

CHAPTER 10

A COMPARISON OF LGGC EQUALISATION MODELS

1. Each of the seven LGGCs uses a different model and methods to determine the distribution of their General Purpose grants. In this chapter, these differences and the impact they are likely to have on LGGC calculations are examined.

Distributing the General Purpose Pool

2. The LGGCs distribute General Purpose grants using two criteria:

- (i) minimum grant; and
- (ii) equalisation.

3. They assess a minimum grant outcome and an equalisation outcome for each LGB, and each LGB receives the higher of the two assessments. If there is insufficient funding in the pool to fund the initial assessment for each LGB, the equalisation outcome is scaled back (this process is also known as 'Factoring Back').

4. **Minimum Grant outcomes.** The minimum grant was discussed in a previous chapter. All LGGCs implement the minimum grant in the same way.

5. **Equalisation outcomes.** It is in the area of equalisation outcomes that differences occur in LGGC approaches. They each appear to have a different appreciation of equalisation concepts (for example, horizontal equalisation, effort neutrality, inclusion), and they therefore use different approaches to arrive at their resulting distribution.

6. Equalisation outcomes depend on a range of LGGC decisions, including:

- (i) the equalisation model used;
- (ii) the scope of equalisation used;
- (iii) the approach taken to assessing expenditure need;
- (iv) the approach taken to assessing revenue capacity; and
- (v) the approach taken to the treatment of SPPs.

7. There are concerns with some aspects of the LGGC's approaches because they are impacting in a way that is preventing them from obtaining the form of equalisation that they set out to achieve.

8. Chapter 8 dealt with the approach taken to the treatment of SPPs. Chapters 11 and 12 deal with expenditure assessment and revenue assessment issues. In this chapter, the equalisation models used and the scope of equalisation are considered.

Equalisation Models

9. The equalisation model is the method by which LGGCs combine their expenditure, revenue and SPP assessments to determine their equalisation outcomes. LGGCs use one of two models:

- (i) balanced budget; or
- (ii) direct assessment.

10. The Commonwealth Grants Commission (CGC) has two ways of presenting its grants distribution model, both of which give the same result. The balanced budget model is very much like the CGC's 'standardised' presentation but it is missing one term. The direct assessment model is very much like the Commission's 'needs' presentation but it too is missing one term. If the missing terms are included, the 'adjusted' balanced budget model will be equivalent to the 'adjusted' direct assessment model and both will be equivalent to the CGC's model.

11. The **Balanced Budget Model**. Five LGGCs use the balanced budget approach (Victoria, Queensland, Western Australia, Tasmania and the Northern Territory). Their models are based around the standardisation of expenditure, revenues and SPPs for each LGB. They can be expressed as:

Grant required

equals

Standardised expenditure

less

Standardised revenue capacity

less

Actual receipt of SPPs

plus

The standard budget result.

12. Such a model can give truly equalisation results but, as used by the LGGCs, it has a flaw – it has a missing term (the standard budget result). It would be sufficient in its current form if there was no imbalance in LGBs' budgets, but this is not the case and there needs to be a budget result term included to correctly imitate the reality of how LGBs are financed. The exclusion of the term means that the LGGC's decision about the scope of expenditures or revenues to include in the equalisation budget affects its assessed equalisation outcomes¹. The omission of this term means that:

- (i) including a new expenditure function effectively rescales downward the needs assessed in other categories (and vice versa); and
- (ii) including a new revenue function rescales upward the needs assessed in other categories (and vice versa).

13. Therefore, changing the scope of equalisation, in either the expenditure or the revenue assessments, can have big impacts when the balanced budget approach is used.

14. If the missing term is included, this effect goes away so that changing the scope of equalisation has no effect on the pre-existing assessments: it is simply an addition to them.

15. **Direct Assessment Model.** Two LGGCs use the direct assessment approach (New South Wales and South Australia). It commences with an objective of assessing needs rather than standardised expenditure and revenues and can be expressed as:

Grant required

equals

An equal per capita share

plus

Expenditure needs

plus

Revenue needs

plus

SPP needs.

¹ In the CGC's equalisation model, it is only the assessment of needs that affects equalisation outcomes.

16. Because the calculations of need are based around the State average experience or some other concept of standard, needs can be either positive or negative. As implemented by the LGGCs, which leave out the EPC distribution, it has a flaw which has the potential to:

- increase the number of minimum grant LGBs; and
- distort grant outcomes in favour of the LGBs with the biggest equalisation assessments.

17. The problem is that, once again, the scope of expenditures and revenues brought into the equalisation budget influences the results other than through the assessment of their needs.

18. Table 10-1 shows the differences in the equalisation models used by each LGGC.

Table 10-1 DIFFERENCES IN THE EQUALISATION MODEL USED

State	Model used
New South Wales	Direct assessment model. Separate assessment for Lord Howe Island, Silvertown and Tibooburra.
Victoria	Balanced budget model. Assistance for natural disaster relief taken out of the pool.
Queensland	Balanced budget model.
Western Australia	Balanced budget model.
South Australia	Direct assessment model. Separate assessment for the Outback Areas Community Development Trust (\$105 per capita) and five Indigenous Communities (\$204 per capita).
Tasmania	Balanced budget model.
Northern Territory	Balanced budget model.

19. **Does the choice of model matter?** If the assessment models were specified differently, the choice of model would not matter, but it does. It does because the two models, as they are used, produce different results. This means that if a LGGC changed from one model to the other — without changing its standard budget, assessed disabilities or something else — its assessed LGB equalisation outcomes would change, as would its assessed grant allocations.

20. The choice of equalisation model should not influence grant outcomes.

Scope of Equalisation

21. LGGCs limit their scope of equalisation by not including all the activities of the LGBs in their State. Table 10-2 shows a summary of functions included or omitted from LGGCs standard budgets.

Table 10-2 DIFFERENCES IN THE SCOPE OF EQUALISATION

Function	NSW	Vic	Qld	WA	SA	Tas	NT
Expenditure							
Administration	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Law, order & public safety	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Education, health and welfare	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Community amenities	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Recreation and culture	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Transport:							
- airports	Yes	Yes	Yes	Yes	Yes	No	No
- buses	Yes	No	No	Yes	Yes	Yes	No
- other transport	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Building control	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Garbage	No	Yes	No	No	No	Yes	Yes
Water	No	No	No	No	No	Yes	No
Sewerage	No	No	No	No	No	Yes	No
Electricity	No	No	No	No	No	No	No
Capital	No	No	Yes	Yes	No	No	No
Depreciation	No	No	No	Yes	No	No	No
Debt servicing	No	No	No	No	No	No	No
Entrepreneurial activity	No	No	No	No	No	No	No
Agency arrangements	No	No	No	No	No	No	No
Revenue							
Rate revenue	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Operation subsidies	No	No	No	No	Yes	No	Yes
Garbage charges	No	Yes	No	No	No	No	No
Water charges	No	No	No	No	No	Some	No
Sewerage charges	No	No	No	No	No	Some	No
Airport charges	No	No	Yes	No	No	No	No
Parking fees and fines	No	No	Yes	No	No	No	No
Other user charges	No	Yes	Yes	Yes	No	No	No

22. In some cases the limited coverage is by choice. For example, the Tasmanian LGGC said that it wishes to wait until it has resolved the issue of depreciation before expanding the coverage to revenues other than general rates. In some cases, LGGCs have said that expanding the coverage of revenues (eg to include parking fees and fines) would create work without any benefits — it would only increase the revenue capacity of minimum grant LGBs and make them ‘minimum grant LGBs to a greater degree’.

23. **Does it matter?** The choice of scope of equalisation does matter if a balanced budget model is used.

24. The choice of scope matters for LGBs that have needs in the functions that are omitted. These LGBs are not being fully equalised and, because of decisions about the scope of equalisation, they will have to fund some needs from their own sources whereas other LGBs have their needs financed from General Purpose grants.

25. One example that was brought to the Commission’s attention during our State consultations was the increase in the use of agency arrangements by Commonwealth and State governments. This trend has also resulted in the withdrawal of service provision in some areas on economic grounds. These changes appear to have impacted most on rural and remote LGBs. These LGBs have been left with the decision of whether or not to provide the withdrawn services themselves (for example, the provision of assistance to retain rural doctors, bank services etc)². If these changes are occurring in functions that are outside LGGCs’ existing scopes of equalisation, the rural LGB receives no additional assistance to enable them to take on the added burden.

26. It is for reasons such as this that the CGC regularly reviews the scope of its equalisation budget. For example, Roads was brought into its standard budget for the first time in 1993 and Depreciation was brought into its budget in 1999.

² It is possible that some of the additional costs arise as a result of a rural LGB’s decision to provide an above standard service.

CHAPTER 11

MEASURING EXPENDITURE NEED

Expenditure Equalisation

1. Expenditure equalisation is about identifying needy LGBs and measuring the extent of their ‘need’ — the differential costs of service provision (either positive or negative) over which LGBs have no control. Expenditure equalisation requires cost influences that affect either unit delivery costs or levels of demand to be measured.

2. The size of expenditure need depends on three things:

- (i) the size of the category standard;
- (ii) the proportion of the standard affected by the relevant cost influence;
and
- (iii) the extent of the cost influence.

3. This chapter examines each of these in turn. It also presents information on the key drivers of the present expenditure equalisation assessments undertaken by the LGGCs, by category and disability.

Calculating Category Standards

4. The Commonwealth Grants Commission (CGC) defines standard expenditure in the same way for all categories. It is total national expenditure by the States, divided by total population.

5. The LGGCs calculate expenditure standards in different ways. Table 11-1 summarises them. The different approaches can impact on expenditure assessments. For example, calculating a standard using road lengths is different to calculating it using population. This has implications for the Direct Assessment approach which calculates expenditure allowances as the difference between standardised and standard expenditure. Changing the method of calculating the standard (using road length or number of properties instead of population) changes the assessed expenditure allowance. It also results in expenditure allowances, within the assessment for an individual LGB, that are not compatible with one another — this is one reason why the CGC calculates all of its expenditure standards using the one basis (population).

Table 11-1 HOW LGGCS ASSESS EXPENDITURE STANDARDS

State	Method
New South Wales	Expenditure per total number of units for the State as a whole. Number of units can be population, properties or road length. Extreme values (outliers) are omitted.
Victoria	Expenditure per total number of units for the State as a whole. Number of units can be population, properties or road length.
Queensland	Services function: For mainstream LGBs, expenditure per capita plus an expenditure per LGB ^(a) . For Indigenous LGBs, expenditure per capita ^(b) . Roads function: Expenditure per road length.
Western Australia	Standard calculated using regression analyses — different equations for different categories.
South Australia	Expenditure per total number of units for the State as a whole. Number of units can be expenditure ^(c) , population, properties, new developments, or road length.
Tasmania	Expenditure per capita for the State as a whole.
Northern Territory	Expenditure per capita for the State as a whole.

- (a) The expenditure per capita and expenditure per LGB amounts are determined after regression analysis.
- (b) The expenditure per capita amount is not State expenditure divided by State population. It is different to the expenditure per capita amount used for mainstream LGBs.
- (c) This allows the South Australian LGGC to use its uniform approach to achieve an Actual Per Capita assessment.

Calculating the Proportion of the Standard Affected by the Cost Influence

Terminology:
 A CGC disability factor is the quantification of a cost disability relative to the average Australian experience. Calculating factors in this way has a number of benefits:

- * the average Australian factor is 1.0000;
- * the CGC's factors centre around one;
- * when the factors are applied to standard expenditure they produce per capita standardised expenditures that centre around the standard; and
- * for a given category and year, the sum of standardised expenditures for all States equals the sum of their actual expenditures.

A CGC disability is a factor minus one. Calculating disabilities in this way has a number of benefits:

- * the CGC's disabilities centre around zero;
- * when the disabilities are applied to standard expenditure they produce per capita expenditure needs that centre around zero; and
- * for a given category and year, the sum of expenditure needs for all States equals zero.

6. For each cost influence, the CGC considers the proportion of expenditure that is affected by it. The purpose of this step is to relate the influence to the expenditure that it affects.

Example:

If a LGB faces a cost disadvantage of 20 per cent but the disadvantage affects only 5 per cent of the category expenditure, its category disability is only 1 per cent ($0.20 * 0.05$).

7. Since expenditures are aggregated into categories it is important to differentiate the expenditure affected by the cost influence from expenditure that is not affected by it. If the level of disadvantage is applied to all expenditure within the category, the assessment of expenditure may be erroneously inflated.

8. Some LGGCs do not appear to make this distinction. For example, the Tasmanian approach appears to be to decide whether or not a dispersion disability applies in a category, if it does, the same disability is used in all other cases that a dispersion disability is considered relevant. This would only be appropriate if, for those categories:

- (i) all category expenditure was affected by the dispersion influence in the same way; or
- (ii) the proportion of category expenditure affected by dispersion was the same for each category and the assessed dispersion factor had been discounted to reflect this proportion.

9. The last point touches on a separate issue. From a measurement perspective, it does not matter whether the discount is determined as a separate element of the factor calculation process or whether factors are discounted before being applied to total expenditure (the CGC uses both approaches). What does matter is that the cost influence is related to the expenditure that it affects.

Calculating the Size of the Cost Disability

10. The differential costs of service provision can be assessed directly or (through the use of factors) indirectly. Although there are some examples of the direct approach (Victoria's assessment of natural disaster expenditure for example), most LGGCs prefer the indirect approach. Table 11-2 sets out how they assess expenditure factors (that is, how they implement the indirect approach).

11. There are three concerns with LGGC approaches to assessing expenditure factors. They may:

- (i) implicitly introduce a disability (through either of two different mechanisms);
- (ii) measure disabilities that do not exist; and
- (iii) not measure disabilities that do exist.

Table 11-2 HOW LGGCs ASSESS EXPENDITURE DISABILITIES

State	How a LGB's disabilities are calculated
New South Wales	Disabilities are not centred around 1.0. The minimum disability is 1.0. Disabilities are combined by addition. All LGBs with a value less than or equal to the State value receive the minimum disability. Disabilities are calculated as ratio of LGB value to State average value for the relevant measure. The disability is then weighted to reflect its significance in terms of its likely cost impact. An isolation disability is assessed for non-Sydney LGBs.
Victoria	Disabilities are combined additively. Disabilities are not centred around 1.0. Disabilities are capped (minimum of 1.0, maximum of either 1.5 or 2.0). Disabilities are not weighted to reflect their significance in terms of their likely cost impact. A weight is applied but it is calculated as one divided by the number of disabilities assessed for the relevant function.
Queensland	For the Services function, disabilities are additive (except for an isolation disability). Minimum disability is usually 1.0 (but for one disability it is possible to have a value less than 1.0). Disabilities are assessed for each component ^(a) and weighted to reflect their component's significance relative to total Service expenditure. They are not weighted to reflect their significance in terms of the likely cost impact on their component. For the roads function, an asset preservation approach is used to determine a factor. Five functions (aerodromes, other transport, agriculture and forestry, urban storm water drainage, parking) are assessed by the Actual Per Capita method.
Western Australia	Disabilities are additive (except for location disability). Minimum disability of 1.0. Disability is not weighted to reflect its significance in terms of its likely cost impact.
South Australia	Disabilities are multiplicative. Disabilities are centred around 1.0. Disabilities have only been calculated for 6 road and 2 stormwater functions. Needs for functions are aggregated and assessed in the Other Needs assessment. These are based on an assessed dollar amount for each disability.
Tasmania	Disabilities are additive. Disabilities are not centred around 1.0. Minimum disability is 1.0. The value of a disability is the same regardless of the function to which it is applied. Disabilities are not weighted to reflect their significance in terms of its likely cost impact.
Northern Territory	Disabilities are multiplicative. Disabilities are not centred around 1.0. Minimum disability is 1.0. The value of a disability is the same regardless of the function to which it is applied. Disabilities are not weighted to reflect their significance in terms of its likely cost impact. Only five disabilities are assessed.

(a) There are separate components for education, health, welfare, garbage, street lighting, community amenities, recreation and sport, libraries, building control, community/regional development, public infrastructure and general public services.

12. **Implicitly introducing a disability — use of regressions.** Two States use regression analyses to calculate expenditure standards. The resultant regression equations include a constant term, implying that each LGB faces a fixed cost in providing the relevant service. This approach will produce the 'correct' assessment of expenditure needs if:

- (i) the LGGC thinks scale economies exist; and
- (ii) the regression equation produces a fixed cost assessment (the scale factor) of the size intended by the LGGC.

13. In at least one case, the fixed cost assessment exceeds an individual LGB's total actual expenditure.

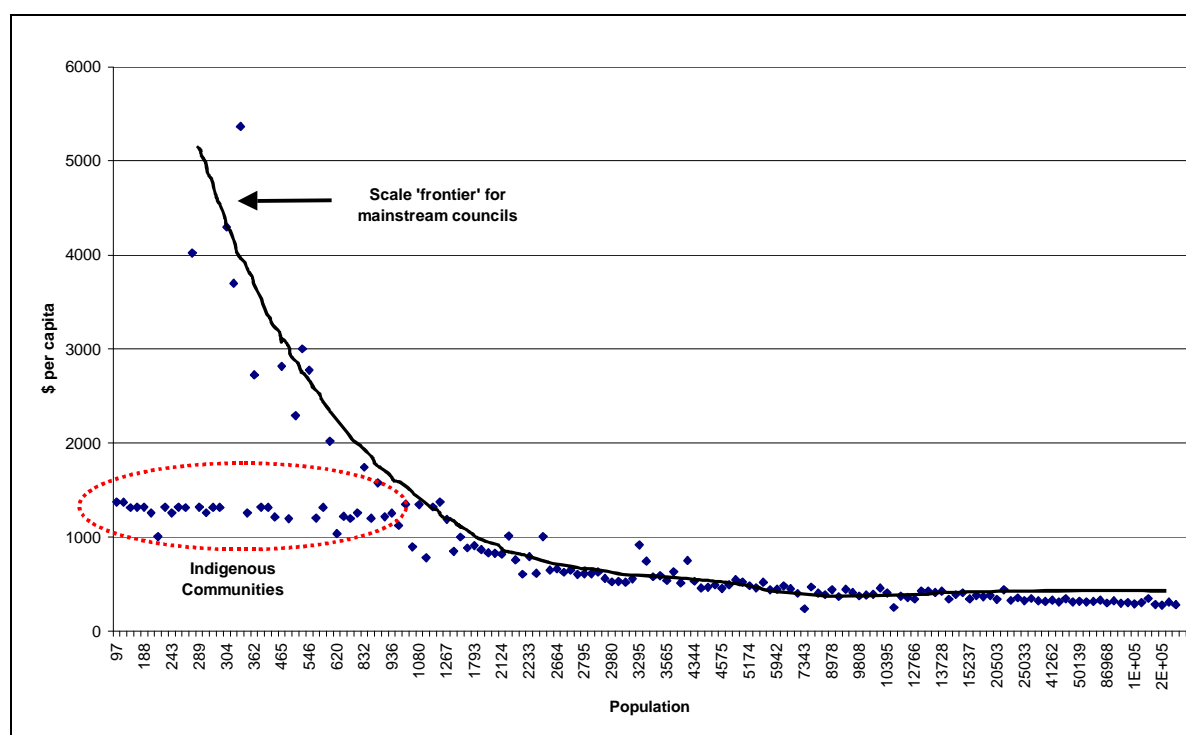
Examples:

The constant term for the Services function assessed by the Queensland LGGC was \$650 000 in 1999–2000. That is, each LGB was assumed to face fixed costs of \$650 000. 119 of the 160 Queensland LGBs had Services expenditure less than \$5 million. This implies a scale disability of 13 per cent or more for all of these LGBs. Scale redistributes \$131 million in Queensland, compared with \$212 million for Roads.

Western Australia has different fixed costs for different functions. The largest are \$95 000 for General Governance (Administration) and \$72 000 for Recreation and Culture.

14. There are two potential problems with the regression approach. First, it has the potential to introduce scale disabilities into the assessments. Figure 11-1 plots the Standardised Services Expenditure per capita assessed by the Queensland LGGC, against population. The chart also shows the per capita assessment for the Indigenous LGBs. The chart demonstrates that scale is a large influence within the mainstream LGB assessments. It also implies that a different assumption about diseconomies of scale is being used in the assessments of the Indigenous LGBs.

Figure 11-1 STANDARDISED SERVICES EXPENDITURE PER CAPITA, QUEENSLAND, 1999–2000



15. Second, the regression approach can ‘hide’ the relationship between disabilities. Because the regression equation’s dependent variable is actual expenditure, it is difficult to know which disabilities have been captured by the regression equation. Layering disabilities on top of the regression equation could lead to double counting.

16. These concerns do not invalidate the use of regressions. They highlight the difficulties of integrating a regression equation within an assessment framework.

17. **Implicitly introducing a disability — different basis of comparison.** An earlier section discussed how using different bases of comparison (road length, number of properties, population) can produce different category standards.

18. Changing the basis of comparison has the same effect as introducing another disability. If all assessments were converted to a per capita basis of comparison it would change the standardised assessments of categories currently assessed on another basis (per property or per road length). A new factor would be required to produce the same standardised assessments as now¹. It is for this reason that a different basis of comparison is equivalent to introducing a new factor.

19. There are two inherent problems with the use of different bases of comparison, although only the second has an impact on grant outcomes.

20. First, if the assessments are converted to a per capita basis by introducing a new factor as described above, the new factor can turn out to be one of the larger key drivers of expenditure assessments. This means that, at the moment, this key driver is being hidden within the assessments and may not be getting the critical evaluation that is required.

21. Second, the Direct Assessment Model effectively calculates expenditure allowances by subtracting standard expenditure from standardised expenditure. The choice of the basis of comparison determines the standard expenditure that is deducted. In rural areas, for example, road lengths are larger than population numbers which are larger than property numbers. Compared with per capita standards, per road length standards are lower (so assessed expenditure allowances are larger) and per property standards are higher (so assessed expenditure allowances are smaller). This means that different basis of comparison produce expenditure allowances that are not compatible. To overcome these problems, it is necessary to express both standardised expenditure and standardised revenue in the same terms. The usual option is to express all expenditure and revenue standards on a per capita basis.

22. **Measuring disabilities that do not exist.** Expenditure equalisation is about measuring the extent to which individual LGBs face unavoidable costs of service provision. These assessments should reflect the actual costs faced by LGBs. There are two practices that appear to be inconsistent with this approach.

- (i) Some LGGCs assess factors that produce standardised expenditures that total to more than total actual expenditure.

¹ The new factor would be calculated as the ratio of a LGB’s properties (or road length) per capita compared to the State average properties per capita.

- (ii) Most States do not appear to weight their disabilities to reflect the expenditure to which they relate².

23. Earlier this chapter noted two features of the way the CGC assesses its factors. They are:

- (i) the average factor is 1.0000; and
- (ii) the sum of standardised expenditures equals the sum of actual expenditures. The category has the same weight in the grant calculations as it does in the standard budget.

24. The CGC thinks that the advantage of this approach is that it ensures that cost disadvantages are matched by cost advantages. In its inquiries, the advantages of States assessed to have a factor below one are exactly offset by the disadvantages of States assessed to have a factor above one.

25. A requirement for ensuring that the sum of standardised expenditures equals the sum of actual expenditures is for the average State factor to be 1.0000. The following example demonstrates this.

Example:

Under the CGC approach, the per capita standard expenditure would equal State expenditure divided by State population.

In the absence of any cost influences, each LGB would be assessed to have a factor of one and the average State factor would also be one.

An individual LGB's standardised expenditure would be assessed as the product of the per capita standard expenditure (it would be assumed to be able to provide the average level of service at the standard cost) and its population. The sum of standardised expenditure for all LGBs would, therefore, be equal to total (actual) expenditure.

26. The implication of this example is that if the average State factor is one, total standardised expenditure will sum to total actual expenditure. The opposite is also true. If the average State factor is not one, the sum of standardised expenditures will not be equal to the sum of actual expenditures.

27. The problem that this causes can be illustrated by considering the Tasmanian assessments.

² For example, two States determine values for disability factors (dispersion for example) and the same factors are then applied to a number of categories. This suggests that they do not take account of how much of the expenditure in the category is affected by dispersion.

Example:

The following lists total actual expenditure and standardised expenditure for each expenditure function for Tasmania for 1999–2000:

	Actual	Standardised
General Administration	\$49.5 million	\$71.4 million
Health, Housing and Welfare	\$7.7 million	\$9.6 million
Protection of the Environment	\$26.9 million	\$34.2 million
Recreation and Culture	\$39.5 million	\$52.5 million
Community and Regional Development	\$23.0 million	\$29.7 million
Law, Order and Public Safety	\$2.3 million	\$2.5 million
Sewerage	\$23.7 million	\$28.8 million
Water	\$48.2 million	\$57.5 million
Other	\$9.7 million	\$9.9 million
Roads	\$85.9 million	\$110.3 million
Total	\$316.5 million	\$406.2 million

Source: Tasmania State Grants Commission, *Annual Report for 1999–00*, Appendices 9 and 10.

28. The difference between total actual and total standardised expenditures arises because Tasmania assesses every LGB with a factor of one or above. If a factor of one for every LGB produces standardised expenditures that sum to total actual expenditure, a factor of one or more for every LGB must produce standardised expenditures that sum to more than total actual expenditure.

29. The example shows that the effect is different for different functions. The conclusion is that Tasmania’s approach to measuring and applying disabilities is resulting in the General Administration function being given too great a weight in its grant calculations. This effect does not occur with their revenue assessments so that there is also an imbalance between their expenditure and revenue assessments.

30. The second practice was discussed earlier. If LGGCs do not relate their disabilities to the expenditure they affect, they will erroneously inflate expenditure needs.

31. Expenditure equalisation is about assessing the extent of cost advantage and cost disadvantage. Expenditure needs should reflect the differential effect of the unavoidable cost influences faced by LGBs. This is not achieved if disabilities are not weighted to reflect the proportion of category expenditure that they affect.

32. **Not measuring disabilities that do exist.** The CGC assesses expenditure needs for advantaged and disadvantaged States. Just as LGGCs do not assess the same degree of disadvantage for all disadvantaged LGBs, assessing a minimum factor of 1.0 implies that all advantaged LGBs experience the same degree of advantage³. Clearly, this is not the case.

33. If a cost influence exists, it is likely to affect LGBs differently — some LGBs will have to spend more than the State average per capita to provide the average level of service while others will be able to provide it but spend less than the average. If LGBs’

³ The minimum grant requirement effectively places a floor on a LGB’s share of the General Purpose pool. However, this requirement has nothing to do with how equalisation assessments should be calculated.

factors are limited to being one or above, it is the equivalent to saying that no LGB needs to spend less than the State average per capita. If the average State factor is to be 1.0, some LGBs must be above 1.0 (experience a cost disadvantage) and others must be below 1.0 (experience a cost advantage)⁴. If factors are limited to 1.0 or above, it means that the State factor cannot be 1.0 and it also means that expenditure needs are not being assessed for LGBs that experience cost advantages.

34. These problems exacerbate the problem of the amount of needs assessed by LGGCs exceeding the amount of assistance available. They mean that the extent of factoring back is greater than it needs to be.

Conclusion

35. The LGGCs, like the CGC, are trying to measure ‘need’ — to identify needier LGBs. The problems identified are in the implementation of this objective.

36. The CGC believes:

- (i) the purpose of an assessment of expenditure need should be to identify the unavoidable differences in costs of service provision; and
- (ii) the approach to assessing expenditure need (including the basis of comparison) should not influence grant outcomes.

KEY DRIVERS OF CURRENT EXPENDITURE ASSESSMENTS

37. The differential costs of service provision can be assessed directly or (through the use of factors) indirectly.

38. An advantage of the direct approach is that the effect of the assessment (the amount it redistributes in dollars) is explicitly shown. If the indirect approach is used, information is not readily available about:

- how much is being moved by a factor; and
- whether the movements are in line with actual costs.

39. How much a factor redistributes depends on:

- its size (larger factors move more per capita than smaller factors);

⁴ The Commission assesses an overall expenditure relativity of less than one for New South Wales, Victoria and Queensland because it believes that they can provide the standard level of service at less than the standard cost but by differing amounts.

- how it is combined with other factors (multiplying factors creates interactions which can magnify the effect of a factor⁵);
- the proportion of the category expenditure it affects; and
- the standard to which they are applied — larger standards move more per capita than smaller standards.

40. The CGC has adopted a practice of calculating the redistribution attributable to each factor (and category). It uses this information as a check on the assessment — does it move grants in the way that is expected?

41. The next two sections set out the amount each category (and factor) redistributes. The amounts shown are the total amount of grant redistribution for the LGBs as a whole. These were calculated by comparing the category (or factor) with an equal per capita distribution. Grant redistributions were calculated for each individual LGB but are not shown. The total redistribution figure in each table is not the sum of the individual category (or factor) results, it is calculated by comparing all assessments (either category or factor) with an equal per capita distribution. For this reason, it is possible for the sum of individual categories (or factors) to exceed the total redistribution.

42. Each of the LGGCs could provide the individual LGB information with their annual report. It would help LGBs to identify the main drivers (movers) of their grant share⁶. This type of analysis could also be useful to the LGGCs themselves. It could provide a check on the assessment.

43. The assessment models and methods of each LGGC vary in terms of complexity and the number of categories and factors they assess. Table 11-3 shows the number of categories and disability factors that each LGGC assesses to determine the grant share of the LGBs.

Table 11-3 NUMBER OF EXPENDITURE CATEGORIES AND DISABILITY FACTORS ASSESSED

	NSW	VIC	QLD	WA	SA	Tas	NT
Categories	21	20	11 ^(a)	8	18	12	6
Disability Factors	45	21	15	20	7	17	6

(a) Queensland LGGC shows 7 expenditure categories, but the services category has 8 sub-components. For this analysis their 5 effort positive (APC) categories have been combined and treated as one category, and the 8 sub-components of the services category have been treated as separate categories.

⁵ Interactions can be positive or negative. They arise whenever elements are multiplied or divided. Interactions make it more difficult to calculate the effect of a factor but in some circumstances they are a better approximation of reality (when influences compound with one another multiplying them gives a more realistic answer than adding them).

⁶ This would enable LGBs to query whether the redistribution (for a particular category or factor) bore any relation to the costs they actually face.

44. The next sections present the key categories and disabilities that move the grant share of LGBs in each State from an equal per capita share.

45. Earlier in this chapter it was pointed out that a number of LGGCs calculated category standards using different bases of comparison. The analysis has followed the suggested approach of assessing standard expenditure as total expenditure divided by total population. It has, therefore, introduced a factor called Units of Measurement to adjust for these different bases of comparison. It must be stressed that this is not a factor that LGGCs have assessed, its introduction enables the calculation of category standards in the CGC way and still produces the standardised expenditures assessed by LGGCs. As concluded earlier, using different bases of comparison is equivalent to introducing a new factor.

46. For those States that use them, the Units of Measurement factor also captures the effect of using regression equations within the assessment process. It measures the difference between the standard calculated using the regression equation and a standard assessed on an equal per capita basis. Again, this is not a factor that LGGCs have assessed. Its introduction enables the category standards to be calculated in the CGC way and still produces the standardised expenditures assessed by LGGCs.

47. The Units of Measurement factor thus captures the effect of:

- (i) Units of Use influences — the use of properties or road length rather than population to calculate expenditure standards; and
- (ii) Flag Fall (Fixed Costs) influences — the constant terms in regression equations.

**KEY DRIVERS OF EXPENDITURE ASSESSMENTS
— BY CATEGORY**

New South Wales.

48. The New South Wales LGGC assesses 21⁷ categories of expenditure. Table 11-4 shows that four categories account for almost three quarters of the total redistribution. The category with the largest redistribution is the Road category with \$185.9 million (27 per cent) of the total redistribution.

Table 11-4 KEY DRIVERS, BY CATEGORY, NEW SOUTH WALES

Category	Amount of	Amount of	Share of Total ^(a)
	Redistribution	Redistribution	
	\$m	\$pc	%
Administration	89.0	14.0	12.7
Aerodromes	7.1	1.1	1.0
Aged Person's Services	2.6	0.4	0.4
Animal Control	1.1	0.2	0.2
Building Control	5.2	0.8	0.7
Cemeteries	1.2	0.2	0.2
Children's Services	3.3	0.5	0.5
Community Services	13.9	2.2	2.0
Cultural Facilities	8.8	1.4	1.3
Fire Control and Emergency Services	32.9	5.2	4.7
Health and Safety	17.0	2.7	2.4
Libraries	22.6	3.6	3.2
Noxious Plants and Pest Control	10.7	1.7	1.5
Planning	29.2	4.6	4.2
Recreation	130.9	20.7	18.7
Street and Gutter Cleaning	15.4	2.4	2.2
Storm Water Drainage and Flood Control	111.7	17.6	15.9
Street Lighting	10.1	1.6	1.4
Roads	185.9	29.3	26.5
Isolation Allowance	15.0	2.4	2.1
All Categories	701.8	110.5	

(a) Percentages do not add to 100.

Source: Information provided by New South Wales LGGC.

⁷ New South Wales has three separate Roads categories. For this analysis, these categories have been combined and treated as one category. Isolation Allowance is an additional allowance calculated for some LGBs, not an expenditure category.

Victoria

49. The Victorian LGGC assesses 20 expenditure categories, including three categories of road maintenance. Table 11-5 shows the key category drivers in the Victorian distribution model. Almost 60 per cent of the total redistribution is accounted for by two categories: Heritage, Culture and Recreation moving \$151.4 million (31 per cent); and Local Sealed Roads moving \$126.8 million (26 per cent).

Table 11-5 KEY DRIVERS, BY CATEGORY, VICTORIA

Category	Amount of redistribution	Amount of redistribution	Share of Total ^(a)
	\$m	\$pc	%
Public Safety, Law and Order	17.8	3.8	3.7
Family Services	33.0	7.1	6.8
Family Services – Fees and Charges	1.6	0.3	0.3
Health and Welfare	25.9	5.6	5.3
Aged Services	55.1	11.8	11.3
Community Services	65.8	14.1	13.5
Heritage, Culture and Recreation	151.4	32.5	31.1
Heritage – Fees and Charges	0.0	0.0	0.0
Local Sealed Roads	126.8	27.2	26.0
Local Formed and Surfaced Roads	54.1	11.6	11.1
Local Natural Roads	1.7	0.4	0.4
Footpaths, Kerbs and Channels	8.3	1.8	1.7
Traffic Management	17.3	3.7	3.5
Traffic Management – Fees and Fines	0.0	0.0	0.0
Street Lighting	27.5	5.9	5.7
Aerodromes	1.7	0.4	0.4
Street Beautification	3.5	0.7	0.7
Sanitation	39.5	8.5	8.1
Street Cleaning	13.3	2.9	2.7
Environment Protection, Drainage	14.1	3.0	2.9
All Categories	487.1	104.5	

(a) Percentages do not add to 100.

Source: Information provided by the Victorian LGGC.

Queensland

50. The Queensland LGGC assesses 11⁸ categories including Roads. As is shown in Table 11-6 below, the Roads category accounts for almost 60 per cent of the total redistribution, it redistributes \$212.1 million (about 57 per cent).

Table 11-6 KEY DRIVERS, BY CATEGORY, QUEENSLAND

Category	Amount of redistribution	Amount of redistribution	Share of Total ^(a)
	\$m	\$pc	%
Education, Health, Welfare, Housing and Public Order	15.7	4.5	4.2
Garbage	49.4	14.3	13.4
Street Lighting	5.8	1.7	1.6
Community Amenities	41.0	11.9	11.1
Libraries	5.9	1.7	1.6
Building Control	14.2	4.1	3.8
Public Infrastructure	28.5	8.3	7.7
General Public Services	42.4	12.3	11.5
Roads	212.1	61.4	57.3
Effort Positive	78.8	22.8	21.3
Other Expenditure (NEC)	24.2	7.0	6.5
All Categories	370.0	107.1	

(a) Percentages do not add to 100.

Source: Information provided by Queensland LGGC.

⁸ Queensland LGGC shows 7 expenditure categories, but the Services category has 8 sub-components. For this analysis their 5 effort positive (APC) categories have been combined and treated as one category, and the 8 sub-components of the Services category have been treated as separate categories.

Western Australia

51. The Western Australian LGGC assesses eight expenditure categories, including Roads. The amount of redistribution is the least of the six States. The majority of the redistribution is accounted for by the Transport (including Roads) category, redistributing \$51.7 million (84 per cent).

Table 11-7 KEY DRIVERS, BY CATEGORY, WESTERN AUSTRALIA

Category	Amount of Redistribution	Amount of Redistribution	Share of Total ^(a)
	\$m	\$pc	%
Community Amenities	8.3	4.4	13.5
Education, Health and Welfare	3.6	2.0	5.9
Law, Order and Public Safety	5.3	2.9	8.7
Recreation and Culture	28.7	15.4	46.9
General Governance (Administration)	11.9	6.4	19.4
Building Control	1.0	0.5	1.6
Capital Works	2.5	1.3	4.0
Transport (Roads)	51.7	27.8	84.3
All Categories	61.3	32.9	

(a) Percentages do not add to 100.

Source: Information provided by the Western Australian LGGC.

South Australia

52. The South Australian LGGC assesses 18 categories, including five for separate road categories. Table 11-8 shows the key drivers of the total redistribution at the category level. Most of the redistribution is accounted for by three road categories, which redistribute \$96.0 million (73 per cent), and the Other Needs category, which moves \$36.9 million (28 per cent).

Table 11-8 KEY DRIVERS, BY CATEGORY, SOUTH AUSTRALIA

Category	Amount of Redistribution	Amount of Redistribution	Share of Total ^(a)
	\$m	\$pc	%
Public Buses	2.4	1.6	1.8
Animal and Plant Control	2.9	2.0	2.2
Garbage	5.5	3.7	4.1
Aged Care	2.8	1.9	2.1
Families and Children	0.5	0.3	0.4
Health Inspection	2.4	1.6	1.8
Libraries	3.9	2.7	3.0
Sport Recreation and Culture	5.7	3.8	4.3
Sealed Roads – Urban	16.6	11.2	12.5
Sealed Roads – Non urban	36.5	24.7	27.5
Unsealed Roads – Urban	1.1	0.7	0.8
Unsealed Roads – Non Urban	42.9	29	32.3
Unformed Roads	0.2	0.1	0.1
Storm Water Construction	4.1	2.8	3.1
Storm Water Maintenance	1.9	1.3	1.4
Emergency Services	2.5	1.7	1.8
Planning and Building Control	3.4	2.3	2.5
Other Needs	36.9	25.0	27.8
All Categories	132.9	89.9	

(a) Percentages do not add to 100.

Source: Information provided by South Australian LGGC.

Tasmania

53. The Tasmanian LGGC assesses 12 expenditure categories including one for roads. Table 11-9 shows that three categories account for more than 60 per cent of the total redistribution. Roads is the main cost driver, redistributing \$24.4 million (26 per cent), followed by General Administration (\$21.9 million, 23 per cent) and Recreation and Culture (\$13.5 million, 14 per cent).

Table 11-9 KEY DRIVERS, BY CATEGORY, TASMANIA

Category	Amount of Redistribution	Amount of Redistribution	Share of Total ^(a)
	\$m	\$pc	%
General Administration	21.9	46.5	23.1
Law, Order and Public Safety	0.2	0.3	0.2
Health, Welfare and Housing	4.5	9.6	4.8
Protection of the Environment	8.3	17.7	8.8
Community and Regional Development	7.1	15.1	7.5
Recreation and Culture	13.5	28.7	14.3
Water	9.3	19.8	9.8
Sewerage	5.3	11.2	5.5
Other	0.2	0.3	0.2
Roads	24.4	51.7	25.7
Allowances – Rural GP	0.1	0.2	0.1
Allowances – Other	0.0	0.1	0.0
All Categories	94.9	201.1	

(a) Percentages do not add to 100.

Source: Information provided by the Tasmania LGGC.

KEY DRIVERS OF EXPENDITURE ASSESSMENTS — BY FACTOR

54. This section shows that there does not appear to be a common definition of need across the LGGCs.

55. In its State inquiries, the CGC assessing factors using one of two approaches:

- (i) a general method; or
- (ii) a category specific method.

56. Common influences (scale, input costs, dispersion) are assessed by general methods. The same method is applied in all categories, only the proportion of category expenditure that is affected by the factor changes. Other influences are assessed by category specific methods. The common influences account for about two thirds of the total expenditure redistribution. The other influences are those which have much smaller impacts across all States or have large effects but for only one or two States or categories.

57. A similar approach (or at least outcome) was expected from the analysis of LGGCs methods. That is, a few major influences would account for the majority of the redistribution and minor influences would account for the balance. From the Commission's consultations, the major influences were expected to be:

- diseconomies of scale;
- the dispersion of the population;
- non-resident use;
- for urban LGBs, maintenance of infrastructure; and
- for rural LGBs, the effect of declining populations and the effect of 'picking up' services that other spheres of government have ceased to provide.

58. These do not appear to figure prominently in any of the LGGC assessments. Aside from the Units of Measurement factor, the largest influence in New South Wales is the Drainage Index disability (11 per cent). Scale and Socio-economic Composition account for around 30 per cent of the redistribution in Victoria. Isolation and Non-resident Use account for 30 per cent of the Queensland redistribution. Location accounts for almost a quarter of the Western Australian redistribution. Most of South Australia's redistribution is within the Other Needs category. Scale is largest for Tasmania (24 per cent) followed by Worker Influx (11 per cent).

59. The tables in this section indicate that LGGCs assess a myriad of small disabilities.

New South Wales.

60. The New South Wales LGGC assesses 45⁹ disability factors. Only three of them move more than \$30 million (4 per cent of the total redistributed). Units of Measurement (which is not explicitly assessed by it, but is due to the way it assesses category standards) accounts for about 15 per cent of the redistribution, followed by the Drainage Index, which redistributes \$77 million (11 per cent).

⁹ New South Wales LGGC does not assess a Units of Measurement factor, a Roads factor or an Isolation Allowance factor. These factors have been introduced for the analysis.

Table 11-10 KEY DRIVERS, BY FACTOR, NEW SOUTH WALES

Factor	Amount of	Amount of	Share of Total ^(a)
	Redistribution	Redistribution	
	\$m	\$pc	%
Aboriginal & Torres Islander	2.4	0.4	0.3
Aged Persons	4.6	0.7	0.7
Age Structure	12.9	2.0	1.8
Beach Lifesaving Activity	12.7	2.0	1.8
Building Activity	1.2	0.2	0.2
Bushfire Expenditure	21.5	3.4	3.1
Climate Measure	11.4	1.8	1.6
Development Activity	5.5	0.9	0.8
Drainage Index	77.4	12.2	11.0
Economies of Scale	26.2	4.1	3.7
Environmental Sensitivity	5.4	0.9	0.8
Flood Boats	0.6	0.1	0.1
Flood Prone Buildings	5.8	0.9	0.8
Food Premises	7.1	1.1	1.0
Duplication of Halls	1.1	0.2	0.2
Heritage	3.6	0.6	0.5
Infestation	1.3	0.2	0.2
Level Measure	0.4	0.1	0.1
Net Expenditure	7.2	1.1	1.0
Non-English Speaking Background	22.1	3.5	3.2
Non-Resident Borrower	8.5	1.3	1.2
Non-Residential Urban Property	5.0	0.8	0.7
Non-Resident Use	19.2	3.0	2.7
Non-Residential Property	0.3	0.1	0.0
Non-Urban Measure	19.8	3.1	2.8
Occupation	0.5	0.1	0.1
One Parent	0.9	0.1	0.1
Other	21.3	3.4	3.0
Pensioner Benefit	5.1	0.8	0.7
Pensioner	0.0	0.003	0.0
Duplication of Playing Fields	6.1	1.0	0.9
Duplication of Pools	5.7	0.9	0.8
Population Distribution	18.1	2.9	2.6
Population Growth	5.7	0.9	0.8
Population Measure	1.0	0.2	0.1
Pre-School Children	1.1	0.2	0.2
Public Toilets	3.8	0.6	0.5
Regional Centre	4.1	0.6	0.6
Sparsity	1.4	0.2	0.2
Student	1.3	0.2	0.2
Terrain	0.2	0.03	0.0
Units of Measurement	107.2	16.9	15.3
Urban Density	23.9	3.8	3.4
Urban Fire	9.3	1.5	1.3
Vandalism	0.2	0.03	0.0
Youth	3.6	0.6	0.5
Roads	185.9	29.3	26.5
Isolation Allowance	15.0	2.4	2.1
All Factors	701.8	110.7	

(a) Percentages do not add to 100.

Source: Information provided by the New South Wales LGGC

Victoria

61. The Victorian LGGC has 21¹⁰ disabilities. Most of the total redistribution is accounted for by seven of them. The key drivers are Units of Measurement, redistributing \$195.3 million (40 per cent), Scale \$104.6 million (22 per cent) and Socio-economic Status \$98.0 million (20 per cent).

Table 11-11 KEY DRIVERS, BY FACTOR, VICTORIA

Factor	Amount of Redistribution	Amount of Redistribution	Share of Total ^(a)
	\$m	\$pc	%
Aboriginality	7.0	1.5	1.4
Aged	12.8	2.7	2.6
Age of Infrastructure	10.0	2.1	2.0
Area of Council	3.6	0.8	0.7
Climate	0.2	0.0	0.0
Drainage	8.8	1.9	1.8
Duplication	11.0	2.4	2.3
Expenditure	28.4	6.1	5.8
Growth	18.0	3.9	3.7
Isolation	31.0	6.7	6.4
Sealed Roads	59.1	12.7	12.1
Formed Roads	8.5	1.8	1.8
Natural Roads	0.1	0.0	0.0
Population Density	2.9	0.6	0.6
Regional Centre	19.7	4.2	4.0
Retail Employment	9.0	1.9	1.8
Scale	104.6	22.4	21.5
Single Parent Families	14.4	3.1	3.0
Socio-economic Status	98.0	21.0	20.1
Traffic Density	36.6	7.9	7.5
Units of Measurement	195.3	41.9	40.1
Urbanisation	7.5	1.6	1.5
All Factors	487.1	104.5	

(a) Percentages do not add to 100.

Source: Information provided by Victorian LGGC.

¹⁰ Victoria LGGC does not assess a Units of Measurement factor. It has been introduced for this analysis.

Queensland

62. The Queensland LGGC assesses 15¹¹ disability factors. Only three move more than \$19 million (5 per cent of the total redistributed) and the three of them account for more than 60 per cent of the total redistribution. Units of Measurement (this captures the influence of the constant term in Queensland's regression approach to assessing category standards) is the biggest cost driver, redistributing \$131.4 million (36 per cent of the total redistributed).

Table 11-12 KEY DRIVERS, BY FACTOR, QUEENSLAND

Factor	Amount of	Amount of	Share of Total ^(a)
	Redistribution	Redistribution	
	\$m	\$pc	%
Climate	2.0	0.6	0.5
Demography	17.7	5.1	4.8
Housing	1.0	0.3	0.3
Isolation	64.0	18.5	17.3
Major Industry	0.6	0.2	0.2
Non-residents	31.0	9.0	8.4
Population Growth	7.1	2.1	1.9
Proximity	2.5	0.7	0.7
Reduced Service Requirement	3.6	1.0	1.0
Regional Role	3.5	1.0	0.9
Units of Measurement	131.4	38.0	35.5
Security	2.3	0.7	0.6
Tip Problems	5.1	1.5	1.4
Urban Scatter	17.3	5.0	4.7
Urban Standards	17.8	5.2	4.8
Road	212.1	61.4	57.3
Effort Positive assessments	78.8	22.8	21.3
Other Expenditure (NEC)	24.2	7.0	6.5
Total Expenditure	370.0	107.11	

(a) Percentages do not add to 100.

Source: Information provided by Queensland LGGC.

¹¹ Queensland LGGC does not assess a Units of Measurement factor, a Roads factor or an Effort Positive factor. These factors have been introduced for the analysis.

Western Australia

63. The Western Australian LGGC assesses 20¹² disabilities. Units of Measurement and Location are the major drivers. Together, they move about \$65 million (108 per cent) of the total redistribution.

Table 11-13 KEY DRIVERS, BY FACTOR, WESTERN AUSTRALIA

Factor	Amount of Redistribution	Amount of Redistribution	Share of Total ^(a)
	\$m	\$pc	%
Units of Measurement (includes Adjusted Population)	41.9	22.5	68.4
Location	24.5	13.1	39.9
Population Dispersion	3.8	2.1	6.2
Tourism	7.6	4.1	12.5
Socio-economic Disadvantage	8.4	4.5	13.7
Health Special	0.2	0.1	0.3
Terrain	0.7	0.4	1.1
Hobby Farms	0.7	0.4	1.1
Cyclone	0.1	0.1	0.2
Aboriginal Environmental Health Allowance	0.5	0.3	0.9
Size/Shape	0.9	0.5	1.4
Climate	4.4	2.4	7.2
Coastal	1.0	0.5	1.6
Development	0.8	0.4	1.3
Drainage	1.0	0.5	1.6
Salinity/Landcare	0.3	0.1	0.4
Population Increase	2.5	1.3	4.0
Environmental Assessments	1.2	0.7	2.0
Heritage	1.2	0.6	2.0
Water Supply	1.6	0.8	2.6
Transport(Roads)	51.7	27.8	84.3
Total Expenditure	61.3	32.9	

(a) Percentages do not add to 100.

Source: Information provided by the Western Australian LGGC.

¹² Western Australian LGGC does not assess a Transport (Roads) factor. It has been introduced for the analysis.

South Australia

64. The South Australian LGGC assesses 7¹³ factors. The key drivers are Units of Measurement (reflecting the different approach to assessing category standards) and Other Needs, which account for 75 per cent and 26 per cent of the total redistribution respectively.

Table 11-14 KEY DRIVERS, BY FACTOR, SOUTH AUSTRALIA

Factor	Amount of Redistribution	Amount of Redistribution	Share of Total ^(a)
	\$m	\$pc	%
Units of Measurement	99.2	67.1	74.6
Cost Relativity Index (CRI)	6.8	4.6	5.1
Duplicated Facilities	1.3	0.9	1.0
Indigenous People	1.0	0.7	0.7
Isolation	3.7	2.5	2.7
Non Resident	2.9	2.0	2.2
Socio Economic	1.0	0.6	0.7
Other	34.7	23.5	26.1
Total Expenditure	132.9	89.9	

(a) Percentages do not add to 100.

Source: Information provided by South Australian LGGC.

¹³ South Australian LGGC does not assess a Units of Measurement factor. It has been introduced for the analysis.

Tasmania

65. The Tasmanian LGGC assesses 17 disability factors. As is shown in Table 11-15 three factors account for about 60 per cent of the total redistribution. The Roads factors account for \$24.4 million (26 per cent of the total redistributed), Scale accounts for \$22.6 million (24 per cent) and Worker Influx \$10.7 (11 per cent).

Table 11-15 KEY DRIVERS, BY FACTOR, TASMANIA

Factor	Amount of Redistribution	Amount of Redistribution	Share of Total ^(a)
	\$m	\$pc	%
Absentee Population	5.7	12.0	6.0
Unemployment	1.1	2.3	1.1
Age profile	0.9	2.0	1.0
Worker Influx	10.7	22.6	11.2
Climate	0.2	0.4	0.2
Day Tripper	3.3	7.1	3.5
Population Dispersion	4.5	9.5	4.7
Isolation	4.1	8.6	4.3
Population Decline	0.1	0.3	0.1
Population Growth	1.5	3.1	1.5
Tourism	6.6	14.0	7.0
Regional Responsibility	5.7	12.0	6.0
Scale	22.6	47.8	23.8
Equivalent Tenements	3.5	7.5	3.7
Roads factors	24.4	51.7	25.7
Allowances Rural GP	0.1	0.2	0.1
Allowances Other	0.0	0.1	0.0
All Factors	94.9	201.1	

(a) Percentages do not add to 100.

Source: Information provided by the Tasmanian LGGC.

Northern Territory

66. There is no analysis for the Northern Territory Local Government Commission (NLGGC), because it did not supply the relevant data.

CHAPTER 12

ASSESSING REVENUE RAISING CAPACITY

1. On several of the Commission's consultation visits during this Inquiry, 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 12-1 shows the different approaches to assessing revenue standards.

Table 12-1 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 12-2 shows the different approaches to assessing revenue disabilities.

Table 12-2 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 6 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 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 Commonwealth Grants Commission's (CGC's) approach to assessing revenue capacity.

THE CGC APPROACH

9. The equalisation principle governing State inquiries requires the CGC 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 CGC would use actual revenue as the measure of revenue capacity. This is referred to as the Actual Per Capita (APC) 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 contamination means that actual revenue can no longer be used as an accurate measure of revenue capacity and the CGC is required to assess capacity another way.

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

- (i) identifies tax policy differences — the CGC has to first determine an average policy before it can identify tax policies that are different to the average;
- (ii) quantifies the impact that any policy differences have on actual revenue; and
- (iii) removes these influences.

13. The CGC's approach to revenue assessments is all about removing policy contamination from actual revenue. 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 CGC's approach requires explicit consideration of State policies and their impacts. The next section considers what it would mean to apply the CGC's approach to the assessment of Municipal Rates capacity. It also considers six assessment options for Municipal Rates and the implications of using them.

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

- which properties are rated? and
- how are they 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 LGB policy;
- identify individual LGB 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, a LGB's revenue capacity is equal to its actual revenue (this approach assumes all differences in revenue collections per capita are caused by non-policy influences). Under the EPC approach, its revenue capacity 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).

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

23. The three effective tax rate approaches assess standardised revenue by applying a rate in the dollar to a 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).

24. Under the CGC 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 12-3 summaries how each method treats various influences. It shows that an influence can be built into a 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).

25. The purpose of Table 12-3 is to show that the choice of assessment method brings with it implications about how various influences are treated. Table 12-3 shows that these treatments can have a material impact on the assessment of revenue capacity. Tables 12-4 to 12-8 summarise the revenue capacities of New South Wales, Victoria, Western 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 12-3 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 12-4 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 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 revenue capacity 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 12-5 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 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 revenue capacity 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 12-6 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 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 revenue capacity to its actual revenue.

Source: Unpublished revenue data from the South Australian LGGC.

Table 12-7 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 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 revenue capacity 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.

26. 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 cent³);
- Victoria \$83 million (9 per cent);
- South Australia \$6 million (2 per cent); and
- Tasmania \$7 million (7 per cent).

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 that are valued

³ 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.

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

The valuation column in Table 12-8 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 12-8 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 revenue capacity to its actual revenue.

(b) Western Australian LGGC assessment of revenue capacity.

Source: Unpublished revenue data from the Western Australian LGGC.

27. 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 region⁴. It suggests that a decision on whether to base revenue capacity on population, actual revenue or valuations is very important.

28. The ETR 1 approach uses a single rate in the dollar for all property types. The ETR 2 approach uses a separate rate in the dollar for each 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 not as important.

⁴ 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.

29. The ETR 3 approach uses a separate rate in the dollar for each property type in each 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 very important. This issue is considered further at the end of this chapter.

30. The choice of method brings with it implications about how certain influences are treated. Table 12-3 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 A LGGC'S CHOICE OF ASSESSMENT METHOD CAUSING ITS
REVENUE ASSESSMENTS TO HAVE A
DISPROPORTIONATE INFLUENCE ON ITS GRANT OUTCOMES?**

Assessment of Rate Revenue

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

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

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

33. 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 assessment 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.

34. Table 12-4 showed that the New South Wales LGGC approach produces a higher assessment of revenue capacity 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 revenue capacities 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).

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

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

37. First it can lead to the same difficulties as the valuation approach — it can lead to influences being treated as non-policy 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.

38. 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.

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

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

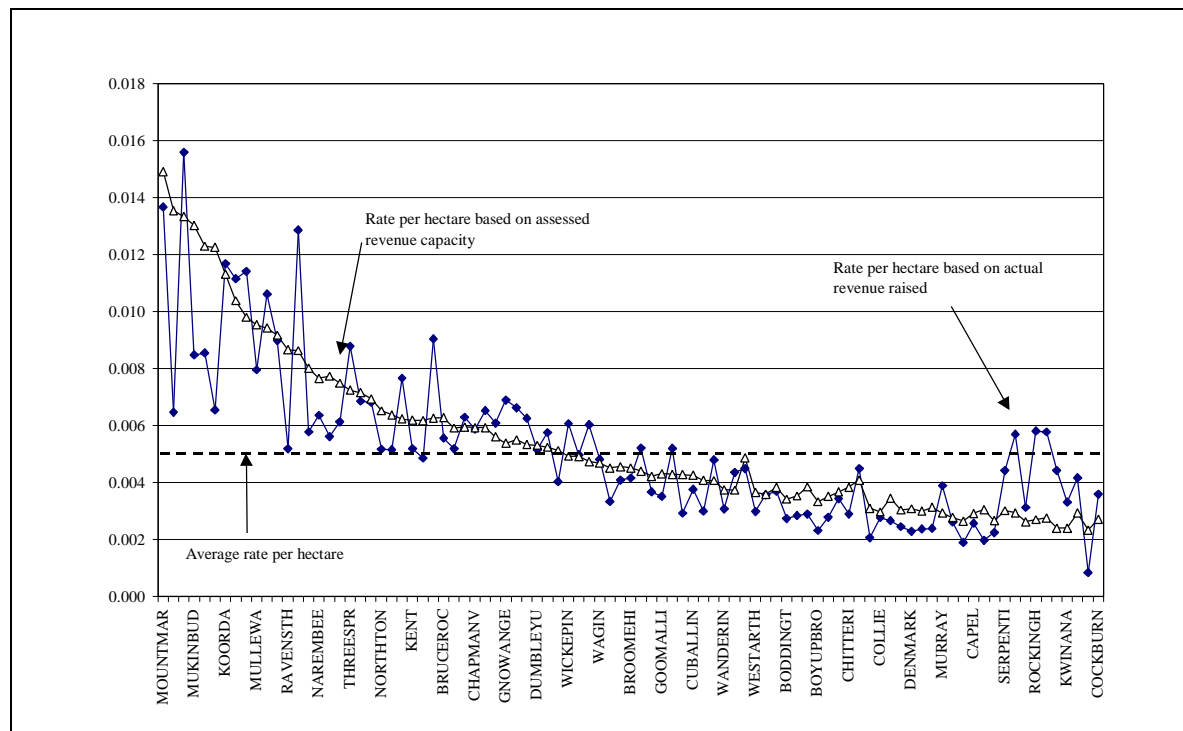
40. Providing it accords with the judgement of the Western Australian LGGC, there is nothing wrong with this assessment⁵. There would be a problem if it were unintended and simply the consequence of using a regression equation which has actual revenue as its dependent variable.

41. 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.

42. 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.

⁵ 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.

Table 12-1 IMPLIED RATES OF TAX PER HECTARE, AGRICULTURAL LAND, WESTERN AUSTRALIA^(a)



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

43. 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 LGAs do. 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 LGAs actually do but on the ability of their ratepayers to pay.

44. 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:

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

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.

45. **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

46. 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.

47. 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.

48. 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.

49. The CGC thinks the full range of non-rate revenue should be equalised, because it is more in keeping with what LGBs do. Also, if two LGBs are identical in all respects except that one has access to significant user charges, then it would be unfair to ignore that revenue source. To do so would place that LGB in a more advantageous position than the other.

Reasons LGGCs do not Assess Non-Rate Revenue Capacity

50. 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.

51. 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 decided that one offsets the other. If this were 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 all expenditures and revenues should be assessed. This 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. Greater transparency would result.

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

52. 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.

53. The CGC does not think that expenditure disabilities are the best measure of user charge revenue capacity. It moved away from that position in the 1993 Review. It implied that, on a per capita basis, the Northern Territory could raise five times the user charges of Victoria.

54. The CGC now thinks that user charges:

- (i) should be separated from their related expenditure; and
- (ii) should be the subject of a separate revenue assessment.

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

55. 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.

56. 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 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. This is an example of different disabilities applying to water and sewerage charges. In this situation, they should probably be separated from general rates and a separate assessment undertaken.

57. If it were not possible to separate them from general rates, the CGC would probably apply the rate assessment as a second best option.

Does the LGB Choice of How to Collect Revenue Matter?

58. 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.

59. In order 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 available⁶.

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

60. 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 a LGB's policy decision to increase or decrease (impose or not impose) parking fees would directly impact on its grant.

61. This would be true if an APC method of assessment were used. The APC method assumes that differences in revenue collections is due to non-policy influences only. In this case, there are policy choices at work so the APC method is not appropriate. 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

62. 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.
- 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.

⁶ 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.

- 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.

SHOULD MUNICIPAL RATE CAPACITY BE ASSESSED ON A REGIONAL BASIS?

63. 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 will depend 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.

64. Table 12-9 shows residential property data, by region, for New South Wales.

Table 12-9 RESIDENTIAL PROPERTY DATA BY REGION, NEW SOUTH WALES

Region	Total Valuation (a)	Number of Properties (b)	Rate revenue collected (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.

65. Table 12-9 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 — there are reasons for this different relationship⁷. The question is whether the different relationship and the different rating practice reflect LGB policy or influences beyond their control?

66. If it is deemed to be LGB policy, then revenue capacity for metropolitan LGBs should be calculated using the average rating practice (0.58 cents in the dollar) rather than their actual rating practice (0.48 cents in the dollar). If it is deemed to be a non-policy

⁷ New South Wales has rate pegging. The very large increase in metropolitan valuations has not led to very large increases in rates. Thus, rate pegging has given rise to a different relationship between rates and valuations in metropolitan areas compared to other areas of the State.

influence, then revenue capacity should be calculated using their actual rating practice (0.48 cents in the dollar). As Table 12-3 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 their actual revenue?

67. These are issues that a LGGC will need to consider when choosing an assessment method.