

14 February 2018

Local Government Division
Essential Services Commission
Level 37, 2 Lonsdale Street
Melbourne VIC 3000

To whom it may concern

MAV Submission to the Draft Proposal for Establishing a Local Government Efficiency Factor

The Municipal Association of Victoria (MAV) welcomes the opportunity to provide a comment on the draft proposal of an appropriate efficiency factor for the rates capping framework that applies to local government.

The MAV highlights its continued belief that the application of an efficiency factor is not warranted and that it would be inappropriate given that the impacts of rate capping are still being assessed. However, the MAV has reviewed the draft proposal on Setting a Local Government Efficiency Factor in which the ESC addresses feedback provided by the sector in response to its earlier Consultation Paper on this issue. This includes further evidence provided by way of additional statistical analysis commissioned by the ESC.

The MAV stands by its critique of the proposals in the Consultation Paper and does not feel that the additional analysis undertaken provides any more comfort, especially with respect to the effect of the proxies being used in the DEA approach. Readers of this submission are referred to the MAV's response to the Consultation Paper which details its concerns with, and possible approaches to, the setting of an efficiency factor and in particular the issue of the proxies. While the ESC has acted on some of these, basic questions which underpin the findings of the DEA-Proxy approach are still a concern.

In its submission to the Consultation Paper the MAV included a very simple example of two councils with very similar levels of the three proxy variables but heavily contrasted differences in actual units of service delivery and cost drivers. No specific comment was made by the ESC with respect to this example, although the ESC Proposal claims that its further analysis concluded that the difference in technical efficiency is marginal when more discrete service-specific variables are used (including planning application processing, library loans, animal management requests and food complaints) across all councils. The MAV sought data on the technical efficiency identified for individual councils in order to better assess the robustness of the proxies when reviewing the Consultation Paper, however this level of transparency has not, and continues not to be provided. The ESC has however indicated that if councils wish to see how they performed in benchmarking exercises they can be contacted for a confidential discussion.

Less than compelling is a review of the DEA analysis by (another) independent consultant who argues that the choice of the specific proxies is advisable because these were favoured by other academics and because of perceived issues around the defining of more representative cost drivers. If the approach has significant issues in the case of two very like councils the MAV would contend that is flawed fundamentally. Given the importance of this issue it seems reasonable that a more detailed comparison of like councils could have been undertaken to provide confidence that the proxies are reflective of similar output levels.

The MAV is however pleased to see that the ESC believes it unreasonable to entertain a proxy value drawn from historic Australian industry productivity data which is generally accepted as having little relevance for the sector. The MAV also sees benefit in a staged approach while the impacts of rate capping are being assessed. The adoption of a notional factor must be considered as quite arbitrary but at least can be seen easily for what it is compared with the DEA-proxy approach. Although there is no certainty there may be less risk in the notional factor.

It should not be lost when considering this issue and in the setting of a factor over a number of years that there will be influences on efficiency and productivity that may be outside a council's control. The recent example regarding recyclables is a good one which may result in increased costs for councils. The ability for annual flexibility needs to be ensured in any approach and therefore the adoption of factors for more than one year (i.e. 3 years) needs to be subject to annual review.

The MAV considers that longer term development in the ability to use more disaggregated data (either VGC or LGPRF or something else) be considered seriously as sources for the basis of commenting on productivity. The fact the LGPRF currently does not include corporate overheads and does not cover the full gamut of services should not preclude this development. Approaches like pooling intermediate services and corporate overheads and separating governance costs as distinct from the more direct service costs, requiring inclusion of corporate overheads in service cost reporting and encouraging better development of corporate overhead allocation systems could be considered. The time made available from the staging of the introduction of efficiency factor could possibly be used by the ESC to consider how alternatives to the DEA-Proxy approach might be fostered.

The MAV is happy to further elaborate on any matter within this submission.

Yours sincerely



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