

CHAPTER 13

ASSESSING REVENUE RAISING CAPACITY

1. On several of the Commission's consultation visits during this review, LGBs voiced concerns about the revenue capacity assessments done by their LGGC. LGBs are concerned about the influence revenue assessments are having on their grant outcomes.

2. Most LGGCs¹ assess revenue capacity for rate revenue only. However LGBs' reliance on municipal rates as a revenue source has declined steadily since 1961–62. Municipal rate revenue now accounts for less than half of all local government expenditure. All own source revenue (including non-rate revenue) should be taken into account by LGGCs, even if there is no differential assessment made of most categories.

3. This chapter analyses the current approaches used by the LGGCs to assess revenue capacity and then addresses the issue of non-rate revenue assessment.

CURRENT APPROACHES

4. The LGGCs have different ways of calculating revenue standards and assessing revenue capacity. Table 13-1 shows the different approaches to assessing revenue standards.

Table 13-1 LGGCS' APPROACHES TO CALCULATING REVENUE STANDARDS

State	Model used
New South Wales	Rate revenue per property for the State as a whole.
Victoria	Not applicable ^(a) .
Queensland	Not applicable ^(a) .
Western Australia	Not applicable ^(a) .
South Australia	Rate revenue per capita for the State as a whole.
Tasmania	Rate revenue per capita for the State as a whole.
Northern Territory	Not applicable ^(a) .

(a) This State does not calculate standard revenue, it goes straight to standardised revenue.

1 The Queensland LGGC is the exception.

5. Table 13-2 shows the different approaches to assessing revenue disabilities.

Table 13-2 HOW LGGCS ASSESS REVENUE DISABILITIES

State	Model used
New South Wales	Based on unimproved capital valuations. Averaged over three years. Discounted by around 70 per cent. Separate assessment of each LGB's share of compulsory Pensioner Rebates.
Victoria	Based on net annual valuations. Averaged over three years. There is a separate calculation of some user charges (creches, child care centres, and traffic fees and fines).
Queensland	Rate revenue by a regression equation ^(a) . Fees and charges assessed by the equal per capita method. Parking fines and fees, aerodrome charges and other transport charges are assessed by the actual per capita method. Indigenous communities are assumed to have zero revenue capacity.
Western Australia	Regression analyses — different analyses are used for different categories of revenue. Separate assessment for extraordinary revenue (payments by mining companies and payments relating to grain handling facilities).
South Australia	Based on improved capital valuations. Averaged over three years.
Tasmania	Based on assessed annual valuations. Averaged over three years.
Northern Territory	Based on share of assessed income. For the six municipal LGBs, assessed income is ABS average personal income multiplied by population aged 18 and over. For the Top End Indigenous LGBs, assessed income is \$4000 multiplied by population aged 18 and over. For the Central Indigenous LGBs, assessed income is \$3200 multiplied by population aged 18 and over. For Indigenous communities, 50 per cent of their operational subsidies from the Territory government are assessed by the actual per capita method.

(a) Independent variables are: number of properties, unimproved capital value, gross value of rural production, residual retail sales and personal income (capped at \$70 000).

6. The LGGCs assess revenue capacity using one of three approaches:

- (i) valuations;
- (ii) regression analysis; or
- (iii) personal income.

7. Assessed revenue capacity can be different under each approach and so the choice of approach can produce markedly different grant allocations. There is also potential to 'mis-assess' revenue capacity under each approach.

8. This chapter begins by considering the Commission's approach to assessing revenue capacity.

THE COMMISSION'S APPROACH

9. The equalisation principle governing State inquiries requires the Commission to measure the revenue a State would raise from its own sources if it made the same tax effort as other States.

10. This would be easy if all States made the same effort — had uniform tax policies². When there is no policy difference, differences in actual collections can only be due to non-policy influences. In this situation, the Commission's practice would be to use actual revenue as the measure of revenue capacity. This is referred to as the actual per capita approach.

11. More commonly, States have different tax policies. Actual revenues, therefore, reflect a mixture of policy and non-policy influences. The Effort Neutrality principle says that an individual government's policy choices should not affect its grant allocation. Therefore, the policy differences mean that actual revenue can no longer be used as an accurate measure of revenue capacity and the Commission's practice would be to assess capacity another way.

12. The Commission approaches the assessment of revenue capacity in three steps. It:

- (i) identifies tax policy differences — the Commission's practice is to first determine an average policy before identifying tax policies that are different from the average;
- (ii) quantifies the impact that any policy differences have on actual revenue; and
- (iii) removes these influences.

13. The Commission's approach to revenue assessments is all about removing the effects of policy differences (the influence of States' policy choices) from the comparisons. If this is achieved, a State is neither rewarded nor penalised for the differences between its policy choices and the average of the States' policies.

14. The Commission's approach requires explicit consideration of State policies and their impacts on actual revenue. The next section considers what it would mean to apply the Commission's approach to the assessment of Municipal Rates capacity. Six assessment options for Municipal Rates are considered, as are the implications of adopting each approach.

2 That is, they had the same policies on the rate of tax, the scope of the tax and compliance effort.

THE IMPLICATIONS AND IMPACTS OF DIFFERENT METHODS OF ASSESSING MUNICIPAL RATE CAPACITY

15. *The Commission's Approach.* The first step in the Commission's approach would be to examine the policies of each of the LGBs in the State, including:

- which properties are rated; and
- how they are rated.

16. The first question is concerned with:

- the range of properties that are rateable. Do LGBs have a common policy about which properties are or are not rateable?
- the types of properties that are rated. Do LGBs have a common policy about which types of properties are rated — residential, industrial, commercial, mining, pastoral, agricultural and other?
- eligibility for reduced rating. Do LGBs have a common policy for determining how the total rate impost will be distributed across rateable properties?

17. The second question is concerned about how LGBs impose rates. Do they impose:

- minimum rates?
- higher rates of tax on properties that have higher values?
- different rates of tax on different types of properties?
- the rate of tax using the same valuation system?
- different eligibilities for exemptions, concessions or remissions?
- different rates of tax in different regions?

18. It would use this information to:

- determine the average revenue raising policy of the LGBs;
- identify individual LGB's policies that differ from the average; and
- quantify the impact of those differences.

19. This process is based on explicitly identifying and removing policy influences. As shall be seen, other assessment methods are not as explicit.

20. **Other Approaches.** This section considers six methods of assessing revenue capacity. The six methods are:

- (i) actual per capita (APC);
- (ii) equal per capita (EPC);
- (iii) valuations; and
- (iv) effective tax rates (ETR) — three options.

21. Under the APC approach, an LGB's assessed revenue³ is equal to its actual revenue (this approach assumes all differences in revenue collections per capita are caused by non-policy influences).

22. Under the EPC approach, its assessed revenue is equal to the State average per capita revenue (this approach assumes all differences in revenue collections per capita are due to LGBs' policy choices).

23. Under the valuation approach, revenue capacity is equal to State revenue multiplied by an LGB's share of State property values.

24. Under the three ETR approaches assessed revenue is calculated by applying a rate in the dollar to an LGB's property values. The only difference is whether:

- a single rate in the dollar is used for all properties in all parts of the State (ETR 1);
- a separate rate in the dollar is calculated for each property type and used for that property type in all parts of the State (ETR 2); or
- a separate rate in the dollar is calculated for each property type in each region of the State (ETR 3).

25. Under the Commission's approach to revenue capacity, an explicit consideration of policy and non-policy influences is required. These six methods make implicit assumptions about policy and non-policy influences. Table 13-3 summarises how each method treats various influences. It shows that an influence can be built into the measure of an LGB's revenue capacity under one method (that is, the method treats the influence as a non-policy influence) but not another (that is, the method treats the influence as a policy choice).

26. The purpose of Table 13-3 is to show that the choice of assessment method brings with it implications about how various influences are treated. Table 13-3 shows that these treatments can have a material impact on the assessment of revenue capacity. Tables 13-4 to 13-8 summarise the revenue capacities of New South Wales, Victoria, Western

3 Assessed revenue is the revenue an LGB would raise if it applied the average revenue raising policies to its circumstances.

Australia, South Australia and Tasmania that would be assessed under each method and compare them with the capacities that would be assessed under the APC method.

Table 13-3 IMPACT OF INFLUENCES ON REVENUE CAPACITY^(a), VARIOUS METHODS

Influence	APC	EPC	Valuation	ETR 1	ETR 2	ETR 3
Differences in population	No	Yes	No	No	No	No
Differences in valuations	Yes	No	Yes	Yes	Yes	Yes
Use of minimum rates	Yes	No	No	No	No	No
Use of progressive rates of tax	Yes	No	No	No	No	No
Use of different rating strategy for different types of properties	Yes	No	No	No	Yes	Yes
Use of different valuation systems for different types of properties	Yes	No	No	No	No	No
Use of different eligibilities for exemptions, concessions or remissions	Yes	No	No	No	No	No
Use of different rating strategy for different regions of the State	Yes	No	No	No	No	Yes

(a) 'Yes' means influence is built into revenue capacity assessment and 'No' means that it is not built in.

Table 13-4 ASSESSED REVENUE CAPACITY, NEW SOUTH WALES, VARIOUS METHODS

Region	APC	EPC	Valuation	ETR 1 ^(a)	ETR 2	ETR 3 ^(b)
	\$m	\$m	\$m	\$m	\$m	\$m
Assessed Revenue Capacity						
Metropolitan	1 115.1	1 132.6	1 314.3	1 314.3	1 316.6	1 115.1
Urban	485.4	495.8	336.5	336.5	335.2	485.4
Rural	198.8	170.7	149.6	149.6	148.4	198.8
Remote	2.0	2.2	0.8	0.8	1.1	2.0
	1 801.3	1 801.3	1 801.3	1 801.3	1 801.3	1 801.3
Sum of Differences from APC assessment						
Metropolitan	0.0	17.5	199.2	199.2	201.5	0.0
Urban	0.0	10.4	-148.8	-148.8	-150.2	0.0
Rural	0.0	-28.1	-49.2	-49.2	-50.4	0.0
Remote	0.0	0.2	-1.2	-1.2	-0.9	0.0
	0.0	0.0	0.0	0.0	0.0	0.0

(a) The result is the same as the Valuation result because both approaches calculate a single rate in the dollar and apply it to all properties in all parts of the State.

(b) The result is the same as the APC result at the regional level because both approaches constrain a region's assessed revenue to equal its actual revenue. The results are not the same at the individual LGB level.

Source: Unpublished revenue data from the New South Wales LGGC.

Table 13-5 ASSESSED REVENUE CAPACITY, VICTORIA, VARIOUS METHODS

Region	APC	EPC	Valuation	ETR 1 ^(a)	ETR 2	ETR 3 ^(b)
	\$m	\$m	\$m	\$m	\$m	\$m
Assessed Revenue Capacity						
Metropolitan	925.6	952.9	1 008.9	1 008.9	na	925.6
Urban	307.5	293.0	240.9	240.9	na	307.5
Rural	84.0	71.1	67.3	67.3	na	84.0
Remote	na	na	na	na	na	na
	1 317.1	1 317.1	1 317.1	1 317.1	na	1 317.1
Sum of Differences from APC assessment						
Metropolitan	0.0	27.3	83.3	83.3	na	0.0
Urban	0.0	-14.4	-66.5	-66.5	na	0.0
Rural	0.0	-12.9	-16.7	-16.7	na	0.0
Remote	na	na	na	na	na	na
	0.0	0.0	0.0	0.0	na	0.0

(a) The result is the same as the Valuation result because both approaches calculate a single rate in the dollar and apply it to all properties in all parts of the State.

(b) The result is the same as the APC result at the regional level because both approaches constrain a region's assessed revenue to equal its actual revenue. The results are not the same at the individual LGB level.

na Not applicable. Victoria does not distinguish property type (ETR 2) and has no remote LGBs.

Source: Unpublished revenue data from Victorian LGGC.

Table 13-6 ASSESSED REVENUE CAPACITY, SOUTH AUSTRALIA, VARIOUS METHODS

Region	APC	EPC	Valuation	ETR 1 ^(a)	ETR 2	ETR 3 ^(b)
	\$m	\$m	\$m	\$m	\$m	\$m
Assessed Revenue Capacity						
Metropolitan	298.3	297.7	303.8	303.8	315.2	298.3
Urban	64.2	77.2	55.6	55.6	55.4	64.2
Rural	97.5	85.1	100.7	100.7	89.4	97.5
Remote	0.0	0.0	0.0	0.0	0.0	0.0
	460.0	460.0	460.0	460.0	460.0	460.0
Sum of Differences from APC assessment						
Metropolitan	0.0	-0.6	5.5	5.5	16.9	0.0
Urban	0.0	13.0	-8.6	-8.6	-8.8	0.0
Rural	0.0	-12.5	3.1	3.1	-8.1	0.0
Remote	0.0	0.0	0.0	0.0	0.0	0.0
	0.0	0.0	0.0	0.0	0.0	0.0

(a) This is the same as the Valuation approach because both methods implicitly calculate a single rate in the dollar and apply it to all properties in all parts of the State.

(b) This is the same as the APC approach because both approaches constrain each region's assessed revenue to its actual revenue.

Source: Unpublished revenue data from the South Australian LGGC.

Table 13-7 ASSESSED REVENUE CAPACITY, TASMANIA, VARIOUS METHODS

Region	APC	EPC	Valuation	ETR 1 ^(a)	ETR 2	ETR 3 ^(b)
	\$m	\$m	\$m	\$m	\$m	\$m
Assessed Revenue Capacity						
Metropolitan	100.7	94.5	107.8	107.8	na	100.7
Urban	71.1	77.7	64.6	64.6	na	71.1
Rural	74.9	74.5	74.3	74.3	na	74.9
Remote	na	na	na	na	na	na
	246.7	246.7	246.7	246.7	na	246.7
Sum of Differences from APC assessment						
Metropolitan	0.0	-6.14	7.10	7.10	na	0.0
Urban	0.0	6.57	-6.47	-6.47	na	0.0
Rural	0.0	-0.43	-0.63	-0.63	na	0.0
Remote	na	na	na	na	na	na
	0.0	0.00	0.00	0.00	na	0.0

(a) This is the same as the Valuation approach because both methods implicitly calculate a single rate in the dollar and apply it to all properties in all parts of the State.

(b) This is the same as the APC approach because both approaches constrain each region's assessed revenue to its actual revenue.

na Not applicable. Tasmania does not distinguish property type (ETR 2) and has no remote LGBs.

Source: Unpublished revenue data from Tasmanian LGGC.

27. The same trend is evident in each of the four States that use valuations in revenue assessments. That is, metropolitan LGBs are assumed to be able to raise much more than they actually do:

- New South Wales \$200 million (18 per cent⁴);
- Victoria \$83 million (9 per cent);
- South Australia \$6 million (2 per cent); and
- Tasmania \$7 million (7 per cent).

28. The trend is not evident in the Western Australian analysis but there is a simple explanation. Western Australia uses a different valuation basis for different property types. The rural region contains a higher proportion of agricultural and pastoral properties

4 The reason for the high difference for New South Wales compared to other States will be due in large part to the effects of rate pegging. Rate pegging has been in place since the late 1970s. Rate pegging means that the rapid growth in metropolitan property values produces a lower average rate in the dollar for these properties than the average rate in the dollar for non-metropolitan properties. In these circumstances, the use of a single rate in the dollar for each property type seems unreasonable.

that are valued using improved capital values compared with residential properties that are valued on an unimproved value basis.

29. The valuation column in Table 13-8 makes no adjustment for this difference and the figures in that column are therefore not useful. Because of this, the analysis has included an additional column showing the Western Australian LGGC's assessment of revenue capacity. It is very close to the APC outcome.

Table 13-8 ASSESSED REVENUE CAPACITY, WESTERN AUSTRALIA, VARIOUS METHODS

Region	APC	EPC	Valuation	ETR 1	ETR 2	ETR 3 ^(a)	WA ^(b)
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Assessed Revenue Capacity							
Metropolitan	348.0	375.3	-	187.7	355.3	348.0	345.4
Urban	55.2	53.9	-	30.8	52.8	55.2	52.9
Rural	88.9	66.8	-	288.7	84.5	88.9	93.3
Remote	20.1	16.1	-	5.0	19.6	20.1	20.6
	512.2	512.2	-	512.2	512.2	512.2	512.2
Sum of Differences from APC assessment							
Metropolitan	0.0	27.3	-	-160.3	7.3	0.0	-2.6
Urban	0.0	-1.3	-	-24.4	-2.4	0.0	-2.3
Rural	0.0	-22.1	-	199.8	-4.4	0.0	4.4
Remote	0.0	-3.9	-	-15.1	-0.4	0.0	0.5
	0.0	0.0	-	0.0	0.0	0.0	0.0

(a) This is the same as the APC approach because both approaches constrain each region's assessed revenue to its actual revenue.

(b) Western Australian LGGC's assessment of revenue capacity.

Source: Unpublished revenue data from the Western Australian LGGC.

30. The fact that the APC and EPC approaches yield similar results for most States suggests that the distribution of actual revenue must be similar to the distribution of population. The valuation outcomes produce a markedly different outcome because the distribution of valuations is very different and, in most cases, is skewed towards the metropolitan region⁵. It suggests that a decision on whether to base revenue capacity on population, actual revenue or valuations is important.

31. The ETR 1 approach uses a single rate in the dollar for all property types. The ETR 2 approach uses a single rate in the dollar for each different property type. The small difference in outcomes produced by the two approaches suggests that a decision on whether or not to have separate assessments for different property types is of lesser importance.

⁵ 62.9 per cent of people live in the metropolitan LGBs, they pay 61.9 per cent of all rates, but their properties account for 73.0 per cent of all valuations.

32. The ETR 3 approach uses a single rate in the dollar for each different property type and for each different region. The large difference in outcomes produced by this approach and the ETR 2 approach suggests that a decision on whether or not to have separate assessments for different regions of the State is important. This issue is considered further at the end of this chapter.

33. The choice of method brings with it implications about how certain influences are treated. Table 13-3 demonstrated that different choices can have very large implications for the assessment of revenue capacity. The next section considers the approaches used by each LGGC.

**IS AN LGGC'S CHOICE OF ASSESSMENT METHOD CAUSING ITS
REVENUE ASSESSMENTS TO HAVE A
DISPROPORTIONATE INFLUENCE ON ITS GRANT OUTCOMES?**

Assessment of Rate Revenue

34. The LGGCs assess revenue capacity using one of three approaches:

- (i) valuations;
- (ii) regression analysis; or
- (iii) personal income.

35. **Valuations.** New South Wales, Victoria, South Australia and Tasmania use this approach. New South Wales has separate assessments for each property type (effectively a version of the ETR 2 approach above). The other three do not (effectively the ETR 1 approach above).

36. Our concern with this approach is what is not shown. For example, consider the issue of minimum rates. Most LGBs levy minimum rates, yet there is no allowance for the effects of minimum rates. This omission means the use of minimum rates is treated as if it were a policy difference, despite the fact that most LGBs levy them.

37. Table 13-4 showed that the New South Wales LGGC approach produces a higher assessed revenue for the metropolitan LGBs, some \$200 million more than they actually raised. It subsequently discounts its revenue assessments by 70 per cent. If the reason for the discount is dissatisfaction with the assessed revenues that are produced, perhaps a different assessment method could be used. For example, the ETR 3 method restricts the influence of volatile valuations within groups of LGBs that are likely to experience similar volatility (metropolitan, urban, rural and remote).

38. Dissatisfaction with the outcomes produced by a valuation approach has led other States to choose different assessment methods.

39. **Regression Model.** Queensland and Western Australia use this approach. There are three potential problems with it.

40. First it can lead to the same difficulties as the valuation approach — it can lead to influences being treated as non-policy (and thus reflect them in the assessment of revenue capacity) without explicit consideration. Consider Figure 12-1. It compares implied tax rates per hectare for agricultural land in Western Australia. LGBs have been sorted from lowest average value of agricultural land per hectare to highest. The chart shows that higher rates of tax tend to be imposed by the LGBs with the lower average values per hectare.

41. If the Western Australian LGGC thought this practice was a reflection of policy choice rather than a non-policy influence, it would want to exclude this effect from its revenue capacity assessments. It could do so by using the average rating experience rather than LGBs' actual rating experience. However, the chart shows that LGBs with the lowest value per hectare have been assessed to have the highest revenue capacity.

42. The regression equation used by the Western Australian LGGC appears to assume that:

- LGBs with the lowest valuations have the highest per capita revenue capacity; and
- this is a non-policy influence.

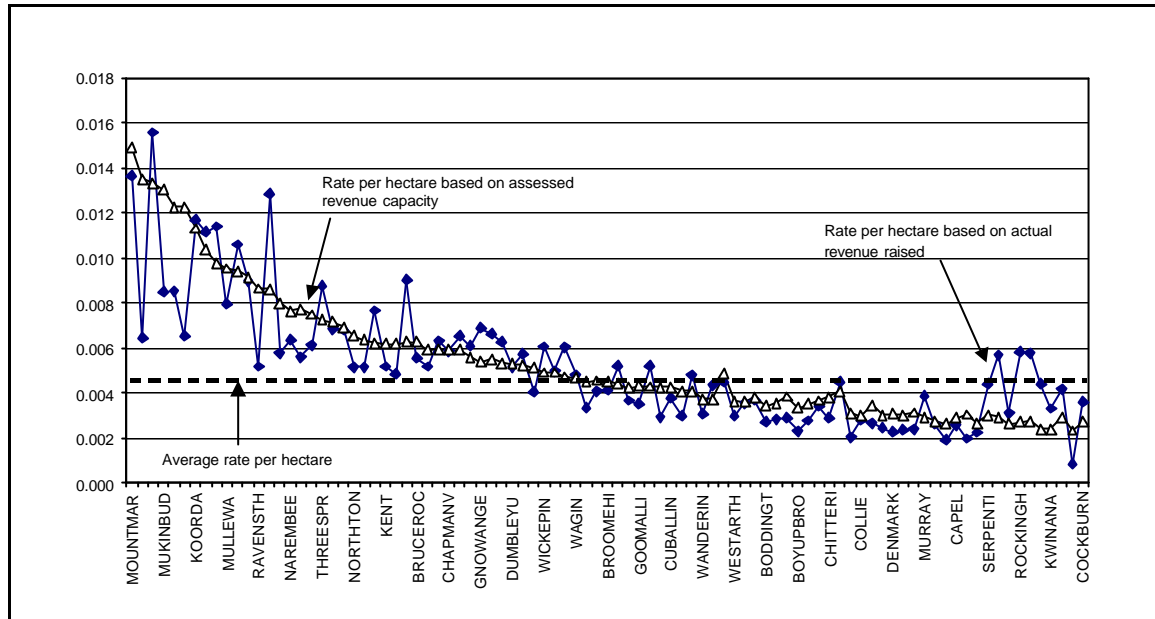
43. Providing it accords with the judgement of the Western Australian LGGC, there is nothing wrong with this assessment⁶. There would be a problem if it were unintended and simply the consequence of using a regression equation which has actual revenue as its dependent variable.

44. If the LGGC wanted to treat this influence as a policy choice, the regression model would need to be respecified to include a variable that would capture this influence. This would be true for every influence that the LGGC wanted to treat as a policy influence.

45. If the LGGCs do not develop their regression models with these considerations in mind, their models can lead to influences being treated as non-policy without explicit consideration.

6 Two possible explanations for the trend are: LGBs with lower average valuations are more likely to charge a minimum rate thus raising the average rate; and previous allocations have not been on an equalisation basis such that LGBs with a lower average value must charge a higher rate to provide an equivalent standard of service. The appropriate way to estimate revenue capacity will differ considerably if the reason for the trend were either of these.

Figure 13-1 IMPLIED RATES OF TAX PER HECTARE, AGRICULTURAL LAND, WESTERN AUSTRALIA^(a)



(a) LGAs ordered by average value per hectare from lowest to highest.

46. The second potential problem with a regression approach is that, if the regression equation includes variables that do not reflect the average rating practice, it can produce a revenue capacity assessment that is inconsistent with what LGBs do.⁷ Examples of such variables include personal income, residual retail sales and gross value of rural production. Including such variables means the LGGC is assessing revenue capacity based not on what LGBs actually do but on the ability of their ratepayers to pay.

47. The third potential problem is the impact of a regression approach on transparency, particularly if the focus is on maximising the fit of the regression equation. For instance, the equation used by Western Australian LGGC for agricultural rates is:

$$\text{Assessed Rates Revenue} = [(127.38 * \text{NumAs}) + (0.001737 * Tval) + (1.21 * Tarea)] * 1.149$$

where:

NumAs = number of rate assessments on agricultural properties, average of 1995–96 to 1997–98

Tval = total valuations of agricultural areas, averaged from 1995–96 to 1997–98

Tarea = total agricultural area in hectares, averaged from 1996 to 1998

Although this equation may provide a good fit with the rate revenue data for agricultural land, it is not obvious why area of agricultural land should be included in the equation.

7 Those that use the regression approach say that the use of the regression approach negates the need to have large numbers of disability factors. They observe that, although LGBs do not levy rates on the basis of personal income, this variable produces some of the ‘best fits’ for revenue. They think a possible explanation might be that, in practise, LGBs take into consideration the capacity of their rate payers to pay when levying rates.

48. **Personal Income.** The Northern Territory LGGC assesses revenue capacity using personal income statistics. It does so because it believes that it is not reasonable to assess rate revenue for municipal LGBs when most land in other LGBs is non-rateable. It uses personal income as its capacity measure. This produces:

- a lower assessed revenue capacity for the municipal LGBs than would be produced by a valuation approach; and
- a higher assessed revenue capacity for other LGBs.

ASSESSMENT OF NON-RATE REVENUE

49. As noted earlier, LGBs' reliance on municipal rates as a revenue source has declined steadily since 1961–62. Over this period, non-rate revenue has become an increasingly important revenue source.

50. The term 'non-rate revenue' covers a multitude of revenue sources. Examples include aerodrome charges, parking fees and fines, garbage and water charges, user charges levied for local governing services, business income, a service charge levied by Community Governments in the Northern Territory and other revenue.

51. At present, the majority of non-rate revenue is not assessed. The Queensland LGGC is the only body that makes an attempt to assess the full range of non-rate revenues. The New South Wales, Victorian, Western Australian and South Australian LGGCs assess some, but a very restricted range of non-rate revenues.

52. The Commission's practice would be to assess the full range of non-rate revenue, because it is more in keeping with a comprehensive assessment of needs. If two LGBs are identical in all respects except that the first has access to significant user charges, then it would be unfair to ignore that revenue source. To do so would place the first LGB in a more advantageous position than the other.

Reasons LGGCs do not Assess Non-Rate Revenue Capacity

53. The LGGCs do not assess non-rate revenue for a variety of reasons. During consultations, the most common reason given was simplicity. Some LGGCs said that including these revenues would increase the complexity of their assessment system without greatly improving its performance — the LGBs with the non-rate revenue capacity are the minimum grant LGBs. Since these LGBs already receive the minimum grant, the only effect of including non-rate revenue would be to make their equalisation assessment more negative and further from the minimum grant threshold. Thus, the work required to include non-rate revenue in the process is not warranted because it will not make any difference to grant outcomes.

54. The Western Australian LGGC does not assess aerodrome charges because it believes that the income raised offsets aerodrome expenditures. Kalgoorlie airport raises significant aerodrome charges because it is the alternate landing strip for planes flying

between the East and Perth. However, it incurs additional expenditures because it has to maintain a landing strip that can accept the largest planes. By not assessing these additional revenues and expenditures, the Western Australian LGGC has assumed that one offsets the other. If this is not the case and the revenue were less than the expenditure, the City of Kalgoorlie-Boulder would have to fund the shortfall from elsewhere in its budget. It is for this reason that the Commission's practice is to assess all expenditures and revenues. This approach would mean the City of Kalgoorlie-Boulder's extra revenue would be taken into account and their additional costs of providing airport services would also be assessed. This is a more transparent process.

A Separate Revenue Assessment or Deduction of User Charge Revenue from Expenditure?

55. Some of the LGGCs bring non-rate revenues into their models by subtracting user charges from the related expenditure function and assessing disabilities for the net expenditure. This implies that the revenue disabilities (relevant to the specific user charges) are identical, but the inverse of, the expenditure disabilities (that relate to providing the service).

56. This was the Commission's practice prior to the 1993 Review. In that review the Commission decided to discontinue that practice because it was convinced that expenditure disabilities were not an appropriate measure of user charge revenue capacity. For example, the overall expenditure factor for the Northern Territory is five times the Victorian factor. The net assessments used prior to the 1993 Review implied that, on a per capita basis, the Northern Territory could raise five times the user charges of Victoria.

57. The current Commission practice is to:

- (i) separate user charges from their related expenditure; and
- (ii) subject them to a separate revenue assessment.

Can Rate Revenue Capacity be Used as a Proxy for Non-Rate Revenue Capacity?

58. If the LGGCs were to include non-rate revenue in their models, they could combine it into the rate revenue assessment. This would be acceptable if the same disabilities applied to both. If different disabilities apply to each, then there should be a separate assessment of non-rate revenue.

59. An example in the local government environment is water and sewerage charges. In some LGBs, water and sewerage charges are a component of general rates while in others they are a separate charge. Therefore in some instances they are being included in the assessment of rate revenue capacity. The revenue capacity measure for these charges is likely to be property related rather than land value related. If this is true, then different disabilities should apply to water and sewerage charges. In this situation, they should probably be separated from general rates and a separate assessment undertaken.

60. If it were not possible to separate them from general rates, the Commission's practice would be to apply the rate assessment as a second best option.

Does the LGBs' Choice of How to Collect Revenue Matter?

61. In essence this is a data issue. For example, some LGBs collect parking fees and fines themselves. Others may set up a separate company to collect them.

62. To do a separate assessment of this revenue source, the LGGCs need to have comparable data. This could be complicated if there are two sources of data. It would be ideal to have both sets of data (with a separate assessment of parking fees and fines revenue undertaken using the combined revenues). However, if that is not possible, a separate assessment should be undertaken on whatever revenue data is available⁸.

Is the Assessment of Non-Rate Revenue Capacity in Conflict with the Effort Neutrality Principle?

63. Parking fees and fines revenue has been a concern for many LGGCs. The Victorian LGGC said that including parking fees for individual LGBs in its revenue assessments would conflict with the principle of Effort Neutrality, because an LGB's policy decision to increase or decrease (impose or not impose) parking fees would directly impact on its grant.

64. This would be true if an APC method of assessment were used. The APC method assumes that differences in revenue collections are due to non-policy influences only. The Victorian LGGC believes policy choices are at work in relation to parking fees so the APC method is not the appropriate capacity measure for parking fees. If an effort neutral measure of revenue capacity was used (say valuation of industrial/commercial land per hectare as a proxy for the tendency for traffic to accumulate) then an individual LGB's choice to increase or decrease parking fees would affect only its total revenue collected. It would not affect its share of revenue capacity.

Conclusion

65. Some issues to consider are as follows.

- LGGCs should choose methods of assessing revenue capacity that are consistent with their assumptions about whether an influence is a policy or non-policy influence. The choice of method builds certain assumptions, about the treatment of influences, into the resultant revenue capacity measure. Different methods can produce very different measures of revenue capacity.

⁸ The missing data would affect the category standard. If an effort neutral measure is used to assess revenue capacity, an individual LGB's share of actual collections would not affect its assessed share of revenue capacity.

- All else being equal, revenue equalisation should reduce the grants of LGBs that have a greater capacity to raise non-rate revenue, and increase the grants to LGBs that have lesser capacity.
- User charge revenue should be separated from the relevant expenditure function and a separate assessment of it should be undertaken.
- Non-rate revenue should not be included with rate revenue unless the revenue disabilities that apply to both sources of revenue are the same.
- LGGCs should include the full range of non-rate revenue in their models.

TECHNICAL APPENDIX — SHOULD MUNICIPAL RATE CAPACITY BE ASSESSED ON A REGIONAL BASIS?

66. Earlier in this chapter the issue of whether LGGCs ought to have a separate municipal rate assessment for different regions of the State was raised. The decision depends upon whether:

- there is a different rating practice in different parts of the State; and
- this difference is deemed to be a policy or non-policy influence.

67. Table 13-9 shows residential property data, by region, for New South Wales.

Table 13-9 RESIDENTIAL PROPERTY DATA BY REGION, NEW SOUTH WALES

Region	Total valuation (a)	Number of properties (b)	Rate revenue levied (c)	Average property value (d) = (a) / (b)	Average rates per property (e) = (c) / (b)	Implied tax rate (f) = (c) / (a)
	\$b	('000)	\$m	\$	\$	%
Metropolitan	157.0	1 327.3	753.1	118 256	567	0.48
Urban	35.4	640.6	325.1	55 242	507	0.92
Rural	3.8	162.7	53.2	23 055	327	1.42
Remote	0.0	3.1	0.7	10 926	235	2.15
Total	196.1	2 133.7	1 132.1	91 921	531	0.58

Source: New South Wales LGGC data.

68. Table 13-9 shows that, on average, metropolitan LGBs impose a lower rate of tax than the State average. It suggests a different relationship between rates and valuations.⁹ The question is whether the different relationship and the different rating practice reflect LGBs' policy or influences beyond their control?

69. If it is deemed to be LGBs' policy, then assessed revenue for metropolitan LGBs should be calculated using the State average rating practice (0.58 cents in the dollar) rather than their average metropolitan rating practice (0.48 cents in the dollar). If it is deemed to be a non-policy influence, then assessed revenue should be calculated using average metropolitan rating practice (0.48 cents in the dollar). As Table 13-4 showed, the difference in outcomes for the metropolitan LGBs is material — \$200 million. Does it seem reasonable to assume that the metropolitan LGBs could raise \$200 million (17 per cent) more than they have actually raised?

9 New South Wales has rate pegging. Therefore, very large increase in metropolitan valuations cannot led to very large increases in rates. Thus, rate pegging might give rise to a different relationship between rates and valuations in metropolitan areas compared to other areas of the State.

CHAPTER 14

FACTORING BACK

1. This chapter discusses the following issues:
 - (i) what is factoring back and why is it needed?
 - (ii) how could LGGCs factor back?
 - (iii) does the choice of method affect grant outcomes? and
 - (iv) which method of factoring back should be used?

What is Factoring Back and Why is it Needed?

2. The Act defines a form of horizontal equalisation that is about identifying disadvantaged (and advantaged) LGBs and bringing all the disadvantaged LGBs up to the financial position of the average LGB. In its report the Commission said the Commonwealth's intentions in providing Relative Need grants were to:

- provide additional assistance to only those LGBs that are relatively disadvantaged; and
- contribute to a reduction in the extent of their disadvantage (but not to provide sufficient assistance that would remove all of their disadvantage).

3. The Commission concluded that the Commonwealth's financial assistance grants are not designed to provide sufficient assistance to meet all of the assessed needs of the disadvantaged LGBs. In these circumstances LGGCs have to decide how to distribute the limited assistance available from the Relative Need pool among the disadvantaged LGBs in their State. This issue is colloquially known as Factoring back.

How Could LGGCs Factor Back?

4. In its report, the Commission discussed three approaches LGGCs could use. It suggested that LGGCs could distribute the Relative Need pool so that it:

- (i) meets some of the disadvantage of every disadvantaged LGB. For example, LGGCs could allocate the funds to meet the same proportion of needs — this is the approach used by the LGGCs of Victoria, Western Australia, Tasmania and the Northern Territory;
- (ii) reduces the level of disadvantage of the most disadvantaged LGBs¹; or
- (iii) provides a safety net which would meet all the needs of very disadvantaged LGBs and meet some of the needs of the remaining disadvantaged LGBs using one of the other two methods — this is the approach favoured by the New South Wales, Queensland and the South Australian LGGCs².

5. The three approaches have different underlying assumptions about how to distribute limited assistance:

- the first approach treats all disadvantaged LGBs the same. It assumes they all require a share of Relative Need grants because they are all disadvantaged. It uses the limited assistance to reduce their level of disadvantage by the same proportion;
- the second approach treats disadvantage in an absolute sense. It assumes that the limited assistance should be restricted to improving only the most disadvantaged LGBs. This approach would provide some disadvantaged LGBs with no Relative Need assistance, in effect, they would receive the same treatment as advantaged LGBs; and
- the third approach identifies ‘special need’ LGBs (for example, the Queensland LGGC identifies the Deed of Grant in Trust councils, the South Australian LGGC identifies the five Aboriginal councils) and treats them differently from other LGBs.

1 The assistance is first used to remove the relative disparity between the most disadvantaged and the second most disadvantaged LGBs. The per capita shortfall of the most disadvantaged LGB is reduced to the level of the second most disadvantaged LGB. The assistance is then used to remove the relative disparities between these two LGBs and the third most disadvantaged LGB. The per capita shortfalls of these two LGBs are reduced to the level of the third most disadvantaged LGB. This process continues until the assistance is exhausted.

2 New South Wales LGGC does not factor back the assessments of Silverton, Tibooburra or Lord Howe Island. The Queensland LGGC does not factor back the assessments of its Deed of Grant in Trust councils. The South Australian LGGC does not factor back the assessments of the five discrete Indigenous communities or the Outback Areas Community Development Trust.

Does the Choice of Method Affect Grant Outcomes?

6. The choice of method does affect individual LGB grant outcomes. This can be demonstrated with a simple example. Suppose there are six LGBs (with the same sized population) and their assessed levels of advantage/disadvantage are:

- LGB A — an assessed advantage of \$150 million;
- LGB B — an assessed advantage of \$50 million;
- LGB C — an assessed disadvantage of \$20 million;
- LGB D — an assessed disadvantage of \$30 million;
- LGB E — an assessed disadvantage of \$60 million; and
- LGB F — an assessed disadvantage of \$90 million.

7. In this simple example, \$200 million would remove all of the assessed needs of the disadvantaged LGBs. But suppose only \$90 million is available. The three approaches listed previously would distribute the \$90 million in different ways. LGBs A and B are advantaged and would receive no Relative Need assistance under any of three approaches.

8. The first approach is to meet some of the disadvantage of every disadvantaged LGB. The simplest method of doing this would be to meet 45 per cent (that is, 90/200) of each LGB's assessed disadvantage.

9. The second approach is to reduce the level of disadvantage of the most disadvantaged LGBs. This approach would use the \$90 million to reduce the level of disadvantage of LGB F to bring it up to the level of disadvantage of LGB E. If there is any assistance left, it would be used to reduce the levels of disadvantage of LGBs E and F to bring them up to the level of disadvantage of LGB D and so on.

10. The third approach is to provide a safety net which would meet all the needs of very disadvantaged LGBs and meet some of the needs of the remaining disadvantaged LGBs. In this example, it might mean the removal of all of LGB F's disadvantage.

Table 14-1 DISTRIBUTION OF ASSISTANCE, VARIOUS OPTIONS

LGB	Method of Distributing the \$90 million of Assistance			
	Assessed level of disadvantage	Meet some of the disadvantage of every disadvantaged LGB	Reduce the level of disadvantage of the most disadvantaged LGBs	The safety net approach
	\$m	\$m	\$m	\$m
LGB A	-150.0	0.0	0.0	0.0
LGB B	-50.0	0.0	0.0	0.0
LGB C	20.0	9.0	0.0	0.0
LGB D	30.0	13.5	0.0	0.0
LGB E	60.0	27.0	30.0	0.0
LGB F	90.0	40.5	60.0	90.0
Total	200.0	90.0	90.0	90.0

11. Table 14-1 shows the distribution of the \$90 million under each of these approaches. Although this is only a simple example, Table 14-1 demonstrates that the choice of method does affect individual LGB's grant outcomes.

Which Method of Factoring Back Should be Used?

12. In its report, the Commission said that:

- (i) there were no overriding conceptual or methodological issues arising from these alternative approaches; and
- (ii) it was a matter of judgement as to whether one delivers outcomes more in line with the underlying equity intention.

13. It concluded that how the limited assistance is to be distributed should be left to the judgement of individual LGGCs, because:

- the diversity of LGBs' circumstances suggests that it would not be sensible to mandate a single approach for every LGGC; and
- it requires LGGCs to balance the equity objective against the practicalities associated with having insufficient assistance to meet all of the assessed needs.

14. In the remainder of this chapter we provide a worked example of how the different approaches might operate. The example is based on:

- 10 fictitious LGBs;
- 2 expenditure categories (Roads and Other);
- 3 revenue categories (Municipal Rates, User Charges and Other); and
- 4 forms of Commonwealth assistance (Per Capita grants, Local Roads grants, Relative Need grants and Other grants).

15. The example is provided in both a Balanced Budget and a Direct Assessment format. It also demonstrates that, correctly specified, these two distribution models produce the same assessed advantage/disadvantage and, therefore, the same LGB grant outcomes.

THE WORKED EXAMPLE — BALANCED BUDGET MODEL

16. Chapter 11 set out the **Balanced Budget Model**. It can be expressed as³:

$$\begin{array}{lcl}
 \text{Relative Need} & \textit{equals} & \text{assessed costs of providing services} \\
 \text{grant} & & \\
 & \textit{plus} & \text{assessed average operating surplus/deficit} \\
 & \textit{less} & \text{assessed revenue} \\
 & \textit{less} & \text{actual receipt of other grant assistance}
 \end{array}$$

17. The Balanced Budget Model as implemented by LGGCs omits the operating surplus/deficit term. The average operating surplus/deficit term is included in the example used in this chapter.

Population

18. Table 14-2 sets out the assumed population for each of the ten LGBs.

Table 14-2 ASSUMED POPULATION

Local Governing Body										Total
1	2	3	4	5	6	7	8	9	10	population
250	750	9 000	18 000	20 000	37 000	65 000	80 000	120 000	150 000	500 000

³ Unless otherwise stated, the figures in the worked example are expressed in millions of dollars.

Standard Budget

19. Table 14-3 sets out total expenditure and revenue by function. It shows that expenditures exceed revenues by \$5 million, so that the LGBs are in overall deficit.

Table 14-3 ASSUMED STANDARD BUDGET

Area of expenditure/revenue	Amount spent/raised/received	
	By all LGBs	Average
	\$m	\$pc
Expenditure		
Roads expenditure	30.0	60.00
Other expenditure	300.0	600.00
Total expenditure	330.0	660.00
Revenue		
Municipal rates	150.0	300.00
User charges	10.0	20.00
Other revenue	50.0	100.00
Total revenue	210.0	420.00
Other Grants		
Relative Need grants	60.0	120.00
Per Capita grants	20.0	40.00
Local Roads grants	30.0	60.00
Other Grant Assistance	5.0	10.00
Total Other Grants	115.0	230.00
Overall Operating Surplus	-5.0	-10.00

Assumed Factors

20. The per capita figures in Table 14-3 form the category standards to which assumed disability factors and revenue capacity ratios are applied to calculate standardised expenditures and revenues. The assumed factors are given in Table 14-4. They have been calculated in accordance with normal Commission practice — the average factor for the LGBs as a whole is 1.0000. A factor of one for each LGB implies an equal per capita (EPC) assessment. The Other Grants Assistance factor is based on each LGB's actual receipt of other grants and is, therefore, an actual per capita (APC) assessment.

21. For expenditure functions, a factor above one signals disadvantage — the LGB has above average costs of service provision. For revenue functions (including other grant assistance) a factor below one signals disadvantage — the LGB has a below average revenue capacity.

22. In the example, the same assessment method has been used both to distribute the Local Roads grants and to assess road needs in the Relative Need calculation.

Table 14-4 ASSUMED FACTORS FOR THE RELATIVE NEED CALCULATION

Function	Local Governing Body									
	1	2	3	4	5	6	7	8	9	10
Roads expenditure	4.98728	4.48855	2.99237	1.99491	1.49618	1.19695	0.94758	0.84784	0.84784	0.84784
Other expenditure	4.63951	1.85580	1.85580	1.39185	1.85580	0.74232	0.83511	1.39185	0.83511	0.83511
Municipal rates	0.79761	0.79761	0.79761	0.89731	0.89731	0.89731	0.89731	1.04686	1.04686	1.04686
User charges	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000
Other revenue	0.00000	0.00000	0.09940	0.29821	0.39761	0.59642	0.69583	0.79523	1.09344	1.49105
Per Capita grants	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000
Local Roads grants	4.98728	4.48855	2.99237	1.99491	1.49618	1.19695	0.94758	0.84784	0.84784	0.84784
Other Grant Assistance	4.00000	5.33333	0.55556	0.55556	1.00000	1.08108	0.76923	0.87500	0.83333	1.33333
Operating Surplus	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000	1.00000

23. Table 14-5 sets out the assessed costs and assessed revenues (in millions of dollars). These were calculated by multiplying the factors in Table 14-4, the per capita standards in Table 14-3 and the populations in Table 14-2. For each function, the sum of assessed costs (revenues) is equal to the total actual expenditure (revenue) shown in Table 14-3. This result occurs because the average factor for each function is 1.00000.

24. In accordance with Commission practice, the overall operating surplus is distributed between LGBs on an EPC basis (factors of 1.00000).

Table 14-5 ASSESSED COSTS OF SERVICE PROVISION AND REVENUES

Function	Local Governing Body										Total
	1	2	3	4	5	6	7	8	9	10	
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Roads expenditure	0.1	0.2	1.6	2.2	1.8	2.7	3.7	4.1	6.1	7.6	30.0
Other expenditure	0.7	0.8	10.0	15.0	22.3	16.5	32.6	66.8	60.1	75.2	300.0
Assessed costs	0.8	1.0	11.6	17.2	24.1	19.1	36.3	70.9	66.2	82.8	330.0
Municipal Rates	0.1	0.2	2.2	4.8	5.4	10.0	17.5	25.1	37.7	47.1	150.0
User Charges	0.0	0.0	0.2	0.4	0.4	0.7	1.3	1.6	2.4	3.0	10.0
Other Revenue	0.0	0.0	0.1	0.5	0.8	2.2	4.5	6.4	13.1	22.4	50.0
Assessed revenues	0.1	0.2	2.4	5.7	6.6	12.9	23.3	33.1	53.2	72.5	210.0
Per Capita grants	0.0	0.0	0.4	0.7	0.8	1.5	2.6	3.2	4.8	6.0	20.0
Local Roads grants	0.1	0.2	1.6	2.2	1.8	2.7	3.7	4.1	6.1	7.6	30.0
Other Grant Assistance	0.0	0.0	0.1	0.1	0.2	0.4	0.5	0.7	1.0	2.0	5.0
Other grants received	0.1	0.3	2.0	3.0	2.8	4.5	6.8	8.0	11.9	15.6	55.0
Assessed Operating Surplus	0.0	0.0	-0.1	-0.2	-0.2	-0.4	-0.7	-0.8	-1.2	-1.5	-5.0
Relative Need grants required^(a)	0.6	0.6	7.1	8.3	14.5	1.3	5.5	29.0	-0.1	-6.8	60.0

(a) Equal to assessed costs plus assessed operating surplus less assessed revenue and other grants received.

25. Two LGBs (numbers 9 and 10) are assessed to require a negative Relative Need grant. This signifies that these LGBs are advantaged overall — they have sufficient assessed revenues and grants to finance their assessed costs. The remaining LGBs are assessed to be disadvantaged.

26. Because of their high relative assessed revenues (including grant assistance) and low relative assessed costs, the advantaged LGBs are, in horizontal equalisation terms, overequalised. If they were to be placed on a ‘full’ horizontal equalisation footing, an amount of money equal to their assessed advantage (their negative Relative Need assessment) would be taken away from them and redistributed among disadvantaged LGBs. In the Australian local government context, this is not a practical option — all that can be done is that they receive no Relative Need grant. However, because they do not contribute funds to the pool for redistribution, these LGBs will remain overequalised.

27. Correspondingly, in the absence of such redistributions from the advantaged LGBs, it is not possible to place the disadvantaged LGBs on a ‘full’ horizontal equalisation footing. They must remain underequalised.

How Should the Available Grants be Allocated?

28. In the example, the amount of grants required by the underequalised LGBs is \$66.9 million but only \$60.0 million is available. The available assistance has to be shared among the disadvantaged LGBs.

29. **Approach 1 – Meet Some of the Disadvantage of Every Disadvantaged LGB.** If the aim is to meet some of the disadvantage of every disadvantaged LGB, there are many ways that this could be done. Two options would be to share the available assistance:

- (i) according to each LGB’s assessed level of disadvantage — in this chapter this option is referred to as the proportional method (it is the option most used by LGGCs); or
- (ii) so that disadvantaged LGBs are underequalised to the same degree — in this chapter this option is referred to as the Equalisation Ratio method.

30. Under the proportional method, the Relative Need grant to each underequalised LGB is reduced by the same proportion, irrespective of differences in capacity to raise revenues from all sources. Under the Equalisation Ratio method, the Relative Need grant to each LGB is reduced according to its overall capacity to suffer the loss, that is, taking into account its assessed revenue from all sources.

31. The proportional method is by far the easiest to implement. Table 14-6 shows how it would be implemented.

Table 14-6 DISTRIBUTION OF RELATIVE NEED GRANTS, PROPORTIONAL METHOD

Function	Local Governing Body									
	1	2	3	4	5	6	7	8	9	10
Grants required ^(a) \$m	0.6	0.6	7.1	8.3	14.5	1.3	5.5	29.0	0.0	0.0
Percentage share ^(b) %	0.91	0.84	10.61	12.39	21.66	1.98	8.22	43.39	0.00	0.00
Grants allocated ^(c) \$m	0.5	0.5	6.4	7.4	13.0	1.2	4.9	26.0	0.0	0.0

- (a) Negative ‘Grants required’ figures are set to zero.
- (b) Calculated as percentage share of ‘Grants required’.
- (c) Calculated by applying percentage share to total available assistance.

32. The Equalisation Ratio method requires the introduction of a new concept — the Equalisation Ratio. It is calculated as:

$$\text{Equalisation Ratio}_i = \frac{\text{Grants required}_i + \text{Assessed revenue}_i + \text{Other Grant Assistance received}_i}{\text{Assessed Costs}_i + \text{Overall Operating Surplus}_s}$$

33. The technical appendix to this chapter explains the derivation of the Equalisation Ratio. It defines the numerator as the LGB's overall assessed capacity and the denominator as its overall expenditure requirement. The Equalisation Ratio relates the revenue resources available to an LGB to its expenditure requirements.

34. The Equalisation Ratio can be used to determine whether an LGB is equalised, overequalised or underqualised:

- if the ratio equals one, the LGB is equalised;
- if the ratio is greater than one, the LGB is overequalised; and
- if the ratio is less than one, the LGB is underqualised.

35. Full horizontal equalisation implies that, after Relative Need grants are distributed, all LGBs would have an equalisation ratio of one.

36. The premise of the Equalisation Ratio method is that the purpose of sharing assistance is to distribute Relative Need grants so that all the disadvantaged LGBs are underqualised to the same degree — that is, after distributing the Relative Need grants, the equalisation ratios of the disadvantaged LGBs are the same. Table 14-7 shows the proportional method does not produce that outcome.

Table 14-7 CALCULATION OF EQUALISATION RATIO, EQUALISATION RATIO METHOD

Function	Local Governing Body										Total
	1	2	3	4	5	6	7	8	9	10	
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Allocation of Relative Need grants	0.5	0.5	6.4	7.4	13.0	1.2	4.9	26.0	0.0	0.0	60.0
Assessed revenue	0.1	0.2	2.4	5.7	6.6	12.9	23.3	33.1	53.2	72.5	210.0
Other grants received	0.1	0.3	2.0	3.0	2.8	4.5	6.8	8.0	11.9	15.6	55.0
Overall assessed capacity	0.7	1.0	10.8	16.2	22.4	18.6	35.0	67.1	65.1	88.1	325.0
Assessed costs	0.8	1.0	11.6	17.2	24.1	19.1	36.3	70.9	66.2	82.8	330.0
Assessed Operating Surplus	0.0	0.0	-0.1	-0.2	-0.2	-0.4	-0.7	-0.8	-1.2	-1.5	-5.0
Overall expenditure requirement	0.8	1.0	11.5	17.0	23.9	18.8	35.6	70.1	65.0	81.3	325.0
Equalisation ratio	0.91835	0.94363	0.93664	0.94976	0.93742	0.99274	0.98409	0.95732	1.00123	1.08383	1.00000

37. Table 14-7 shows:

- two LGBs are overequalised (their overall assessed capacity exceeds their overall expenditure requirement) — an equalisation ratio above one;
- eight LGBs are underequalised (their overall assessed capacity falls short of their overall expenditure requirement) — an equalisation ratio below one; and
- the eight LGBs are underequalised to a different degree — their equalisation ratios are different.

38. The last point highlights the difference between the proportional method and the Equalisation Ratio method. The proportional method reduces each disadvantaged LGB's required grant by the same proportion. The Equalisation Ratio determines the adjustment to each LGB's required grant by taking into account:

- its overall expenditure requirement; and
- its overall assessed capacity.

39. Under this method the shortfall in grants (the \$6.9 million) should be shared in accordance with the LGBs' overall assessed capacities. The steps involved are:

- (i) calculate the level of grants that would be required to fully equalise all the disadvantaged LGBs (the \$66.9 million figure in our example);
- (ii) calculate the difference between this level of grants and the grants available — the shortfall (the \$6.9 million figure in our example);
- (iii) calculate an adjustment for each disadvantaged LGB by distributing the shortfall in accordance with each disadvantaged LGB's share of the overall assessed capacity for all disadvantaged LGBs; and
- (iv) deduct each LGB's adjustment from its grant assessed in step (i).

40. Table 14-8 shows how each LGB's adjustment would be calculated.

Table 14-8 CALCULATION OF ADJUSTMENT, EQUALISATION RATIO METHOD

Function	Local Governing Body										Total
	1	2	3	4	5	6	7	8	9	10	
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Relative Need grants required	0.6	0.6	7.1	8.3	14.5	1.3	5.5	29.0	-0.1	-6.8	60.0
Assessed revenue	0.1	0.2	2.4	5.7	6.6	12.9	23.3	33.1	53.2	72.5	210.0
Other grants received	0.1	0.3	2.0	3.0	2.8	4.5	6.8	8.0	11.9	15.6	55.0
Overall assessed capacity	0.8	1.0	11.5	17.0	23.9	18.8	35.6	70.1	65.0	81.3	325.0
Percentage share ^(a)	0.43	0.58	6.46	9.52	13.36	10.50	19.93	39.22	0.00	0.00	100.00
Adjustment	0.0	0.0	-0.4	-0.7	-0.9	-0.7	-1.4	-2.7	0.0	0.0	-6.9

(a) For each underequalised LGB, this is calculated as its percentage share of the aggregate overall assessed capacity for all underequalised LGBs. For overequalised LGBs, the figure is set to zero.

41. Table 14-9 shows the distribution of the Relative Need grants under the Equalisation Ratio method.

Table 14-9 DISTRIBUTION OF RELATIVE NEED GRANTS, EQUALISATION RATIO METHOD

Function		Local Governing Body									
		1	2	3	4	5	6	7	8	9	10
Grants required	\$m	0.6	0.6	7.1	8.3	14.5	1.3	5.5	29.0	-0.1	-6.8
Adjustment	\$m	0.0	0.0	-0.4	-0.7	-0.9	-0.7	-1.4	-2.7	0.0	0.0
Grants allocated ^(a)	\$m	0.6	0.5	6.7	7.6	13.6	0.6	4.1	26.3	0.0	0.0

(a) Advantaged LGBs do not require grants, so their 'Grant allocated' figure is set to zero.

42. Table 14-10 confirms that the Equalisation Ratio method distributes Relative Need grants in a way that equalises the underequalised LGBs to the same degree — that is, after distributing the Relative Need grants, their equalisation ratios are the same.

Table 14-10 CALCULATION OF EQUALISATION RATIO, EQUALISATION RATIO METHOD

Function	Local Governing Body										Total
	1	2	3	4	5	6	7	8	9	10	
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Allocation of Relative Need grants	0.6	0.5	6.7	7.6	13.6	0.6	4.1	26.3	0.0	0.0	60.0
Assessed revenue	0.1	0.2	2.4	5.7	6.6	12.9	23.3	33.1	53.2	72.5	210.0
Other grants received	0.1	0.3	2.0	3.0	2.8	4.5	6.8	8.0	11.9	15.6	55.0
Overall assessed capacity	0.7	1.0	11.1	16.4	22.9	18.0	34.2	67.4	65.1	88.1	325.0
Assessed costs	0.8	1.0	11.6	17.2	24.1	19.1	36.3	70.9	66.2	82.8	330.0
Assessed Operating Surplus	0.0	0.0	-0.1	-0.2	-0.2	-0.4	-0.7	-0.8	-1.2	-1.5	-5.0
Overall expenditure requirement	0.8	1.0	11.5	17.0	23.9	18.8	35.6	70.1	65.0	81.3	325.0
Equalisation ratio	0.96141	0.96141	0.96141	0.96141	0.96141	0.96141	0.96141	0.96141	1.00123	1.08383	1.00000

43. The Equalisation Ratio method places those LGBs that receive Relative Need assistance in the same relative position. They are able to finance the same proportion of their overall expenditure requirement. The disadvantage of this method is that, like equalisation itself, it is complex and would not be easy to explain to LGBs.

44. Table 14-11 shows the total grants received by each LGB under the Equalisation Ratio method. It shows that:

- LGBs receive four separate forms of Commonwealth assistance — Relative Need grants, Per Capita grants, Local Roads grants and (assuming they are provided by the Commonwealth) Other Grant Assistance grants;
- the Relative Need assessment takes into account the LGB's receipt of other assistance;
- an LGB's share of Per Capita and Local Roads grants does not depend on its Relative Need assessment — LGBs assessed to have a negative Relative Need assessment still receive a Per Capita and a Local Roads grant; and
- an LGB's total receipt of Commonwealth assistance is the sum of its Relative Need, Per Capita, Local Roads and (assuming it was provided by the Commonwealth) Other Grant Assistance grants.

Table 14-11 DISTRIBUTION OF TOTAL COMMONWEALTH ASSISTANCE, EQUALISATION RATIO METHOD

Local Governing Body	Relative Need grant	Per Capita grant	Local Roads grant	Other Grant Assistance	Total grants
	\$m	\$m	\$m	\$m	\$m
LGB 1	0.6	0.0	0.1	0.0	0.7
LGB 2	0.5	0.0	0.2	0.0	0.8
LGB 3	6.7	0.4	1.6	0.1	8.7
LGB 4	7.6	0.7	2.2	0.1	10.6
LGB 5	13.6	0.8	1.8	0.2	16.4
LGB 6	0.6	1.5	2.7	0.4	5.1
LGB 7	4.1	2.6	3.7	0.5	10.9
LGB 8	26.3	3.2	4.1	0.7	34.3
LGB 9	0.0	4.8	6.1	1.0	11.9
LGB 10	0.0	6.0	7.6	2.0	15.6
Total	60.0	20.0	30.0	5.0	115.0

45. The preceding analysis was based on the first approach to distributing the limited assistance — to meet some of the assistance of every disadvantaged LGB. But there are two other approaches.

46. *Approach 2 – Reduce the Level of Disadvantage of the Most Disadvantaged LGBs.* If the aim is to reduce the level of disadvantage of the most disadvantaged LGBs, then the LGGCs would have to define what most disadvantaged meant. Possible definitions are:

- the LGB with the largest requirement for Relative Need grants; or
- the LGB with the largest per capita requirement for Relative Need grants.

47. The latter definition is used in the following example. Table 14-12 sets out the per capita requirements of each LGB and the allocation of Relative Need grants based on this approach.

Table 14-12 DISTRIBUTION OF RELATIVE NEED GRANTS, APPROACH 2

Function	Local Governing Body										
	1	2	3	4	5	6	7	8	9	10	
Relative Need grants required	\$m	0.6	0.6	7.1	8.3	14.5	1.3	5.5	29.0	-0.1	-6.8
Population		250	750	9 000	18 000	20 000	37 000	65 000	80 000	120 000	150 000
Relative Need grants required	\$pc	2434.42	750.87	788.70	460.54	724.53	35.75	84.60	362.78	-0.67	-45.43
Ranking		1	3	2	5	4	8	7	6	na	na
Relative Need grants allocated	\$m	0.6	0.5	6.8	7.8	13.9	0.2	3.6	26.6	0.0	0.0

Note: The available assistance is sufficient to bring all disadvantaged LGBs up to a level of disadvantage of \$29.98 per capita. Relative Need grants are allocated to place each disadvantaged LGB in that position.

48. **Approach 3 – Provide a Safety Net for Some LGBs.** An LGGC might decide to remove all the need of some very disadvantaged LGBs. After doing so it would distribute the remaining assistance using one of the other methods (for simplicity, assume it is the proportional option, the first option under the first approach).

49. Suppose the LGGC wanted to remove all the disadvantage of LGBs 1, 2, 3 and 5. This would reduce the level of assistance available to the other LGBs by \$37.2 million. The remaining \$22.8 million would be allocated among LGBs 4, 6, 7 and 8 based on their assessed level of disadvantage. The \$22.8 million is about 84 per cent of their collective assessed disadvantage so that each of these LGBs would receive about 84 per cent of its assessed disadvantage. Table 14-13 shows this distribution of assistance.

Table 14-13 DISTRIBUTION OF RELATIVE NEED GRANTS, APPROACH 3

Function	Local Governing Body										
	1	2	3	4	5	6	7	8	9	10	
Relative Need grants required	\$m	0.6	0.6	7.1	8.3	14.5	1.3	5.5	29.0	-0.1	-6.8
Relative Need grants allocated	\$m	0.6	0.6	7.1	7.0	14.5	1.1	4.6	24.5	0.0	0.0

Note: After removing all the disadvantage of LGBs 1, 2, 3, and 5, there is only sufficient assistance to meet 84.38 per cent of the disadvantage of LGBs 4, 6, 7 and 8. They receive 84.38 per cent of their required grants. LGBs 1, 2, 3 and 5 receive all of their required grant. LGBs 9 and 10 are advantaged and receive no grant.

53. Expenditure, revenue and Other Grant Assistance needs for each LGB are calculated using the formulae⁴:

Expenditure needs	<i>equals</i>	LGB's assessed cost of providing services
	<i>less</i>	LGB's population share of total expenditure ⁵
Revenue needs	<i>equals</i>	LGB's population share of total revenue
	<i>less</i>	LGB's assessed revenue
Other Grant Assistance needs	<i>equals</i>	LGB's population share of total grant assistance
	<i>less</i>	LGB's actual receipt of grant assistance.

54. Table 14-15 sets out the expenditure, revenue and Other Grant Assistance needs.

- Expenditure needs were calculated by subtracting an LGB's population share of total expenditure from its assessed costs in Table 14-5;
- Revenue needs were calculated by subtracting an LGB's assessed revenue in Table 14-5 from its population share of total revenue; and
- Other Grant Assistance needs were calculated by subtracting an LGB's actual receipt of Other Grant Assistance in Table 14-5 from its population share of total Other Grant Assistance.

4 This is similar to the New South Wales and South Australian approach to calculating expenditure and revenue allowances. The only difference is that category standards are calculated using population rather than numbers of properties or road lengths.

5 The Commission's practice is to calculate standard expenditure (revenue or Other Grants) in per capita terms, by dividing total expenditure (revenue or Other Grants) by total population. However, this worked example is expressed in millions of dollars rather than in per capita terms. For each LGB, its standard revenue is obtained by multiplying the per capita standard revenue by its population. The result is identical to its population share of total revenue.

Table 14-15 ASSESSED EXPENDITURE, REVENUES AND OTHER GRANT ASSISTANCE NEEDS

Function	Local Governing Body										Total
	1	2	3	4	5	6	7	8	9	10	
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Share of assistance	0.0	0.1	1.1	2.2	2.4	4.4	7.8	9.6	14.4	18.0	60.0
Roads expenditure	0.1	0.2	1.1	1.1	0.6	0.4	-0.2	-0.7	-1.1	-1.4	0.0
Other expenditure	0.5	0.4	4.6	4.2	10.3	-5.7	-6.4	18.8	-11.9	-14.8	0.0
Expenditure needs	0.6	0.5	5.7	5.3	10.9	-5.3	-6.6	18.1	-13.0	-16.2	0.0
Municipal rates	0.0	0.0	0.5	0.6	0.6	1.1	2.0	-1.1	-1.7	-2.1	0.0
User charges	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other revenue	0.0	0.1	0.8	1.3	1.2	1.5	2.0	1.6	-1.1	-7.4	0.0
Revenue needs	0.0	0.1	1.4	1.8	1.8	2.6	4.0	0.5	-2.8	-9.5	0.0
Per Capita grants	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Local Roads grants	-0.1	-0.2	-1.1	-1.1	-0.6	-0.4	0.2	0.7	1.1	1.4	0.0
Other Grant Assistance	0.0	0.0	0.0	0.1	0.0	0.0	0.2	0.1	0.2	-0.5	0.0
Other grant assistance needs	-0.1	-0.2	-1.0	-1.0	-0.6	-0.5	0.4	0.8	1.3	0.9	0.0
Grants required	0.6	0.6	7.1	8.3	14.5	1.3	5.5	29.0	-0.1	-6.8	60.0

55. The grant required figures are identical to those calculated in Table 14-5 (under the Balanced Budget Model). This confirms that, correctly specified, the Balanced Budget and Direct Assessment Models produce identical results.

56. As was the case under the Balanced Budget model, LGBs 9 and 10 are advantaged (their assessed cost and revenue advantages exceed their population share of available assistance and they are assessed to have a negative Relative Need requirement). These LGBs are overequalised and (relative to other LGBs) do not require additional assistance.

57. Again, the grants required to equalise the other LGBs total \$66.9 million, but there is only \$60.0 million available. The issue remains how to share the available assistance among the disadvantaged LGBs.

58. In its report, the Commission discussed three approaches LGGCs could use. It suggested that LGGCs could distribute the Relative Need pool so that it:

- (i) meets some of the disadvantage of every disadvantaged LGB. For example, LGGCs could allocate the funds to meet the same proportion of needs — this is the approach used by the LGGCs of Victoria, Western Australia, Tasmania and the Northern Territory;
- (ii) reduces the level of disadvantage of the most disadvantaged LGBs⁶; or
- (iii) provides a safety net which would meet all the needs of very disadvantaged LGBs and meet some of the needs of the remaining disadvantaged LGBs using one of the other two methods — this is the approach favoured by the New South Wales, Queensland and the South Australian LGGCs⁷.

59. The share of assistance under the second and third approaches do not change from the figures shown in Tables 14-12 and 14-13 and they are not be considered here.

60. Under the first approach, two options were considered:

- (i) sharing the available grants according to grants required — the method used by most LGGCs; or
- (ii) sharing the available grants so that all the disadvantaged LGBs are underequalised to the same degree.

61. The first option is easy to implement. The numbers are unchanged from those shown in Table 14-6.

62. As discussed earlier, the second option requires an adjustment to be made to the grants required figures. The adjustment subtracts the shortfall in the grants (\$6.9 million) from the underequalised LGBs. It is distributed in accordance with an underequalised LGB's share of their combined overall assessed capacity.

6 The assistance is first used to remove the relative disparity between the most disadvantaged and the second most disadvantaged LGBs. The per capita shortfall of the most disadvantaged LGB is reduced to the level of the second most disadvantaged LGB. The assistance is then used to remove the relative disparities between these two LGBs and the third most disadvantaged LGB. The per capita shortfalls of these two LGBs are reduced to the level of the third most disadvantaged LGB. This process continues until the assistance is exhausted.

7 New South Wales LGGC does not factor back the assessments of Silverton, Tibooburra or Lord Howe Island. The Queensland LGGC does not factor back the assessments of its Deed of Grant in Trust councils. The South Australian LGGC does not factor back the assessments of the five discrete Indigenous communities or the Outback Areas Community Development Trust.

63. Overall assessed capacity is calculated as:

$$\text{Overall Assessed Capacity}_i = \text{Grants required}_i + \text{Assessed revenue}_i + \text{Other Grant Assistance received}_i$$

64. It is a more difficult to calculate overall assessed capacity in the Direct Assessment Model, because not all the variables are calculated in that model. Assessed revenue is not calculated but revenue needs are. Assessed revenue can be calculated by subtracting an LGB's revenue needs from its population share of total revenue. As defined earlier, an LGB's share of standard revenue is calculated as:

$$\begin{aligned} \text{LGB's share of standard revenue} &= \frac{\text{Total Revenue}}{\text{Total Population}} * \text{LGB's Population} \\ &= \text{LGB's population share of total revenue} \end{aligned}$$

65. Table 14-16 shows how the adjustment would be calculated in the Direct Assessment Model.

Table 14-16 CALCULATION OF ADJUSTMENT, DIRECT ASSESSMENT MODEL

Function	Local Governing Body										Total
	1	2	3	4	5	6	7	8	9	10	
Population	250	750	9000	18000	20000	37000	65000	80000	120000	150000	500000
Share of population %	0.05	0.15	1.80	3.60	4.00	7.40	13.00	16.00	24.00	30.00	100.00
Share of standard \$m revenue ^(a)	0.1	0.3	3.8	7.6	8.4	15.5	27.3	33.6	50.4	63.0	210.0
Grants required \$m	0.6	0.6	7.1	8.3	14.5	1.3	5.5	29.0	-0.1	-6.8	60.0
Share of standard \$m revenue	0.1	0.3	3.8	7.6	8.4	15.5	27.3	33.6	50.4	63.0	210.0
Revenue needs \$m	0.0	0.1	1.4	1.8	1.8	2.6	4.0	0.5	-2.8	-9.5	0.0
Other Grant Assistance received \$m	0.1	0.3	2.0	3.0	2.8	4.5	6.8	8.0	11.9	15.6	55.0
Overall assessed \$m capacity^(b)	0.8	1.0	11.5	17.0	23.9	18.8	35.6	70.1	65.0	81.3	325.0
Percentage share ^(c)	0.43	0.58	6.46	9.52	13.36	10.50	19.93	39.22	0.00	0.00	100.00
Adjustment \$m	0.0	0.0	-0.4	-0.7	-0.9	-0.7	-1.4	-2.7	0.0	0.0	-6.9

(a) Calculated by applying an LGB's population share to the total revenue collected by all LGBs.

(b) Calculated as 'Grants required' plus 'Share of standardised revenue' less 'Revenue needs' plus 'Other Grant Assistance received'.

(c) For each underequalised LGB, this is calculated as its percentage share of the aggregate overall assessed capacity for all underequalised LGBs. For overequalised LGBs, the figure is set to zero.

66. The adjustment is identical to that calculated for the Equalisation Ratio method under the Balanced Budget Model — reinforcing the conclusion that the two models produce identical results if correctly specified.

67. Because the numbers in this table are identical to those in Table 14-8, other tables are not replicated:

- the calculation of the Equalisation Ratios under each option are in Table 14-9 and Table 14-10; and
- the distribution of total Commonwealth assistance is in Table 14-11.

WHAT IS THE EFFECT OF CHANGING THE SPECIFICATION OF THE DIRECT ASSESSMENT MODEL

68. Both the New South Wales and the South Australian LGGCs omit the EPC share of available assistance from their Direct Assessment Models. Their practice is to calculate each LGB's Relative Need grant requirement using the formula:

$$\begin{aligned} \text{Relative Need} & \text{ equals } \text{expenditure needs} \\ \text{grant} & \text{ plus } \text{revenue needs} \\ & \text{ plus } \text{other grant assistance needs.} \end{aligned}$$

69. This specification of the Direct Assessment Model produces an assessment of advantage and disadvantage that differs from the assessments in the version of the model that included this EPC term. Table 14-17 shows that it does and the difference is each LGB's population share of the available assistance.

70. The important issues are:

- (i) does the different specification lead to a different allocation of grants among LGBs? and
- (ii) if so, is the difference in allocations large?

Table 14-17 ASSESSED EXPENDITURE, REVENUES AND OTHER GRANT ASSISTANCE NEEDS

Function	Local Governing Body										Total
	1	2	3	4	5	6	7	8	9	10	
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Share of assistance	0.0	0.1	1.1	2.2	2.4	4.4	7.8	9.6	14.4	18.0	60.0
Roads expenditure	0.1	0.2	1.1	1.1	0.6	0.4	-0.2	-0.7	-1.1	-1.4	0.0
Other expenditure	0.5	0.4	4.6	4.2	10.3	-5.7	-6.4	18.8	-11.9	-14.8	0.0
Expenditure needs	0.6	0.5	5.7	5.3	10.9	-5.3	-6.6	18.1	-13.0	-16.2	0.0
Municipal Rates	0.0	0.0	0.5	0.6	0.6	1.1	2.0	-1.1	-1.7	-2.1	0.0
User Charges	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Revenue	0.0	0.1	0.8	1.3	1.2	1.5	2.0	1.6	-1.1	-7.4	0.0
Revenue needs	0.0	0.1	1.4	1.8	1.8	2.6	4.0	0.5	-2.8	-9.5	0.0
Per Capita grants	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Local Roads grants	-0.1	-0.2	-1.1	-1.1	-0.6	-0.4	0.2	0.7	1.1	1.4	0.0
Other Grant Assistance	0.0	0.0	0.0	0.1	0.0	0.0	0.2	0.1	0.2	-0.5	0.0
Other grant assistance needs	-0.1	-0.2	-1.0	-1.0	-0.6	-0.5	0.4	0.8	1.3	0.9	0.0
Grants required	0.6	0.5	6.0	6.1	12.1	-3.1	-2.3	19.4	-14.5	-24.8	0.0
Grants required (Table 14-14)	0.6	0.6	7.1	8.3	14.5	1.3	5.5	29.0	-0.1	-6.8	60.0
Difference	0.0	0.1	1.1	2.2	2.4	4.4	7.8	9.6	14.4	18.0	60.0
EPC share of assistance	0.0	0.1	1.1	2.2	2.4	4.4	7.8	9.6	14.4	18.0	60.0

71. Table 14-17 shows that omitting the EPC term leads to a different outcome:

- four (rather than two) LGBs are assessed to be advantaged and six (rather than eight) are assessed to be disadvantaged; and
- only \$44.7 million is required to remove the disadvantage of all the disadvantaged LGBs.

72. Whether or not these differences lead to a different allocation of grants among LGBs depends on how the assistance is shared. If it is shared on a proportional basis (Option 1 of Approach 1) then it will make a difference. If it is shared on the basis of meeting the needs of the most disadvantaged LGB first then it will not change LGBs' grant allocations (Approach 2).

73. Table 14-18 shows the grant allocations when the \$44.7 million is used to remove the assessed disadvantage of the disadvantaged LGBs and the remaining \$15.3 million (\$60 million less \$44.7 million) is shared on an EPC basis. This outcome is compared with the outcome from Table 14-16 (the Direct Assessment Model with an EPC share of available assistance term included).

Table 14-18 COMPARISON OF GRANT ALLOCATIONS UNDER DIFFERENT SPECIFICATIONS OF THE DIRECT ASSESSMENT MODEL

Local Governing Body	Relative Need Allocations (omitting EPC Term)	Relative Need Allocations (including EPC Term)	Difference
	\$m	\$m	\$m
LGB 1	0.6	0.6	0.0
LGB 2	0.5	0.5	0.0
LGB 3	6.3	6.7	-0.4
LGB 4	6.7	7.6	-1.0
LGB 5	12.7	13.6	-0.9
LGB 6	1.1	0.6	0.5
LGB 7	2.0	4.1	-2.1
LGB 8	21.9	26.3	-4.4
LGB 9	3.7	0.0	3.7
LGB 10	4.6	0.0	4.6
Total	60.0	60.0	0.0

74. This simple worked example shows that the difference in allocations can be large. However, these differences depend on many assumptions. When the actual assessments of New South Wales or South Australia are examined, the differences (if any exist) might not be large.

TECHNICAL APPENDIX

75. This appendix presents a simplified version of the LGGC's distribution models and highlights some useful relationships.

76. In this chapter, the Balanced Budget Model was set out as:

Relative Need grant	<i>equals</i>	assessed costs of providing services
	<i>plus</i>	assessed average operating surplus/deficit
	<i>less</i>	assessed revenue
	<i>less</i>	actual receipt of other grant assistance.

77. It also set out the Commission's definition of assessed costs, assessed revenues and actual grant assistance as:

Expenditure needs	<i>equals</i>	LGB's assessed cost of providing services
	<i>less</i>	LGB's population share of total expenditure
 Revenue needs	 <i>equals</i>	 LGB's population share of total revenue
	<i>less</i>	LGB's assessed revenue
 Other Grant Assistance needs	 <i>equals</i>	 LGB's population share of total grant assistance
	<i>less</i>	LGB's actual receipt of grant assistance.

78. The following notation is used⁸.

s	=	subscript that denotes a standard
i	=	subscript that denotes an individual LGB
E_s	=	standard expenditure (that is, total expenditure per capita)
EN_i	=	expenditure needs
$(E_s + EN_i)$	=	assessed costs ⁹
R_s	=	standard revenue (that is, total revenue per capita)

8 Unless otherwise stated, all figures are in per capita terms. This means we do not have to introduce a population variable.

9 A positive needs figure implies disadvantage. A positive expenditure needs figure means that the relevant LGB faces higher costs of service provision (other things equal, it costs more than the average to provide the service). Its standardised expenditure would therefore exceed its standard expenditure, thus expenditure needs are added to expenditure standards.

RN_i	=	revenue needs
$(R_s - RN_i)$	=	assessed revenue ¹⁰
O_s	=	standard Other Grant Assistance (that is, total Other Grant Assistance per capita)
ON_i	=	Other Grant Assistance needs
$(O_s - ON_i)$	=	actual Other Grants Assistance received ¹¹
G_s	=	grants available
G_i	=	grants required
B_s	=	standard Operating Surplus (that is, the total operating surplus per capita)

79. The standard Operating Surplus term (B_s) is not a term familiar to most LGGCs. In the Commission's model, the standard Operating Surplus term is equal to:

$$B_s = G_s + R_s + O_s - E_s \quad \text{A-1}$$

80. If positive (negative) it implies a surplus (deficit) of revenue over expenditure. In a local government context, it would be the surplus (or deficit) for all of the LGBs as a whole. The standard Operating Surplus recognises that budgets are not in balance and that LGBs should be given the capacity to fund the average imbalance.

81. Under the Balanced Budget Model, grants required by an individual LGB is defined as:

$$G_i = (E_s + EN_i) + B_s - (R_s - RN_i) - (O_s - ON_i) \quad \text{A-2}$$

Equalisation, Overequalisation and Underequalisation

82. If an LGB receives Relative Need assistance equal to its assessed grants required, it is equalised. If it receives less than this level of assistance it is underequalised. If it is assessed to required negative Relative Need assistance (because its combined own source revenue capacity, Per Capita grant, Local Roads grant and Other Grant Assistance are more than its expenditure requirements) it is overequalised.

10 A positive needs figure implies disadvantage. A positive revenue needs figure means that the relevant LGB has a low revenue capacity (other things equal, it would raise less than the average). Its standardised revenue would therefore fall short of its standard revenue, thus revenue needs are subtracted from revenue standards.

11 A positive needs figure implies disadvantage. A positive Other Grants needs figure means that the relevant LGB receives a less than the average share of the Other Grants. Its actual share of Other Grants falls short of the average level of Other Grants, thus Other Grants needs are subtracted from Other Grants standards. Other Grants include Per Capita grants and Local Roads grants.

83. The nature of this distribution model is such that it produces an equalisation level of grants for a given level of:

- Relative Need grants (G_s);
- own source revenue (R_s);
- Other Grant Assistance (O_s);
- own purpose expenditure (E_s);
- assessed expenditure needs (EN_i) — these needs depend on the assessments of LGGCs; and
- assessed revenue needs (RN_i) — these needs depend on the assessments of LGGCs.

84. Equation A-2 can be reorganised by moving all the revenue terms to the one side.

$$G_i + (R_s - RN_i) + (O_s - ON_i) = (E_s + EN_i) + B_s \quad A-3$$

85. The revenue terms on the left hand side of this equation calculate an individual LGB's overall assessed capacity. That is, its assessed capacity from all sources (Relative Need grants, assessed revenue, Per Capita grants, Local Roads grants and Other Grant Assistance).

86. The terms on the right hand side of Equation A-3 calculate the LGB's overall expenditure requirement. That is, what it would need to spend to provide the average level of services (assessed costs) and to finance the average budget imbalance (the budget result).

87. This equation can be used to determine whether an LGB is equalised, overequalised or underequalised:

- if its overall assessed capacity equals its assessed overall expenditure requirement, the LGB is equalised;
- if its overall assessed capacity is greater than its assessed overall expenditure requirement, the LGB is overequalised; and
- if its overall assessed capacity is less than its assessed overall expenditure requirement, the LGB is underequalised.

88. Overequalisation and underequalisation occur because the pattern of own source revenue capacity¹² (and possibly Other Grants) is so uneven that some LGBs can more than finance their overall expenditure requirement. In this sense, they are overequalised and do not require Relative Need grants.

12 This can occur if revenue capacity is not assessed correctly.

89. Collectively, all the other LGBs are underequalised and will remain so after the Relative Need grants have been distributed.

Equalisation Ratio

90. Equation A-3 can be respecified to calculate an Equalisation Ratio.

$$\text{Equalisation Ratio}_i = \frac{\text{Overall Assessed Capacity}_i}{\text{Overall Expenditure Requirement}_i} = \frac{G_i + (R_s - RN_i) + (O_s - ON_i)}{(E_s + EN_i) + B_s}, \text{ or}$$

$$\text{Equalisation Ratio}_i = \frac{\text{Grants required}_i + \text{Assessed revenue}_i + \text{Other Grant Assistance received}_i}{\text{Assessed costs}_i + \text{Standard Operating Surplus}_s} \quad \text{A-4}$$

91. The Equation Ratio can also be used to determine whether an LGB is equalised, overequalised or underequalised:

- if the ratio equals one (that its overall capacity equals its assessed overall outlays) the LGB is equalised;
- if the ratio is greater than one, the LGB is overequalised; and
- if the ratio is less than one, the LGB is underequalised.

92. This ratio can be used to:

- (i) determine whether a particular LGB is equalised, overequalised or underequalised; and
- (ii) choose a method of rationing the available assistance so that all the underequalised LGBs are underequalised to the same degree. That is, after the grants are distributed, their Equalisation Ratios are the same.

Calculating Overall Assessed Capacity

93. In the chapter, the method of rationing was to distribute the shortfall in available assistance amongst the underequalised LGBs on the basis of their overall assessed capacity. Equation A-4 set out that overall assessed capacity can be assessed as:

$$\text{Overall Assessed Capacity} = G_i + (R_s - RN_i) + (O_s - ON_i)$$

94. These terms are readily available under the Balanced Budget Model. Under that model, the overall assessed capacity would be calculated as:

$$\begin{aligned} \text{Overall assessed capacity} & \quad \textit{equals} \quad \text{grants required (G}_i\text{)} \\ & \quad \textit{plus} \quad \text{assessed revenue (R}_s\text{ - RN}_i\text{)} \\ & \quad \textit{plus} \quad \text{Other Grant Assistance (O}_s\text{ - ON}_i\text{)}. \end{aligned}$$

95. It is a slightly more difficult to calculate overall assessed capacity in the Direct Assessment Model, because not all the variables are calculated in that model. Standardised revenue is not assessed but revenue needs are. Standardised revenue can be calculated by subtracting an LGB's revenue needs from its share of standard revenue. As defined earlier, an LGB's share of standard revenue is calculated as:

$$\begin{aligned} \text{LGB' s share of standard revenue} & = \frac{\text{Total Revenue}}{\text{Total Population}} * \text{LGB' s Population} \\ & \equiv \text{LGB' s population share of total revenue} \end{aligned}$$

96. This calculation of standard revenue is not used in the production of the grants required figures. It is only used if an adjustment has to be made because some LGBs are overequalised, forcing others to be underequalised. An adjustment is required to the grants required figures of the underequalised LGBs — they are all reduced in a fashion that leaves all underequalised LGBs with the same Equalisation Ratio.

CHAPTER 15

LOCAL GOVERNMENT FINANCE

1. The terms of reference required the Commission to examine:
 - (i) the impact of the Act on the raising of revenue by LGBs;
 - (ii) the impact of the Act on the assistance provided by the States to LGBs; and
 - (iii) the implications of any changes in the functions or responsibilities of LGBs.
2. In supporting the Commission's response to this part of the terms of reference, this chapter provides an overview of local government finances in Australia.

WHAT'S HAPPENED TO LOCAL GOVERNMENT?

3. The Commission has interpreted the terms of reference broadly — to refer to assistance provided under the series of Acts which culminate in the *Local Government (Financial Assistance) Act 1995* — rather than a narrow reference to the 1995 Act alone.
4. This section provides analyses of local government revenue and expenditure for the period 1961–62 to 1997–98¹. The data relate to mainstream councils and, in 1997–98, Community Government councils in the Northern Territory.

1 The analysis is based on unpublished Government Finance Statistics (GFS) data for the general government sector compiled by the Australian Bureau of Statistics (ABS). Data for 1998–99 are not included in the analysis because they are prepared on an accrual basis and are not comparable with earlier years. The data have been converted to constant prices using an ABS Gross Domestic Product price deflator.

5. Two important aspects of the analysis are:

- whether there have been big changes in revenue and expenditure patterns over this period; and
- whether the introduction of local government financial assistance grants in 1974–75 or the introduction of the 1995 Act had any influence on these changes.

6. Chapter 16 provides State by State analysis. Because of the particular interest in the Commonwealth's financial assistance grants, 1974–75 has been used as a base point for many of the State comparisons.

7. As part of its consultation process, the Commission held meetings with representatives of local government in each State. A number of participants to those hearings said that:

- local government was more important today than it has ever been;
- local government is increasingly being 'drawn into' new areas of service provision, often without access to additional funding;
- local government's revenue raising abilities have been restricted by policies imposed by other spheres of government, such as rate pegging in New South Wales, the 20 per cent mandated rate cut in Victoria in 1995–96 and State Agreement Acts² in Western Australia;
- Commonwealth and State assistance has not been sufficient to enable it to finance its expanding services; and
- local government has responded by increasing rates and user charges, contracting out for private works, greater efficiencies, cutting back on other services, spending less on roads and increasing borrowings.

8. This section provides support for some of these views.

2 The Acts override LGBs' scope to raise revenue from land in their jurisdictions.

Vertical Fiscal Imbalance

9. There are three levels of governments in Australia: Commonwealth; State; and local government. Each has its own revenue raising powers and expenditure responsibilities. Figure 15-1 shows the growth in real terms (in 1997–98 prices) in own-source revenue³ and own-purpose outlays⁴ of each level of government over the period 1961–62 to 1997–98. It confirms that:

- the Commonwealth has the largest own-source revenues and own-purpose outlays, and local government the smallest;
- the Commonwealth's own-source revenue exceeds its own-purpose outlays; and
- the State and local governments' own-purpose outlays exceed their own-source revenue.

10. The degree of imbalance between the revenue raising and expenditure responsibilities of different levels of government is known as vertical fiscal imbalance (VFI). The States and local government require additional revenue if they are to have the capacity to provide the services they do. The Commonwealth could address the vertical fiscal imbalance by providing States and local government with new revenue-raising powers or financial assistance in the form of grants. While the Commonwealth has, in the past, transferred a revenue power⁵ to the States, its preference has been to provide assistance in the form of grants.⁶

11. Table 15-1 shows that between 1961–62 and 1997–98, the degree of VFI⁷ declined — implying that States and local government are financing a greater proportion of their own-purpose outlays from their own revenue sources.

3 Own-source revenue excludes transfers from other levels of government.

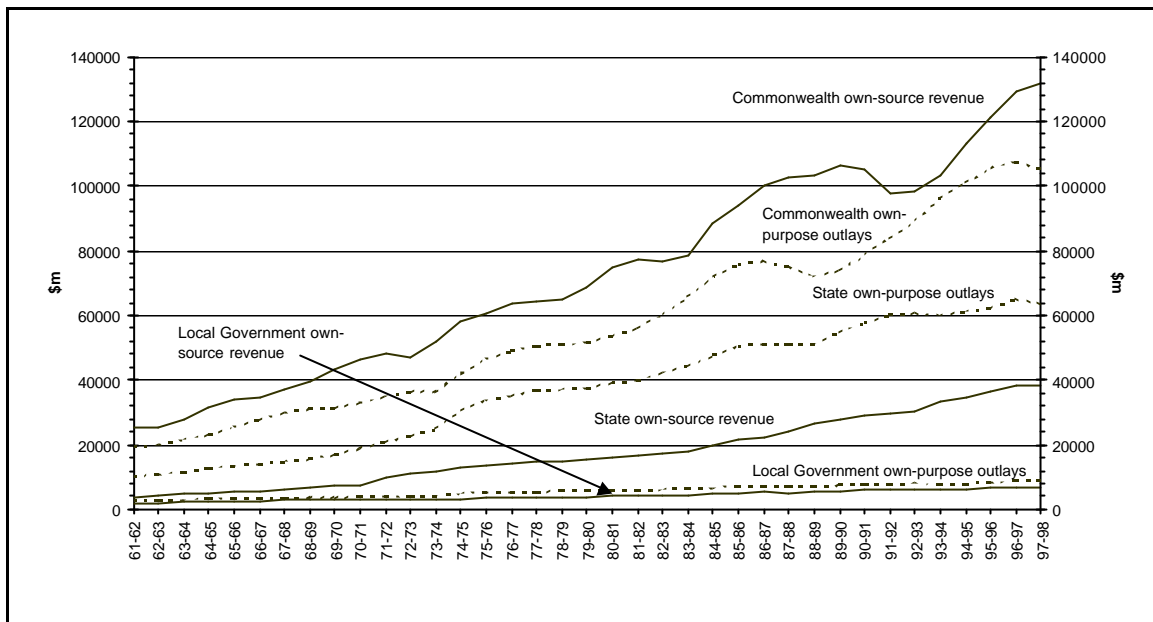
4 Own-purpose outlays includes transfers to other levels of government.

5 The Commonwealth transferred the power to levy Payroll Taxation to the States in 1971.

6 In 1998–99, the Commonwealth provided \$16.8 billion of general revenue grants and \$14.4 billion of specific purpose payments to the States. It provided \$1.2 billion as financial assistance grants and \$0.2 billion in specific purpose payments to local government.

7 The degree of VFI is calculated as a sphere's percentage of national own-source revenues divided by its percentage of national own-purpose outlays.

Figure 15-1 OWN-SOURCE REVENUE AND OWN-PURPOSE OUTLAYS AT 1997-98 PRICES



12. Table 15-1 also shows that while the three levels of government have expanded over the period 1961–62 to 1997–98, the pace of growth has been different for each. State own-purpose outlays have experienced average annual rates of growth of 5.2 per cent and their own-source revenues have grown at 6.6 per cent⁸. Commonwealth own-purpose outlays have grown at an average annual rate of about 4.7 per cent, as have its own-source revenues. Local government own-purpose outlays and own-source revenues have both grown at about 3.5 per cent per annum.

13. These trends imply that, in relative terms, the size of the State sector has grown while the size of the local government sector has declined. The major determinant for the differing performance of the spheres over this period appears to be the growth in their own-source revenue. That is, the growth in own-purpose outlays appears to be limited by the growth in own-source revenue. Local government had the slowest growing revenues, so it had the slowest growing expenditures.

14. To overcome its VFI, local government receives transfers from both the Commonwealth and the State. Grant transfers are another source of revenue for local government. It is possible that increased transfers (from the spheres that had the faster growing revenues) could partially offset the effect of its own slow growing revenues.

8 One reason for the increase in State revenue over this period was the transfer of Payroll Taxation from the Commonwealth to the States in 1971.

Table 15-1 OWN-SOURCE REVENUE AND OWN-PURPOSE OUTLAYS AT 1997-98 PRICES, AND THE DEGREE OF VERTICAL FISCAL IMBALANCE

	Commonwealth	State	Local
A. Own-source Revenue (\$m)			
1961-62	25 542	3 876	1 924
1973-74	51 905	11 679	3 091
1974-75	57 788	12 802	3 325
1997-98	131 855	38 423	6 986
Average annual growth (%)			
1961-62 to 1973-74 ^(a)	6.1	9.6	4.0
1974-75 to 1997-98 ^(b)	3.7	4.9	3.3
1961-62 to 1997-98	4.7	6.6	3.7
B. Own-purpose Outlays (\$m)			
1961-62	19 192	10 231	2 593
1973-74	36 405	24 762	4 094
1974-75	42 045	30 812	4 852
1997-98	104 952	63 543	8 781
Average annual growth (%)			
1961-62 to 1973-74 ^(a)	5.5	7.6	3.9
1974-75 to 1997-98 ^(b)	4.1	3.2	2.6
1961-62 to 1997-98	4.8	5.2	3.5
C. Degree of VFI (=A / B)			
1961-62	1.33	0.38	0.74
1973-74	1.43	0.47	0.76
1974-75	1.37	0.42	0.69
1997-98	1.26	0.60	0.80

(a) Before the introduction of financial assistance grants to local government.

(b) After the introduction of financial assistance grants to local government.

15. Figures 15-2 and 15-3 show each sphere's percentage share of the national own-source revenue and own-purpose outlays for 1961-62 to 1997-98. Both charts confirm:

- the increase in the relative size of the State sector; and
- the decrease in the relative size of the local government sector.

Figure 15-2 COMPOSITION OF GOVERNMENT OWN-SOURCE REVENUE

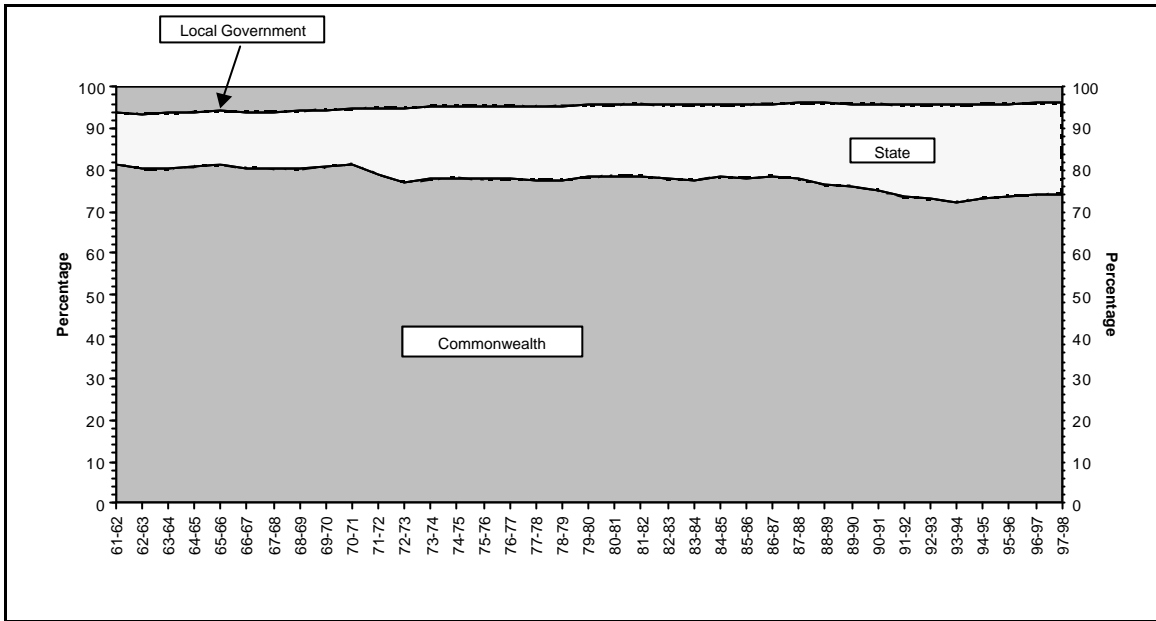
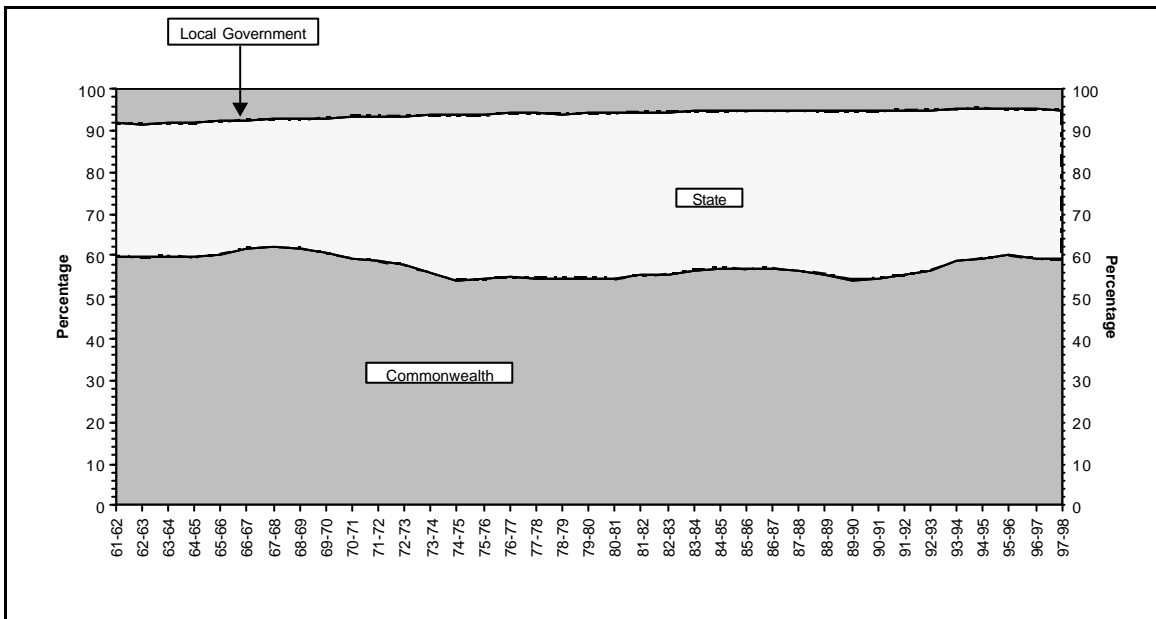


Figure 15-3 COMPOSITION OF GOVERNMENT OWN-PURPOSE OUTLAYS



Local Government Revenue

16. The terms of reference do not tell us how to assess the impact of the Act on local government revenue raising and the provision of State assistance. The impact can be assessed in different ways. We have examined the impact from three perspectives:

- (i) whether own source revenue and State assistance have grown in absolute terms over time;
- (ii) if so, whether they have grown faster or slower than the inflation rate; and
- (iii) whether the relative importance of each form of own source revenue and of State assistance has changed over time.

17. Figure 15-4 shows the contribution (relative importance) of the different revenues and transfers to total local government revenue since 1961–62. It shows that, over the period:

- own-source revenues⁹ have maintained their importance, in despite of a dip in 1974–75 and 1975–76¹⁰;
- Commonwealth transfers have become a larger proportion;
- State transfers¹¹ contribution has been reduced since the mid-1970s, and is now at the same level as the 1960s;
- municipal rates are now a smaller proportion; and
- user charges have become a larger proportion.

18. For the purpose of the review, we are particularly interested in the trend after the introduction of financial assistance grants in 1974–75.

19. Table 15-2 also shows that since 1974–75, each of local government's revenue sources has grown and grown faster than inflation rate.

20. Since 1974–75, local government's relative revenue raising effort has risen. Municipal rates remain the sector's primary revenue source but the slow rate of growth has been a major constraint on the sector's development. Their share of total revenue has declined from 54 per cent to 47 per cent.

9 Total of municipal rates, user charges and other revenue.

10 The introduction of untied financial assistance in 1974–75 caused each of the other sources of revenue to decline as a share of total local government revenue. As Table 14-2 shows, each of the other sources of revenue grew in absolute terms between 1973–74 and 1974–75.

11 Includes Commonwealth payments through the States to local government.

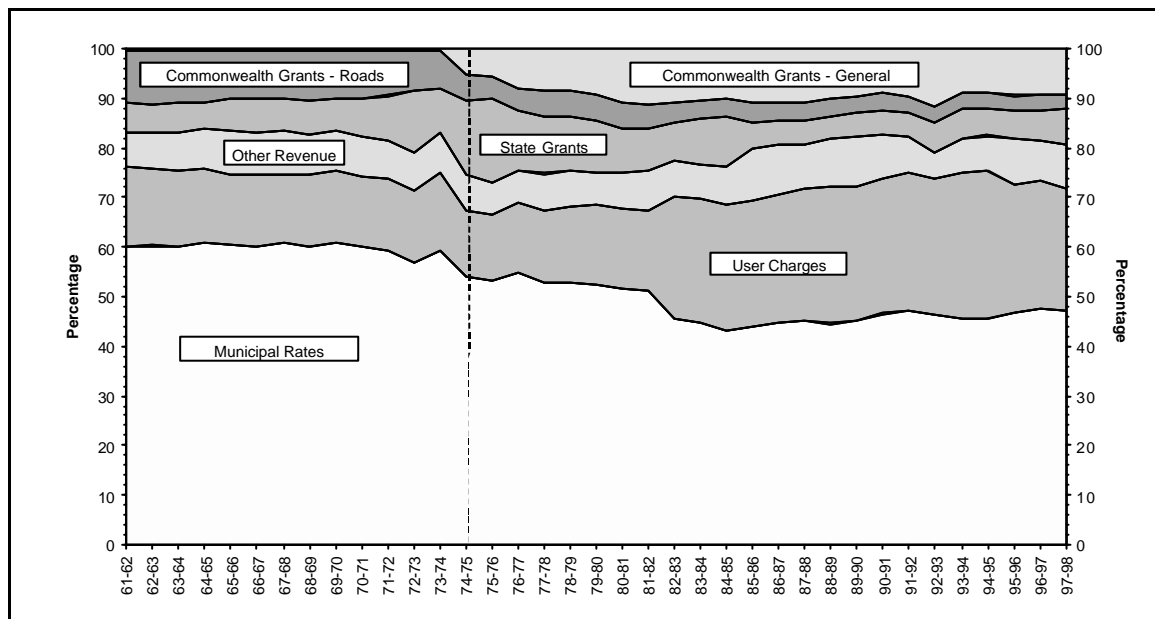
21. The slow growth in municipal rates has been offset by the fast growth in user charges. User charges have become an increasingly important source of local government revenue. In 1997–98, they account for a quarter of total revenue.

22. Since 1974–75, total Commonwealth and State transfers to local government have decreased in importance. They comprise a smaller proportion of total local government revenue (19 per cent) than they did in 1974–75 (25 per cent).

23. The relative contribution of Commonwealth support has increased slightly (from more than 10 per cent in 1974–75 to 12 per cent in 1997–98). The introduction of financial assistance grants marked a major shift in Commonwealth support.

24. Although the amount of State assistance has increased in real terms since 1974–75, its rate of increase (0.4 per cent per annum) is about one-tenth of the rate of increase of local government own-source revenue (4 per cent per annum). Its decline in importance is almost exactly matched by the increase in importance of Commonwealth transfers.

Figure 15-4 LOCAL GOVERNMENT REVENUE SOURCES



Note: State Grants include all Commonwealth payments through the States to local government except for the local government financial assistance grants and Local Roads grants. Commonwealth Grants - General include financial assistance grants and specific purpose payments paid directly to local government.

Table 15-2 LOCAL GOVERNMENT REVENUE SOURCES AT 1997–98 PRICES

Year	Own-source Revenue			Transfers		Total Revenue
	Municipal Rates	User Charges	Other Revenue	Common-wealth	State	
Revenue (\$m)						
1961–62	1 694	453	191	305	169	2 811
1973–74	2 628	697	351	356	398	4 430
1974–75	2 842	703	381	550	779	5 256
1997–98	5 620	2 947	1 052	1 443	848	11 911
Share of total revenue (%)						
1961–62	60.3	16.1	6.8	10.9	6.0	100.0
1973–74	59.3	15.7	7.9	8.0	9.0	100.0
1974–75	54.1	13.4	7.2	10.5	14.8	100.0
1997–98	47.2	24.7	8.8	12.1	7.1	100.0
Average annual growth (%)						
1961–62 to 1973–74	3.7	3.7	5.2	1.3	7.4	3.9
1974–75 to 1997–98	3.0	6.4	4.5	4.3	0.4	3.6
1961–62 to 1997–98	3.4	5.3	4.9	4.4	4.6	4.1

Local Government Expenditure

25. Figure 15-5 shows the pattern of local government expenditure since 1961–62. For ease of analysis, expenditure has been classified to seven categories. The figure shows that, over the period:

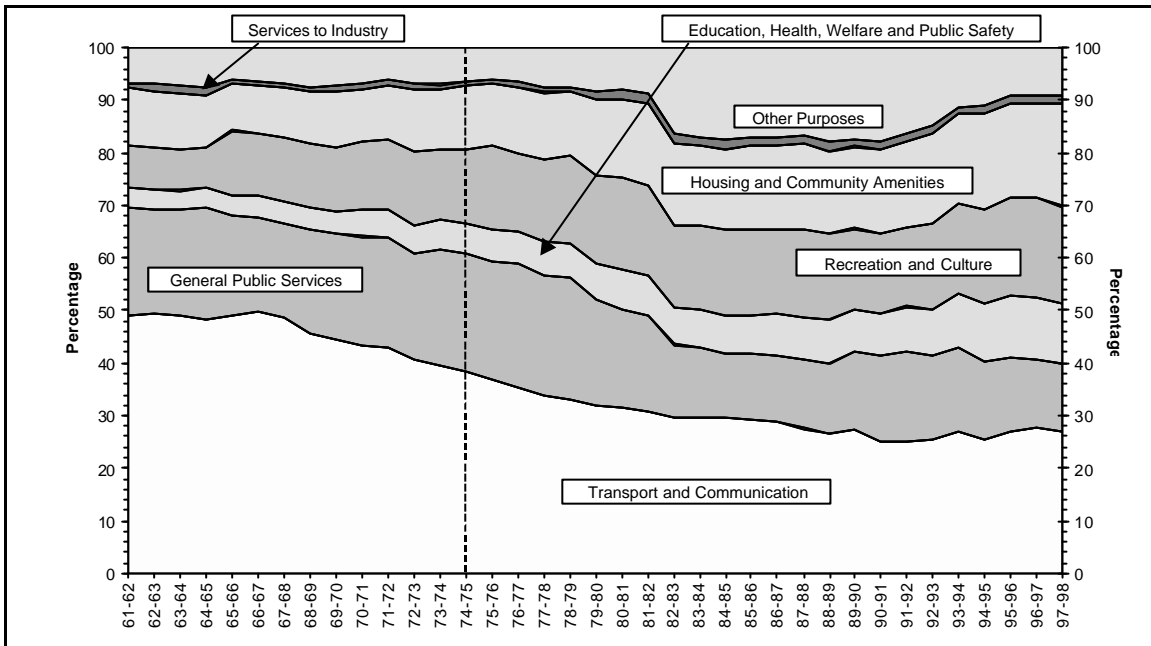
- the pattern of expenditure has changed markedly;
- the importance of Roads (Transport and Communications) has declined steadily;
- the importance of General Public Services has declined; and
- the importance of people services (Education, Health, Welfare and Public Safety and Recreation and Culture) has increased steadily.

26. This evidence supports the views that were put to the Commission during its consultation process. It does suggest that local government is increasingly being drawn into new areas of service provision. It also suggests that local government is funding these expanding areas by spending proportionally less on its traditional areas of service provision (particularly roads).

27. Table 15-3 shows expenditure for each of the expenditure categories in real terms. It shows that each category has grown and grown faster than the inflation rate since 1961–62.

28. Table 15-3 also shows that while expenditure on roads has doubled in real terms over the last 37 years, expenditure on the people services has grown tenfold. The introduction of financial assistance grants in 1974–75 has changed this trend only slightly.

Figure 15-5 LOCAL GOVERNMENT EXPENDITURE COMPOSITION



Source: Unpublished ABS Government Finance Statistics data.

Table 15-3 LOCAL GOVERNMENT EXPENDITURE AT 1997–98 PRICES

Year	Transport	General Public Services	Education Health, Welfare and Public Safety	Recreation and Culture	Housing and Community Amenities	Services to Industry	Other Purpose	Total
Expenditure (\$m)								
1961–62	1 534	651	120	248	341	30	210	3 133
1973–74	1 899	1 060	281	639	545	49	338	4 810
1974–75	2 132	1 258	318	790	673	52	358	5 582
1997–98	3 275	1 539	1 403	2 217	2 348	188	1 121	12 090
Share of total outlays (%)								
1961–62	48.9	20.8	3.8	7.9	10.9	1.0	6.7	100.0
1973–74	39.5	22.0	5.8	13.3	11.3	1.0	7.0	100.0
1974–75	38.2	22.5	5.7	14.2	12.1	0.9	6.4	100.0
1997–98	27.1	12.7	11.6	18.3	19.4	1.6	9.3	100.0
Average annual growth (%)								
1961–62 to 1973–74	1.8	4.2	7.4	8.2	4.0	4.2	4.1	3.6
1974–75 to 1997–98	1.9	0.9	6.7	4.6	5.6	5.8	5.1	3.4
1961–62 to 1997–98	2.1	2.4	7.1	6.3	5.5	5.2	4.8	3.8

29. Local government's pattern of expenditure has changed markedly over the period. The move away from property services into people services has continued since the introduction of financial assistance grants in 1974–75.

30. Roads remain the sector's largest expenditure function but its level of importance has declined from about half of all expenditure in 1961–62 to a little more than a quarter of all expenditure in 1997–98.

31. Recreation and Culture, and Housing and Community Amenities are now very large areas of local government expenditure — each is a little less than 20 per cent of total expenditure.

32. Education, Health, Welfare and Public Safety has been the fastest growing area of local government expenditure. Since 1961–62, it has grown from about 4 per cent of all expenditure to about 12 per cent of all expenditure.

Conclusion

33. Local government has changed since the early 1960s. While it has expanded over that period, its rate of growth has been slower than that experienced by the Commonwealth and the States so that its relative size has declined.

34. Local government is increasingly being drawn into new areas of service provision. It has responded by increasing rates and user charges and spending proportionally less on roads. It has been constrained in what it can do because its primary revenue source (municipal rates) is a slow growth tax.

35. Local government revenue raising has decreased slightly over the period but it has remained unchanged since the introduction of financial assistance grants in 1974–75.

36. The level of assistance from the Commonwealth and State has declined slightly over the period. The introduction of financial assistance grants, signalled a passing of the baton and it is now the Commonwealth rather than the State which provides the greater share of transfers to local government.

CHAPTER 16

LOCAL GOVERNMENT FINANCE — STATE ANALYSES

1. This chapter examines local government finance by State for the period 1961–62 to 1997–98 to determine whether the national trends (discussed in Chapter 15) are evident at the State level.

2. In this chapter, the analysis for each State focuses on three issues:

- (i) the apparent impact of the introduction of Commonwealth financial assistance grants on local government own-source revenue;
- (ii) the apparent impact of the introduction of Commonwealth financial assistance grants on State assistance to local government; and
- (iii) changes in functions or responsibilities of local government implied by changes in the composition of expenditure since 1961–62.

3. To examine these issues, the composition of local government revenue and expenditure from 1961–62 to 1997–98 for each State has been plotted.

4. Before looking at the charts for each State, this chapter first examines the growth of total revenue and total expenditure by State.

GROWTH IN LOCAL GOVERNMENT REVENUE AND EXPENDITURE

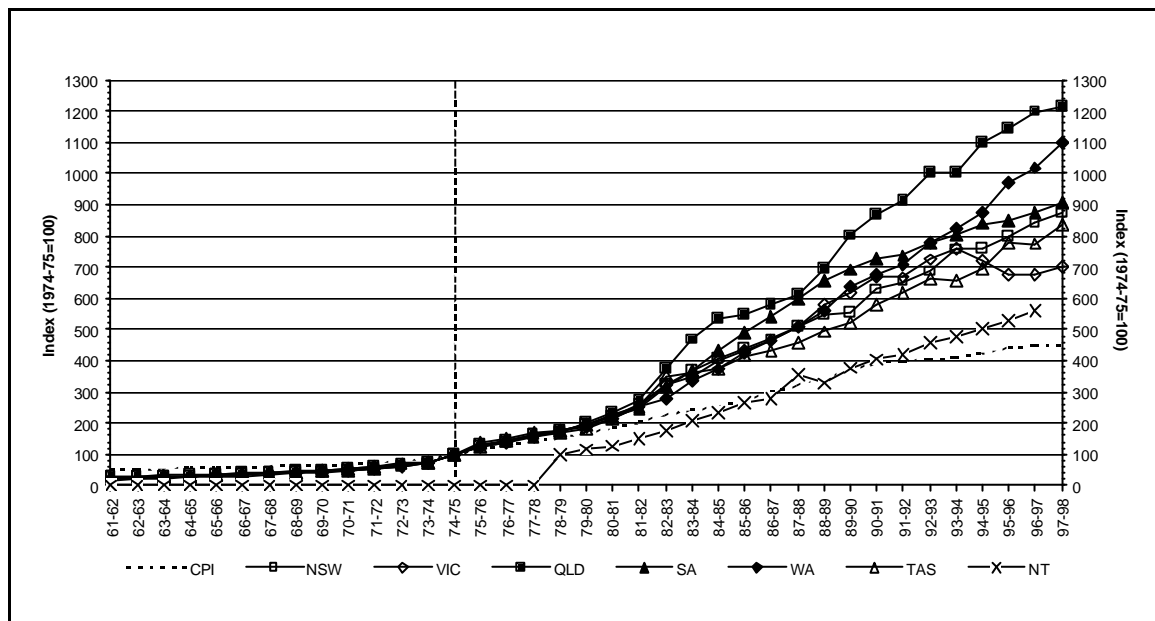
5. All figures in this section show the movements in the Consumer Price Index (CPI) for comparison purposes. To allow growth comparisons, each series¹ has also been rebased so that the value equals 100 in 1974–75, the year the Commonwealth started providing financial assistance grants to local government.

¹ Local government data for the Northern Territory is available only from 1978–79 — after it gained self-government.

6. Figure 16-1 shows the growth of total local government revenue by State. The chart shows that:

- (i) over the period, total local government revenue has grown at a rate faster than CPI in all States;
- (ii) there are different rates of growth of total revenue between the States, with Queensland growing the fastest followed by Western Australia — their higher growth rates may be influenced by population growth;
- (iii) New South Wales, which has had rate pegging legislated by the State Government since the late 1970s, has still had several States below it in terms of rates of growth; and
- (iv) Victoria — with a State government-mandated 20 per cent rate cut in 1995–96 — had the second slowest rate of growth.

Figure 16-1 GROWTH IN TOTAL REVENUE BY STATE, 1961–62 TO 1997–98

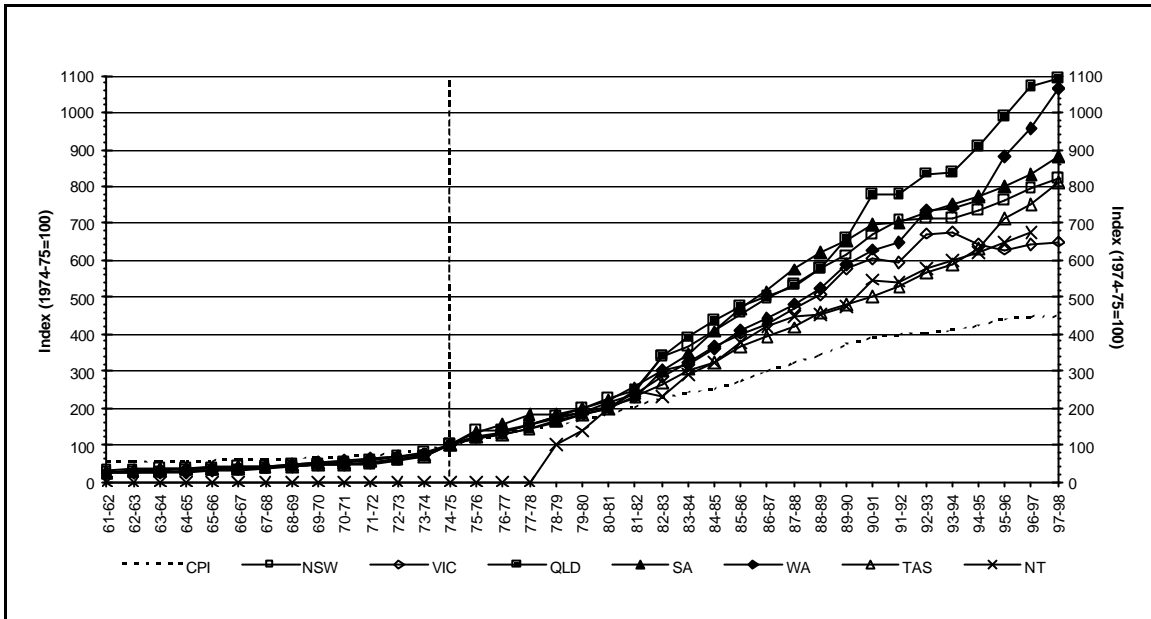


Notes: All series (except the NT series) have been rebased so that their value in 1974–75 equals 100. For the NT, the value in 1978–79 equals 100. Also for the NT, the 1997–98 figure is not included because the ABS includes the figures for all types of LGBs for the first time in that year. In other years, ABS uses only the figures for municipalities. CPI is the ABS Consumer Price Index: All Groups Index Numbers – Annual Indexes.

Source: Unpublished ABS Government Finance Statistics data.

7. Figure 16-2 plots the growth of total expenditure for local government by State. As expected, the results are similar to those for Figure 16-1.

Figure 16-2 GROWTH IN TOTAL EXPENDITURE BY STATE, 1961–62 TO 1997–98



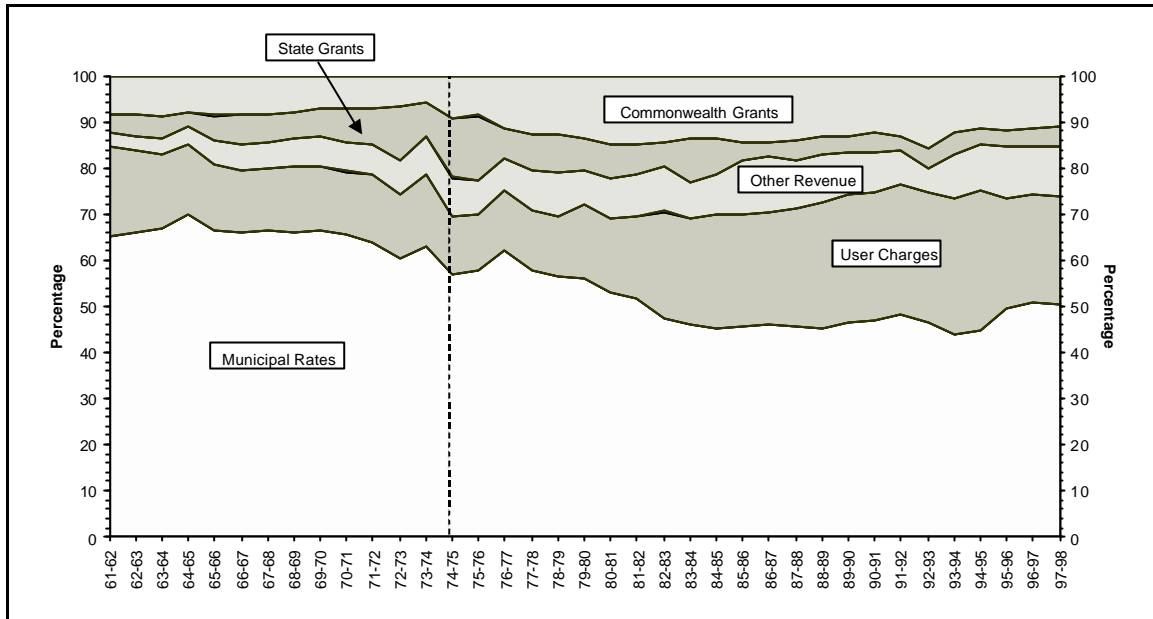
Notes: All series (except the NT series) have been rebased so that their value in 1974–75 equals 100. For the NT, the value in 1978–79 equals 100. Also for the NT, the 1997–98 figure is not included because the ABS includes the figures for all types of LGBs for the first time in that year. In other years, ABS uses only the figures for municipalities. CPI is the ABS Consumer Price Index: All Groups Index Numbers – Annual Indexes.

Source: Unpublished ABS Government Finance Statistics data.

NEW SOUTH WALES

8. For local government in New South Wales:
 - (i) Figure 16-3 shows that, the share of revenue from own-sources appears to have increased after the introduction of the local government financial assistance grants;
 - (ii) Figure 16-3 shows the share of revenue from State assistance appears to have declined after the introduction of the local government financial assistance grants; and
 - (iii) Figure 16-4 shows the proportion of expenditure on Transport and Communication and General Public Services has declined but the proportion of expenditure has increased for all other expenditure categories.

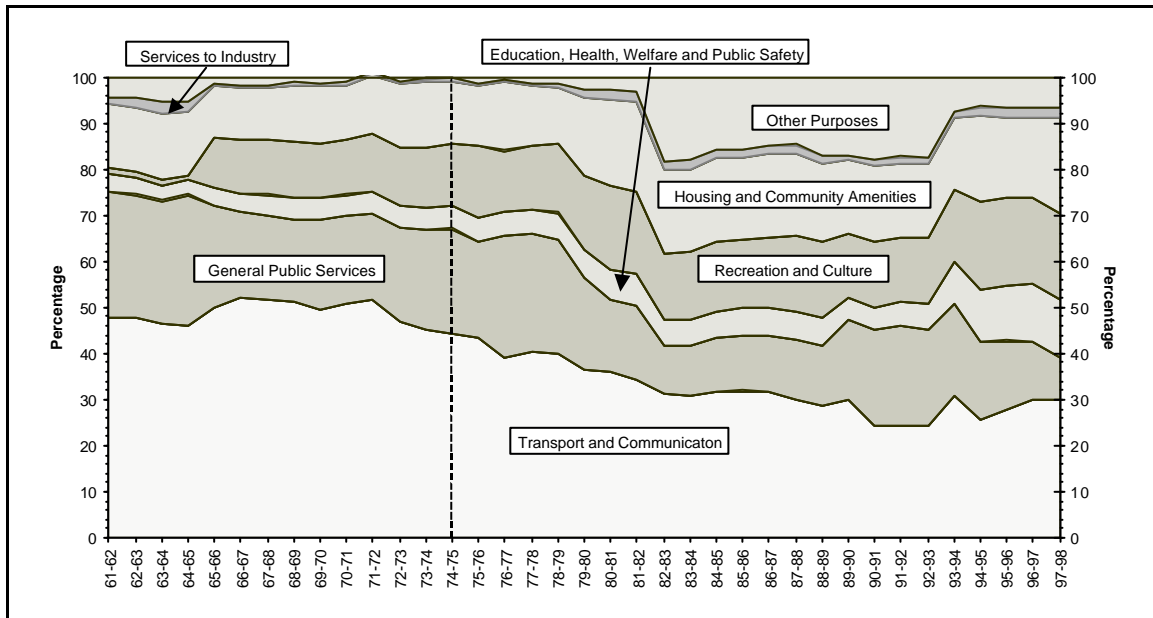
Figure 16-3 REVENUE, NEW SOUTH WALES, 1961–62 TO 1997–98



Notes: State Grants include all Commonwealth payments through the States to local government except for the local government financial assistance grants and Local Roads grants. Commonwealth Grants include financial assistance grants and Local Roads grants, and specific purpose payments paid directly to local government.

Source: Unpublished ABS Government Finance Statistics data.

Figure 16-4 EXPENDITURE, NEW SOUTH WALES, 1961–62 TO 1997–98

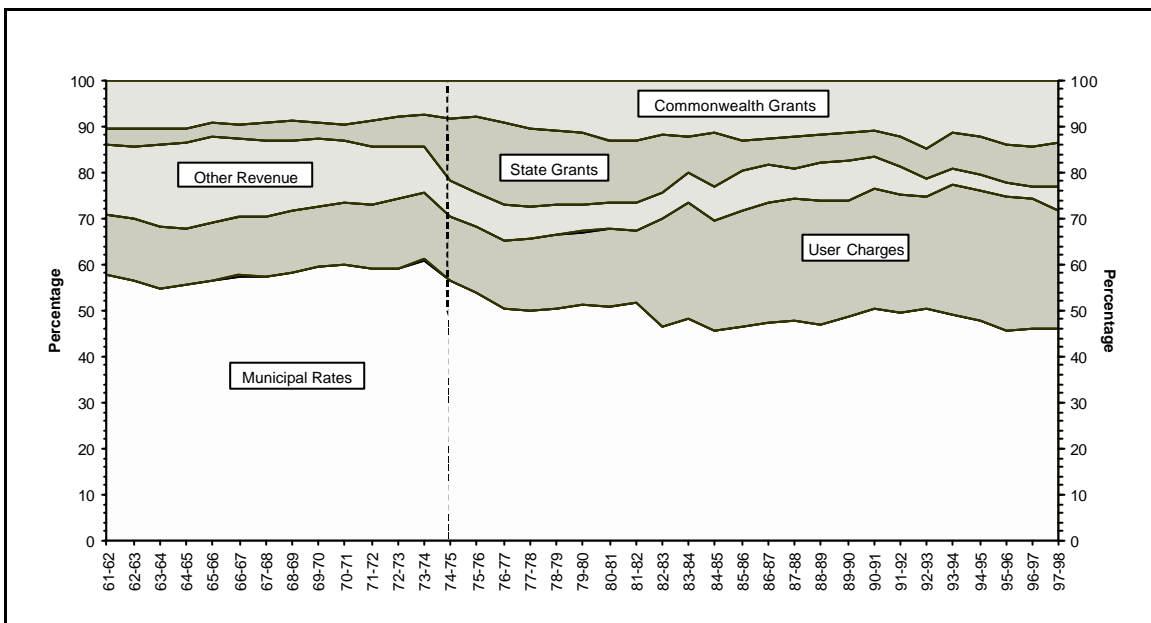


Source: Unpublished ABS Government Finance Statistics.

VICTORIA

9. For local government in Victoria:
- (i) Figure 16-5 shows the share of revenue from own-sources appears to have remained reasonably constant since the introduction of local government financial assistance grants;
 - (ii) Figure 16-5 shows State grants appear to have declined after the introduction of the Commonwealth assistance; and
 - (iii) Figure 16-6 shows relative expenditure on Transport and Communication, and General Public Services have declined, and all other functions have increased.

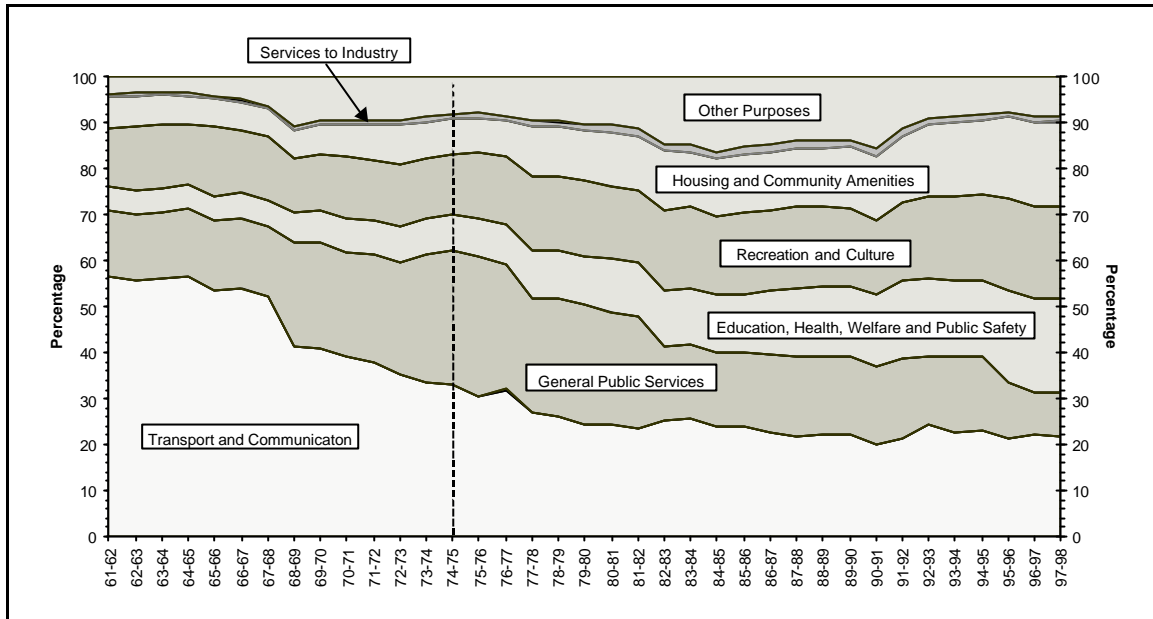
Figure 16-5 REVENUE, VICTORIA, 1961–62 TO 1997–98



Notes: State Grants include all Commonwealth payments through the States to local government except for the local government financial assistance grants and Local Roads grants. Commonwealth Grants include financial assistance grants and Local Roads grants, and specific purpose payments paid directly to local government.

Source: Unpublished ABS Government Finance Statistics data.

Figure 16-6 EXPENDITURE, VICTORIA, 1961–62 TO 1997–98



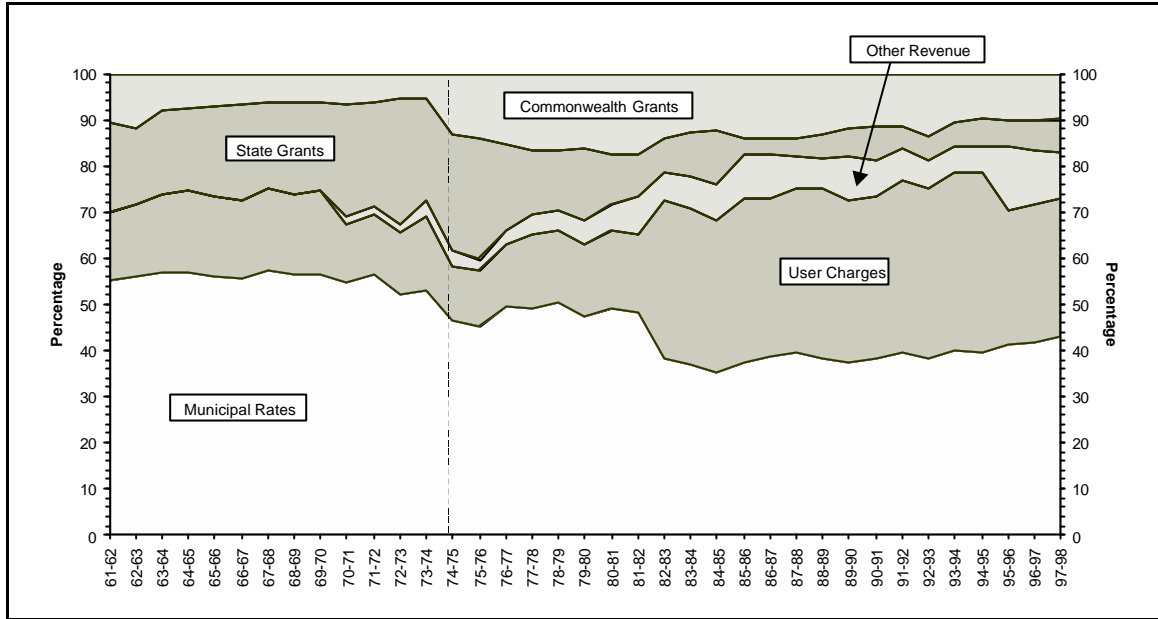
Source: Unpublished ABS Government Finance Statistics.

QUEENSLAND

10. For local government in Queensland:

- (i) Figure 16-7 shows the share of revenue from own-sources appears to have increased since the introduction of local government financial assistance grants;
- (ii) Figure 16-7 shows the share of revenue from State assistance has declined after the introduction of the local government financial assistance grants; and
- (iii) Figure 16-8 shows the proportion of expenditure on Transport and Communication and General Public Services declined but all others increased.

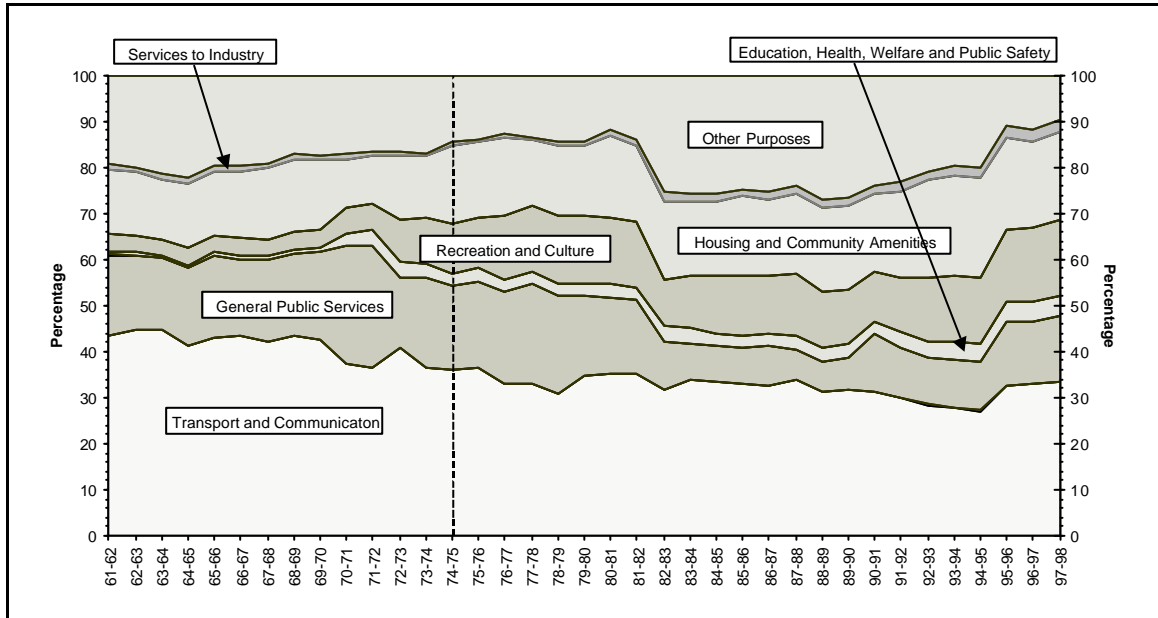
Figure 16-7 REVENUE, QUEENSLAND, 1961-62 TO 1997-98



Notes: State Grants include all Commonwealth payments through the States to local government except for the local government financial assistance grants and Local Roads grants. Commonwealth Grants include financial assistance grants and Local Roads grants, and specific purpose payments paid directly to local government.

Source: Unpublished ABS Government Finance Statistics data.

Figure 16-8 EXPENDITURE, QUEENSLAND, 1961-62 TO 1997-98

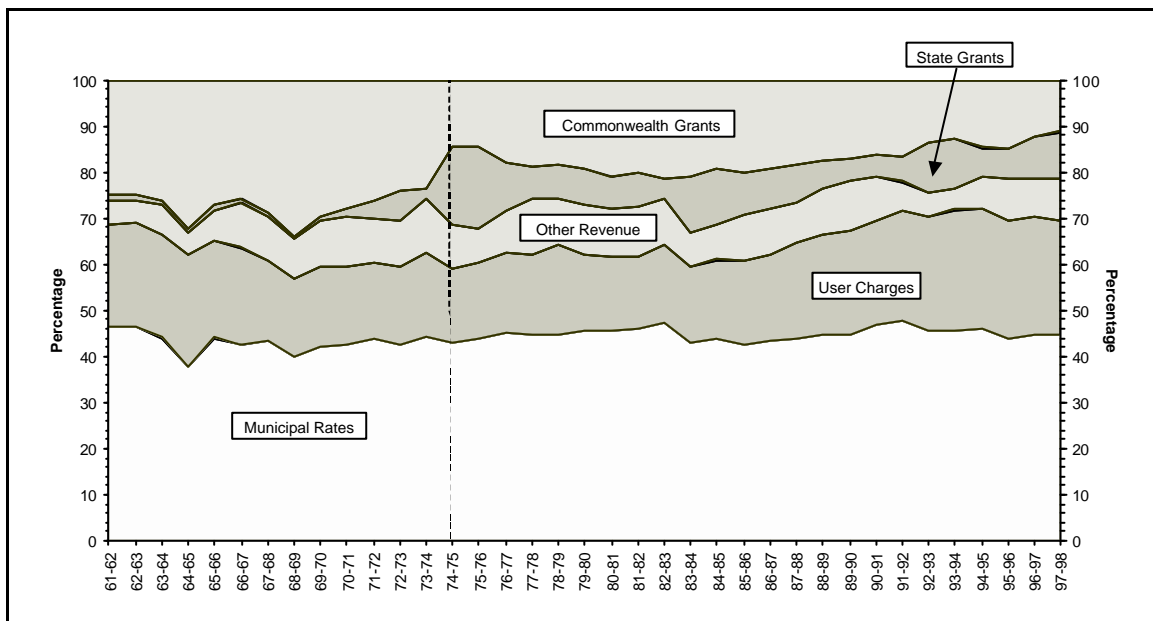


Source: Unpublished ABS Government Finance Statistics.

WESTERN AUSTRALIA

11. For local government in Western Australia:
- (i) Figure 16-9 shows the share of revenue from own-sources appears to have increased since the introduction of local government financial assistance grants;
 - (ii) Figure 16-9 shows the share of revenue from State assistance has fluctuated after the introduction of the local government financial assistance grants but generally it has declined; and
 - (iii) Figure 16-10 shows the proportion of expenditure on Transport and Communication, General Public Services, Recreation and Culture and Services to Industry has declined since 1961–62 but for all others it increased. Changes in the share of expenditure on Transport and Communication are different from those in the other States — there was an initial increase up to the early 1970s then a gradual decline whereas in other States there was a decline over the whole period.

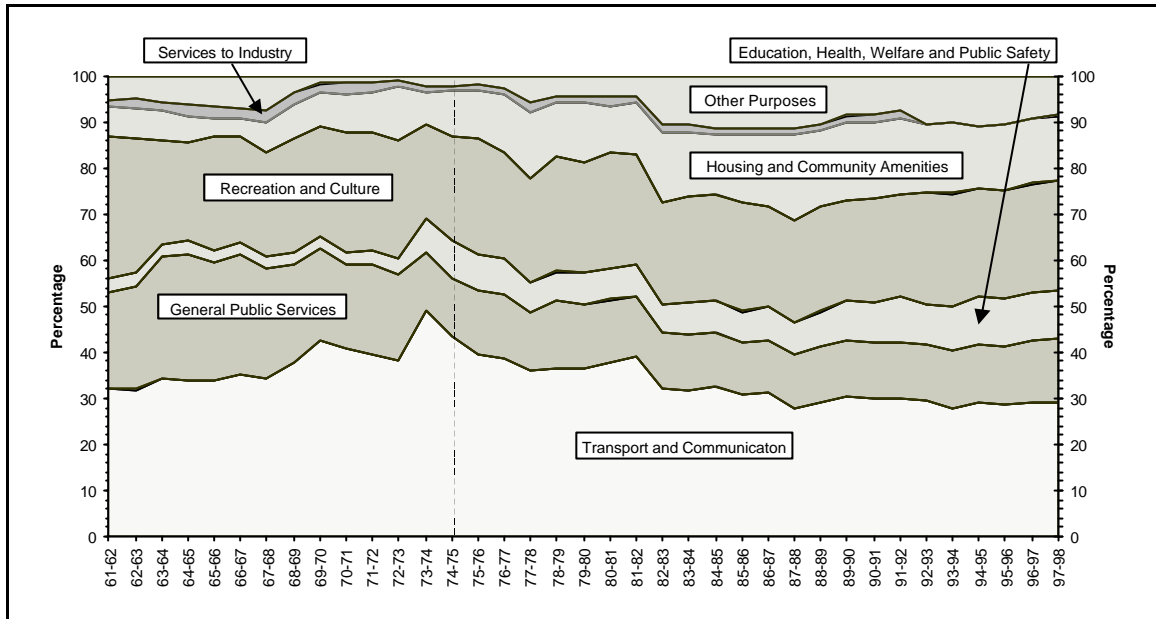
Figure 16-9 REVENUE, WESTERN AUSTRALIA, 1961–62 TO 1997–98



Notes: State Grants include all Commonwealth payments through the States to local government except for the local government financial assistance grants and Local Roads grants. Commonwealth Grants include financial assistance grants and Local Roads grants, and specific purpose payments paid directly to local government.

Source: Unpublished ABS Government Finance Statistics data.

Figure 16-10 EXPENDITURE, WESTERN AUSTRALIA, 1961–62 TO 1997–98

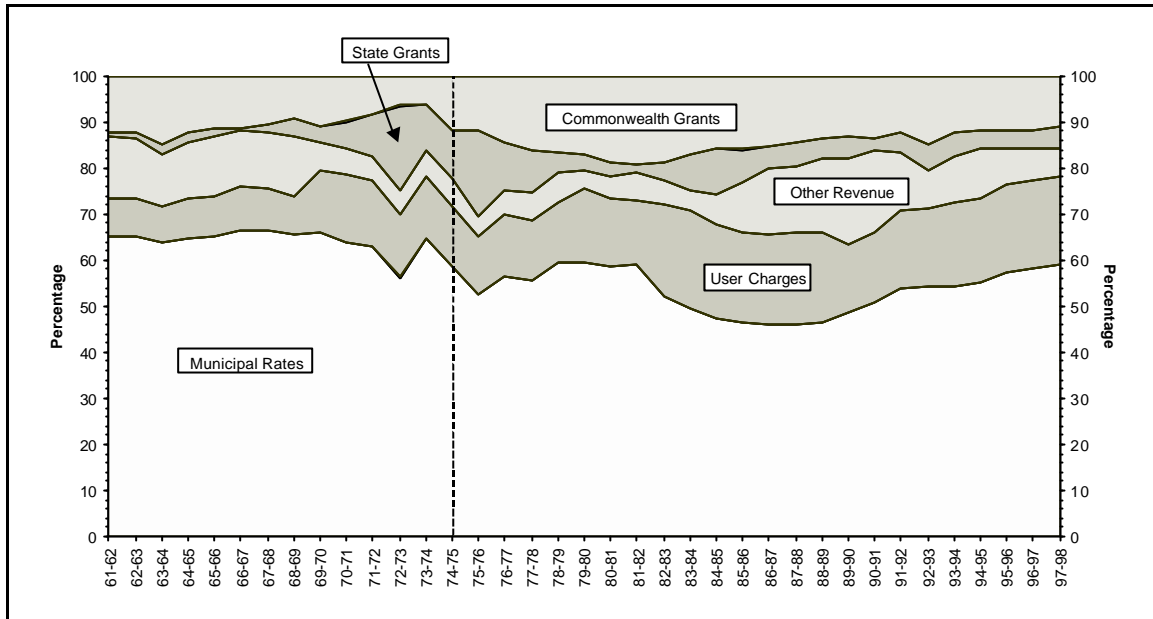


Source: Unpublished ABS Government Finance Statistics.

SOUTH AUSTRALIA

12. For local government in South Australia:
- (i) Figure 16-11 shows the share of revenue from own-sources appears to have increased since the introduction of local government financial assistance grants;
 - (ii) Figure 16-11 shows the share of revenue from State assistance has fluctuated after the introduction of the local government financial assistance grants but generally it appears to have declined; and
 - (iii) Figure 16-12 shows the proportion of expenditure on Transport and Communication has declined since 1961–62 but for all others it increased.

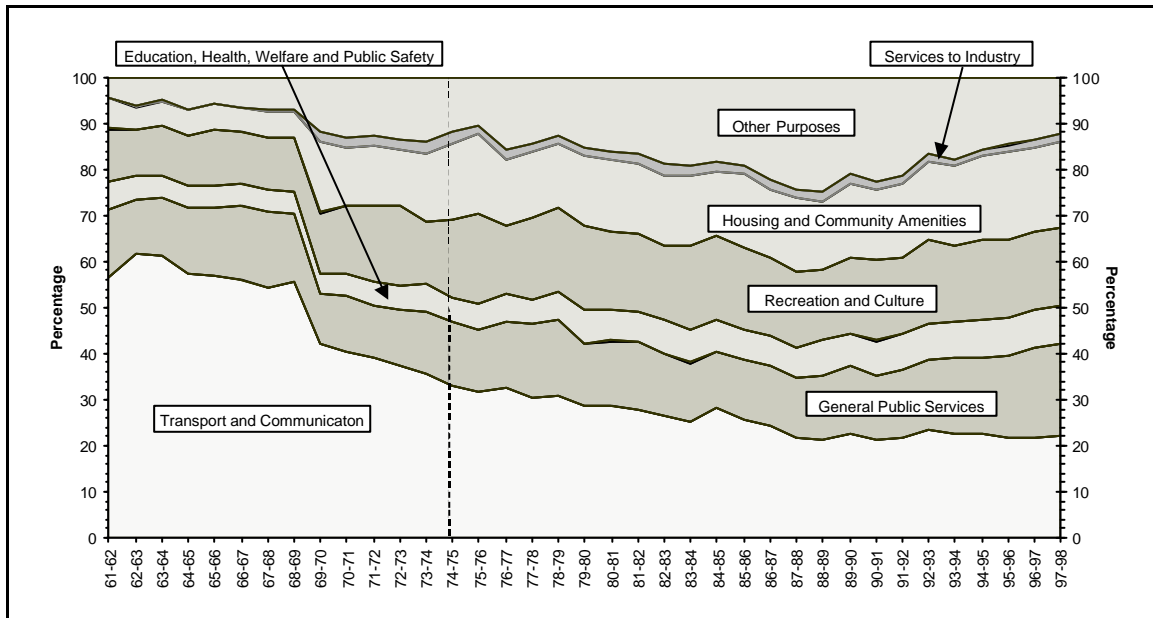
Figure 16-11 REVENUE, SOUTH AUSTRALIA, 1961–62 TO 1997–98



Notes: State Grants include all Commonwealth payments through the States to local government except for the local government financial assistance grants and Local Roads grants. Commonwealth Grants include financial assistance grants and Local Roads grants, and specific purpose payments paid directly to local government.

Source: Unpublished ABS Government Finance Statistics data.

Figure 16-12 EXPENDITURE, SOUTH AUSTRALIA, 1961–62 TO 1997–98



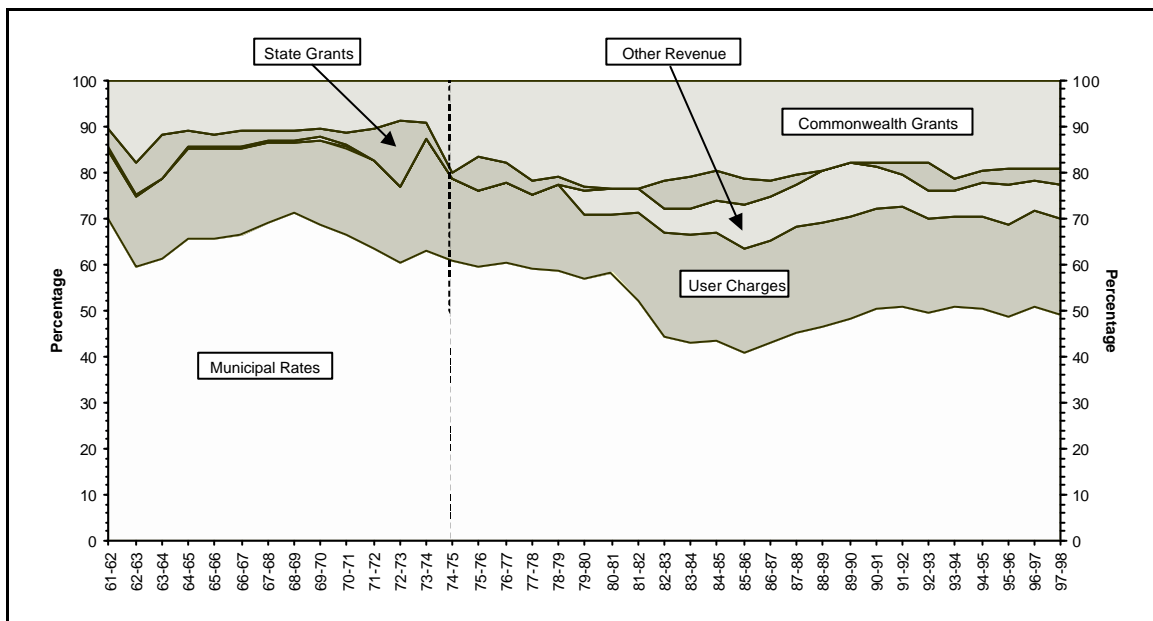
Source: Unpublished ABS Government Finance Statistics.

TASMANIA

13. For local government in Tasmania:

- (i) Figure 16-13 shows the share of revenue from own-sources appears to have remained constant since the introduction of local government financial assistance grants;
- (ii) Figure 16-13 shows the share of revenue from State assistance has fluctuated after the introduction of the local government financial assistance grants but generally it appears the share has been maintained; and
- (iii) Figure 16-14 shows the proportion of expenditure on Transport and Communication and General Public Services has declined since 1961–62 but for all others it has increased.

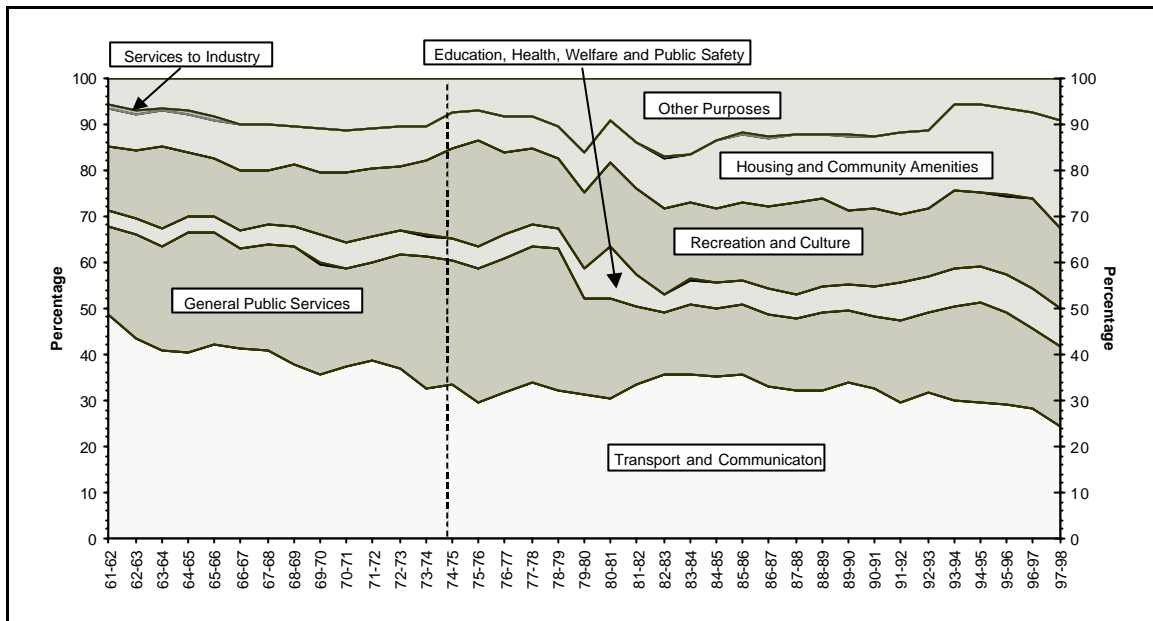
Figure 16-13 REVENUE, TASMANIA, 1961–62 TO 1997–98



Notes: State Grants include all Commonwealth payments through the States to local government except for the local government financial assistance grants and Local Roads grants. Commonwealth Grants include financial assistance grants and Local Roads grants, and specific purpose payments paid directly to local government.

Source: Unpublished ABS Government Finance Statistics data.

Figure 16-14 EXPENDITURE, TASMANIA, 1961–62 TO 1997–98



Source: Unpublished ABS Government Finance Statistics.

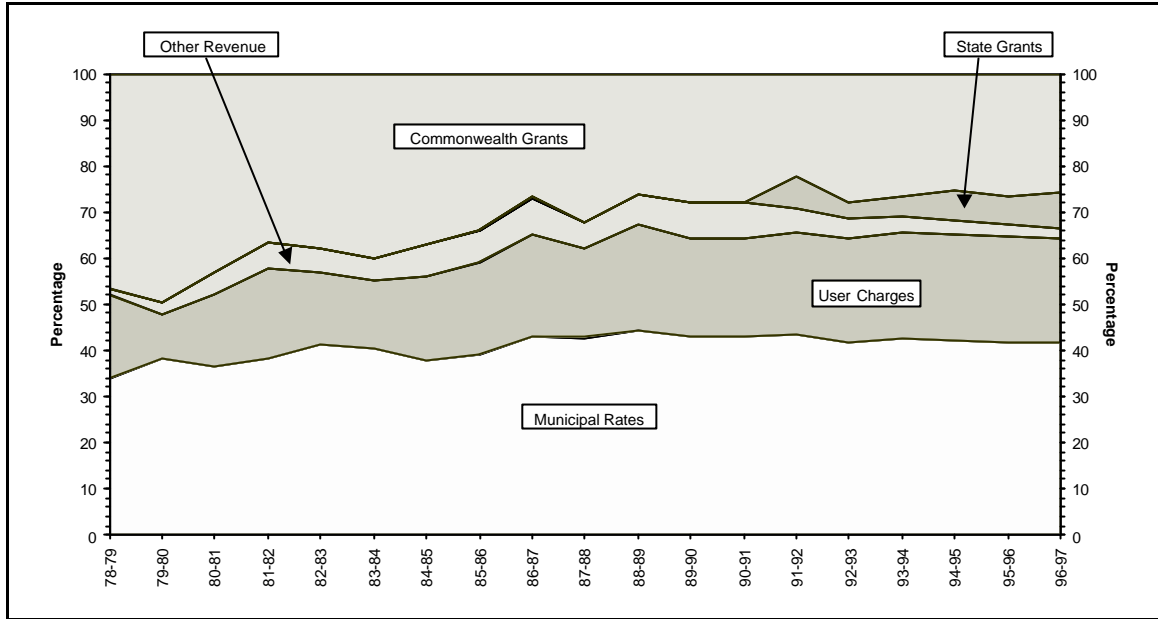
NORTHERN TERRITORY

14. Data for local government in the Northern Territory is only available from 1978–79. Data for 1997–98 is not included because for that year, the ABS data include Community Councils and Association Councils for the first time.

15. For local government in Northern Territory:

- (i) Figure 16-15 shows the proportion of own-source revenue has increased over the period;
- (ii) Figure 16-15 shows State assistance started in the early 1990s; and
- (iii) Figure 16-16 shows the proportion of expenditure for the various components has been relatively constant since 1978–79. The proportion of expenditure on Transport and Communications has generally been less than 20 per cent — the lowest proportion of all the States.

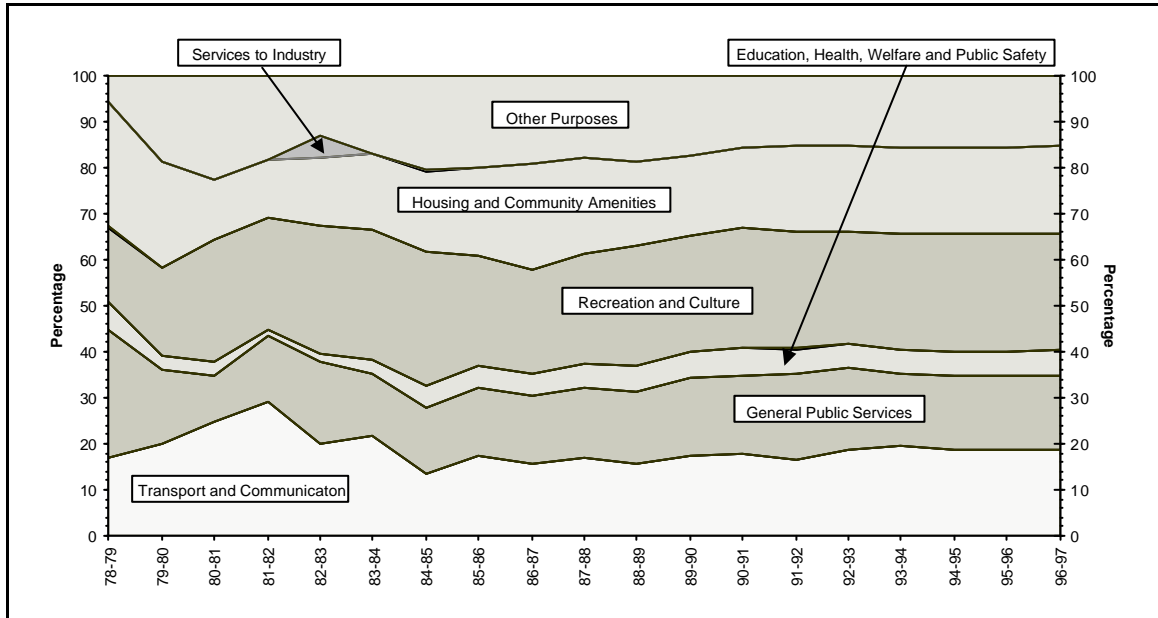
Figure 16-15 REVENUE, NORTHERN TERRITORY, 1978-79 TO 1996-97



Notes: State Grants include all Commonwealth payments through the States to local government except for the local government financial assistance grants and Local Roads grants. Commonwealth Grants include financial assistance grants and Local Roads grants, and specific purpose payments paid directly to local government.

Source: Unpublished ABS Government Finance Statistics data.

Figure 16-16 EXPENDITURE, NORTHERN TERRITORY, 1978-79 TO 1996-97



Source: Unpublished ABS Government Finance Statistics.