



Australian Government

Commonwealth Grants Commission

**REVIEW OF THE INTERSTATE DISTRIBUTION OF
LOCAL ROAD GRANTS**

ISSUES PAPER CGC 2005/2

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Introduction

- 1 On 26 October 2005, Dr Sharman Stone, Parliamentary Secretary to the Minister for Finance and Administration, referred Terms of Reference to the Commonwealth Grants Commission (the Commission) for a review of the current interstate distribution of the identified local road component of the financial assistance grants provided to local government. A copy of the Terms of Reference is at Attachment A. The Australian Government had foreshadowed the review in its formal response to recommendation 16 of the Hawker Report¹.
- 2 The Terms of Reference ask the Commission to recommend:
 - the interstate distribution of the local road grants; and
 - how the distribution could be updated in future years.
- 3 The Terms of Reference require the Commission to base its recommendation of the interstate distribution on an assessment of the relative needs of the States and Territories² for expenditure on maintenance and preservation of local roads, and to the extent practicable, bridges. Expenditure on new construction and upgrading is excluded from the review.
- 4 The Commission is to report by 30 June 2006.

Background to local road grants funding

- 5 The Australian Bureau of Statistics estimates that in 2003–04 around a quarter of local government expenditure (or \$4.54 billion) was on Transport and Communications³. At least 80 per cent of this expenditure will have been on local roads.
- 6 In 2004–05, the Australian Government provided local government with \$752 million in local roads funding under:
 - the local road component of the financial assistance grants;
 - supplementary funding to South Australian councils for local roads;
 - the Roads to Recovery programme; and
 - the National Black Spot programme.
- 7 Details of funding by programme and State are in Table 1. This review is considering only the interstate distribution of the local road component of the financial assistance grants.

¹ The Hawker Report is a report of the House of Representatives Standing Committee on Economics, Finance and Public Administration for its inquiry into local government and costs shifting. The report was tabled in Parliament in November 2003 and a copy is at www.aph.gov.au/house/committee/efpa/localgovt/report.htm. The Government's response to the report was tabled in Parliament in June 2005 and a copy is at www.dotars.gov.au/localgovt/publications/hawker_report.

² In the rest of this paper, the term State(s) includes the Australian Capital Territory and the Northern Territory unless the context indicates otherwise.

³ Australian Bureau of Statistics, *Government Finance Statistics, Australia 2003–04*, Cat. No. 5512.0. Note that expenditure by the ACT on local roads is excluded from ABS local government expenditure figures.

Table 1 Australian Government funding to local government for local roads, 2004–05

State	Local road financial assistance grants	Supplementary funding to South Australian councils for local roads	Roads to Recovery programme	National Black Spot programme	Total
	\$m	\$m	\$m	\$m	\$m
New South Wales	138.7		70.9	8.2	217.7
Victoria	98.5		58.5	2.1	159.2
Queensland	89.6		44.9	4.3	138.7
Western Australia	73.1		40.2	3.8	117.1
South Australia	26.3	4.3	19.9	0.8	51.2
Tasmania	25.3		7.4	0.4	33.2
Australian Capital Territory	15.3		1.9	0.0	17.2
Northern Territory	11.2		6.2	0.1	17.5
Total	478.0	4.3	249.9	19.7	751.9

Sources: Department of Transport and Regional Services.
 Australian Government, *Final Budget Outcome 2004–05*.

- 8 In 2004–05, the Australian Government provided \$1.555 billion in local government financial assistance grants under the *Local Government (Financial Assistance) Act 1995* (the Act). Under this Act, only bodies that are local governing bodies⁴ in the States and the Northern Territory, and the Australian Capital Territory government⁵ are entitled to receive these grants.
- 9 Financial assistance grants are in two parts — general purpose grants (paid under section 9 of the Act) and local roads grants (paid under section 12). Local road grants are around 30 per cent of the total grants pool (\$478 million in 2004–05). The national pool for both components is increased annually so that on a per capita basis, the grants are maintained in real terms.
- 10 There is a two step process for allocating the grants:
- Both grants are notionally allocated to States and Territories with the general purpose grants allocated on an equal per capita basis and the local road grants on a fixed shares basis. Table 2 shows the allocations for 2004–05.
 - Within each State and the Northern Territory, the available funding for the two components is allocated to local governing bodies based on recommendations of the relevant local government grants commission. In determining the allocation of grants, local government grants commissions are guided by distribution guidelines called National Principles⁶.

⁴ Local governing bodies include all councils constituted under State and Northern Territory local government Acts as well as other bodies declared by the Federal Minister on the advice of the State Minister to be local governing bodies for the purposes of the Act. Most declared bodies are Indigenous community councils.

⁵ In the Australian Capital Territory, local government is integrated with the Territory government.

⁶ A more detailed explanation of the operation of the *Local Government (Financial Assistance) Act 1995*, including the National Principles, is in the Local Government National Report that is produced annually by the Department of Transport and Regional Services. The National Report is available at: www.dotars.gov.au/localgovt/publications.

Table 2 General purpose and local road grants, by State, 2004–05

State	General purpose grant		Local road grant		Total grant	
	\$m	%	\$m	%	\$m	%
New South Wales	361.5	33.6	138.7	29.0	500.2	32.2
Victoria	266.2	24.7	98.5	20.6	364.7	23.5
Queensland	207.1	19.2	89.6	18.7	296.6	19.1
Western Australia	105.9	9.8	73.1	15.3	179.0	11.5
South Australia	82.4	7.7	26.3	5.5	108.7	7.0
Tasmania	25.9	2.4	25.3	5.3	51.2	3.3
Australian Capital Territory	17.4	1.6	15.3	3.2	32.7	2.1
Northern Territory	10.7	1.0	11.2	2.3	21.9	1.4
Total	1 077.1	100.0	478.0	100.0	1 555.1	100.0

Source: Department of Transport and Regional Services.

- 11 The Australian Government pays the financial assistance grants through the States to local governing bodies. Once in the hands of local governing bodies, the grants are untied which means that the local road grants do not have to be spent on local roads.
- 12 Prior to July 1991, local road grants were paid as a tied grant to local government under the *Australian Land Transport Development Act 1988*. A decision of the 1990 Special Premiers' Conference resulted in the local road grants being paid to local government under an amended *Local Government (Financial Assistance) Act 1986*. Although the grants became untied, the Australian Government agreed to continue to identify them as local road grants⁷. The current interstate distribution of the local road grants is based largely on the allocations under the previous tied arrangements⁸. Table 3 shows the current interstate distribution of the local road grants compared to population and local road length.
- 13 Details of changes since 1991–92 to Australian Government funding for local roads are outlined in Attachment B.

Our Approach to the review

- 14 The Terms of Reference ask the Commission to recommend an interstate distribution of local road grants and to advise on how the interstate distribution might be updated for future years.
- 15 The Commission is required to base its recommended interstate distribution on the relative needs of local government to incur maintenance and preservation expenditure for local roads and, to the extent practicable, bridges. Local roads in unincorporated areas are to be excluded from the assessment.

⁷ As a result, these grants are often referred to as 'identified local road grants'.

⁸ A more detailed explanation of the current interstate distribution is in Appendix D of the Hawker Report.

Table 3 **Distribution of local road grants, population and local road length by State**

State	Local road grants ¹	Population ²	Local road length ³
	%	%	%
New South Wales	29.0	33.4	22.2
Victoria	20.6	24.7	19.9
Queensland	18.7	19.5	22.7
Western Australia	15.3	9.9	19.0
South Australia	5.5	7.6	11.6
Tasmania	5.3	2.4	2.2
Australian Capital Territory	3.2	1.6	0.3
Northern Territory	2.3	1.0	2.2
Total	100.0	100.0	100.0

Sources: 1 Department of Transport and Regional Services.

2 Australian Bureau of Statistics *Australian Demographic Statistics*, Cat. No. 3101.0, March 2005.

3 Department of Transport and Regional Services based on data provided by local government grants commissions and the ACT Department of Urban Services.

- 16 The assessment of relative needs for local road expenditure will be informed by the Commission's assessment of State road expenditure as well as assessments by the local government grants commissions of local road expenditure. Local government grants commissions have provided the Commission with descriptions of the methods they use for assessing local road expenditure.
- 17 The following sections outline some of the issues that will need to be considered during the review. The Commission welcomes views on these issues. Details of when and how submissions should be lodged and of the procedures and timetable for the review are outlined at the end of this paper.

How should we interpret 'relative needs'?

- 18 The Commission's approach to assessing **relative needs** will be based on estimating the expenditure local government in each State would incur in performing maintenance and preservation tasks on local roads to a uniform standard. A State's share of the local roads grants would be what it would need to spend to achieve the uniform standard compared to what the States in total would need to spend.
- 19 The Commission will assess only relative expenditure needs. It will not be examining the relative capacities to raise revenue that might be used to help fund expenditure on roads.
- 20 The approach to assessing relative expenditure needs would seem to raise at least two questions:
- How should the Commission determine the scope of the maintenance and preservation tasks and the uniform standard?
 - How should the Commission deal with differences between the States in the allocation of responsibilities for roads between the State and local governments?
- 21 ***Determining the scope of the maintenance and preservation tasks and the uniform standard.***
The Terms of Reference require the Commission to consider **expenditure on maintenance and**

- preservation** of local roads. It is not asked to consider expenditure on, or the relative needs for, road construction and upgrading. This is consistent with the aim of the local roads grants to fund existing needs, not to facilitate future growth. The comparisons will therefore exclude expenditure on road construction and upgrading, and will relate to the maintenance and preservation of existing local roads.
- 22 There are two approaches that the Commission could use to define and measure the scope of the maintenance and preservation tasks and the uniform standard. The assessment could be based on an average standard approach or an asset preservation approach.
- 23 An average standard approach. Such an approach would be similar to the Commission's assessment of State roads and the assessments made by some local government grants commissions. Under this approach the nature of the tasks performed is implied by an average across all States of what is actually done in a year.
- 24 The first step would be to derive the average expense per capita incurred on maintenance and preservation of local roads — aggregate expenses incurred by all local authorities divided by their total population. This average expenditure implies an average level of maintenance and preservation work is performed in average conditions and at average cost levels for each input.
- 25 The assessments would then proceed on the basis that spending the average amount per capita would deliver the average road maintenance and preservation task in all States, unless there are identifiable reasons why:
- more (or less) road maintenance and preservation work must be done in one State compared with the average; and
 - given tasks cost more (or less) than the average amount.
- 26 An asset preservation or whole of life costing approach. Some State grants commissions, including those in Victoria and Western Australia, follow this approach. The approach involves identifying and costing the various tasks that need to be done over the life of a road to maintain and preserve it to a given standard and converting the costs to equivalent annual expenses. The tasks that need to be performed and the costs of them would be based on engineering criteria that reflect the average practices of all local authorities.
- 27 In deriving the expenses incurred in each State, the assessments would allow for the effects of differences between the States that lead to some tasks being done more (or less) frequently than the standard or which affect the costs of those tasks.
- 28 An asset preservation approach is consistent with considering local road expenditure for maintenance and preservation of local roads. The asset preservation approach reflects a standard life cycle but applying it could be complex and would involve judgments about what are the appropriate life cycles and tasks to be performed, their normal frequency and the benchmark costs. An asset preservation approach appears more appropriate for assessing the expenditure needs of individual local governing bodies than it does for assessing expenditure needs at the State level. Some influences that are important for assessing the relative needs of individual local authorities may offset each other at the State level.

- 29 The average standard approach is relatively simple. Because it reflects an average of the work done by all local authorities, it avoids the need for judgments about the tasks to be performed, their desirable frequency and the standards to which they should be performed. The assessment task largely becomes one of identifying and measuring the influences that affect the level, frequency and unit costs of maintenance and preservation tasks and determining how those influences affect expenses incurred.
- 30 A disadvantage of the average standard approach is that the average standard could be subject to annual fluctuations and it may understate the level of expenditure required to preserve the roads for their full life. This is because road maintenance and preservation work is cyclical and there is some discretion about when some tasks need to be performed.
- 31 Attachment C describes the Commission's assessment of State road expenditure and two different approaches used by local government grants commissions for allocating local road grants including an asset preservation approach.
- 32 A notional service provision approach. A third possible approach for estimating local road funding shares has been developed by the National Institute of Economic and Industry Research (NIEIR) and outlined in a report for the Municipal Association of Victoria⁹. NIEIR says that its approach is objective, effort neutral and uses data that are available or can be estimated with reasonable reliability.
- 33 This model is based on weighting the populations in urban, rural and remote areas of each State by factors that allow for the:
- the level of road services provided (or road density) in each region — measured in terms of a standard number of lane-kilometres per capita in each region. There are more lane-kilometres of road per capita in remote areas than in urban areas. The standard could be derived from data on the length of roads in each region in the States; and
 - the relative costs of road works in each area. Unit costs are generally higher in urban areas than rural and remote areas due to the higher standards of roads.
- 34 NIEIR suggest the model could be further refined to allow for the different levels of road use (measured in terms of tonnes of freight).
- 35 A State's share of the available funds would be proportional to its share of the Australian weighted population.
- 36 This model would be simple. But further work would be required to establish the appropriate relationships between road density, road costs and road use and population in urban, rural and remote areas.
- 37 ***Dealing with differences in responsibilities between States.*** There are differences across States in the allocation of responsibilities between State and local governments for local roads¹⁰. Some of the differences are:

⁹ See Appendix 3 of National Institute of Economics and Industry Research 2001, *Road funding in Australia — there must be a better way*. The report is available from www.mav.asn.au.

¹⁰ Some differences were identified in Bureau of Transport Economics 2001, *Spending on local roads, working paper 44*, BTE, Canberra.

- the New South Wales, South Australian and Northern Territory governments are responsible for local roads in unincorporated areas;
- a substantial amount of bridgework on local roads in Western Australia is carried out by the State, without the funds going through the accounts of local government; and
- arterial roads are generally the responsibility of State governments, but in some States some roads that perform an arterial function (and would be classified as arterial roads in other States) are the responsibility of local government.

38 The question for the Commission is whether its recommendations should be based on the actual allocation of responsibilities in each State (what actually happens in States) or whether it should seek to apply a uniform interpretation of the local roads function across all States. In this context, local government would be considered responsible for the task if it sets the extent and standard of the work and is financially responsible for it. It would not include cases where local government performs the work as an agent for, and is paid by, the State.

39 In its assessment of State road expenditure, which is done as part of the allocation of the GST revenue among the States, the Commission applies a uniform interpretation of the State road maintenance function to all States. Examination of practices prior to the introduction of AusLink indicated that State governments were in general responsible for arterial roads, defined essentially in terms of the NAASRA functional definitions. So, the Commission's analysis covers all arterial roads in all States.

40 Basing the calculations for this review on the actual allocation of responsibilities to local government in each State could mean that some roads are counted twice. For example, arterial roads that are the responsibility of local government in some States would be included once in determining the interstate allocation of the GST revenue and again in determining the allocation of the identified local roads grants. This would appear to be inappropriate. Also, adopting this approach could provide incentives for jurisdictions to change the classifications of roads to maximize their grant outcomes.

41 The Commission thinks it more appropriate that the scope of roads covered by this review be determined on an effort (or policy) neutral basis. That is, on the basis that the same policy on the allocation of responsibility for roads to local government is followed in all States.

42 Effort (or policy) neutrality is one of the fundamental pillars of the relative needs assessment processes adopted by the Commonwealth Grants Commission. It is also one of the national principles that must be followed by all the State grants commissions¹¹. Effort neutrality means that the inter-jurisdictional allocation of funds should not be affected by policy choices made by individual jurisdictions. In this way, the interstate allocation of local roads grants, and the

¹¹ One of the National Principles for the distribution of the general purpose component of the financial assistance grants is called Effort Neutrality. The National Principle defines Effort Neutrality as follows:
An effort or policy neutral approach will be used in assessing the expenditure requirements and revenue raising capacity of each governing body. This means as far as practicable, that policies of individual local governing bodies in terms of expenditure and revenue effort will not affect grant determination.

In its assessment of local roads, the Commission will only be assessing expenditure requirements.

relative needs on which it is based, should reflect only those factors that affect costs and which are beyond the control of States and local governing bodies.

- 43 Effort neutrality requires the Commission to use a consistent definition of ‘local roads’ across all States, with that definition based on the function or purpose performed by local roads. Excluding those roads (primarily arterial roads) that the Commission takes into account in its assessment of State road expenditure would seem desirable.
- 44 The Commission is aware that there is not a consistent definition of ‘local roads’ applied across States and is considering possible definitions. There are existing NAASRA and PSMA road classifications (see Attachment D). The Commission is attracted to the PSMA road classification and would appreciate views on the following definition:
- Local roads are:
- (a) roads whose prime purpose is to provide access to properties; and
 - (b) roads acting to provide for traffic movement (connects roads providing access to properties to higher level roads) or to distribute traffic to local street systems.
- 45 The Commission will use the eligibility conditions under the *Local Government (Financial Assistance) Act 1995* to determine the local governing bodies that have a local roads responsibility.

Should the inventory of local roads be adjusted to reflect effort neutrality considerations?

- 46 Local government seems to base its decisions on the provision of local roads on the needs of the community, engineering criteria and the funding available. While there will be examples where other criteria influence decisions, there is no reason to expect that they would be more or less prevalent in any States and their effect on total road lengths would be minimal. That is, interstate comparisons based on existing roads would not be materially affected.
- 47 On this basis, the inventory of existing roads, and bridges, that satisfy the chosen definition of a local road will be used as the basis of the assessments without adjustments. This is consistent with assessments of road expenditure by the Commission and local government grants commissions.

At what level should the assessment be done?

- 48 Potentially, the Commission’s assessments could derive the funding requirements of local government in each State by:
- building them up as the sum of the needs of each local governing body in the State; or
 - by making broader assessments at the whole of State level.
- 49 Building up from the individual local governing body level would be a large and detailed task. It would require detailed knowledge of issues affecting individual local governing bodies, which is the role of the local government grants commissions.
- 50 A whole of State approach is consistent with the distributional arrangements for the grants — they are first distributed to States and then to local authorities within the States.
- 51 The Commission appears to have little practical alternative but to use a State-level approach.

What factors affect local road expenditure?

- 52 In its assessments, the Commission will need to take into account only those factors that are beyond the control of local governing bodies in a State and which affect local road expenditure through their effects on the type and frequency of work required and the cost of that work. State grants commissions refer to these factors by different names including disabilities, cost drivers, cost adjusters and cost relativity indexes.
- 53 Based on assessments by the Commission for State road expenditure and by local government grants commissions for local road expenditures, factors could include:
- road use (which may be measured using population or traffic volumes);
 - road length;
 - road surface type (sealed, unsealed, formed);
 - road location (urban, rural, remote areas);
 - environmental factors (climate, terrain, soil types, salinity);
 - availability of materials; and
 - bridges (number, type, length, area).
- 54 The Commission seeks advice on what factors have important effects on local road expenditure at the State level and would drive differences between States in those expenditures.
- 55 Submissions should argue the case for including factors that are considered to have a material effect on aggregate expenditure on local roads in a State and should identify available data that could be used to measure the factor and its effects. Submissions must:
- establish the links between the factor and the level of expenditure on local roads — demonstrate how, and to what extent, it affects the amount or type of maintenance and rehabilitation work that must be done or the costs of those tasks; and
 - show that there are differences between States in the prevalence of the factor.
- 56 For example, the availability of road building materials is often seen as an important factor when assessing expenditure needs for individual local governing bodies in a State. But, when analysis is done at the whole of State level, would differences between States in the availability and accessibility of road building materials be an important influence? How might interstate differences in the availability and accessibility of road building materials be measured? Parties that wish to argue that availability of materials is an important influence on local road expenditure would need to ensure that their submissions address those types of issues.
- 57 Advice on sources of available and comparable cost data that could be used to measure the factors across all States would also be welcome.

Local roads in unincorporated areas

- 58 The Terms of Reference require the Commission to exclude local roads in **unincorporated areas**. These local roads are usually the responsibility of State and Territory governments. However, the Commission is inclined to include in its assessment any access roads and other internal community roads maintained by Indigenous communities within unincorporated areas

that are treated as local governing bodies for the purposes of the *Local Government (Financial Assistance) Act 1995*. This appears to be consistent with the existing scope of the grants and the approach of local government grants commissions. The Commission is seeking clarification of this aspect of the Terms of Reference from the Department of Transport and Regional Services.

What data are available on local roads?

- 59 The availability of reliable and comparable data across States will be critical to the Commission's assessments. In fact, the availability of data is likely to be a major determinant of its approach to the assessment of relative needs.
- 60 The Commission is aware that local government grants commissions have the most comprehensive databases on local roads. It has already asked them for data, including:
- data on road length and traffic levels by local governing body and type of road;
 - data on bridges and culverts on local roads;
 - data on expenditure by each local governing body on local roads; and
 - other data that could be important for assessing needs for local road funding.
- 61 Data have been received from all States on road length by type of road and expenditure on local roads. However, data on traffic levels and bridges and culverts are not available for all States.
- 62 We are also aware of the National Local Roads Data Project being coordinated by the Australian Local Government Association as a potential national data source on local roads. This project aims to aggregate existing sources of local road information to provide a consolidated national local roads database. Data for the database would come from local government grants commissions and State transport authorities. Data are expected to be available in the first half of 2006.
- 63 Other potential sources of data on the length of local roads are Austroads and the Public Sector Mapping Agencies Pty Ltd. Potential sources of other data include ABS, BTRE, Department of Transport and Regional Services and the ARRB Transport Research.
- 64 One of the major issues for data will be ensuring that it is comparable across States. For example, the Commission has received data from some local government grants commissions on the average costs of work on roads with different levels of traffic and other features, but it is not clear how compatible the data are across States. This is illustrated by the following data on local road costs provided by the Victoria Grants Commission (Table 4) and the Queensland Local Government Grants Commission (Table 5).

How could the interstate distribution be updated in future years?

- 65 The Terms of Reference ask the Commission to recommend how the interstate distribution of the local road grants could be updated in future years.
- 66 Such updating is generally done to ensure that the interstate allocation of the grants reflects the most recent conditions in the States — that is it reflects the effects on the relative needs of the States of differences in the growth of demand for and supply of local roads. In this case,

updating may also be desirable if improvements in the coverage and comparability of data would allow improved assessments to be made.

Table 4 Asset preservation costs used by the Victoria Grants Commission

Local roads type	Daily traffic volume	Standard annual asset preservation cost
		\$/km
Kerbed	< 500	2 700
	500 – 1000	4 000
	1000 – 5000	5 500
	> 5000	9 000
Unkerbed	Natural Surface	300
	< 100	2 000
	100 – 500	4 000
	500 – 1000	4 900
	> 1000	5 400

Table 5 Annual maintenance allowances used by the Queensland Local Government Grants Commission

Local road type	Weighted traffic volume ^(a)	Base cost
	Vehicles per day	\$/km
Urban	< 500	5 040
	500 – 1000	9 360
	1000 – 5000	16 800
	5000 – 10 000	27 600
	> 10 000	43 200
Rural	Unformed	250
	< 40	500
	40 – 150	2 300
	150 – 250	3 000
	250 – 1000	4 000
	1000 – 3000	6 350
	> 3000	8 400

Note: (a) Traffic volumes are weighted to account for increased costs incurred to maintain roads carrying heavy vehicles. For instance, light to medium trucks with two axles are counted as one vehicle while road trains are counted as 5 vehicles.

Summary of the issues raised

67 The Commission would welcome comments on the issues raised in this paper. The main issues raised are how we might:

- interpret ‘relative needs’;
- determine the scope of the maintenance and preservation task;

- choose the most appropriate approach to measuring the relative needs — use an asset preservation model approach, an average standard approach or a different approach;
- deal with differences between States in the allocation of responsibility for local roads;
- define ‘local roads’;
- determine at what level the assessment is done — State or local governing bodies;
- decide which factors affect differences between States in the need to incur local road expenditure;
- obtain local roads data that are reliable and comparable across States; and
- update the interstate distribution of local road grants in future years.

Review processes

68 The proposed timetable for the review is:

Release of issues paper	mid-November 2005
Submissions received	15 January 2006
Draft report issued	mid-April 2006
Conference to discuss draft report	18 May 2006
Final report	June 2006

Submissions

69 The Commission would welcome submissions by 15 January 2006. The submissions should address the issues outlined in this paper as well as any other issues pertinent to the review.

70 Consistent with the Commission’s aim to ensure the review is as open and transparent as possible, all submissions will be posted on its web site, unless the provider explicitly requests otherwise.

71 Wherever possible, submissions should be provided in electronic format. The email address for submissions is:

Secretary@cgc.gov.au

72 Submissions can be sent to:

The Secretary
Commonwealth Grants Commission
5 Torrens Street
CANBERRA ACT 2612

Commission contacts

73 Please direct any questions on the review to Malcolm Nicholas (telephone (02) 6229 8812, email malcolm.nicholas@cgc.gov.au) or to Geof Watts (telephone (02) 6229 8866, email geof.watts@cgc.gov.au).

Terms of Reference for the Review of the Interstate Distribution of the Local Road Grants



The Hon Dr Sharman Stone MP
Federal Member for Murray
Parliamentary Secretary to the Minister for Finance and Administration

Mr Alan Morris
Chairman
Commonwealth Grants Commission
Cypress Court
5 Torrens Street
BRADDON ACT 2612

26 OCT 2005

Dear Mr Morris

I am writing to convey to you the attached Terms of Reference for the Commission's review of the interstate distribution of the local road grants paid as local government financial assistance grants (FAGs). The Terms of Reference provide guidance to the Commission to recommend a new methodology for the distribution of identified local roads grants to local government. The methodology should ensure that the distribution of this funding is based on the relative needs of local government in States and Territories for local roads rather than the current historical share.

The Terms of Reference require the Commission to report to Ministers by 30 June 2006 on possible changes to the interstate distribution.

Yours sincerely

Dr Sharman Stone

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Terms of Reference for the Review of the Interstate Distribution of the Local Road Grants paid as Local Government Financial Assistance Grants

COMMONWEALTH GRANTS COMMISSION ACT 1973

1. I, Sharman Stone, Parliamentary Secretary to the Minister for Finance and Administration, pursuant to section 17 of the *Commonwealth Grants Commission Act 1973*, refer to the Commission for review and report upon, by 30 June 2006, the interstate distribution of the local road grants paid under section 12 of the *Local Government (Financial Assistance) Act 1995*.

2. For the review, the Commonwealth Grants Commission should recommend a distribution between the States and Territories of the section 12 grants. The allocation method used in deriving the recommendation should:

- (a) assess the relative needs of local government in the States and the Northern Territory, and the ACT Government for expenditure on maintenance and preservation of local roads and, to the extent practicable, bridges on local roads; and
- (b) not take account of local roads in unincorporated areas of the States and Territories.

3. The Commission should also recommend how the interstate distribution of the section 12 grants could be updated in future years.

4. The review will not address the quantum of funds available for section 12 grants.

5. The Commission should use the latest available data for the review.

The Australian Government's Department of Transport and Regional Services has undertaken to provide information in its possession required for the review in a timely manner.

Main changes in arrangements for local road grants since 1991–92

- 1 The main changes since 1991–92 in Australian Government arrangements for local roads funding are as follows:
- 2 Following their inclusion in the financial assistance grants programme, there was an intention that the local road grants would be combined with the general purpose grant from 1995–96. However, the Australian Government accepted a recommendation of the 1994 review of the local government financial assistance grants arrangements for the local road grants to be retained as a separate component of the financial assistance grants. These arrangements were incorporated in the *Local Government (Financial Assistance) Act 1995*.
- 3 Under the 1995 Act, National Principles were introduced to guide local government grants commissions in the allocation of grants to local governing bodies. The National Principle for the local road grants is:

The grants should be allocated to local governing bodies as far as practicable on the basis of the relative needs of each local governing bodies for roads expenditure and to preserve its road assets. In assessing road needs, relevant considerations include length, type and usage of roads in each local governing area.
- 4 In November 2000, the Australian Government committed \$1.2 billion in funding to local government for local roads under the Roads to Recovery programme. This was to run from 1 January 2001 to 30 June 2005. Funding was provided as tied grants paid directly to local government but the Government used an interstate distribution different from that for the local road grants. The interstate distribution was based on historical precedents, length of local roads and population. However, allocations between local governing bodies used the recommendations of local government grants commissions for 2000–01. Additional Roads to Recovery funding was subsequently provided for local roads in unincorporated areas maintained by New South Wales, Victoria, South Australia and the Northern Territory.
- 5 In 2000–01, the Commonwealth Grants Commission reviewed arrangements for the payment of local government financial assistance grants. The Terms of Reference for the review did not allow the Commission to examine the interstate distribution of the general purpose and local road grants or the quantum of funds available under the Act. In its report, the Commission did not recommend any substantial changes to the arrangements for the distribution of the local road grants¹².
- 6 The inquiry by the House of Representatives Standing Committee on Economics, Finance and Public Administration was asked to consider the Commission's recommendations. In its final report, the Committee recommended that a new methodology for the distribution of the financial assistance grants to local government be adopted that would have seen the local road and the general purpose grants combined as one pool. Grants would have been allocated to local governing bodies on the basis of needs using a national distribution model.

¹² The Commission's final report is available from www.cgc.gov.au.

- 7 In March 2004, the Australian Government announced that it would provide \$26.25 million over 3 years starting in 2004–05 as supplementary funding to South Australia for local roads. The Government stated that this was an interim response to the Hawker Report to address an apparent disadvantage to South Australian councils because of the State’s low share of local roads component of financial assistance grants. The Government announced that its formal response to the Hawker Report would provide a longer-term solution to the South Australian local road-funding situation.
- 8 The Australian Government extended the Roads to Recovery programme for a further four years from 2005–06 under AusLink¹³. A further \$1.2 billion is to be paid directly to local governing bodies under arrangements largely similar to the initial programme as well as \$30 million for unincorporated areas and \$120 million under the AusLink Strategic Regional Programme.
- 9 The Australian Government’s formal response to the Hawker Report was tabled in June 2005. The Government did not support the changes to existing arrangements for the financial assistance grants recommended by the Committee. The Government announced its intention to ask the Commonwealth Grants Commission to review the interstate distribution of the local road grants and stated that it would provide a longer term solution to South Australia’s apparent disadvantage after the Commission reports.
- 10 The Australian Government announced in November 2005 that it would provide an additional \$100 million for the AusLink Strategic Regional Programme bringing total funding to \$250 million over the four years from 2005–06.

¹³ Details of the AusLink Roads to Recovery programme are at www.auslink.gov.au/policy/programmes/r2r/roads_to_recovery.aspx

Examples of assessment models of road expenditure

- 1 This attachment provides an explanation of three of the existing approaches to assessing road expenditure needs:
 - the Commission’s assessment of State road expenditure;
 - the Western Australian Local Government Grants Commission’s asset preservation model; and
 - the Queensland Grants Commission’s model for allocating local road grants.
- 2 These models were chosen because they provide a range of approaches.

The Commission’s assessment of State road expenditure

- 3 In the Commission’s expenditure assessments, a comparison is made of, among other things, State needs for services that they are responsible for providing. The comparison is made on a State-by-State basis relative to the Australian average level of service. Expenditures vary between individual States because of policies specific to the individual States and disabilities of the States (influences beyond a State’s control that cause it to spend more or less than the average to provide a similar standard service). Only the effects of disabilities are reflected in the assessments of relative need.
- 4 One of the services we compare is roads.
- 5 The Roads assessment covers, among other things, expenses associated with the maintenance and rehabilitation of roads (mainly arterial roads) and bridges that were the responsibility of the States.
- 6 Expenses on local roads that were the responsibility of local authorities were not included. There is, however, an allowance for local roads in unincorporated areas that each State is considered to be responsible for maintaining.

Arterial roads

- 7 The Commission considers that the roads function of States relates predominantly to arterial roads. To ensure the comparisons were not affected by differences between States in the allocation of responsibility for roads between the State and local government, they covered all arterial roads, even though some local government authorities (such as the Brisbane City Council) fund and control some arterial roads.
- 8 The Commission considered that the key drivers of differences between States in the per capita expenses for the maintenance and renovation of arterial roads were differences in the per capita length of the roads and the use of the roads. It considered that 60 per cent of maintenance expenses were attributable to road length and 40 per cent were attributable to road use.
- 9 Six disabilities were considered to be important to determining the relative expenditure needs of States for maintenance of arterial roads.

- 10 **Road length (rl).** Expenditure per capita on arterial roads was heavily influenced by the per capita length (measured in lane kilometres) of a State’s arterial road network. States with more lane kilometres per capita were considered to have higher assessed expenses (and vice versa).
- 11 **Physical Environment (pe).** Certain aspects of the physical environment (such as rainfall, temperature, soil type and relief) affect the frequency and cost of road maintenance tasks. Allowances for the effects of differences between States in environmental circumstances were made by applying cost weights to the proportion of each State’s arterial road network located in various environmental regions. The cost weights reflected the average effect of each environmental feature on maintenance costs. States with a greater proportion of their road network in the relatively more expensive areas were considered to have higher assessed expenses (and vice versa).
- 12 **Road use (ru).** The frequency and extent of road maintenance is affected by road use and heavy vehicles have a greater effect than light ones. Consequently, allowances were made for differences in the quantity and severity of road use (measured in terms of Average Vehicle Kilometres Travelled (AVKT)). In making those allowances, the AVKT for various classes of vehicles (light trucks, rigid trucks, articulated trucks and road trains) were weighted according to the relative damage they cause. States with higher weighted road use were considered to have higher assessed expenses (and vice versa)
- 13 **Urban influences (ui).** The urban influences factor captures the effect of urban influences (other than the volume of traffic and environment) on maintenance costs. The factor was intended to recognise costs not fully captured by the road use factor. For example, in large cities, maintenance work was often done at night to avoid traffic disruption, and road repair materials were more expensive.
- 14 The factor is based on differences in average State expenditure per lane kilometre on roads in rural areas, urban areas and heavily trafficked urban areas. States with a higher proportion of their road network in urban areas and heavily trafficked urban areas were considered to have higher assessed expenses (and vice versa).
- 15 **Dispersion (d).** Captures the effects of the geographic dispersion of the population on road maintenance costs. More specifically it allows for the generally higher telecommunication, freight, travel and other costs incurred in providing services in dispersed localities — States with relatively larger proportions of their population in dispersed areas were considered to have higher assessed expenses (and vice versa) .
- 16 **Input costs (ic).** Recognises differences between States in the costs of labour, office accommodation and electricity.
- 17 The overall level of expenditure a State was estimated to require to provide the average maintenance service in its circumstances was derived by applying all its disability factors to the average per capita expenditure on maintenance in the following way:

Overall assessed arterial roads maintenance expense for State i =

$$\text{Average cost per capita} * [(0.4 * ru) + (0.6 * pe * rl)] * ui * (d + ic - 1)$$

Bridges

- 18 States have responsibility for funding bridges and tunnels along their arterial road networks. The bridges component contains estimated expenses incurred in the maintenance and renovation of bridges and tunnels. The Commission considered that there were four factors relevant to the bridges component.
- 19 **Bridge maintenance.** This factor recognised differences in the unit costs of maintaining different types of bridges and tunnels. The factor was calculated by applying average cost weights derived from State data which reflected the cost per metre of work on concrete bridges, steel bridges, other bridges, ferries, culverts and tunnels to the length of each of these structures in each State. The weighted lengths were then converted to a per capita basis.
- 20 **Physical Environment.** Differences between the States in terms of rainfall, temperature, soil type and relief also affect the costs of maintaining bridges. The State's average physical environment was applied to its cost weighted length of bridges and tunnels.
- 21 **Dispersion.** The same as for arterial roads.
- 22 **Input costs.** The same as for arterial roads.
- 23 The overall level of expenditure a State was estimated to require to provide the average bridges maintenance service in its circumstances was derived by applying all its disability factors to the average per capita expenditure on bridges maintenance in the following way:

$$\text{Overall assessed bridge maintenance expense for State } i = \\ \text{Average cost per capita} * pe * rl * (d + ic - 1)$$

Local roads

- 24 Most States met the maintenance costs of some local roads. These were mostly in areas with very low population density and where local councils could not raise sufficient revenue for their upkeep. This factor recognised the effects on road maintenance expenses of differences between States in the length of roads in sparsely settled areas — the greater the length of roads in sparsely settled areas, the greater the disability.
- 25 The factor relied on State road lengths of local roads in areas with a population of less than 10 persons per 1000 square kilometres.

The Western Australian Local Government Grants Commission's asset preservation model

- 26 The Asset Preservation Model assesses the average annual cost of maintaining each council's road network. It takes into account:
- annual and recurrent maintenance costs; and
 - reconstruction at the end of a road's useful life.

- 27 For each road type (see Table C-1) and work type category of reconstruction/maintenance (see Table C-2), the model calculates the expected annual expenditure needs, for each council, in the general form:

unit cost per kilometre (+ traffic allowance) * disability factor * frequency factor * length

Table C-1 Road type categories used in asset preservation model

Roads in Built-up Areas		Roads Outside Built-up Areas
Residential streets	Local industrial and distributor roads	Local Roads
Aggregate seal	Aggregate seal	Aggregate seal
Asphalt seal	Asphalt seal	Gravel
Gravel	Gravel	Formed
Kerbing	Kerbing	Unformed
Longitudinal piped drainage	Longitudinal piped drainage	
Bridges	Bridges	Bridges
		River crossings

Note: Sealed road lengths are converted to lane kilometres with a standard width of 3.5 metres.

Table C-2 General work standards used in asset preservations model

Work Type	Road type	Pavement Thickness	Frequency
Resealing	Aggregate seals		15 years
Resealing	Asphalt Seals (Residential)	25 mm	25 years
Resealing	Asphalt Seals (Local)	30 mm	20 years
Regravelling	Gravel Roads	100 mm	25 years
Reformation	Formed Roads		5 years
Reconstruction	Sealed Roads (Residential Metropolitan)		55 years
Reconstruction	Sealed Roads (Other)		45 years

- 28 The *frequency factor* converts costs to an annual equivalent for a given work type. For example, if resealing only occurs every fifteen years, a frequency factor of 1/15 is applied to give an annual cost.
- 29 *Disability factors* are applied to the unit cost for gravel and sealed roads, to take into account the effect of:
- purchase and transport costs of pavement materials;
 - soil conditions — which affect the required thickness of sealed pavements;
 - terrain (flat, undulating, rolling or hilly) — which affects reconstruction costs; and
 - salt — which affects road life.

- 30 The State is broken up into 21 regions and the disability factors are applied at the regional level. Adjustments to *unit costs* are also made for the six councils that include major towns.
- 31 Unit costs and other statistics are derived for each of:
- 15 road types;
 - longitudinal drainage; and
 - bridges and river crossings.
- 32 Unit costs are also increased according to Equivalent Annual Average Annual Traffic (EQ AADT) that takes into account the impact of different vehicle types on local roads. Where EQ AADT exceeds 75, there are 5 levels of *traffic allowances* that can be added to annual cost for maintenance and re-sheeting.
- 33 Other factors are included in the model to adjust for the cost of:
- rural traffic safety;
 - traffic control devices;
 - widening of main road in country towns; and
 - dual use paths.
- 34 For each council, a minimum needs standard is also calculated. These standards help councils that have not been able to develop their road systems to the same degree as more affluent councils. Minimum needs standards are assigned to each road type. If the council's calculated needs are less than the minimum needs standard, then council's needs are set to the minimum needs standard.
- 35 The local road grant is distributed to each council in proportion to its share of the State's calculated asset preservation needs.

The Queensland Local Government Grants Commission's allocation model for local road grants

- 36 The Queensland Local Government Grants Commission uses a very simple model to allocate the local road grants. It allocates 62.85 per cent of the local road grants between local governing bodies according to local road length and 37.15 per cent according to population. In 2004–05, this meant that local governing bodies in Queensland received a local road grant based on \$372.51 per kilometre of road and \$8.64 per capita.
- 37 Queensland has a different model to assess transport expenditure as part of the assessment model for general purpose grants.

Existing road classifications

1 Two existing road classifications are provided in Table D-1 and D-2.

Table D-1 The NAASRA and ‘Commonwealth’ road classifications

Functional class	Definition	Commonwealth classification
Rural areas		
Class 1	Those roads that form the principal avenue for communications between major regions of Australia including direct connections between Australian capital cities.	
Class 2	Those roads, not being Class 1, whose main function is to form the principal avenue of communications for movements: (i) between a capital city and adjoining States and their capital cities; (ii) between a capital city and key towns; and (iii) between key towns.	Rural arterial ^a
Class 3	Those roads, not being Class 1 or 2, whose main function is to form an avenue of communication for movements: (i) between important centres and the Class 1 and Class 2 roads or key towns; (ii) between important centres; and (iii) of an arterial nature within a town in a rural area.	Rural arterial ^a
Class 4	Those roads, not being Class 1, 2 or 3, whose main function is to provide access to abutting property (including property within a town in a rural area).	Rural local ^b
Class 5	Those roads which provide almost exclusively for one activity or function and which cannot be assigned to Classes 1, 2, 3 or 4.	Rural local ^b
Urban Areas		
Class 6	Those roads whose main function is to perform the principal avenue of communications for massive traffic movements. (Arterial roads)	Urban arterial ^c
Class 7	Those roads, not being Class 6, whose main function is to supplement the Class 6 roads in providing for traffic movements or which distribute traffic to local street systems. (Sub-arterial roads)	Urban arterial
Class 8	Those roads not being class 6 or 7, whose main function is to provide access to abutting properties.	Urban local
Class 9	Those roads which provide almost exclusively for one activity or function and which cannot be assigned to Classes 1, 2, 3 or 4.	Urban local

(a) Except those declared as National Roads or, in Queensland, Beef Roads.

(b) Except those Queensland roads declared as Beef Roads.

(c) Except those declared as National Roads.

Source: BTRE Working Paper 56, p.105

Table D-2 PSMA classification of road by type

Feature Code	Classification	Description of Classification
301	National or State Highway	Roads which are of importance in a national sense, and/or are a major intrastate through route, and/or are principal connector roads between Capitals and/or major regions and/or key towns
302	Arterial Road	Well maintained and widely used roads which are major connectors National Highways and/or State Highways, and/or major centres, and/or key towns, or have major tourist importance or which main function is to form the principle avenue of communication for metropolitan traffic
303	Sub-Arterial Road	Road, which acts as a connector between highways and/or arterial roads, or an alternate route for class 2 roads, or a principal avenue for massive traffic movements
304	Collector Road	Road acting to provide for traffic movement (connects class 3 to class 5) or to distribute traffic to local street systems
305	Local Road	Road providing property access
306	Track – 2 Wheel drive	Unimproved roads which are generally only passable in two wheel drive vehicles during fair weather and are used predominantly by local traffic
307	Track – 4 Wheel drive	Unimproved roads which are generally only passable with four wheel drive vehicles
308	Undetermined	Road type unknown or undetermined, may also include emergency vehicle access
400	Footpath	Bicycle tracks, Pedestrian walkways, walking tracks

Source: PSMA Australia Limited, *Transport Theme Specification*, Version 3.0, August 2005, Table 2.1