Submission No 15

INQUIRY INTO FIRE AND EMERGENCY SERVICES LEVY

Organisation: Local Government NSW

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LGNSW Submission to the Legislative Council (Portfolio Committee No. 4) Inquiry into the Fire and Emergency Services Levy (FESL)

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LOCAL GOVERNMENT NSW
GPO BOX 7003 SYDNEY NSW 2001
L8, 28 MARGARET ST SYDNEY NSW 2000
T 02 9242 4000 F 02 9242 4111
LGNSW.ORG.AU LGNSW@LGNSW.ORG.AU
ABN 49 853 913 882

LOCAL GOVERNMENT NSW

Table of contents

LOCAL GOVERNMENT NSW

1. Opening

Local Government NSW (LGNSW) is the peak body for local government in NSW, representing all NSW general-purpose councils and associate members including special-purpose councils. LGNSW facilitates the development of an effective community based system of local government in the State.

The funding of emergency services[1] in NSW is a matter of critical importance to local government. Councils provide a wide range of support to the activities of the emergency services and are required to fund 11.7% of the emergency services budget. This will amount to around $155 million in 2017-18. Local government has repeatedly raised concerns about the complete lack of transparency and accountability in the framing of emergency services budgets and the process for determining levies on individual councils. Local government was also to play a pivotal role in the implementation and operation of the proposed Fire and Emergency Services Levy, undertaking such tasks as land classification, levy collection and debt recovery. LGNSW therefore welcomes the opportunity to make this submission to the Legislative Council (Portfolio Committee No. 4) Inquiry into the Fire and Emergency Services Levy (FESL).

This submission:

- presents LGNSW's policy position on funding the emergency services
- provides a response to each of the Terms of Reference:

  (a) the policy process and financial modelling underlying the provisions of the *Fire and Emergency Services Levy Act 2017*,

  (b) the policy and financial implications for all stakeholders of repealing this Act,

  (c) alternative models for ensuring that fire and emergency services are fully funded in a fair and equitable manner; and

  (d) any other related matter.

- proposes actions that LGNSW believes are required to improve the transparency and accountability of the budgeting processes of the Emergency Services (i.e. Fire and Rescue NSW (FRNSW), the Rural Fire Service (RFS) and the State Emergency Services (SES).

This submission is in draft form until it is considered by the LGNSW Board. Any revisions made by the Board will be forwarded in the form of an updated submission.

2. LGNSW Policy Position on Funding Emergency Services

LGNSW advocates the introduction of a broad based property levy (BBPL) to replace ***both*** *the Emergency Services Levy (ESL) on councils and insurance policies.*

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[1] In this submission, 'emergency services' refers to the Fire & Rescue NSW (FRNSW), Rural Fire Service (RFS) and the State Emergency Service (SES).

LGNSW has maintained this policy position for nearly 15 years. This policy was advocated in LGNSW's submission to the NSW Legislative Assembly Public Accounts Committee *Review of Fire Services Funding* in 2003.

LGNSW maintains that the current system is deficient in terms of equity, transparency and accountability:

- Equity – the current funding system is heavily reliant on contributions collected by insurance companies from policy holders providing 73.7% of funding. Inequity arises as a significant proportion of the population is either uninsured or under-insured, thereby failing to make a fair contribution- they are commonly referred to as free-riders.

- Transparency – The 11.7% ESL collected from councils is appropriately called a hidden tax. As it is collected from councils not individual ratepayers or residents, it is embedded in council rates, fees and charges and is not directly visible.

  The lack of a standard practice among insurance companies in disclosing the emergency levy on insurance policies also means that that the actual contributions being paid by individuals is often obscured.

  The average ratepayer or resident is not aware of increases in the ESL to cover expanding emergency services budgets.

  Furthermore, most people would not be aware that they making two ESL contributions, one through their insurance policy and another through rates. The lack of transparency has allowed this practice of 'double dipping' to continue unchecked.

- Accountability – The lack of public transparency re both the insurance and council levies erodes accountability. As the costs are obscured, the public is less sensitive to increases. As 85.4% of the combined emergency services budget is funded by the external ESL levies, and another 7.3% from the stamp duty the Government collects on the insurance levies, the State Governments net contribution from consolidated revenue has only been 7.3%. It is no wonder why successive state governments have found it easy to increase emergency services budgets without the budget scrutiny that applies to other state government agencies.

  From a political and bureaucratic perspective the current system is both politically and administratively convenient.

Features of the BBPL model advocated by LGNSW include:

- It would be based on property valuation, as provided by the NSW Valuer General. This would preferably be valuations based on Capital Improved Valuation (CIV) which provides a better proxy for the value of property being protected than the Unimproved Value currently available in NSW, particularly in urban areas. This would improve equity in the system, particularly in urban areas.
- Concessions for pensioners and low income earners.
- The use of both base and ad-valorum components in determining levies.
- The potential application of maximum and minimum levies to avoid extreme outliers.

- Limited exemptions. The BBPL would apply to all private property, building structures and vacant land.
- Properties would be classified to reflect type and risk.
- Consideration of the use of zones i.e. dividing the state into zones aligned with service availability/service expectation.
- Ideally, the BBPL would be collected by Revenue NSW to make it clear that it is a State Government levy and to avoid confusion with council rates. Revenue NSW already has access to the all the land valuation information required to do this and as it already collect land tax for the State Government, it already has systems in place. It would seem to be consistent with the OSR's current push to expand its business by offering debt recovery services to councils and potentially the collection of council rates fees and charges the future. However, LGNSW has previously indicated that councils would consider collecting the levy provided:
  - the ESL on local government is removed;
  - the BBPL/FESL is clearly identified as a State Government levy; and
  - provision is made for full cost recovery by councils.

3. Terms of Reference

a) the policy process and financial modelling underlying the provisions of the Fire and Emergency Services Levy Act 2017

LGNSW's last formal engagement in the policy process leading to the NSW Government's announcement that it was to introduce the FESL was our submission to the *NSW Government Review of Emergency Services Funding* in October 2012. The submission reaffirmed LGNSW's policy of support for the introduction of a BBPL to replace the ESL on both insurance policies and councils.

Once advised of the Governments most recent proposal, LGNSW expressed disappointment at the Government's failure to include the removal of the 11.7% ESL on councils as part of the proposal. LGNSW emphasised that support for a BBPL (including collection of the levy) was conditional on the removal of the ESL on local government. LGNSW was advised that the Government had excluded the removal of the ESL on local government as it would erode the projected savings to insurance policy holders.

LGNSW was not given the opportunity to review the detailed financial modelling underlying the FESL proposal, however, it did emphasise the importance of equity throughout the process.

Despite the short comings of the Government's FESL proposal, LGNSW became closely engaged in the development of legislation, implementation policy and operational processes. Recognising what then appeared to be the firm commitment of the Government, LGNSW felt obliged to be at the table to influence the FESL legislation and related implementation and cost compensation arrangements. LGNSW was determined to ensure that the interests of councils and communities were protected and that implementation of the FESL would proceed as seamlessly as possible. LGNSW's policy commitment to removing the ESL on councils was maintained and would be subject to ongoing advocacy to have this modification made to FESL at a future date.

From March 2016 to May 2017 LGNSW participated on an implementation working group which included representatives from councils, NSW Treasury, Office of State Revenue, and the Valuer General's Office. While the working group discussions were confidential and some government policy decisions non-negotiable, the group was critical to helping protect councils' interests.

Advocacy by LGNSW, council representatives and the NSW Local Government Revenue Professionals on the working group resulted in numerous wins for the sector, including:

- Securing full cost recovery for councils for any costs associated with the implementation and administration of the FESL;
- Requiring the FESL to be separately identified on rates notices as a NSW Government levy; and
- Securing a NSW Government communications campaign informing the public about the FESL, making it clear that it was a NSW Government levy and providing comprehensive information on the FESL to minimise inquiries to councils.

LGNSW also headed off significant issues, such as a proposal to drastically change the land valuation notification processes.

Following the deferral, LGNSW advocated strongly for costs associated with the deferral to be fully compensated. Treasury agreed to implement a process to ensure full compensation for any cost associated with the FESL deferral that were not covered by existing cost compensation arrangements.

LGNSW considers this part of the policy process to be an exemplary example of consultation and collaboration between state and local government. LGNSW commends NSW Treasury for its openness and responsiveness during this part of the process.

While the FESL was deficient from a local government perspective, the NSW Government's 11th hour decision on 30 May 2017 to defer the FESL was both surprising and disappointing. Surprising in that the FESL had progressed almost to the point of implementation before being indefinitely deferred. It was disappointing in that there had been already major financial expenditure in addition to the large investment of time and effort expended by state and local government staff working towards introduction of the FESL.

It is difficult to believe that Cabinet would not have been aware of the financial modelling and the projected distributional impacts of the FESL well in advance of deferral decision. FESL represented a major tax reform and should have been subject to intense scrutiny. It should have been expected that there would be winners and losers in any change to the emergency services funding methodology. Indeed, that was one of the objectives – free-riders were now to contribute and insurance policy holders were to receive savings.

The Government states that it reason for deferring the FESL was to "*ensure property owners - especially small to medium businesses - do not face an unreasonable burden in their contribution to the State's fire and emergency services. In the majority of cases across NSW, fully insured people would be better off under the new system. However it had become clear that some fully insured businesses were facing unintended consequences".*

It would be reasonable to expect this to be identified in financial modelling earlier in the process and that there would have been time to recalibrate the model

Other states who have introduced a land valuation based BBPL were invariably subject to criticism when they were first introduced. State Governments in South Australia, Western Australia and Victoria maintained their resolve and removed levies on councils at the same time. Successive NSW Governments have shied away from introducing this reform. The NSW Public Accounts Committee *Review of Fire Services Funding* (2003-04) also recommended against the introduction of a property based scheme for funding fire services on similar grounds. This recommendation was embraced by the Government of the time.

b) the policy and financial implications for all stakeholders of repealing this Act,

The primary implication is that by deferring the introduction of the FESL (or other BBPL) to fund the emergency services, NSW is prolonging the existing insurance policy/local government based system that is widely acknowledged as failing in terms of:

- equity;
- transparency; and
- accountability.

1. Financial Implications

<u>NSW Government</u>

LGNSW is not in a position to know the full costs incurred by the NSW Government in preparing to implement the FESL. The Sydney Morning Herald (27/7/17) reported that the costs ran to more than $25 million. LGNSW is aware that Treasury made significant expenditures in developing the FESL and preparing for implementation. The system had been developed and tested, advertising and education had commenced, and the FESL was ready to 'switch on' by the time the deferral was announced.

In the absence of signs that the NSW Government is likely to reintroduce a modified FESL or other alternative emergency services funding model in the near future (at least within the term of the current government), it is likely that much of this expenditure will have been wasted. A lot of the groundwork will need to be repeated if, or when, a revised FESL is reintroduced in future.

<u>Local Government</u>

As a result of the cost recovery arrangements negotiated by LGNSW and the NSW Local Government Revenue Professionals with the NSW Government, councils have been reimbursed for the direct costs incurred in preparing to implement the FESL. A set of cost heads had been agreed and councils had the choice between adopting a formula for reimbursement or recorded cost reimbursement. The reimbursement arrangements were later extended to include any additional costs incurred in unwinding the FESL after the deferral was announced.

While direct costs have largely been covered, time and effort was expended by local government staff in preparing for implementation of the FESL. The opportunity cost of time that would otherwise have been spent on other council priorities, can't be recovered.

Insurance Companies

LGNSW is unaware of the actual costs incurred by insurers in preparing for the implementation and later unwinding of the FESL. However, we note that the Insurance Council of Australia stated that "*the resumption of ESL collection will come with significant additional costs that the industry will be forced to pass on in full to policy holders* and that *insurers have spent more than a year and tens of millions of dollars on consultants and technological system changes in preparation for the removal of the ESL from June 30.*[2] LGNSW is not in a position to know if, or to what extent these costs are being passed on to insurance policy holders.

However, LGNSW supports the State Government's decision to retain the Insurance Monitor, (originally established to ensure insurance cost savings were passed on to policy holder), to oversee a smooth continuation of the existing system and ensure insurance companies collect only the amounts necessary to meet fire and emergency services funding requirements.

2. Policy Implications

The decision of the NSW Government not to implement the FESL means that NSW remains out of step with other mainland states in retaining a funding system based on an ESL on insurance policies and councils.

All other mainland states fund their fire services through BBPLs. Most are based on property valuation, although Queensland has a flat levy based on service expectation. Victoria was the most recent state to introduce broad based property levy in 2013, the Victorian Fire Services Property Levy (VFSPL). This was prompted by the 2009 Victorian Bushfires Royal Commission's Recommendation 64:

> *The State replace the Fire Services Levy with a property-based levy and introduce concessions for low-income earners.*

This recommendation was based on the Royal Commission's findings that that the current, largely insurance based system was inequitable and lacking in transparency.

The Royal Commission cited several major reviews in making this recommendation.[3] These included the:

- 2003 HIH Royal Commission which said that this 'cascading' application of taxes '… lacks transparency, is inequitable and is contrary to good tax policy'. It recommended that Victoria, New South Wales and Tasmania abolish their Fire Services Levies."
- The Review of Australia's Future Tax System 2009 (the Henry review) that recommended 'that all specific taxes on insurance products, including the fire services levy, be abolished.
- Tax reviews in New South Wales in 2008 and Victoria in 2001 which recommended replacing the levy with an equivalent property-based levy collected by local councils.150

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[2] Insurance Council of Australia - media release, 30 May 2017.
[3] Victorian Bush Fires Royal Commission 2009, p.383

Given the weight of the findings of successive high level reports, it seems certain that NSW will be under pressure from COAG and other quarters to reapproach the implementation of a FESL/BBPL like model to fund emergency services at some-time in the future.

To satisfy the transparency criterion, a revised FESL/BBPL must replace the ESL on local government. This would also be consistent with the models introduced in other jurisdictions where the BBPL replaced both the insurance and local government levies. For example, the VFSPL replaced the 12.5% mandatory contribution to the budget of the Melbourne Metropolitan Fire Brigade. (There had been no existing requirement for local government to contribute to the Victorian Country Fire Authority).

c) alternative models for ensuring that fire and emergency services are fully funded in a fair and equitable manner;

There are a limited number of viable options for the funding of fire and emergency services. LGNSW has ruled out the current insurance/local government based model as an acceptable model for the future.

1. Consolidated Revenue

Many would argue that the most equitable and efficient method of funding the emergency services is from Consolidated Revenue. That way the cost burden is distributed across all the revenue sources of state government. The broad base helps maximise the number of NSW residents making a contribution to the costs. This would put the emergency services on the same footing as the NSW Police Force.

While a contribution from consolidated revenue features in each of the state funding models, it has not historically been the major source of funding fire and emergency services in any jurisdiction. No other state has adopted this model when reforming their emergency services funding model.

2. Service Expectation/Flat Rate Model (Queensland Model)

The levy is applied to all properties at a flat rate within different categories of utilisation (for example, residential, commercial, industrial, community use, rural or vacant). The levy is not related to property value. Different levies apply in different areas based on fire brigade response capabilities, with the highest levies being applied in major urban centres serviced by large permanently staffed brigades and lower levies applying in areas with lesser levels of service availability. The costs are shared by all owners of property, and not just those who are insured.

This model was originally introduced to Queensland in 1984.

3. Property Value Based Property Levy (e.g. FESL)

Western Australia (introduced 2003), South Australia (introduced 1999) and most recently, Victoria (2013), use property valuation based models, similar to the proposed FESL except that council contributions were removed.

d) any other related matter

As noted above, local government has repeatedly raised concerns about the lack of transparency and accountability in the framing of emergency services budgets and the process for determining levies on individual councils. The fact that there is a complete lack of information about the way the three services come up with a budget figure – of which councils must pay 11.7% - is completely unacceptable. Councils and those with insurance simply must pay, regardless of the figure. No-one would argue that front line services should not be properly resourced, but the process by which the budget must be disclosed

With the indefinite deferral of the FESL, NSW is retaining the existing insurance and local government based system with all of its acknowledged weaknesses in terms of equity, transparency and accountability.

LGNSW recommends that measures be taken to compensate for these flaws until such time that a BBPL is introduced. LGNSW recommends that:

- the Committee enquire specifically into the budgetary and financial management practices of the NSW emergency services; and
- that the Auditor General conduct a review the budgetary and financial management practices of the NSW emergency services and publish her report.

4. Conclusion

LGNSW encourages the NSW Government to move forward with the introduction of a BBPL to replace both the Emergency Services Levy (ESL) on councils and insurance policies.

The current system is seriously flawed in terms of taxation principles and lags behind the practice of other jurisdictions. With the pressure of COAG and the national tax reform agenda, it is inevitable that that NSW will need to implement a BBPL of one form or another, some-time in the near future.

While the proposed FESL was lacking from a local government perspective, LGNSW commends the Government and NSW Treasury in particular, for engaging collaboratively with local government on its implementation. Building on this, we request that local government be more closely consulted in the policy development stage of a revised FESL or alternative BBPL.

With the retention of the existing insurance and local government based system of funding the emergency services, it is incumbent on the Government to introduce measures that will improve transparency and accountability about the framing of emergency services budgets and the process for determining levies on individual councils.

As a starting point and to provide guidance on such measures, LGNSW recommends that a Parliamentary Committee inquire into, or be tasked with a separate inquiry into the budgetary and financial management practices of the NSW emergency services.

LGNSW also recommends that the Auditor General conduct a review the budgetary and financial management practices of the NSW emergency services and makes her report public.

LGNSW would be pleased to work with the State Government on the development of an equitable, transparent and accountable funding system for NSW emergency services.