Submission to the Inquiry into Local Government funding and services

Victorian Parliament

Legislative Council Economy and Infrastructure Committee

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I. Introduction

The Victorian Farmers Federation (VFF) welcomes the opportunity to make this submission to the Legislative Council Economy and Infrastructure Committee's Inquiry into Local Government funding and services.

The VFF's interest in this inquiry stems from our long-term advocacy concerning the disproportionate impact of local government rates (as the significant portion of funding to local government) on all rural ratepayers, particularly farm businesses.

Local government rates are a tax. By principle, taxation should be fair and equitable. Unfortunately, the current local government rating system is anything but fair and equitable for all rural ratepayers, and particularly farm businesses.

The present system presumes that the higher the land valuation the greater capacity the owner has to pay. In practice however there is a great divide between land valuations, capacity to pay and what is actually paid. What's more, rural ratepayers receive and have access to fewer services from local government than ratepayers in the city.

The VFF is concerned that the local government rating system does not accurately reflect a farm ratepayer's capacity to pay, nor the benefits they receive.

The VFF also believes that there should be an appropriate balance between the commonly used taxation principles: efficiency; benefit; capacity to pay; horizontal/vertical equity; simplicity and sustainability. Fundamentally the VFF believes that as a wealth tax, the local government rating system has failed and is producing inequitable outcomes for farmers and other rural ratepayers and provides an unsustainable foundation for the funding of local government.

These reasons are why the VFF supports a comprehensive overhaul of the rating system through an equalised funding model where the state government redistributes rates to local government based on equity and need. This model is explored further in this submission.

The VFF would welcome the opportunity to appear before the Committee at a public hearing to talk through our submission.

Emma Germano
President
Victorian Farmers Federation

II. Discussion

The VFF's submission is structured around the inquiry's terms of reference and will cover:

- Cost shifting from state and commonwealth to local government.
- Whether councils are adequately delivering on their core service delivery objectives.
- The overall revenue structure of local government.
- Whether the existing revenue structure is sustainable and appropriate or if alternative models of funding would be more sustainable and appropriate.
- Any other related matters.

Cost shifting to local government

The VFF rejects the process of cost shifting, whereby state and federal governments initially fund local government to provide programs and then ceases funding so that if the council wants to continue the program, it must use its own funding. Alternatively, costs may progressively shift overtime even if the state or federal government continues to provide some funding, but it does not keep pace with the cost of delivering the services incurred by the council.

There have been many examples of cost shifting from the state to local government in Victoria. For example:

- Libraries were once funding on a 50/50 basis by the State and local government. It has been estimated that since the 50/50 funding split in 1975, Victorian Government funding has declined to 17 percent of public library operating costs, with 83 per cent of costs borne by councils.[1]
- School crossing supervisors were once funded by the State, but the cost is now borne by the local council.
- The cost of maintaining local roads and infrastructure – which is critical to agricultural production and productivity – is increasingly borne by local government with insufficient state government support.

Cost shifting can also involve other levels of government passing the cost for administering regulatory requirements onto local government without compensation for the costs involved. For example, Energy Safe Victoria requires councils to comply with the electrical line clearance requirements under Electricity Safety Regulations. However, the cost of complying with these regulations is borne by the local council. Mornington Peninsula Shire has estimated that the cost of complying with the electrical line clearance requirements would be $991,000 in 2023-24 and estimated to be $5.3 million over five years.[2]

Local governments are being forced into a situation where they are obliged to continue funding programs that were initiated by state and federal government. This forces them to seek additional revenue or cut back on the provision of other services to community members.

[1] https://www.viccouncils.asn.au/what-councils-do/council-funding/cost-pressures#cost-shifting
[2] https://www.finpro.org.au/wp-content/uploads/pdf/MPSC-Cost-Shifting-Report-2024-for-Edition-4-2024-Member-Update.pdf

In some cases, local governments may be obligated to fund projects that they or their ratepayers would not have initiated given a choice. It is more difficult to stop a program or initiative once it has been running for some time than choosing not to start in the first place.

Delivery of core services

The VFF believes the role of Local Government should be limited to a set of core responsibilities that provide an agreed basic level of service across Victoria. In the context of the funding requirements of local government it is imperative that what councils should, and should not do be clearly defined, otherwise council funding will always be lacking, and no accountability is afforded to provision of core services.

The core responsibilities should include maintenance of local roads; control of municipal planning and provision of planning services; waste disposal; control of pest animals and plants on council owned land; social and economic services only where those services provide a benefit to the community as a whole; provision of information to the community on council activities; advocacy to state government on matters relevant to the interest of the community.

These core services should be funded from rate revenue – the VFF provides comment on the appropriate structure of the rating system in the following section. As an elected body, councils are free to offer additional service and products above the 'core' offering. In this case, the VFF supports the use of special user charges for services provided by local government that are beyond its core responsibilities to maintain the 'user pays' principle.

Revenue structure of local government

Local government rates are a tax, and taxation should be fair and equitable. Unfortunately, the current local government rating system is anything but fair and equitable for all rural ratepayers, and in particular farm businesses.

The present system presumes that the higher the land valuation the greater capacity the owner has to pay. In practice however there is a great divide between land valuations, capacity to pay and what is actually paid. What's more, rural ratepayers receive and have access to fewer services from local government than ratepayers in the city.

This distortive burden on agriculture is further compounded by the degree of variation in municipal rates from shire to shire and the clear discrepancies that fundamentally exist between the abilities for metropolitan councils to generate rate income, against the capacity of rural and regional councils. For example, in 20204-25 the City of Melbourne's total budget was $781 million dollars compared with the City of Shepparton's expenditure of $162.81 million or Buloke's total budget of $43.9 million.

It is the long-held concern of the VFF that local government rates derived from farmland ratepayers are inequitable. As farm businesses have become increasingly aggregated, the rating burden faced by individual farmers has been compounded. The local government rating system does not accurately capture a farm ratepayer's capacity to pay, nor the benefits they receive.

The VFF believes there are five major inequities associated with the local government rating system:

- Farmers in general pay more in rates than residents in urban areas -based on analysis of the 2024-25 rural, regional and interface council draft budgets, the VFF has determined that farmers pay an average $3,457 per assessment in rates. This is compared to an average of $1,425 per residential rate assessment. It is also important to note that many farmers have multiple plots of land on different titles – and so an individual famer may have to pay several assessments on the individual plots of land which comprise their farm. On average, farmers will pay rates over four assessments.

- Rating structures rarely account for the ability to pay and farmers' ability to pay rates fluctuates to a far greater degree than wage and salary earners - farmers' incomes fluctuate because they are more exposed to factors beyond their control including seasonal variability such as rainfall, natural disasters, and changes in international commodity markets. These factors have little impact on land values but have a significant impact on famers' incomes and ability to pay.

- Farmers in general don't have access to many of the services they pay for through rates which are provided in urban areas - in general farmers have little demand for, use and lack of access to facilities and services such as rubbish collection, libraries, parks, gardens, street lighting, footpaths which are provided in towns to enhance the quality of living for residents, or provide economic benefit to businesses located in towns.

- Land is a farmers' working capital and is taxed disproportionately compared with the working capital owned by other people and businesses - farming generally utilises a large amount of 'unimproved' land, and as a result municipal rates are a tax on a means of production. For example, about 70% of a woolgrower's working capital is land. Conversely, the proportion of working capital that consists of land could be extremely small in the case of businesses in a local town. From this viewpoint, it is inequitable that 70% of a farmer's working capital should be taxed whereas another businessperson may be taxed on, say, only 30% of their capital.

- Victoria's rating system produces vast inequalities between metropolitan and regional ratepayers which compounds pressures faced by farm ratepayers - even though property values in metropolitan Melbourne are higher than those in rural Victoria, the average rates paid per assessment is similar across metropolitan and regional Victoria. For example, the rates paid on a $500,000 home in the City of Greater Shepparton in 2024/25 will be $1,699, more than double the rates paid on the same value property in the City of Banyule at $839.

The VFF's view on how the rating system can be reformed to address these inequities is provided in the following section.

Sustainability and alternative measures

The VFF believes that Victoria's local government rating strategy is unsustainable. Poorer rural councils are increasingly reliant on taxing farmers to prop up their finances. This places an increasing and undue burden on agricultural production.

Rate capping

VFF has concerns with how the current rate capping is being applied, with adverse consequences for Victorian farmers. Each year the Minister for Local Government determines the maximum councils can increase rates. The Essential Services Commission provides advice to the minister on the recommended cap each year. For the 2024-25 financial year the Minster has determined that the rate cap will be 2.75 percent.

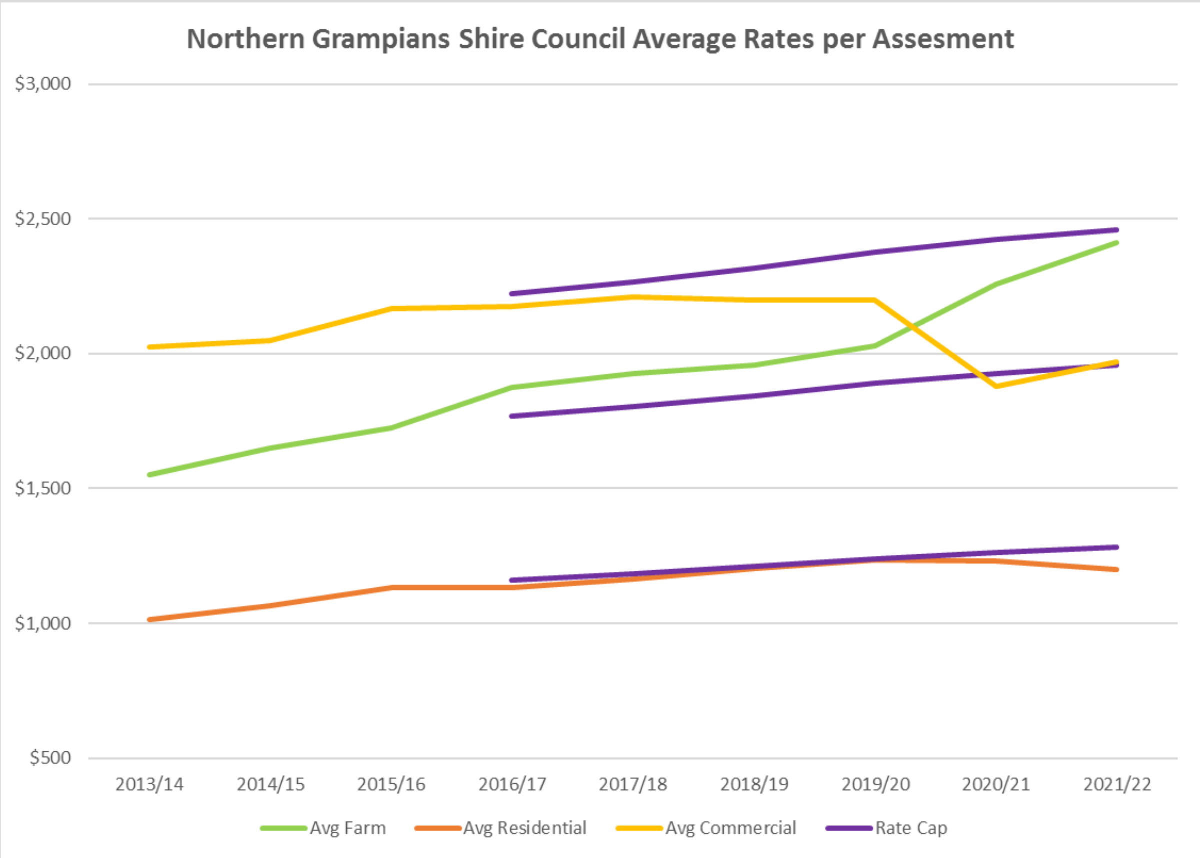
The issue is that the cap is applied to the total revenue from rates across all categories of land. As long as the overall cap is achieved there is significant scope for councils to increase rates on particular land categories. Unfortunately, the VFF has observed over time that rates for farming land have increased more quickly than and disproportionately toother land types.

VFF analysis of draft and adopted council budgets for 2024-25 shows that 19 regional councils increased farm rates above the government rate cap of 2.75%, whilst residential rate increases remained at or below the cap. Table 1 provides data on the top 10 local governments increasing rates for farm/agricultural land.

Table 1: Top 10 rate increases for farmers in 2024-25

LGA	Average Residential Rate Increase	Average Farm Rate Increase
Ballarat City Council	1.45%	12.57%
Greater Bendigo City Council	2.46%	10.22%
City of Hume	0.04%	14.38%
South Gippsland Shire	0.05%	10.14%
Campaspe Shire Council	0.39%	7.91%
Central Goldfields Shire Council	0.91%	7.29%
Mildura Rural City Council (Dryland farms)	-0.23%	15.91%
Moira Shire Council	-4.72%	25.84%
Swan Hill Rural City Council (Dryland farms)	5.86%	8.7%
Murrindindi Shire Council	-2.22%	8.38%

Source: Local government budgets and draft budgets 2024-25.



Analysis undertaken by the VFF in 2021 of the Northern Grampians Shire Budget showed the effect of rate capping across differential rating categories. If a nominal cap had been placed on each differential category of land, we see the Council failing to maintain an equitable increase across those categories. Consequently, farm rates were allowed to increase almost exponentially, whilst residential rates remained true to the cap and commercial rates were heavily discounted.

It is clear from the data provided that the rate capping system is failing to stop regional councils from forcing undue rate increases onto farmers.

The VFF recommends, that if the system of rate capping is to be retained that the cap must be applied to each category of land used for rating purposes. The annual cap determined by the Essential Service Commission would be applied to residential, farming, commercial, industrial and any other differential land category.

Councils would still have flexibility to vary rate changes between land types, but these would be limited by the cap. Instead, councils would need to dynamically use their differential rating power to account for valuation asymmetries between land types on an annual basis. The fundamental principle should be that as the value of farmland increases, the differential rate is adjusted to reduce the rate in the dollar so that the rate burden paid by the farm sector remains stable. This approach has been applied with great effect in the Ararat Rural City Council for the past seven years, and in the Mansfield Shire Council more recently.

Importantly, such a method of setting rates would not impact the overall rate take by councils and the VFF is able to provide evidence where we have remodelled council budgets to show this to be the case. The methodology is also wholly consistent with the intent of current government policy with respect to rate capping.

This system would ensure a fairer distribution of the rate burden between land types. It would also put pressure on councils to look for greater efficiencies and cost savings rather than passing costs onto particular land types.

A more fundamental change: A system of equalisation

Ad hoc changes to the current rating system will help improve the rating system but will not address the underlying structural flaws which leads to inequality between rural and metropolitan communities. A more fundamental rethink of how the rating system operates and local governments are funded is warranted.

A key concern of the VFF is the inequity in the rates paid for similarly valued properties between municipalities. In particular, the VFF is concerned by the inequity between disadvantaged rural councils compared to metropolitan councils. Ratepayers in rural and regional councils also have lower incomes and therefore pay a higher percentage of their income towards rates.

The wide discrepancy in rates charged even among rural councils on the same value farm/agricultural land is show in the selection of councils in table 2.

Table 2: Rates levied on Farm/Agricultural land

LGA	Rate (cents/$CIV)	Rates payable on $10m farm property ($)
Alpine Shire	0.001685	16,850
Ballarat City Council	0.00214272	21,427
Buloke Shire Council	0.0021281468	16,850
Macedon Ranges Shire Council	0.0014861	14,861
Shepparton Council	0.00307483	30,748
City of Wyndam	0.001758	17,580
Yarriambiack Shire	0.001739	17,390

Source: Local government budgets and draft budgets 2024-25.

In recognising the inequity in rates paid by rural and regional ratepayers compared to metropolitan ratepayers, the VFF supports the restructuring of Victoria's rating system to one based on an equalised funding system whereby the state government redistributes rates to local government based on equity and need.

This is not a new idea and was raised by Ararat Rural City Council (Ararat Council) in its submission to the 2019 Local Government Rating System Reivew. In its submission Ararat Council noted the rating inequity between regional and metropolitan councils and further noted that grants provided through the Victorian Grants Commission are insufficient to address this inequity. Ararat Council stated:

> *Quite often when the issue of rating inequality and small rural councils is discussed the 'equalisation' impact of Victorian Grants Commission (VGC) grants is used to indicate that*

rating inequality is being compensated for. While the VGC grants provide some equalisation it is not sufficient to have any real impact.[3]

Under the model proposed by Ararat Council, which was and remains endorsed by the VFF, each council would still receive the same rating revenue, but ratepayers would contribute according to a state average rate applied the CIV of property in the local government area. At the time of preparing its submission, Ararat Council estimated that:

> *Under this model ratepayers in 60 of 79 municipalities would be required to pay less rates – ratepayers in larger, metropolitan Councils would be required to pay more rates to balance the system. In some cases the contribution to rating equity would be significant.*
>
> *No municipality would actually receive less income - it would be managed at a state level to equalise the system so that all Councils received revenue based on a universal rate in the dollar.*[4]

Local councils would still have flexibility to determine the rates applied to different type of land uses:

> *There would need to be provisions to ensure that differential rating models, particularly farm rates could be maintained. The average rate as percentage of CIV model would be used to determine the quantum of rates received by individual municipalities, individual rating strategies would determine individual rate payer contributions based on differential rating models.*[5]

The VFF recommends the Legislative Council Economy and Infrastructure Committee investigate the implementation of an equalisation funding system as follows:

- The State Government would establish a general rate in the dollar based on the state-wide valuation of property and the state-wide population or the state-wide number of rate assessments.
- The State Government could establish a different general rate according to council type (metro, interface, regional, rural).
- The State Government would redistribute the revenue based on equity and need like the allocation of Financial Assistance Grants and that this function should be performed by the Victorian Grants Commission.

As part of an equalised funding system, consideration should be given to tying rate revenue to the delivery of a standard set of core services, standard costs and levels for each service and a standard allowance for administration and overheads. That standard set of services would be classified according to council type (metropolitan, rural, regional etc.). Councils wishing to deliver services over and above the standard set of core services would need to generate additional revenue to cover the cost of those services on a user pays basis or through alternative revenue sources.

Other aspects of the rating system

Other reforms to the rating system which could be undertaken as a reform to the existing rating system or as part of a move to an equalisation system which would benefit farmers include:

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[3] Ararat Rural City Council (2019) *Submission to the Victorian Local Government Rating System Review*, p. 3.
[4] Ararat Rural City Council (2019) *Submission to the Victorian Local Government Rating System Review*, p. 4.
[5] Ararat Rural City Council (2019) *Submission to the Victorian Local Government Rating System Review*, p. 4.

- the averaging of individual property valuations for the purposes of rating to prevent volatility and the effects of 'rate shock'. The key concern of most ratepayers regarding the current rating system is the large and sudden shifts in the individual rates bills that occur. Valuations change continuously by prevailing market and economic conditions and have no relationship to capacity to pay, fairness and levels of council service provided. It is unreasonable for a council to continuously vary the amount it taxes property owners/occupiers by percentages in the order of how valuations can change from year to year.

  Valuation averaging was a key recommendation of the 2019 Rating System Review.

- the use of minimum and maximum rates to flatten the rating profile across local government authorities and to take the rating burden away from productive agriculture. This approach was supported by the Municipal Association of Victoria in its submission to the 2020 Independent Review of Rating in Victoria. Where minimum rates are not implemented, the VFF supports the use of a municipal charge to be raised at no less than 20% of the total rates and charges within a council area.

- where farmland is to be rated the VFF supports the separation of house and curtilage from the farmland to be rated differentially. Separating house and curtilage from farmland would create greater equity for farmers and other ratepayers by recognising the distinction between the home and the business. In terms of the benefit principle, the house and curtilage mechanism allow for separate rating based on the services received by the property – that is councils' people orientated services for the home and the limited services received by and for the farm property.

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The voice of Victorian farmers and rural communities since 1979

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