.

7.1.4 Airports

Due to operating on Commonwealth land, airport lessee companies are exempt from many State and local government Acts and regulations. This includes the need to comply with State and local building codes and the requirement to pay local government rates under the *Local Government Act 1995*. Instead lessee companies are required to make such payments ex gratia with specific provisions included in their lease contracts. This allows for competitive neutrality and to prevent financially disadvantaging local governments whose boundaries encompass airport land.

Since the Perth Airport was privatised, the payment of rate equivalent payments to local governments has become an issue of contention. The main issue relates to the lack of full payment of rates when not all local government services are provided.

Proposition 11

It is unclear if local government would be better off under a reciprocal taxation arrangement where local government receives rates on State government owned land and pays State payroll tax, land tax and stamp duty.

Having regard to the large financial assistance provided to local government by Western Australia, any transfer of local government rate equivalent revenue to local government should be on a revenue neutral basis.

8*. Developer Contributions*

Developer contributions are legally enforceable contributions that a developer may be required to make to a local government for the provision of infrastructure which is directly related to the needs arising from the development.

However, the agreements that developer contributions are contained within are established on a voluntary basis between the relevant local government and developer. These contributions usually take three forms:

- the ceding of land for roads, public open space, primary school sites, drainage and other reserves;
- construction of infrastructure works which are transferred to public authorities on completion; or
- monetary contributions to acquire land or undertake works by public authorities or others.

A review of the operation of the developer contributions process commenced in 2006 and has been overseen by a joint advisory committee comprising representatives from the Department for Planning and Infrastructure (DPI), WALGA and the Urban Development Institute of Australia (UDIA). The initial part of the review resulted in the report Contributions to Community Infrastructure.

The report recommends a continuation of the current system of developer contributions based on Western Australian Planning Commission policy, as set out in Planning Bulletin 18: Developer Contributions for Infrastructure (1997) and Planning Bulletin 41: Draft Model Text Provisions for Developer Contributions (2000), with some refinement and elaboration for greater clarity and consistency and possible adoption as a State Planning Policy to give a higher status to the current arrangement.

Some of the key changes recommended in the report are:

- there will be core services and infrastructure that developers will be required to fund;
- local governments will be able to require funding for additional services if it can be demonstrated that a new land development will require the provision of services and infrastructure that would not otherwise be the case; and
- local governments will be required to have prepared and adopted a Strategic Infrastructure Plan and a Developer Contribution Plan which is to be incorporated into its Town Planning Scheme.

Proposition 12

The review of the process used to determine the size and type of developer contributions is under review to ensure that there is adequate provision of funding and/or infrastructure accompanying new residential development.

9*. Commercial Activities*

Section 3.59 of the Act gives provision for local government to undertake commercial enterprises such as land transactions and trading undertakings. However, before a local government undertakes either a trading undertaking or a land transaction a local government must prepare and seek comment on a business plan. The plan must include:

- the expected effect on the provision of facilities and services by the local government;
- the expected effect on other persons providing facilities and services in the district;

- the expected financial effect on the local government;
- the expected effect on matters referred to in the local government's current plan;
- the ability of the local government to manage the undertaking or the performance of the transaction; and
- any other matter prescribed for the purposes of this subsection.

Commercial activities undertaken by local governments may include:

- caravan parks;
- post offices;
- property ownership;
- race courses;
- recreation centres/swimming pools/sporting complexes;
- service stations;
- supermarkets; and
- waste management.

However, Section 3.60 of the Act prohibits local government from forming or acquiring an incorporated company or body unless it is permitted to do so by other regulations.

Proposition 13

Local government does have the scope to undertake commercial activities, which provides an alternative source of own source revenue for local governments. However, local governments are restricted in their business practises, for example, their inability to control corporate bodies. When combined with the legislative requirement for business accountability and transparency, this may place local government in a disadvantageous competitive position.

Moreover, engaging in commercial activity purely for revenue purposes is argued to be outside the purpose of local government, and a distraction from the effective delivery of goods and services to the community.

Appendix 1- Western Australian ACLG Categorisation

Table 1- No. of Local Government Areas by ACLG Category, Western Australia, July 2007

URBAN (U)	39	**Capital City (CC)**	1		(1)	**UCC**
		Metropolitan Developed (D)	18	**Small (S)**	12	**UDS**
				Medium (M)	3	**UDM**
				Large (L)	2	**UDL**
				Very Large (V)	1	**UDV**
		Regional Towns/City (R)	10	**Small (S)**	8	**URS**
				Medium (M)	2	**URM**
				Large (L)		**URL**
				Very Large (V)		**URV**
		Fringe (F)	10	**Small (S)**	1	**UFS**
				Medium (M)	4	**UFM**
				Large (L)	4	**UFL**
				Very Large (V)	1	**UFV**
RURAL (R)	101	**Significant Growth (SG)**	6	**Not applicable**	(6)	**RSG**
		Agricultural (A)	74	**Small (S)**	53	**RAS**
				Medium (M)	17	**RAM**
				Large (L)	2	**RAL**
				Very Large (V)	2	**RAV**
		Remote (T)	21	**Extra Small (X)**	6	**RTX**
				Small (S)	3	**RTS**
				Medium (M)	6	**RTM**
				Large (L)	6	**RTL**
Total	140		140		140	

(Source: *DOTARS, 2002-2003 and LGAB, 2006*)

Appendix 2- Commonwealth Financial Assistance Grants

1. Financial Assistance Grants (FAGs)

Financial Assistance Grants were introduced by the Australian Government in 1974-75 as a way of distributing taxation revenue to local government. The primary objectives of FAGs are to:

- improved the capacity of local government to provide their residents with an equitable level of services;
- improve the financial capacity of local government;
- provide certainty of funding; and
- improve the efficiency and effectiveness of local government.

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*)

FAGs are distributed on the basis of a set of National Principles.

These include:

- allocation on the basis of horizontal fiscal equalization to ensure that each local government is able to function at a standard not lower than the average of other local governments;
- effort neutrality (i.e. policies of individual local governments in terms of revenue and expenditure effort should not effect grant determination);
- minimum grant – a minimum per capita allocation of general purpose grants regardless of service level and capacity;
- recognition of other relevant grant support;
- recognition of the needs of Aboriginal and Torres Strait Islanders; and
- local government amalgamations – when local governments merge their grants are maintained for four years as if they remained separate.

However, the achievable level of equalisation is limited both by the quantum of FAGs and the minimum grant condition. This particularly impacts on the financial capacity of local governments in regional and remote areas of Western Australia. To achieve full equalisation there would need to be an increase in the FAG pool and no minimum grant.

1.2 The Impact of the Size of the FAG Pool

Local Government Grants Commissions in each State determine the distribution of grants in accordance with the National Principles and taking into account local circumstances.

- They assess the amount each local government would need to be able to provide a standard range and quality of services, while raising revenue from a standard range of rates and other income sources.
- They determine each local government's raw grant by subtracting its revenue capacity from its expenditure need.
- In some cases a local government's raw grant does not comply with the minimum grant requirements. To increase the grants to local governments with raw grant allocations below the minimum grant, the grants to other local governments must be proportionally reduced. This process is termed factoring back. A "factoring back ratio" represents the percentage of the total equalisation requirement which has been funded in each year.

In Western Australia, the factoring back ratio was 91% in 2005-06 (even though the current Western Australian Local Government Grants Commission methodology is conservative[1]). The factoring back process would be unnecessary if the FAG pool were larger.

1.3 The Impact of the Minimum Grant

The minimum grant principle requires a minimum payment to all local governments not less than 30% of what they would receive if grants were allocated on a per capita basis.

The minimum grant requirement results in many local governments receiving more than an equalisation entitlement, at the cost of other local governments having their entitlements factored back.

The validity of the minimum grants principle is questionable, as it decreases the potential total funds available to local governments that have more need of grant support, either because of lower revenue raising capacity or higher expenditure requirements.

However, even if the minimum grant were removed some local governments would still receive more than their equalisation entitlements. To achieve full equalisation would require wealthy local governments to make payments into the FAGs pool.

Table 3 is taken from the 2004-05 Local Government National Report and shows that the minimum grant is a more significant limit on the achievement of fiscal equalisation in Western Australia than other States.

[1] Although possibly less conservative than some other States.

This could reflect the varying equalisation methodologies used across the States and/or a greater variability in financial capacity of local governments in Western Australia.

The table also suggests that the impact of the minimum grant on equalisation has grown significantly in recent years.

Table 2: Number of Local Governments on Minimum Grant 1996-97 to 2004-05

	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
2004-05								
Number of local governments	20	8	7	28	22	1	1	87
% of population	24	14	55	70	56	10	36	34

(Source: *DOTARS, 2006*)

The 2004-05 National Local Government Report, p52, indicates that from 1995-96 to 2005-06 the per capita funding for rural and regional local governments has increased by 38 per cent compared to 8 per cent for local governments in major cities (DOTARS, 2006).

“However 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.” (DOTARS, 2006).

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