

ESC RESPONSE TO THE RECOMMENDATIONS OF THE INDEPENDENT REVIEW OF THE 2016-17 HIGHER CAP APPLICATION PROCESS

1.1 BACKGROUND

1.1.1 THE FAIR GO RATES SYSTEM

The Victorian Government's Fair Go Rates System (FGRS) was introduced in December 2015. It limits the maximum amount councils can increase average rates in a year, without seeking additional approvals. Each year the Minister for Local Government (the Minister) sets the average rate cap, that is, the maximum increase in councils' average rates and charges for the forthcoming financial year. The Minister has the capacity to set a cap that applies to all councils, a group of councils or a single council.

To provide for situations where the average rate cap is insufficient to meet a council's specific needs, councils can apply to the Essential Services Commission (the Commission) for a higher cap.

In seeking a higher cap, councils are required by legislation¹ to specify the following legislative matters in their applications:

- a proposed higher cap for each specified financial year
- the reasons for which the Council seeks the higher cap
- how the views of ratepayers and the community have been taken into account in proposing the higher cap
- how the higher cap is an efficient use of Council resources and represents value for money
- whether consideration has been given to reprioritising proposed expenditures and alternative funding options and why those options are not adequate, and
- that the assumptions and proposals in the application are consistent with the Council's long term strategy and financial management policies set out in the Council's planning documents and annual budget.

In considering an application, we are required to have regard to the above legislative matters and the objectives of the FGRS, which are:

- to promote the long-term interests of ratepayers and the community in relation to sustainable outcomes in the delivery of services and critical infrastructure, and
- to ensure that a council has the financial capacity to perform its duties and functions and exercise its powers.

The 2016-17 rating year is the first year of the FGRS' implementation — that is, the first financial year to which a cap has applied and for which councils could apply to the Commission for a higher cap. We received 10 higher cap applications from councils for 2016-17 although one council subsequently withdrew its application. We released our nine decisions and an overview paper on 31 May 2016.

¹ Section 185E(3), *Local Government Act 1989*.

1.1.2 BACKGROUND TO THE INDEPENDENT REVIEW

Given that the FGRS is new to both councils and the Commission, we decided to engage an independent reviewer to:

- review the process and approach we used to assess higher cap applications in 2016-17
- assess whether we have fulfilled our obligations as effectively as possible, and
- identify possible improvements.

Mr Peter Brown (former CEO of Moreland City Council) undertook this independent review, consulting widely with councils, peak bodies and other interested stakeholders. Mr Brown provided his report to the Commission on 28 September 2016, which the Commission released on 5 October 2016. A copy of this report is available on the Commission's website (<http://www.esc.vic.gov.au/wp-content/uploads/2016/10/Fair-go-rate-system-independent-external-review-20160927.pdf>).

In undertaking the review, Mr Brown was asked to consider the:

- usefulness and usability of the Commission's Guidance material (including baseline templates) provided to councils to assist in the preparation of their applications
- interactions between the Commission and councils before and during the application process (including the Commission's request for information)
- workability of the timelines in the application process
- burden (cost and time) placed on councils seeking a higher cap including the drivers of those costs
- approach taken by councils in preparing their applications and responding to the Commission's information requests, including any best practice that could be shared with sector
- relevance of the information sought by the Commission in making its decisions
- approach adopted by the Commission in assessing whether a higher cap was appropriate
- clarity of the Commission's final decisions.

Importantly, the terms of reference specified that the views expressed by Mr Brown in his report were to be independent of the Commission. Mr Brown made a number of recommendations in each of the above areas.

1.2 ESC RESPONSE

Table 1 lists the recommendations made by Mr Brown for consideration by the Commission, together with our response. Additional recommendations for consideration by the local government sector, or collective consideration by Local Government Victoria (LGV), Essential Services Commission (ESC), Victorian Auditor General (VAGO), Victorian Grants Commission (VGC), and the local government sector are included in Attachment 1 for information.

TABLE 1 ESC RESPONSE TO PETER BROWN'S RECOMMENDATIONS

Recommendation	ESC Response
Section 5.1 — The usefulness and usability of the Commission’s guidance material (including baseline templates) provided to Councils to assist in the preparations of their applications	
<p>i. The FGRS guidelines to provide advice on the financial ratios that Councils should use to assist the ESC assessment</p>	<p>Accept in part. We have included more detail in our guidance material on our expectations of councils in relation to addressing the legislative matters.</p> <p>Our guidance now makes it clear that we will examine Councils’ LGPRF forecast indicators as part of our assessment process. We have also indicated which of the LGPRF financial indicators we will be using. We will work with LGV and VAGO to ensure that the financial indicators used by us in our assessments are the best available indicators of a council’s financial position.</p>
<p>ii. A worked example of a higher cap application be available and that it be annotated to indicate how the ESC uses the information for its assessment purposes</p>	<p>Accept in part. We have included more detail in our guidance about what information and supporting documents councils should provide to address each of the legislative matters and how this information will be used by us in the assessment of council applications.</p> <p>We will ensure that our decision making remains consistent and transparent by continuing to publish separate decision reports for each application received, which summarise our analysis and decision.</p> <p>Due to the complexity of issues and the unique circumstances relevant to each application, it would be impractical and unhelpful to construct a worked example. However, we consider that over time, the accumulation of past applications and decision reports will form a useful resource for councils preparing their applications. All our decision reports are available on our website.</p> <p>We will also conduct workshops in November and December to assist councils understand our assessment process in order for them to draft their applications. Further, all councils who notify us of their intention to apply for a higher cap will be offered an opportunity to discuss their unique circumstances with us as part of the pre-application process.</p>
<p>iii. Clear guidance that the ESC will use the LGPRF information for assessment purposes</p>	<p>Accept. Our guidance now makes clear that we will seek LGPRF forecast information as part of our assessment process (see response to 5.1(i)).</p>

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TABLE 1 (CONTINUED)

Recommendation	ESC Response
Section 5.1 (continued)	
iv. A review is undertaken into any special financial issues associated with growth area councils	<p>Accept. We are commencing a study of the issues faced by growth area councils. This study will involve consultation with the sector and will be completed in 2017. More information will be made available via our website and regular newsletters.</p>
Section 5.2 — The interactions between the Commission and Councils before, during and after the application process (including request for information)	
i. Consideration is given by the ESC to allow staff exchanges with councils to assist with the understanding of ESC and Council staff of their respective roles and challenges	<p>Accept. We welcome and are keen to explore any opportunities to work with the sector to build mutual understanding and develop the skills and knowledge of our staff, including staff exchanges and attendances at workshops, conferences and seminars. The details of any staff exchanges will be discussed on an individual basis with reference to the circumstances of the staff and councils concerned.</p> <p>We will continue to draw on expert advice from individuals and consultants with a deep knowledge of the sector to supplement our knowledge and expertise. We will publish external advice concerning financial capacity or need that is directly relevant to a particular application together with our decision report.</p>
ii. The ESC considers allowing councils to make a presentation to the ESC at the pre-application or submission stage of the application process	<p>Accept. We will invite all Councils that notify us of their intention to submit an application to attend a pre-application meeting to discuss the application, the council's unique circumstances and our expectations about what information should be provided in the application.</p> <p>We will also conduct workshops in November and December following the release of our guidance and will be available to meet with any council considering an application prior to the formal notification of intent stage.</p>
iii. The ESC advises councils if there is media interest and before the public release of information concerning council's expression of interest, application and/or the final decision on the application by the ESC	<p>Accept. We will provide relevant council CEOs with an embargoed copy of any media release we issue relating to a council's notification of intent to apply, application or final decision. We will continue with our long-held practice of not making any public comment on an individual application while it is under consideration.</p>
iv. The ESC provide councils with a copy of the final decision and an opportunity for a debrief and comment prior to public release	<p>Accept in part. We will provide council CEOs with an embargoed copy of the relevant decision report prior to its public release and council staff will be given an opportunity to attend a debrief session following its release. Our commitment to releasing a decision within two months of receipt of an application does not allow sufficient time to debrief councils and receive comments prior to releasing our decision report.</p>

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TABLE 1 (CONTINUED)

Recommendation	ESC Response
Section 5.3 — Burden (Cost and Time) placed on Councils seeking a higher cap including the drivers of those costs and identifying best practice among Councils in preparing applications and responding to information requests	
i. The ESC considers what assistance they could give smaller rural councils in applying for a higher rate cap	<p>Accept.</p> <p>We have revised our guidance to include more detail about our expectations and will host workshops with councils in November and December following the release of this guidance material. We will continue with our program of visits to councils in regional Victoria.</p> <p>In addition to these workshops, we will be available to meet at any stage with any council considering applying for a higher cap to discuss our expectations of what should be included in an application in both general terms and specifically in relation to the circumstances of the council (see above).</p> <p>We will work with our technical working group to ensure the instructions provided in our data templates are as clear as possible and that the burden on councils is as low as possible. We are always available to answer questions by phone or email.</p> <p>Further, our guidance makes clear that any council having difficulty completing our data templates should contact us and we will work with them to populate the template and make allowances for certain requirements where necessary.</p> <p>We will also consider any suggestions from the sector about ways to assist councils understand and engage in our application, assessment and compliance processes.</p>
Section 5.5 — Was the approach adopted by the Commission in assessing applications appropriate?	
i. The ESC release all information that was used to determine a council's application including any independent consultant review reports	<p>Accept.</p> <p>We will publish external advice concerning financial capacity or need that is directly relevant to a particular application together with our decision report.</p>

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TABLE 1 (CONTINUED)

Recommendation	ESC Response
Section 5.5 (continued)	
ii. When the proposal outlined within the draft of the new Local Government Act concerning the adoption by councils of a community endorsed consultation framework is enacted and councils have implemented, the ESC accept that if the Mayor on behalf of the Council sign off that the criterion concerning community consultation on the higher rate cap has been undertaken in accordance to the framework that this criterion is met	Deferred. As the review of the LG Act has not been finalised and legislative changes have not been determined, it is premature to comment on this recommendation. We will continue to liaise with LGV about the review of the LG Act and will revisit this recommendation after that review has been finalised.
iii. The ESC clearly indicates what does not constitute a financial case for a higher rate cap and this information is in the form of guidelines to councils	Accept in principle. We have outlined in the guidance material a number of circumstances where we would not approve a higher cap. However, this discussion is not meant to be exhaustive, nor could it be, due to the complexity of issues and circumstances relevant to each application.
Section 5.6 — Workability of the timelines in the application process	
i. The ESC introduce two submission dates for higher rate cap submissions, one as currently applied, 31 March and another at 30 September	Accept in principle. We are open to the possibility of having two submission dates for higher cap applications. However, the implications of accepting applications prior to the announcement by the Minister of the average rate cap would necessitate changes to our current data requirements and assessment approach that need further consideration. We will explore with the sector the option of September applications from the 2018-19 rating year onwards in addition to the current March application date. We expect to incorporate any detailed process changes in the next update of the guidance (early in 2017). We will also continue to consult with the sector about ways to improve the flexibility and accessibility of the application process.

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TABLE 1 (CONTINUED)

Recommendation	ESC Response
Section 5.6 (continued)	
ii. The ESC advise the Minister of the proposed rate cap by August of the year preceding the financial year of use to assist the community consultation and budget planning process of councils	Accept in principle. Our legislative role is limited to advising the Minister only in response to a request for such advice. We will respond as early as possible to any request for advice from the Minister. We note that regardless of how early we provide our advice, the timing of the setting of the average rate cap may currently be constrained by the provisions of the LG Act and <i>Financial Management Act 1994</i> . These provisions specify that the Minister is to set the average rate cap based on the forecast Melbourne CPI as published in the budget update, which might not be released before 15 December each year. We have referred this matter to Local Government Victoria for their consideration.
Section 5.7 — The clarity of the Commission’s final decision	
i. That the ESC places on their website all relevant information they used to form their decision on a council higher rate cap application, including any consultant or advisor review	Accept. We will publish external advice concerning financial capacity or need that is directly relevant to a particular application together with our decision report (see response to 5.5(i)).
Section 5.8 — Miscellaneous issues	
i. That the ESC determines, in what form and format applications are to be presented and where the ESC wants the application sent to	Accept. Our guidance material indicates that our preferred method of receiving applications is by email. However, we recognise the need to be flexible and responsive to the circumstances of individual councils and applications. We will therefore contact each of the councils notifying us of their intent to submit an application to discuss the most appropriate format and delivery method for the council’s application and supporting documentation.
ii. That all application forms be able to be filled in electronically	Accept. We will make both Word and PDF versions of the cover sheet available to councils who have notified us of their intent to submit an application.
iii. That the ESC requires all councils to nominate a contact position and person within council to receive information and that copied in are the CEO and records area of council	Accept. We will ask all councils to nominate a key contact to receive any information we provide to the sector on the FGRS. We will also copy in the CEO and the records area of council.

ATTACHMENT 1 — ADDITIONAL RECOMMENDATIONS OF THE INDEPENDENT REVIEW

This attachment lists the additional recommendations made by Mr Brown for consideration by the local government sector, or collective consideration by Local Government Victoria (LGV), the Commission, Victorian Auditor General (VAGO), Victoria Grants Commission (VGC), and the local government sector. Where relevant, we will work with the sector, peak bodies and other agencies to address the issues raised by Mr Brown in relation to these recommendations.

Recommendations for consideration by the local government sector

Section 5.1: The usefulness and usability of the Commission’s guidance material (including baseline templates) provided to Councils to assist in the preparations of their applications

- i. Councils need to tell the story of where council is at financially, where it is going and why the higher cap was required rather than just filling in the form.

Section 5.3: Burden (Cost and Time) placed on Councils seeking a higher cap including the drivers of those costs and identifying best practice among Councils in preparing applications and responding to information requests.

- i. Councils incorporate any higher cap community consultation into the council planning process required under the Local Government Act.
- ii. Councils express more clearly what trade-offs they considered with their community prior to submitting a higher rate cap application.

Recommendations for consideration by Local Government Victoria (LGV), the Commission, Victorian Auditor General (VAGO), Victoria Grants Commission (VGC), and the local government sector

Section 5.1: The usefulness and usability of the Commission's guidance material (including baseline templates) provided to Councils to assist in the preparations of their applications

- i. That a model chart of accounts, common definition of the services and assets councils provide and standardised quality and effort measures for local government be developed.
- ii. That a common definition of each of the components of the rate revenue stream be developed to ensure non rate cap revenue streams are being used fairly.
- iii. That a method for the calculation of the asset renewal gap, strategic asset planning versus the accounting depreciating asset value method be agreed to for the purposes of determining council financial sustainability.
- iv. That the LGV, ESC, VGC and VAGO work with local government to coordinate and rationalise the reporting requirements for the sector to improve the quality and relevance of the datasets for measuring the sectors' financial and operating performance.