LEGISLATIVE ASSEMBLY

# Public Accounts Committee

## REVIEW OF FIRE SERVICES FUNDING

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# Charter of the Committee

The Public Accounts Committee has responsibilities under Part 4 of the *Public Finance and Audit Act 1983* to inquire into and report on activities of Government that are reported in the Total State Sector Accounts and the accounts of the State's authorities.

The Committee, which was first established in 1902, scrutinises the actions of the Executive Branch of Government on behalf of the Legislative Assembly.

The Committee recommends improvements to the efficiency and effectiveness of Government activities. A key part of Committee activity is following up aspects of the Auditor-General's reports to Parliament. The Committee may also receive referrals from Ministers to undertake inquiries. Evidence is gathered primarily through public hearings and submissions. As the Committee is an extension of the Legislative Assembly, its proceedings and reports are subject to Parliamentary privilege.

# Terms of Reference

1. Prepare a report evaluating the current fire services funding arrangements and alternative funding arrangements.
2. The report should
    a. present recommendations on future funding arrangements that meet the current and prospective needs of the fire services and would be as near as possible to cost neutral;
    b. provide detailed information on how the recommended arrangements would apply to facilitate their possible implementation in 2004-05; and
    c. identify any administrative and compliance issues associated with the current and recommended funding arrangements, including transitional issues and the earliest practical commencement date for the proposed reforms.
3. In conducting the inquiry, the Committee should
    a. consider the impact of current and proposed funding arrangements on decisions by households and businesses to insure;
    b. consider the funding approaches adopted in Queensland and South Australia and soon to come into effect in Western Australia as well as the findings of the Victorian review of fire service funding;
    c. consider the implications of any changed fire service funding arrangements for the role of Local Governments in funding and facilitating the provision of fire services, particularly in rural NSW;
    d. consider how the State Government's contribution to funding the fire services should be determined within any new funding framework;
    e. undertake modelling of the impact of the proposed funding arrangements on taxpayers to assist in determining proposed funding arrangements;
    f. not consider general taxation issues such as the GST and stamp duty on insurance unless these issues affect the operation of fire services funding arrangements; and
    g. not consider issues that relate to the cost of fire service provision or its cost effectiveness.
4. The Committee's proposed funding arrangements should
    a. ensure, to the maximum extent possible, that all those that benefit from the provision of fire services contribute to funding the fire services;
    b. broadly match funding contributions to the level of service provided to the taxpayer and/or the risk of fire affecting each taxpayer;
    c. be difficult to avoid through changed taxpayer behaviour; and
    d. provide a stable base for funding fire services.
5. The report should also consider the appropriate funding arrangements for meeting the extraordinary costs associated with fighting major bushfires. In particular, the

Committee should examine the possible development of a fire fighting reserve - funded by a fire service levy - to assist in meeting future extraordinary costs associated with major bushfires.

6. The Committee is to report by 29 February 2004.

# Chairman's Foreword

I am pleased to present this report reviewing the arrangements for the funding of fire services. This provides a comprehensive analysis of the current arrangements and makes some recommendations about improving them to provide stable, reliable and equitable funding for these vital services.

This was an unusual inquiry for the Committee as our powers do not extend to inquiring into Government policy unless we are asked to do so by a Minister or the Legislative Assembly. We welcomed the opportunity to investigate this complex area of taxation policy.

The Committee notes that the two fire services, NSW Fire Brigades and the NSW Rural Fire Service, provide a range of essential services to the entire community and they deserve a stable, reliable funding source for their continued operations.

However, the Committee considers that such funding arrangements should also be transparent, efficient and equitable.

The current funding system is based on contributions collected by insurance companies from policy holders. In its investigations and deliberations, the Committee attempted to address the issue of concern most commonly raised in relation to this system – that is, that the system is not equitable.

This inequity is created by the ability of some members of the community and corporate sector to avoid contributing their fair share to the funding of the State's fire services in the secure knowledge that they would still receive the fire services' assistance should they need it. These so-called "free riders" can avoid paying their fair share by choosing not to insure their properties and contents, or by insuring at inappropriately low values. This places a higher burden of funding on those who do insure and arguably discourages people from insuring prudently.

However the Committee was unable to determine with any certainty the extent of this problem.

Other concerns raised were that the system is not transparent because policy holders are not informed of the amount of levy paid.

The Committee provides recommendations in relation to improving the current system to reduce the impact of these weaknesses.

The Committee's inquiry was supported by detailed modelling of the effects of alternative funding arrangements. The options for improvement show that there is a clear benefit for replacing the current system with a levy on property in the residential sector because this would broaden the base of those contributing to the scheme.

However, there remains a great deal of uncertainty about the impacts of such a change on the commercial sector. A levy on commercial properties would narrow the base of those contributing to the fire services. This is because, in the commercial sector, levies are currently paid on a broader range of insurance policies than those linked to property. There is also a lack of information available about the amount of Fire Services Levy currently paid by commercial tenants. This requires further investigation and the possible development of other criteria such as fire risk factors for commercial buildings.

On the basis of the evidence before it, the Committee considers that the Government should not introduce a property-based scheme for funding fire services at present.

As required by our Terms of Reference, the Committee makes a number of detailed recommendations about the administration of a property-based scheme should it be introduced.

Should the Government decide to introduce a change to a property-based system, the current contributions from Local Government should be replaced by a levy on each council's properties. The Committee also considers that the State Government should continue to provide at least the same proportion of funding as it currently does.

I would like to thank all the groups that made submissions and appeared before the inquiry. The Committee is particularly grateful to NSW Fire Brigades and the NSW Rural Fire Service for providing information throughout this inquiry and for arranging for the Committee to inspect their operations in Queanbeyan. The Insurance Council of Australia also provided a great deal of assistance and support to the Committee.

I would like to thank the Commonwealth Department of Transport and Regional Services for agreeing to appear before the Committee.

The Committee is also grateful to those organisations in Western Australia and South Australia which explained the operations of the property-based schemes in those States to the Committee in February 2004.

I would particularly like to thank Doug Drysdale, Thach Huynh and other staff at Professional Financial Solutions for the detailed financial modelling of the effect of the options on various sectors of the community they provided to the Committee.

The Committee considers that PFS provided an extraordinary level of service on a complex technical area. The Committee hopes that the Government continues to work with PFS to refine the modelling of the impact of changes to the system.

I would also like to thank Melissa Power of NSW Treasury and Vicki Buchbach of the Secretariat for drafting this report for the Committee's consideration.

Matt Brown MP
Chairman

# Executive Summary

## Chapter One

The Committee was asked to undertake this review of the funding arrangements for fire services by the Treasurer.

The Committee consulted widely, received 64 submissions and held three days of hearings. Consultants prepared a report on financial modelling to demonstrate the effects of different scenarios for funding. This was released for comment as an interim submission in March 2004. A further 23 submissions were received in response. The Committee held additional public hearings in May 2004.

## Chapter Two

Taxes should be assessed against the principles of taxation policy which include efficiency, equity, simplicity, stability and transparency. Fire services have the characteristics of a "public good" where consumption by one user does not reduce the demand by other users and users cannot be excluded from the service.

The beneficiaries of fire services are identified as the community, businesses, insurance companies, governments and the environment. There are four basic means of funding fire services: through consolidated revenue, user charges, full cost recovery and earmarked or "hypothecated" taxes. All of these options have advantages and disadvantages which are outlined in Chapter Two.

## Chapter Three

The two main fire services in New South Wales are the NSW Fire Brigades and the Rural Fire Service (RFS).

NSW Fire Brigades is responsible for managing fire services in metropolitan areas and in larger country towns which cover 90 per cent of the population. It provides a range of protection including: fire, motor vehicle accidents and building collapses. It also manages hazardous materials emergencies. NSW Fire Brigades has 335 fire stations throughout NSW staffed by 3,100 full time and 3,300 part time fire fighters.

The RFS is responsible for fire prevention and suppression in 90 per cent of the state. It has around 67,000 volunteer fire fighters in 139 rural fire districts. Although most recognised for its role in suppressing bushfires, the RFS also attends road accidents and structural fires in 1,200 towns and villages. It also assists in search and rescue operations and during natural disasters.

The first fire services in New South Wales were provided by insurance companies for the sole use of protecting their customers' properties. Volunteer fire brigades were also established. The two brigades were combined in the late nineteenth century to provide fire fighting services in metropolitan areas. The current NSW Fire Brigades is the descendant of these arrangements.

Rural fire brigades were organised by local councils from early in the twentieth century. A fund was established in 1949 to enable councils to purchase fire fighting equipment. The first Department of Bush Fire Services was established in 1990. The current Rural Fire Service was established in 1997 in response to coronial inquiries into the 1993-94 bushfires.

Insurance companies and the State and Local Governments have jointly funded the metropolitan fire services since 1884 and the rural fire services since 1949. Since 1989, NSW Fire Brigades has received 73.7% of its statutory funding from insurance companies, 12.3 % from Local Government and 14% from the State Government. From 2001, the Rural Fire Service has received 73.7% of its statutory funding from insurance companies, 13.3% from local councils and 13% from the State Government.

## Chapter Four

The two fire services receive funds from statutory contributions, miscellaneous contributions, contributions from the Commonwealth and offshore contributions.

Funding requirements for the services are established by the Minister for Emergency Services in consultation with the Treasurer a year in advance.

Fire services determine the amount of funding required from insurance companies by aggregating reports of premium income in certain classes of insurance from the previous financial year to determine each company's share of the market. These can be adjusted once actual income is determined.

Insurance companies pass on the costs through a Fire Services Levy (FSL) on certain types of insurance premiums. The Insurance Council of Australia (ICA) provides advice on recommended rates to apply to four different types of insurance however the use of these rates is a matter for each company. In 2002-03 insurance companies provided the NSW Fire Brigades with $276 million and the Rural Fire Service with $89 million.

Contributions to the NSW Fire Brigades by local councils in the Greater Sydney Area are based on an assessment of average land values over the past five years. Other councils contribute 12.3% of the estimated cost of operating the NSW Fire Brigades in the area. Councils also contribute 13.3% of the cost of the local Rural Fire Service brigades. Many councils also make significant voluntary contributions.

People take out insurance as a way of managing the risks of adverse events which could lead to losses. Insurance products subject to the FSL also have Goods and Services Tax (GST) and stamp duty added to the cost of the premium. At 2004 rates, the combination of FSL, GST and stamp duty adds 32 per cent to the cost of household insurance premiums and 43 per cent to the cost of commercial premiums (not including any GST input tax credits). If the FSL was not applied, taxes would add only 16 per cent to the cost of these premiums.

## Chapter Five

Three basic models for funding fire services are used in Australia. In the Northern Territory and the Australian Capital Territory, fire services are funded from consolidated revenue. New South Wales and Victoria use an insurance-based model. Queensland, South Australia and Western Australia impose a levy on property. South Australia and Tasmania also impose a levy on motor vehicles. Tasmania has a hybrid system with a property levy and a levy on insurance.

Each property-based system is calculated on a different basis and covers different services. In Western Australia, Queensland and Tasmania, local councils collect the property levy but the State Government collects it in South Australia. In Tasmania, the State Government collects the motor vehicle levy. Concessions are available to certain groups in all four States with property-based fire services levies.

When compared to taxation principles of efficiency, equity, simplicity, stability and transparency, the property-based levies compared favourably to the Victorian insurance-based scheme. Consolidated revenue models ranked higher than both other models against these criteria.

The fire services funding scheme was reviewed in Victoria in 2003. The Government decided to retain an insurance-based scheme with some administrative improvements. The insurance industry commented that this review did not model the effects of a property levy in any depth. This review was seen positively by the NSW Fire Brigades and the Fire Brigade Employees' Union.

Most submissions to the inquiry supported replacing the current funding arrangements with a property levy of some sort. Some also supported a levy on motor vehicles. The calculation of a levy based on risk of fire or service level or the improved value of land were suggested. Other groups opposed changing arrangements.

Submissions noted that the funding base in the current system was narrow because insurance coverage is not universal. Some supported exemptions for organisations managing their own risks or providing their own services. Others discussed the need for concessions for disadvantaged groups or in recognition of voluntary support to the fire services.

Many submissions supported the collection of a property levy by local councils although it was considered important that the levy be identified as a State tax and councils receive adequate compensation for the costs of collecting the levy. The Roads and Traffic Authority did not support collecting a motor vehicle levy through registration.

Some suggested extending the funding arrangements to include other emergency services such as the State Emergency Service (SES), but this issue is outside the scope of the current inquiry's Terms of Reference. However, the Committee would recommend that SES funding be considered in future studies on this issue.

## Chapter Six

Some groups consider the current funding arrangements in NSW to be inefficient because they increase the cost of insurance and could deter people from insuring prudently. Efficient taxes are broadly based. The current system has a narrow base because only those insuring pay the levy and therefore carry a disproportionate share of the burden. In other words, those who do not insure do not contribute.

The FSL is calculated on the entire premium rather than only that part related to fire risk so that costs of FSL can be higher for premiums in areas with relatively greater rates of theft than fire. The collection process contributes to inefficiency because there is a possibility of over and under collecting in each year, although the Committee was not presented with any evidence suggesting that insurance companies consistently over-collected FSL.

It is inequitable that those who do not insure or under-insure their properties benefit from fire services. Estimates of the extent of non-insurance and under-insurance vary considerably. It is difficult to obtain reliable information on the extent of non-insurance and under-insurance with estimates of non-insurance in households ranging from 4.5 per cent to 25 per cent. Some surveys indicate that up to 17 per cent of small businesses are not insured. Around 7.5 per cent of residential buildings and 35 per cent of contents are insured for less than 70 per cent of their replacement value. Tenants and low income groups are less likely to have insurance than other groups. There is very little information about the extent of non-insurance and under-insurance by commercial property owners.

Other sources of inequity identified are that local council contributions in the Greater Sydney Area vary on the basis of land values rather than any difference in service level and that the level of FSL collected in relation to motor vehicles does not reflect the proportion of the services used in attending incidents involving these vehicles. Businesses may artificially lower their liability to contribute to the fire services through such business practices as the use of deductibles, netting of premiums, self-insuring and insuring in cheaper insurance markets overseas. The Committee heard that some of those insuring internationally may not remit FSL to NSW as they are legally required to do.

The current arrangements are administratively efficient and relatively inexpensive to the Government. There are, however, significant costs to the insurance industry. The revenue source is also relatively stable as demand for insurance is quite constant but the system does not provide transparency to those paying FSL on insurance policies or contributing to the Local Government's contribution through rates notices.

The Committee considers there is a strong theoretical case for replacing the current insurance-based system for funding fire services.

## Chapter Seven

Financial modelling work was commissioned from Professional Financial Solutions (PFS) to assess different funding options for the Committee. This work compared the impact of moving to a property-based levy to the current arrangements.

The consultants matched information about the amount of FSL currently paid on insurance by the commercial and residential sectors to information about the value of properties.

The model examined four scenarios for a property-based levy. The first three were based on principles that the commercial and residential sectors in the metropolitan and non-metropolitan areas should contribute to fire services in proportion to:

- The level of benefit received from fire services;
- The amount of use made of fire services; and
- The level of service available in the area.

These three options could also be applied to modify an insurance-based system or introduce a hybrid scheme.

A fourth option was developed based on some features of the previous three for the purpose of minimising the impact on small businesses of the other options.

The consultants designed levy options with minimum and maximum thresholds and rates based on land value.

The Committee released the interim submission by PFS for public comment and received 23 further submissions in response. Local Government representatives were concerned that the modellers did not address their contributions to the fire services and that the estimated administrative costs were inadequate. State Forests considered its properties should be exempt from a levy as the agency contributed to fire suppression. The Department of Housing estimated that it would cost around $10 million annually if its properties were subject to a levy. The fire services were concerned about the statistical reliability of the data and the underlying assumptions of the three scenarios. Some submissions supported the introduction of a new levy, particularly those organisations which would face lower costs. Other submissions commented that a property levy was not related to risk of fire. The Property

Council of Australia was particularly concerned about the large increases in direct costs for high value commercial properties.

The PFS submission was refined after further information was received. In their final submission, the consultants included a fifth option which aimed to minimise the effect of a levy on owners of the small number of high value commercial properties. These costs are high because, in the commercial sector, the Fire Services Levy is applied to a broader range of insurance products than related to property ownership. Replacing the current system with a property levy would narrow the base in the commercial sector. That is, commercial tenants would no longer contribute.

## Chapter Eight

The Committee notes that the modelling work shows that replacing the current insurance-based arrangements with a property-based levy would broaden the base of the contributions to the fire services in the residential sector. The majority of property owners currently holding insurance would be contributing less to fire services through a property levy.

However, despite the scale of this project and the thoroughness of the consultants in undertaking the work, there were significant limitations to the available data and, therefore, on the conclusions drawn as a result. Importantly, the consultants were only able to match insurance records with properties for around 11 per cent of the commercial properties. This sample does not seem to be representative of the level of FSL applied to commercial policies.

There are also unresolved issues about the level of current FSL contributions in the commercial sector. The Committee is unable to ascertain the level of FSL paid by commercial tenants and the ability of property owners to recoup these costs.

On the grounds of equity, more work is needed to ensure the commercial sector is not unfairly disadvantaged by a change to the current system. The Committee has been advised that the insurance industry is currently surveying commercial clients to seek improved information about the amount of levy paid on insurance by commercial property owners and tenants.

The Committee considers that this work does not provide adequate support for adopting a property-based levy at this time.

There are a number of options for improving the operation of the current insurance-based system. The way insurance companies' liability to contribute to fire services is calculated could be reviewed to ensure it reflects the pattern of activity by fire services.

Measures should be implemented to reduce the likelihood of those organisations which insure offshore not remitting FSL to the fire services. The insurance industry could also increase the level of FSL imposed on motor vehicle policies so that this sector contributes in accordance with its use of fire services. The levels of user charges applied by the Fire Brigades could be reviewed to determine whether these remain adequate. The scheme could be made more transparent if insurance companies notified individual policy holders of the amount of FSL imposed on each policy and reported annually on the amount of FSL collected from policy holders.

Local councils could be advised earlier in the year of their annual contributions to the fire services.

The Committee also considered ways of improving the feasibility of alternative funding arrangements as it was required to do it the Terms of Reference.

If the Government does decide to pursue these options for alternative funding arrangements for fire services, it should be confident that this is justified for both the residential sector and commercial sectors. The Committee does not consider it prudent to introduce a new administratively complex system for the residential sector alone. This would double the administrative burden of collecting fire services funding.

As the modelling work showed that the cost of a property-based levy for residential properties would be quite low, and most householders should benefit from reduced insurance premiums, the Committee does not consider any concessions from the scheme would be necessary.

If a property-based system is introduced, it should be reviewed annually to reflect the required budget of the fire services and changed property values.

A simple property-based system also does not consider the impact of risks of fire within sectors. Unlike South Australia and Western Australia, where improvements to land are included in property valuations, there is less connection between the NSW system of property valuation and fire risk.

A risk rating factor may be appropriate as a way of reducing the impacts on the high value commercial properties although care should be taken to ensure it is cost-effective to administer.

The Committee was asked to assess how any changed system would affect Local Government's contributions to the fire services and considers that if there is such a change, these contributions should be based on the value of council land. This would mean the direct contributions from councils is reduced. This would remove the current inequity where metropolitan councils contribute in proportion to the value of land in the Local Government Area and would improve transparency for ratepayers.

The most administratively efficient means of collecting a property-based levy would be through the council rates billing system although the levy should be separately identified as a contribution to the fire services.

The Committee was also asked to determine how State Government contributions should be determined. In the modelling work, the consultants reduced the Government's direct contribution by the estimated amount of stamp duty and GST foregone by removing the levy on insurance. This reduced State Government contributions to 7.6 per cent of the funding required. Some organisations criticised the equity of this approach and queried the amount of stamp duty revenue which would be foregone. The Committee considers that if a property-based system is introduced, the State Government should continue to provide at least the same proportion of direct contributions to the fire services in recognition of the large number of State Government properties benefiting from fire services. Efforts should also be made to value State Government properties appropriately to assess whether a levy should be paid on these properties instead of a direct contribution. For instance, the Committee understands that if the Department of Housing paid a levy on its properties on current valuations, it would contribute in the order of $10 million annually. This is more than a quarter of the direct State Government contribution identified in the consultants' financial model.

## Chapter Nine

The Committee was asked to describe administrative arrangements required to introduce a new funding scheme in 2004-05 . The Committee does not consider that new arrangements could be implemented in the immediate future.

The insurance industry has advised that three months notice would be required for implementing changes although six months was provided for implementation in Western Australia. Local councils in Western Australia required 12 months to implement a change and train staff. If a motor vehicle levy is introduced, the Roads and Traffic Authority requires up to 12 months to implement administrative changes.

Any public education effort should commence as soon as possible after a decision is made to change the funding arrangements.

The transition from the current system to any new arrangements presents significant administrative challenges. Because of the different timing of rate collection to the remission of payments of levy by insurance companies, there may be a funding shortfall between the abolition of one scheme and the commencement of a new one. Unless transitional arrangements are introduced, insurance policy holders may contribute too much to fire services if a property levy is introduced while they are paying FSL on insurance. Feasible arrangements would provide for a lower rate of FSL on insurance and on a property levy in a transitional year.

Implementation costs of a new scheme are likely to be considerable. It would be appropriate for administrative costs to be provided to local councils by State Government if they are selected as collection agencies.

If new funding arrangements are introduced, it is important that the public is assured that lower costs to insurance companies and local councils are passed on. In Western Australia and South Australia, the cost of premiums was independently audited following the removal of the levy on insurance and reported to Parliament. This approach seems reasonable. Local councils should also report on reductions in rates.

The public should have the opportunity to seek information directly about the removal of the FSL from insurance policies. The insurance industry could be involved in managing this process.

## Chapter Ten

The Committee was asked to evaluate the feasibility of establishing a separate fund for fighting major bushfires. In the past decade, the two fire services have spent $243 million on fighting major bushfires and these additional unexpected costs can be difficult to manage. This option would require the collection of an additional $20 million per year for a period of three years until a reserve of $60 million was created. This option was not supported by most of the few submissions to the inquiry which commented on the proposal.

Such a fund would not affect the State's eligibility for Commonwealth natural disaster relief funding. The reserve would simply smooth out budgetary fluctuations in providing extraordinary funding following natural disasters. The regularity of providing this funding does not necessitate the creation of the reserve and planned over-collection would detract from the transparency of any funding arrangements.

# Findings and Recommendations

The Committee was asked to prepare a report evaluating both the current fire services funding arrangements and alternative funding arrangements. The findings and recommendations consider these issues in two separate parts.

Part 1 is the Committee's overall finding along with its recommendations.

Part 2 comprises the Committee's views in relation to a new funding system, should the Government wish to pursue that option further.

The findings and recommendations of Part 1 are to prevail to the extent of any inconsistency and ambiguity with those of Part 2.

## PART 1

### FINDING A

A1 The Committee finds that the current insurance-based scheme for funding fire services has provided the essential fire services with a stable and administratively simple revenue source.

A2 However, the current system is flawed because it is not universal and not all who benefit from fire services contribute to funding them. Anyone can choose not to contribute by not taking out insurance at prudent levels.

A3 In the residential sector, there is likely to be a proportion of individuals who do not insure at prudent levels but the Committee was unable to determine conclusively the scope or value of this non-insurance and under-insurance. Estimates of non-insurance range from 4.5 to 25 per cent.

A4 In the commercial sector, some organisations choose to self-insure or use deductibles. Some may choose to insure overseas and not remit FSL to the NSW Treasury as they are legally required to do.

A5 The weighting applied to the types of insurance policies used to determine the percentage of levy required from each insurance company has not been updated for some time and may not reflect the pattern of fire services activity.

A6 The amount of Fire Services Levy (FSL) levy raised from individual policies has limited connection to the benefit derived from fire services by individuals.

A7 The FSL charged on motor vehicle insurance is not in proportion to the level of fire services used.

A8 The Fire Services may not recover adequate funds to cover the costs of certain services such as attendance at false alarms or fire safety inspections.

A9 The scheme is not transparent as individual policy holders are not always informed of the amount of FSL imposed on insurance policies.

A10 There is no clear mechanism used by insurance companies to report the amount of FSL collected. In certain years, insurance companies may collect more FSL from policy holders than their liability to the fire services. In other years they may under-collect. The Committee does not find that insurance companies consistently over-collect their liability from policy holders.

A11 Local Government contributions are not always in accordance with the use of fire services in the area and it can be difficult for councils to budget for their contributions at short notice when their ability to increase rates is limited by rate pegging. They also have limited information about the level of service available in the area in the future.

**RECOMMENDATION 1** On the current evidence, the Committee recommends that the Government retain the current insurance-based system having regard to the improvements outlined in recommendation 2 below.

**RECOMMENDATION 2**: The current funding arrangements be improved by adopting the following measures:

**RECOMMENDATION 2.1** The Insurance Council of Australia increase the advisory rate of FSL imposed on motor vehicle insurance to reflect the proportion of use made of fire services by motor vehicles without increasing the total amount collected from policy holders..

**RECOMMENDATION 2.2** The Minister in consultation with relevant stakeholders review the types of insurance and weightings listed in the legislation as the basis for calculating the contribution required from insurance companies to determine whether they reflect the pattern of activity of fire services.

**RECOMMENDATION 2.3**The Government review the extent of offshore insurance by commercial policy holders and options for monitoring of FSL remissions from offshore insurance to enhance compliance with legislative requirements.

**RECOMMENDATION 2.4** Insurance companies notify individual insurance policy holders of the amount of FSL paid on policies.

**RECOMMENDATION 2.5:** The Government review the charges payable for services rendered by the NSW Fire Brigades to ensure they remain appropriate.

**RECOMMENDATION 2.6:** The insurance industry report annually on the amount of FSL collected from policy holders.

**RECOMMENDATION 3:** The Committee recommends continued investigation of funding arrangements which eliminate the flaws acknowledged in the current system.

## PART 2

Findings B to E, and related recommendations, discuss alternative arrangements for funding fire services. These are presented in accordance with the inquiry's terms of reference requiring the Committee to evaluate alternative arrangements for funding fire services.

### FINDING B

B1 The Committee finds that the majority of submissions to the inquiry supported introducing new arrangements and there is a perception in the submissions that a levy based on unimproved capital value (land value) would be the most efficient, equitable and transparent way of funding fire services.

B2 The Committee finds that detailed financial modelling shows that, in the residential sector, replacing the current insurance-based arrangements with a property-based system would broaden the base of the contributions to the fire services in this sector. However the majority of property owners currently holding insurance would be contributing only marginally less to fire services through a property levy than they currently do.

B3 In the commercial sector, a property-based system would narrow the base of those contributing funds to fire services. A significant number of property owners would be contributing a great deal more than they currently do. Further research is needed to ascertain the true impacts of this approach.

B4 Unlike South Australia and Western Australia, where improvements to land are included in property valuations, there is less connection between the NSW system of property valuation and fire risk. In the commercial sector, it would be appropriate for risks of fire to be considered as an additional basis of calculating contributions to the fire services.

B5 The Committee does not consider it efficient to introduce a new, administratively complex system for the residential sector alone.

B6 The Committee considers that it would be equitable for a levy to be imposed on motor vehicle registrations in proportion to their use of services by the two fire services and reduce the amount raised from a levy on real property by the same amount. This could be administered through the vehicle registration system.

**RECOMMENDATION 4.1** The Government should commission further research to ascertain as far as possible the impacts of introducing a property-based levy for funding fire services on the commercial property sector.

**RECOMMENDATION 4.2:** In relation to commercial properties only, the Government should explore a simple system of fire risk factors or property use factors to identify those commercial properties most at risk of fire to use in conjunction with a levy on land value.

**RECOMMENDATION 4.3:** In order to distribute the burden of funding fire services more equitably, there should also be a levy on motor vehicles to raise funds in proportion to this sector's use of fire services without increasing the total amount of funds to be raised. This should be collected by the Roads and Traffic Authority.

**RECOMMENDATION 4.4:** The property-based system should be reviewed annually to reflect the amount of revenue required to fund the fire services and changes in property values.

## FINDING C LOCAL GOVERNMENT ROLE AND CONTRIBUTIONS

C1 The Committee finds that the current arrangements for determining local council contributions to fire services are disproportionate in some cases and not transparent to ratepayers. If the insurance-based system is changed, Local Government contributions to fire services should be based on the value of council land. This would mean that the direct contributions from councils would be lower.

C2 The most administratively efficient means of collecting a property-based levy would be through the council rates billing system although the levy should be separately identified as a contribution to the NSW fire services.

**RECOMMENDATION 5.1:**Under a property-based system, Local Government should no longer be required to maintain direct contributions to the funding of fire services, but instead councils should pay a levy based on the value of their land.

**RECOMMENDATION 5.2:**The levy for a property-based system should be collected by councils at the same time as collecting rates. Such a levy should be clearly identified as a NSW fire services levy.

**RECOMMENDATION 5.3:** Local councils should be paid a suitable amount per collection. This amount should be set at a rate that adequately covers the administrative costs of collecting the levy and should be determined in consultation with the Local Government and Shires Associations.

## FINDING D STATE GOVERNMENT CONTRIBUTION

D1 The Committee finds that there are strong arguments for the State Government to continue to contribute the same proportion of funding to the fire services if a property-based system was introduced. There may be additional net costs to the Government because of reduced stamp duty collections from lower insurance costs but this is by no means certain and these funds would not be provided to the fire services.

**RECOMMENDATION 6.1:** The State Government contribution should be maintained at 14 per cent for the NSW Fire Brigades and 13 per cent for the Rural Fire Service.

**RECOMMENDATION 6.2:** The Valuer-General should value all State Government properties and provide these values to the Government within a suitable timeframe following any decision to alter the funding of fire services. Once these values are provided, the State may be required to contribute through a levy rather than a direct contribution.

## FINDING E – TRANSITIONAL ARRANGEMENTS

E1 Should the Government choose to implement a property-based levy, the Committee does not believe it is feasible to introduce the new arrangements in the immediate future.

E2 In order to assist the transition, the Committee finds that early notice to the public and the administrators of the scheme would be required.

E3 A transition to a new scheme presents significant costs and administrative challenges. Special arrangements to ensure stability of revenue for the fire services and to minimise the costs to the public during the transition are required.

E4 Unless compliance and reporting mechanisms are in place there are also risks that savings from reduced contributions are not passed on to the public by insurance companies and Local Government.

**RECOMMENDATION 7.1:** The Government should publicly announce any change to the current funding arrangements in such a way that there is adequate notice to the public of these changes.

**RECOMMENDATION 7.2:** If a property-based system is introduced, there should be a transitional period where both the old and new funding systems operate concurrently. During this period, the property levy should be paid at half the required rate, as well as any insurance policy that is renewed during the transitional period, up to and including the last day of the transitional period. Any part of the annual premium that spans the end of the transitional period should be charged FSL.

**RECOMMENDATION 7.3:** If local councils are used to collect a levy through rates, it would be appropriate for funding to be provided to implement the new arrangements.

**RECOMMENDATION 7.4:** In establishing legislation for the introduction of a property-based system, provision should be made for:

- Insurers to provide a report to the Minister and or Treasurer (depending on who is responsible for overseeing any new funding arrangements) outlining the reduction in premiums due to the abolition of the FSL, average savings to policyholders and refunds provided to policyholders in relation to policies that span the implementation date;
- Upon receipt of the report, the Minister/Treasurer is to present the report to the Auditor-General for certification;

- Upon certification from the Auditor-General the Minister/Treasurer is to table this report before both Houses of Parliament; and
- These arrangements should be reviewed after five years to determine whether they continue to be required.

**RECOMMENDATION 7.5:** The Department of Local Government is to present a report to the Minister/Treasurer on behalf of all local councils, for the applicable financial year, detailing the expected savings from each council of removing the annual fire service contribution. This report will be publicly presented prior to the commencement of a new funding system. Six months after the end of the applicable financial year, the Department of Local Government is to present an updated report to the Minister/Treasurer outlining the actual savings per local council from removing the annual fire service contribution. The Minister should take the report into account when determining the rate pegging setting for the following year.

**RECOMMENDATION 7.6:** Mechanisms should be established for policyholders to query or dispute the impact of savings from the abolition of the FSL. In the first instance, policyholders should be able to direct their concerns to the ICA. Disputes should be referred to a joint Government-industry committee for resolution.

## FINDING E FIRE FIGHTING RESERVE FUND

The Committee finds there is no administrative need to establish a separate fund for fighting major bushfires.

**RECOMMENDATION 8:** The Committee does not support the creation of a fire fighting reserve fund under current or any future funding arrangements for fire services.

# Glossary

| | |
|---|---|
| Fire services | NSW Fire Brigades and NSW Rural Fire Service |
| FSL | Fire Service Levy, a levy imposed on certain types on insurance policy by insurance companies to recover costs of their contributions to the fire services |
| ICA | Insurance Council of Australia |
| Insurance-based system | The current system of funding fire services in New South Wales where the majority of funding is provided by insurance companies. |
| Land improvements | Improvements included in the land value as determined by the Valuer-General. These are defined in section 4 of the *Valuation of Land Act 1916* as including clearing, improving soil quality and draining. |
| Land value | The unimproved capital value of land as determined by the Valuer General. This is defined in section 6A of the *Valuation of Land Act 1916*, as: The capital sum which the fee-simple of the land might be expected to realise if offered for sale on such reasonable terms and conditions as a bona-fide seller would require, assuming that the improvements, if any, thereon or appertaining thereto, other than land improvements, and made or acquired by the owner or the owner's predecessor in title had not been made. |
| Legislation | *Fire Brigades Act 1989* and *Rural Fires Act 1997* |
| Minister | Minister for Emergency Services |
| PFS | Professional Financial Services |
| Property-based system | Any system of funding fire services from a levy imposed on real estate and/or moveable property such as motor vehicles. In New South Wales, this would be based on land value. |
| Robson Review | Ken Robson, *Review of the Funding Arrangements for the Fire Service of New South Wales*, September 1994 |

# Chapter One - Introduction

1.1 In New South Wales, the two main fire services, NSW Fire Brigades and the Rural Fire Service are funded by the State and Local Governments and by a levy on insurance companies. The Committee notes that some industries and companies have private fire fighting capability that complement these services.

1.2 This inquiry was prompted by the Royal Commission into the collapse of the HIH Insurance Group which recommended “that the states that have not already done so abolish fire service levies on insurers."[1]

## THE INQUIRY

1.3 On 22 August 2003, Treasurer, the Hon Michael Egan MLC, wrote to the Committee asking it to review funding arrangements for fire services. Mr Egan provided comprehensive Terms of Reference in relation to the scope of this review and asked that the Committee report by 29 February 2004.

1.4 At its meeting on 28 August 2003 the Committee resolved to accept the Terms of Reference provided by the Treasurer and to commence the inquiry.

1.5 The Committee called for submissions by writing directly to key stakeholders and advertising in the metropolitan press. 64 submissions were received from a range of Government agencies, businesses, local councils and the public. These are available from the Committee website and are listed in Appendix 1.

1.6 The Committee held public hearings in Sydney on 21 and 26 November 2003. Because of the high level of interest in this inquiry from regional councils, the Committee held further public hearings in Queanbeyan on 27 November. A list of witnesses appearing at these hearings is included in Appendix 2. Transcripts of the evidence are available on the Committee website.

1.7 The Terms of Reference required the Committee to examine the arrangements in other States. Accordingly, the Committee visited Perth and Adelaide in February 2004 to discuss the operation of fire services funding schemes in Western Australia and South Australia. A list of organisations with which the Committee held meetings is included at Appendix 3.

## FINANCIAL MODELLING

1.8 The Terms of Reference required the Committee to commission detailed financial modelling to assess the effect of funding options on the community.

1.9 Professional Financial Solutions (PFS) were selected to perform this work by NSW Treasury and the Insurance Council of Australia.

1.10 Representatives of PFS met with the Committee a number of times to discuss options for alternative funding arrangements. An informal working party consisting of representatives from NSW Treasury, the Insurance Council of Australia and the Committee’s secretariat addressed more routine issues in relation to this project.

[1] *Royal Commission into Collapse of HIH*, recommendation 56, April 2003, available from http://www.hihroyalcom.gov.au/finalreport/

1.11 The modelling project was designed to compare the costs paid by residential and commercial property owners under the current system to the costs under a levy on property. The project relied on matching data from the Valuer-General and insurance companies. This data was provided much later than originally planned and the Committee would not have been able to consider the results of the modelling work prior to its original reporting date.

1.12 The Committee also considered it appropriate to conduct further public consultation on the outcomes of the modelling project. At its meeting on 18 February 2004, the Committee resolved to extend its reporting date until 28 May 2004.

1.13 PFS prepared an interim report for the Committee in March. The Committee launched this at a public forum at Parliament House on 29 March 2004 and sought further public comments. The Committee received 23 submissions in relation to the interim report.

1.14 The Committee held additional public hearings in relation to the modelling work on 5 and 7 May 2004 in Parliament House, Sydney. A list of witnesses appearing at these hearings is at Appendix 2.

1.15 At its meeting on 12 May 2004, in order to give a full consideration of the outcomes of these consultations, the Committee resolved to defer its reporting date until 10 June 2004. At a meeting on 23 June 2004 the Committee resolved to defer further consideration of the draft report until a meeting on 10 August when the was adopted as amended.

## STRUCTURE OF THIS REPORT

1.16 In Chapter Two the report discusses criteria for assessing taxation policy which include efficiency, equity, simplicity, stability and transparency. It describes and evaluates different taxation systems for funding services.

1.17 Chapter Three describes the institutional arrangements for providing fire services in New South Wales. Chapter Four describes the funding arrangements for fire services in New South Wales.

1.18 Chapter Five canvasses alternative ways of funding fire services used in other States and Territories. It evaluates these against taxation principles. It also describes options for funding fire services raised in submissions to the inquiry.

1.19 The current fire services funding arrangements in New South Wales are evaluated against taxation principles in Chapter Six. Chapter Seven describes the financial modelling of the impact of a property-based system for funding fire services.

1.20 Chapter Eight contains the Committee’s conclusions drawn from comparing the current system to a property-based system for funding fire services. It evaluates options for improving the current system and provides the Committee’s findings and recommendations.

1.21 As required by the Committee’s Terms of Reference, Chapter Nine describes the administrative and transitional requirements for changing to a new method of funding fire services and Chapter Ten evaluates whether there is a need to establish a Fire Fighting Reserve Fund for fighting major bushfires.

# Chapter Two - Principles of Taxation Policy

## INTRODUCTION

2.1 Point 4 of the Terms of Reference to this review asks that the Committee's proposed funding arrangements:

a. ensure, to the maximum extent possible, that all those that benefit from the provision of fire services contribute to funding the fire services;

b. broadly match funding contributions to the level of service provided to the taxpayer and/or the risk of fire affecting each taxpayer;

c. be difficult to avoid through changed taxpayer behaviour; and

d. provide a stable base for funding fire services.

2.2 As a first step in assessing proposed funding arrangements against these criteria, it may prove useful to begin with a background discussion of public finance. This chapter examines in detail the principles of public finance, beneficiary principles and concepts of public goods.

## CRITERIA ASSESSMENT

2.3 General principles of public finance state that when evaluating a tax system, certain criteria should apply. The criteria should include principles of:

- efficiency;
- equity;
- simplicity
- stability; and
- transparency.

2.4 The "appropriateness" or "acceptability" of a tax system is often compared against these principles.

### Efficiency

2.5 Taxes are considered efficient if the imposition of the tax does not distort taxpayer behaviour. The more uniform the basis of taxation, the less chance there is of creating distorting economic behaviour.

2.6 Taxes can be imposed to change or distort consumer choice, such as taxes on tobacco or liquor. Distortions of these products can be justified on the grounds that their use results in significant costs to the community through high health costs, lower productivity and even deaths.

2.7 If a product produces external costs to the community, then the use of a distortion tax can again be justified. These may be appropriate, for instance, in the case of pollution charges.

### Equity

2.8 Equity generally refers to the capacity of taxpayers to meet their tax liabilities. There are two basic concepts of equity, vertical and horizontal. Vertical equity requires progressive tax rates and is based on the premise that those with a greater capacity to contribute should pay more. Horizontal equity, on the other hand, states that individuals with a similar capacity should contribute the same amount.

### Simplicity

2.9 This refers to the level of administration and compliance costs faced by taxpayers for each dollar of revenue raised. Broad-based taxes are often cited as a good example of a simple tax to administer, given there are few exemptions available.

### Stability or flexibility

2.10 This refers to the responsiveness of the tax to changes in economic conditions. Revenue sources should be relatively stable and have growth potential.

2.11 A good tax mix should not have a large reliance on highly volatile revenue sources because of the difficulty in predicting the amount to be raised. While the revenue derived from these sources may be higher in periods of buoyancy, a heavy reliance can be detrimental in times of slowdown. The recent period of buoyancy in the housing market is a good example of a highly volatile revenue source. As a result of this buoyancy, stamp duty collections rose and may fluctuate in the short to medium term.

### Transparency

2.12 This refers to the level of openness and accountability in collecting or reporting against a specific tax. Taxes that are easily identifiable and have details published of where the funds are spent are considered transparent.

## FIRE SERVICES HAVE PUBLIC GOOD CHARACTERISTICS

2.13 The history of the fire service suggests that the presence of the Government in providing fire services has not restricted the presence of the service. Rather, it demonstrates that the involvement of the Government extended the coverage and availability of the service. Government involvement ensured that the service was more widely available, with better access for all individuals and property.

2.14 The provision of fire services, through fire prevention, suppression, management and other roles such as hazardous materials and rescues, can be viewed as a public good or service. Public goods are non-rival and non-excludable.

2.15 The concept of public goods can be broken down into either pure public goods or impure public goods. **Pure** public goods are characterised by the following features:

- Non rivalry - Where consumption by another individual will not lower another individual's consumption. Alternatively, "a good is said to be non-rival in consumption when the marginal cost of adding another person to consume the good is zero."[1]
- Non-excludability – users cannot be excluded from consuming the good.

2.16 In reality however, there are not many pure public goods (with the exception of national defence). The Government does not just allocate pure public goods. Rather, there is a considerable number of **impure** public goods, where the degree of

[1] Brown, C.V & Jackson, P.M, 1990, *Public Sector Economics*, 4th Edition, Basil Blackwell Ltd, p35

excludability and non-rivalness vary. As the Government allocates a variety of goods and services, there are different degrees of exclusion and rivalry.

2.17 Fire services can be considered non-rival in consumption until the point where there are too many people demanding fire services and there is not enough of the service, either in terms of brigades or equipment, to service the fires. As the situation may arise where there are not enough brigades to service the community, fire services cannot be considered as a pure public good.

2.18 On the point of non-excludability, fire services could once again be provided to a select group of individuals. For instance, the service could be restricted to individuals who take out insurance (as was the case in the $19^{th}$ century). This restriction could exclude individuals from accessing the service.

2.19 However, the act of excluding individuals from the service may prove too difficult or too expensive to enforce. For example it would be highly problematic for the Government to prove individuals had insurance, given the various types of insurance and the variations in the adequacy of insurance.

2.20 From a practical point of view, fire services can be viewed as a public good. However, the inherent nature of public goods results in market failure. As public goods are non-excludable, there is no incentive for private producers to supply the public good because they cannot exclude individuals from consuming the good and cannot charge for the good. The market also cannot address the free rider problem, where consumers benefit from the provision of a good or service without directly paying for it or contributing an amount equal to the benefit derived.

2.21 As such, there will be situations where individuals or businesses do not have insurance cover, or in the case of renters, do not explicitly pay councils rates (though the rates would be recouped through the rent) and so do not directly contribute to the funding of the fire service. They do, however, have access to the fire service if required. It could be argued that these individuals or businesses are free-riding on the provision of the service if they are not directly contributing through insurance or rates.

2.22 As private markets for public goods are inefficient, pure public goods are therefore generally provided through consolidated revenue in the budget. As outlined earlier, the majority of funding for fire services is not provided from the budget. Therefore, there is an argument that fire services, like that of police services, should be funded from the public sector budget. This issue is discussed later in the report.

2.23 Public goods are characterised by “externalities”, or spillovers. An externality can be simply defined as an economic cost or benefit that flows onto other parties as a result of the actions of others. Externalities can have both positive and negative characteristics.

2.24 The actual provision of the service and maintenance of the service, whether it is needed or not, is a positive benefit for the community. The protection of property and human lives, lowering the risk of harm and damage, lessening the financial costs involved in fire and rescue operations and the protection of the environment and ecosystems are all positive benefits that arise from fire services. Everyone enjoys the benefits without being excluded from utilising them.

2.25 Externalities share the pure public good characteristics of non-rivalry and non-excludability. In addition, externalities, like public goods, are an example of market failure:

> Externalities [are] nearly synonymous with the non-existence of markets. We define an externality to be a situation in which the private economy lacks sufficient incentives to create a potential market in some good and the non-existence of this market results in losses in Pareto efficiency.[2]

## WHO BENEFITS FROM FIRE SERVICES?

2.26 As noted above, the Terms of Reference ask the Committee to ensure to the maximum extent possible that all those that benefit from the provision of fire services contribute to the funding. This section will discuss whom the beneficiaries of fire services are and what benefits they derive from the service. Additionally, the section will discuss how fire services can be funded, given it can be considered as a public good, by various beneficiaries.

2.27 As with most services, provided either by the public or private sector, there are various groups or individuals who either derive an individual or collective benefit from the provision of the service or good produced.

2.28 As outlined above, the whole community benefits from fire services, either directly or indirectly. At a direct level, the main beneficiaries are:

- household property owners;
- commercial/industrial businesses;
- insurance companies;
- Local, State and Federal Governments; and
- the environment.

2.29 When fire services were first introduced in the early 1800s the main beneficiaries of the service were insurance companies. Protecting property and assets, and therefore securing wealth, was of greater importance to insurers who would have suffered considerable loss and possible financial ruin if properties were lost. There was a commercial incentive to maintain property and protect it from fire.

2.30 However, insurance companies are no longer the sole beneficiaries. While insurance companies derive a benefit from reducing the incidence of fires and damage caused to buildings from fires, the other beneficiaries listed above derive similar benefits, either individually or collectively.

2.31 For example, fire services lower the risk of people being injured from a fire, which is an individual benefit. Alternatively, the prevention of a fire in a building lowers the level of claims through insurance companies, which in turn lowers the flow on of increased premiums to policyholders.

2.32 The following table outlines the beneficiaries of fire services and examples of benefits they derive.

[2] ibid, p38

| **Who benefits** | **Benefits Enjoyed** |
|---|---|
| Households (property owners) | Maintenance/protection of capital asset;<br>Financial security;<br>Place of occupancy:<br>Lower risk of danger. |
| Businesses | Avoids loss of income;<br>Reduces pressure on increasing premiums;<br>Maintains profitability;<br>Benefits for shareholders. |
| Insurance companies | Lower level of claims;<br>Less pressure on increased premiums and hence a more affordable product;<br>Maintains profitability. |
| Governments | Lowers provision of financial assistance;<br>Supports budgetary position;<br>Less need to restore/repair damaged infrastructure;<br>Protects revenue in sectors such as tourism, timber plantations and exports. |
| Others<br>- environment<br>- social | <br>Maintenance of ecosystem and water quality (positive externality);<br>Sense of community responsibility. |

## HOW SHOULD BENEFICIARIES FUND FIRE SERVICES?

2.33 If all sectors of the community benefit from the provision of fire services, how should the service be funded? As outlined in the interstate comparison (Appendix 4), there are a number of variations amongst the jurisdictions. The comparison shows that regardless of whether fire services are considered a public good, only a minority of jurisdictions fund the service from consolidated revenue. The reason for and against this type of funding will be discussed later, as will a number of other options.

2.34 However, the main argument used by Governments against not funding through consolidated revenue is fiscal constraint. In environments of increasing demands for services and constraints on new revenue measures, Governments have used alternative options to fund fire services, rather than through the public account.

2.35 The broad funding options available for Governments to fund services include:

- general tax revenue (consolidated revenue)
- user charging;
- full cost recovery; and
- earmarked or "hypothecated" taxes.

## Consolidated revenue

2.36 As with other emergency services such as police and ambulance services, fire services could be completely provided from consolidated revenue, via general taxation arrangements. As discussed above, fire services can be considered a public good.

2.37 Fire services could be entirely funded through general taxation receipts. However, the main reason not to fund from consolidated revenue includes high budgetary impacts. For NSW, the budgetary cost is estimated to be around $513 million in 2004-05.[3] This compares to the current State funding contribution of $71 million in 2003-04. The funding out of consolidated revenue may be argued to come at the expense of other essential services such as schools and hospitals.

2.38 However, this argument can in turn be applied to police services, ambulance services and other emergency services, which are predominately funded from consolidated revenue. In the case of police services, the funding comes directly from consolidated revenue. Other emergency services such as State Emergency Services (SES) receive the majority of their funding from the Government with the remainder coming from donations, contributions and fundraising.

2.39 On the issue of taxation, two important principles should be discussed:

- the benefit principle; and
- the ability to pay principle.

2.40 The benefit principle states that individuals will contribute to a good or service where they receive a direct benefit. However, the principle suffers from the fact that taxation is not voluntary in nature. Taxpayers are required to pay taxes at a predetermined rate, regardless of any benefit they may or may not derive. If individuals could contribute only up to the point of the benefit they received, the result would be that people would state a lower benefit and therefore contribute a small amount. This would generate strategic free-rider issues.

2.41 The ability to pay principle prefers "to levy taxes on how much the individual could afford to pay."[4] As such, the principle builds in notions of equity, where unequals are treated unequally. In the case of fire services that would suggest that wealthier individuals would contribute more than would less well off individuals, even though the less well off are often more in need of such services.

2.42 On the principles of benefit taxation and ability to pay, the funding of fire services could potentially fall very short of actual funds required. Whilst these notions of taxation may appear possible in theory, in reality, funding from general consolidated revenue would better meet the needs of funding fire services.

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[3] NSW Treasury, *Budget Statement 2003-04 Budget Paper No 2*, pp3-14
[4] Brown and Jackson op cit, p300

## User charges

2.43 User charges are primarily used in the areas of public transportation and utilities, such as electricity and telephones, based on the use of the service. Those who use the service more pay more.

2.44 However, it can be argued that this approach imposes a heavier burden on lower-income groups, as user-pays charges will take a higher proportion of their income. For example people with low incomes spend a higher proportion of their income than others for access to urban physical infrastructure because demand of these services is relatively inelastic.[5]

2.45 Applying the principle of user charges, similar to billing for the use of ambulances, to fire services may prove difficult to implement. The New South Wales Fire Brigades states in its submission that its own research suggests:

> People from non-English speaking backgrounds, children, frail elderly, disabled and Aboriginal people have higher vulnerability to fire.[6]

2.46 These groups have lower socio-economic status and therefore do not contribute to fire services through insurance or council rates.

2.47 Despite the financial burden of imposing a charge on these groups and their lack of ability to pay for the service, the charging for the service:

> …may not be economically effective as charging for some services may reduce their uptake and create greater downstream costs from emergencies and risks that could have been mitigated.[7]

2.48 Again, other emergency services could likewise charge for the services provided, but it would seem contrary to the spirit of community service and could result in greater harm and more emergencies. For example, individuals are not required to pay for the attendance of a police officer at the scene of a robbery. If there was a requirement to do so, there may be higher levels of crime and unreported incidents.

2.49 It is unlikely though that user charges would cover the full costs of providing the fire service. Any attempt to fund from user charges would need an additional revenue source. For example, the Ambulance Service receives 50 per cent of funds through the Budget.

## Full cost-recovery

2.50 Full cost recovery was an issue raised in the recent Victorian review of fire services funding arrangements. Areas to address for full cost recovery could cover incidents involving property that is not insured, fire incidents outside designated fire districts, false alarms and hazardous material call-outs.

2.51 As with the user charges concept, it would not be publicly acceptable nor economically viable to impose a charge on individual properties after a fire event. In addition to the senseless nature of imposing a fee on an individual who may have lost their property, there is also the issue of the services being required to chase debt and the inability of individuals to pay.

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[5] Neutze, Max, 1997, *Funding Urban Services*, Allen & Unwin, Sydney, p127
[6] Submission No 54, NSW Fire Brigades, p19
[7] ibid, p19

2.52 Another point raised in the Victorian review was the adjustment period. The Victorian report found that:

> An appropriate adjustment period, potentially several years, would be required to achieve any significant move towards this objective.[8]

2.53 In addition, the report also stated that:

> Increased charges are also likely to require consideration of concessional rates and exemptions and enhanced debt collection processes and a public information strategy.[9]

### Earmarked taxes

2.54 Revenue raised from hypothecated taxes are identified for a particular purpose. Examples include parking space levy that is used to fund urban transport infrastructure.

2.55 The general view of hypothecated taxes is that quarantining revenue for a certain service means that some services are not subject to the same level of scrutiny or competition against other services. This decreases the flexibility of decision making and inefficient service provision or misallocation of resources may result.

2.56 Alternatively, if the level of taxes paid is equal to the charges placed on the consumer, hypothecated taxes can be seen as appropriate in determining benefit taxation.

## CONCLUSION

2.57 As outlined above, there are a number of funding arrangements available to collect revenue for providing fire services to the community. All funding arrangements outlined have advantages and disadvantages, depending on the good or service that is being provided to the community, the message that the Government is communicating to taxpayers through providing the good or service, or the role of the Government in providing the good or service.

2.58 The more advantageous options are funding through consolidated revenue or hypothecated taxes. Both options provide transparency in service provision and a linkage between taxation and benefits.

2.59 In selecting the most appropriate method for the funding of fire services, the Committee needs to consider sound taxation principles as well as who benefits from the services.

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[8] Department of Treasury and Finance, July 2003, *A Review of Victorian Fire Services Funding Arrangements*, Melbourne, p82
[9] ibid, p82

# Chapter Three - Provision of Fire Services in New South Wales

## INTRODUCTION

3.1 In this chapter, the report examines the current structural arrangements of the fire services and the work they do. It briefly describes the history of the fire services in the State and outlines the funding arrangements used in the past and how these have changed over the years.

3.2 There are four main statutory authorities in New South Wales providing fire services:

- NSW Fire Brigades
- Rural Fire Service
- State Forests of NSW
- Parks Service Division of the Department of Environment and Conservation (formerly the NSW National Parks and Wildlife Service)

3.3 Of these, the fire services of State Forests of NSW and Parks Service Division are of limited scale and funded from consolidated revenue or from the agencies' commercial activities. Funding for the NSW Fire Brigades and Rural Fire Service come from a combination of consolidated revenue, local council rate collections and a Fire Services Levy (FSL) collected on certain insurance policies. This review concentrates on these two services.

## NEW SOUTH WALES FIRE SERVICES

### NSW Fire Brigades

3.4 The NSW Fire Brigades is the seventh largest urban fire service in the world. The brigade has over 3,100 full-time firefighters and 3,300 part-time (retained) firefighters, serving at 335 fire stations across New South Wales.[1]

3.5 The brigade is responsible for protecting 90 per cent of the State's population from fire emergencies, motor vehicle accidents and other dangerous situations. The service also protects 100 per cent of the population from hazardous material emergencies and building collapses. In 2002-03 the brigade responded to over 128,000 fire, hazardous materials (hazmat) and rescue emergency calls.[2]

3.6 NSW Fire Brigades is responsible for metropolitan fires and fires in larger country cities and towns, generally with a population of 1,000 or more. Members are paid fire fighters, either full time employees or part time "retained" fire fighters who are only paid when they attend a fire.

3.7 The main services provided by the NSW Fire Brigades include:

- Fast response capability to undertake rescue and minimise damage and risk in events such as fire, explosion, motor vehicle accident, building collapse, hazardous material release, agricultural emergencies;

[1] Submission No 54, NSW Fire Brigades, p15
[2] ibid, p15

biological/chemical/radiological threat, flood, storm etc – all day everyday to everyone; and

- Research, planning, education, training, information, expert advice and salvage assistance to prevent and prepare for emergencies and aid recovery from emergencies.[3]

3.8 The following table provides statistics on the number of incidents NSW Fire Brigades has responded to over the past five years.

| | 1998-99 | 1999-2000 | 2000-01 | 2001-02 | 2002-03 |
|---|---|---|---|---|---|
| **Fires and Explosions** | | | | | |
| Structural fires | 7,985 | 7,684 | 8,230 | 8,252 | 7,784 |
| Outside storage fires | 788 | 453 | 485 | 454 | 446 |
| Mobile property fires | 6,321 | 6,207 | 6,706 | 6,496 | 5,138 |
| Trees, shrubs and grass fires | 7,624 | 8,035 | 14,958 | 14,360 | 13,511 |
| Rubbish fires | 7,079 | 7,804 | 9,979 | 9,086 | 8,159 |
| Other fires | 360 | 532 | 281 | 265 | 248 |
| **Total fires** | **30,157** | **30,715** | **40,639** | **38,913** | **35,286** |
| **Other Emergencies and Incidents** | | | | | |
| Overpressure ruptures | 316 | 159 | 208 | 177 | 174 |
| Non-fire rescues calls | 5,713 | 5,869 | 6,522 | 6,995 | 7,527 |
| Hazardous conditions | 12,337 | 12,114 | 11,478 | 12,350 | 12,258 |
| Service/salvage calls | 4,849 | 3,914 | 4,705 | 5,106 | 4,419 |
| Good intent calls – false alarms | 7,784 | 8,297 | 9,538 | 9,788 | 8,852 |
| False calls – malicious | 6,776 | 6,300 | 6,612 | 6,220 | 6,413 |
| System initiated false alarms | 42,865 | 46,870 | 43,905 | 46,126 | 50,503 |
| Other emergencies and incidents | 2,084 | 5,294 | 2,703 | 2,245 | 2,799 |
| **Total** | **82,724** | **88,817** | **85,664** | **89,007** | **92,945** |
| **Total fires and emergencies** | **112,881** | **119,532** | **126,302** | **127,920** | **128,231** |

Source: Submission No 54, NSW Fire Brigades, p18

[3] ibid, p15

3.9 The service and value for money provided by the NSW Fire Brigades was outlined by Commissioner Mullins in evidence:

> **Mr MULLINS:** During 2002-03 we responded to more than 128,000 emergency calls. Our net cost of services was $350.5 million, which equates to $52.79 per person in New South Wales or just 14.4¢ per person per day. I think that this demonstrates good value for money. For example, by comparison the annual cost of an NRMA basic care membership that entitles the user to four on-call roadside assist services, including towing for less than eight kilometres, is $111.50 per year, including a $44 joining fee. That service does not guarantee fast response times or manage risk to life and property and access to the service is limited to four times per year. In comparison the two fire services together cost $80.30 per person in New South Wales in 2002-03 for unlimited fast and far more dangerous service delivery.[4]

## Rural Fire Service

3.10 The Rural Fire Service is the world's largest fire service. The service has a combined membership of 67,058 volunteers in New South Wales, operating at 2,099 fire brigades in approximately 139 rural fire districts (areas outside fire districts form rural fire districts which generally follow local council boundaries).[5]

3.11 The service has responsibility for fire prevention and suppression in over 90 per cent of the state and 10 per cent of its population. In addition to bush fires, the Rural Fire Service also attend road accidents, assist in search and rescue operations, provide assistance during storms and floods and are responsible for structural fires in 1,200 towns and villages in the state.

3.12 Appendix 5 details the regional boundaries for the Rural Fire Service.

3.13 The following table provides statistics on the number of incidents responded to by the Rural Fire Service for 2002-03.

| | **Region North** | **Region East** | **Region South** | **Region West** | **Total** |
|---|---|---|---|---|---|
| **Incident Type** | | | | | |
| Bushfire | 1,273 | 2,866 | 920 | 583 | 5,642 |
| Grassfire | 383 | 1,071 | 375 | 225 | 2,054 |
| Building fire | 140 | 296 | 147 | 88 | 671 |
| Vehicle fire | 190 | 950 | 171 | 101 | 1,412 |
| MVA | 625 | 1,495 | 558 | 236 | 2,914 |
| False alarm | 155 | 1,082 | 141 | 68 | 1,446 |
| Other incidents | 948 | 4,043 | 917 | 334 | 6,242 |
| Total | 3,714 | 11,803 | 3,229 | 1,635 | 20,381 |

Source: Information provided to the Public Accounts Committee Secretariat from Rural Fire Service, as per 2002-03 Annual Report.

[4] Greg Mullins, Commissioner, NSW Fire Brigades, Transcript of Hearing, 26 November 2003, p1
[5] Submission No 55, Rural Fire Service, p1

# HISTORY OF FIRE SERVICES IN NEW SOUTH WALES

## NSW Fire Brigades[6]

3.14 Insurance companies originally established fire services in New South Wales. The Australian Insurance Company (established on 1 May 1836) was the first insurance company to provide a small brigade of around seven to eight men to attend fires.

3.15 Further insurance brigades, such as Alliance Insurance Company and Imperial Companies, were formed. A small group of insurance brigades operated in the city until the increased fire risk necessitated the amalgamation of the small units into the Insurance Companies Fire Brigade (later called the Sydney Fire Establishment). The creation of a single insurance brigade was still not a universal service and only attended premises that displayed plaques or firemarks from the affiliated insurance companies.

3.16 It was the selective nature of the insurance fire brigades that raised the need for a true public fire service. A Bill was introduced to the Legislative Council on 10 October 1854 to form a fire brigade within the City of Sydney. The brigade was to be funded by a levy on all property in the City according to its assessed annual value of one penny in the pound as well as contributions from insurance companies (£1,000 annually). However, the Bill did not progress beyond the second reading speech because of a lack of support.

3.17 Despite the failure of the legislation, in October 1854 the first volunteer brigade, Victoria Volunteer Fire Company No 1, was formed. The brigade grew from the Victoria Theatre Fire Company, which was formed soon after the Royal Theatre fire of 1840. The proprietor of the theatre moved to the adjacent Victoria Theatre and purchased an engine that appeared at several fires during the 1840s.

3.18 Members of the brigade paid fees to join the brigades and other funds were raised by fundraising and subscriptions from insurance companies.

3.19 Fire services continued to be provided by the two services until the 1883 Fire Brigades Bill was introduced by the Stuart Government. It was amended extensively before it was enacted. On 14 February 1884 the Metropolitan Fire Brigades were formed.

3.20 The decision to form one fire brigade resulted from public complaints about the adequacy of water supply and the equipment and efficiency of the two services in light of the growing population of the city. Tension between the two services also grew and there were cases of axes being drawn between the volunteer companies and the Insurance Brigade.

3.21 In 1910 the Board of Fire Commissioners of New South Wales was formed. This Board was the central fire authority and replaced the Metropolitan Fire Brigade and other fire boards in New South Wales. The Board was responsible for fire service provision in Sydney and other urban areas of New South Wales (the Act actually applied to 41 metropolitan municipalities, 85 municipalities and parts of 6 shires).

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[6] Information regarding the history of the NSW Fire Brigades was sourced from: Adrian, Colin, 1984, *Fighting Fire: A Century of Service, 1884 – 1984*, George Allen and Unwin, Sydney

3.22 The service continues today and is constituted under the *Fire Brigades Act 1989*. The current fire service is known as the NSW Fire Brigades.

### Rural Fire Service[7]

3.23 Up to the early 1900s, rural fire services were rather haphazard, with no formal collective group. The *Local Government Act 1906* authorised local councils to form brigades and to prevent bushfires. These provisions were carried forward into the *Local Government Act 1919*.

3.24 The Bush Fire (Emergency) Committee was formed in 1945. This Committee recommended enactment of the *Bush Fires Act 1949* which established a Bush Fire Fighting Fund. This fund allowed local councils to purchase fire equipment for their area. This fund is the same fund that the insurance companies, local councils and State Government contribute to today, except the name has been changed to the Rural Fire Fighting Fund.

3.25 In the 1970s the *Bush Fires Act 1949* was amended due to the large number of statutory and volunteer organisations involved in firefighting. The Committee was reformed into the Bush Fire Council, which included representatives from all organisations.

3.26 In 1990, the Department of Bush Fire Services was set up to administer the NSW Minister for Emergency Services' responsibilities under the Bush Fires Act. NSW Bush Fire Brigades was renamed as the NSW Bush Fire Service. This later became known as the Rural Fire Service.

3.27 The current Rural Fire Service was proclaimed in September 1997, under the *Rural Fires Act 1997*. The Act was introduced following the coronial inquiries from the 1993-94 bushfires. Amongst a number of recommendations by the Senior Deputy State Coroner, Mr John Hiatt, was the proposal to amalgamate NSW Fire Brigades and the Bush Fire Service. The recommendation was later rejected by the then Minister for Emergency Services, the Hon Bob Debus MP, on 28 February 1996.

## HISTORY OF FUNDING FIRE SERVICES IN NEW SOUTH WALES

### NSW Fire Brigades[8]

3.28 As outlined above, the funding for metropolitan fire services in New South Wales was provided by insurance companies and, later, from municipal councils. The establishment of the Metropolitan Fire Brigade in 1884 was funded by contributions from fire insurance companies, councils and Treasury in equal proportions.

3.29 Insurance company contributions were based on a percentage of the amount they held at risk on fire insurance policies within the metropolitan areas. Council funding was determined on a pro rata apportionment of the assessed rateable property situated in each council.

[7] Information regarding the history of the Rural Fire Service was sourced from: Rural Fire Service Web Site, www.rfs.nsw.gov.au (accessed 16 January 2003) and Submission No 42, Local Government Association of NSW and Shires Association of NSW

[8] Information regarding the history of funding the NSW Fire Brigades was sourced from: Adrian, Colin, op cit and Submission No 42, Local Government Association of NSW and Shires Association of NSW

3.30 Funding arrangements remained at the same level following the establishment of the Board of Fire Commissioners of New South Wales in 1910. It was not until the introduction of the *Fire Brigades (Amendment) Act 1927 (No.4)* that funding splits were altered.

3.31 Insurance companies were given two additional insurance representatives on the Board, but were required to increase their contribution from 33.3 per cent to 50 per cent. Additionally, contributions from local councils and the NSW Government decreased to 25 per cent each.

3.32 Arrangements continued until the *Fire Brigades Act 1956* changed the funding splits to 75 per cent from the insurance companies, 12.5 per cent from local councils and 12.5 per cent from the Government.

3.33 The *Fire Brigades Act 1989* again altered the funding arrangements. Local councils are now required to contribute 12.3 per cent, the State Government contribution increased to 14 per cent and the insurance contribution decreased slightly to 73.7 per cent.

**Funding Of Fire Brigades From 1884 To 2004**

| | Insurance Companies % | Local Councils % | State Government % |
|---|---|---|---|
| 1884 – 1926 | 33.3 | 33.3 | 33.3 |
| 1927 – 1949 | 50.0 | 25.0 | 25.0 |
| 1950 – 1989 | 75.0 | 12.5 | 12.5 |
| 1989 - | 73.7 | 12.3 | 14.0 |

Source: Submission No 49, NSW Treasury, p6

## Rural Fire Service[9]

3.34 The *Bush Fire Act 1949* established a state-wide organisation for bush fire prevention. The Department of Local Government administered the financial provisions. In addition to outlining equipment and training requirements, the Act also specified the funding contributions. Funding splits between local councils, State Government and insurance companies were 25 per cent, 25 per cent and 50 per cent respectively.

3.35 The *Rural Fires Act 1997* altered the funding contributions. Insurance companies funding increased to 73.7 per cent, while the contributions from local councils and the State Governments were reduced to 12.3 per cent and 14 per cent respectively.

3.36 Recent amendments to the Act have increased the funding contributions for local councils to 13.3 per cent and State Government contributions have decreased to 13 per cent. This change in the funding contributions was due to the transfer of Fire Control Officers from local councils to the Rural Fire Service. The control of the brigades became a function of the Rural Fire Service.

[9] Information regarding the history of funding the Rural Fire Service was sourced from: Submission No 42, Local Government Association of NSW and Shires Association of NSW

| Funding Of Rural Fire Service From 1949 To 2004 | | | |
|---|---|---|---|
| | **Insurance Companies** % | **Local Councils** % | **State Government** % |
| 1949 – 1994 | 50.0 | 25.0 | 25.0 |
| 1994 – 2001-02 | 73.7 | 12.3 | 14.0 |
| 2001-02 - | 73.7 | 13.3 | 13.0 |

Source: Submission No 49, NSW Treasury, p6

# Chapter Four - Fire Services Funding Arrangements in New South Wales

## INTRODUCTION

4.1 In this chapter, the report examines the current funding arrangements for New South Wales fire services and how the budgets for the services are established. It also examines the reasons for taking out insurance and the effect the Fire Service Levy has on the cost of insurance.

4.2 The current funding arrangement for fire services in New South Wales is an insurance-based system. The funding of the services is predominantly collected through statutory contributions, of which the Fire Services Levy (FSL) is the largest component. Insurance companies pass on these costs to policy-holders by collecting a levy on certain insurance policies.

## CURRENT FIRE SERVICES FUNDING ARRANGEMENTS

4.3 The total level of funding for fire services in 2002-03 was $505 million. For 2003-04 estimated revenue is $514 million, representing a 2 per cent growth in funding. The forward years are expected to remain relatively flat.[1]

4.4 The NSW Fire Brigades and Rural Fire Service are funded from the following sources:

- statutory contributions from insurance companies, local councils and State Government;
- miscellaneous charges (incl. false alarm charges, Hazmat calls, testing of equipment and training);
- contributions from Commonwealth; and
- offshore contributions.

4.5 The level of funding for the NSW Fire Brigades and Rural Fire Service respectively for the financial years 2000-01 to 2002-03 is detailed below.

[1] NSW Treasury, Budget Statement 2003-04, Budget Paper No.2, NSW Treasury, p3-14

| **NSW Fire Brigades Funding 2000-01 to 2002-03** | | | | | | |
|---|---|---|---|---|---|---|
| **Funding Source** | **2002-03** | | **2001-02** | | **2000-01** | |
| | **$'000** | **% - All sources** | **$'000** | **% - All sources** | **$'000** | **% - All sources** |
| **Statutory Contributions** | | | | | | |
| Insurance companies | 275,775 | 68.3 | 264,143 | 69.5 | 239,248 | 70.2 |
| Local Government | 48,532 | 12.0 | 43,503 | 11.4 | 40,266 | 11.8 |
| State Government | 51,914 | 12.9 | 49,471 | 13.0 | 44,523 | 13.1 |
| Total statutory contributions | 376,221 | | 357,117 | | 324,037 | |
| **Other contributions** | | | | | | |
| Others * | 6,196 | 1.5 | 6,861 | 1.8 | | |
| NSW OCA-Olympic urban domain | | | | | 825 | 0.2 |
| **Directly charged services** | | | | | | |
| Commonwealth Government | 3,344 | 0.8 | 2,312 | 0.6 | 2,562 | 0.8 |
| False alarms | 2,546 | 0.6 | 723 | 0.2 | 949 | 0.3 |
| Monitoring alarms | 9,238 | 2.3 | 6,077 | 1.6 | 5,141 | 1.5 |
| Education (Comsafe) | 1,267 | 0.3 | 1,200 | 0.3 | 872 | 0.3 |
| Hazardous materials | 20 | 0.0 | 17 | 0.0 | 5 | 0.0 |
| Interest from Treasury | 2,207 | 0.5 | 845 | 0.2 | 1,144 | 0.3 |
| Property Rentals | 431 | 0.1 | 527 | 0.1 | 419 | 0.1 |
| Insurance Adjustment | 335 | 0.1 | 3,535 | 0.9 | 3,611 | 1.1 |
| Fees for service to other Depts | 116 | 0.0 | 331 | 0.1 | 276 | 0.1 |
| Underwriting contributions (prior period) | 1,449 | 0.4 | | | | |
| Commissions | 20 | 0.0 | 16 | 0.0 | 20 | 0.0 |
| Sundry Items | 147 | 0.0 | 409 | 0.1 | 814 | 0.2 |
| **Total other revenue** | **27,316** | | **22,853** | | **16,638** | |
| **Total funding** | **403,537** | | **379,970** | | **340,675** | |

* Relates to funding received as a result of the declaration of an emergency under Section 44 (offset by equivalent expenditure)
Source: Correspondence from NSW Fire Brigades, provided 5 November 2003

| Rural Fire Service Funding 2000-01 to 2002-03 | | | | | | |
|---|---|---|---|---|---|---|
| **Funding Source** | **2002-03** | | **2001-02** | | **2000-01** | |
| | **$'000** | **% - All sources** | **$'000** | **% - All sources** | **$'000** | **% - All sources** |
| **Statutory Contributions** | | | | | | |
| Insurance companies | 88,979 | 37.0 | 83,338 | 48.1 | 67,051 | 73.0 |
| Local Government | 16,057 | 6.7 | 15,039 | 8.7 | 11,190 | 12.2 |
| State Government | 15,695 | 6.5 | 14,700 | 8.5 | 12,737 | 13.9 |
| Total statutory contributions | 120,731 | | 113,077 | | 90,978 | |
| **Other contributions** | | | | | | |
| Others * | 116,980 | 48.7 | 58,573 | 33.8 | | |
| Grants – other ** | 225 | 0.1 | 225 | 0.1 | 255 | 0.3 |
| Other revenue # | 2,498 | 1.0 | 1,553 | 0.9 | 598 | 0.7 |
| **Total other revenue** | **119,703** | | **60,351** | | **853** | |
| **Total funding** | **240,434** | | **173,428** | | **91,831** | |

*Relates to grants from NSW Fire Brigades and Natural Disaster Welfare Relief emergencies declared under section 44 of the *Rural Fires Act 1997*.
**Relates to grants provided by the NSW Fire Brigades
#Includes items such as sale of minor goods and services, development applications and minor services to other agencies.
Source: Correspondence from Rural Fire Service, provided 5 November 2003

## STATUTORY CONTRIBUTIONS

4.6 The largest component of funding for fires services comes from statutory contributions. The *Fire Brigades Act 1989* and the *Rural Fires Act 1997* outline the contributions for the funding of the services from each of the three bodies.

| **Contributors** | **NSW Fire Brigades** | **Rural Fire Service** |
|---|---|---|
| Insurance companies | 73.7% | 73.7% |
| Local councils | 12.3% | 13.3% |
| State Government | 14.0% | 13.0% |

4.7 Funding for the NSW Fire Brigades is determined each year by the Minister for Emergency Services in consultation with the Treasurer for the following financial year, as outlined in section 45 of the *Fire Brigades Act 1989*. Funding levels are determined a year in advance, with adjustments for over and under expenditure made where required. In evidence, the Insurance Council of Australia (ICA) noted that these adjustments evened out over time:

> **Mr MASON:** To be completely up-front, the Victorian Government review highlighted something we highlighted to it in our submission; that is, that the methodology for calculating the fire service levy is fundamentally flawed because the system itself is flawed. Therefore, depending on what is happening in the insurance market, insurance companies either under or overcollect what they need to give to the fire brigades at any given point in time. The Victorian review involved a desktop calculation and came up with a number suggesting the insurance industry overcollected by $50 million. We have been through that with most of our major members in Victoria, and over time, if we take a longer view, there is little doubt that last year companies generally overcollected because of the rising commercial insurance market. In previous years it was exactly the reverse. Over a 10-year spread, companies have found that they neither under nor overcollect, other than by very marginal amounts.[2]

4.8 Funding contributions under the Act are required in quarterly instalments, paid on or before 1 July, 1 October, 1 January and 1 April.

4.9 For the Rural Fire Service, the Minister is again required to provide information to the Treasurer, under section 103 of the *Rural Fires Act 1997*, concerning the estimated rural fire brigade expenditure, taking into regard information provided by councils for the next financial year.

4.10 Similar to NSW Fire Brigades, funding contributions for the Rural Fire Service are required in quarterly instalments, paid on or before 1 July, 1 October, 1 January and 1 April, as outlined in the Act.

## Contributions from insurance companies

4.11 Of the statutory contributors, insurance companies provide most funding. Section 54 of the *Fire Brigades Act 1989* and section 111 of the *Rural Fires Act 1997* specify that insurance companies must contribute 73.7 per cent to the fund for each financial year.

4.12 Early in a new financial year each insurance company is required to report to the fire services their actual level of gross premiums for the previous financial year.[3] Fire services aggregate the premium amounts and then advise individual insurers what their share of the total market is. Only certain types of insurance premiums are counted for this purpose and only certain proportions of this income. The shares are then applied to each insurer's portion of the budgets for the two fire services for the new financial year. For example, if $300m was required from all insurance companies, if one insurance company provided a statement showing they had written relevant premiums equating to 5 per cent of the market, it would be required to pay $15 million to the fire services.

4.13 Contributions are adjusted once actual premiums written are declared for the previous financial year. The table below shows the types premiums and weightings on them used to assess each company's liability.

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[2] Alan Mason, Executive Director, Insurance Council of Australia, Transcript of Hearing, 21 November 2003, p16

[3] Submission No 45, Insurance Council of Australia, p7

| Classes of policies of insurance | Proportion of premiums subject to contribution (%) |
|---|---|
| 1. Any insurance of property including consequential loss (but not including any insurance of a class specified elsewhere in this Schedule | 80 |
| 2 Houseowners and householders, however designated (buildings or contents or both) | 50 |
| 3 Personal combined on personal jewellery and clothing, personal effects and works of art | 10 |
| 4 Motor vehicle and motor cycle | 2.5 |
| 5 Marine and baggage—any insurance confined to maritime perils or confined to risks involving transportation on land or in the air, including storage incidental to transportation by sea, land or air, but not including *static risks (which are to be declared under Item 1) [Note: *static risks includes all movements of goods and/or stock and/or material associated with processing or storage operations at any situation | 1 |
| 6 a)Combined fire and hail on growing crops<br>b) Livestock | 1 |
| 7. Aviation hull | Nil |
| 8. Any insurance solely covering:<br>(a) Loss by theft<br>(b) Plate glass<br>(c) Machinery—confined to mechanical breakdown and/or consequential loss arising from mechanical breakdown<br>(d) Explosion or collapse of boiler and pressure vessels—confined to damage other than by fire<br>(e) Inherent or latent defects—confined to damage and/or consequential loss arising out of defective design, defective workmanship or defective materials but excluding any damage or consequential loss arising from fire | Nil |

Source Schedule 1 *Fire Brigades Act 1989* and Schedule 2 *Rural Fire Services Act 1997*

4.14 Insurance companies contribute to the funding of the fire services by imposing a levy on certain insurance types, known as the Fire Services Levy (FSL). The FSL is not outlined in the relevant Acts, but is described as "a mechanism put in place by insurers to collect the tax from their customers."[4] The rates applying to different insurance products are, however, decided by individual insurance companies, based on advice from the ICA. The Council has advised the Committee that:

> It is the individual responsibility of insurers to remit FSL payments to the fire services and to calculate how they recoup these funds from insureds. While ICA provides advisory rates for insurers to apply, these are for information purposes only. We are aware that some insurers choose to apply the ICA advisory rates while others do not. We do not monitor the extent to which insurers do or do not apply the ICA advisory rates.[5]

4.15 The recommended FSL rates only apply to certain types of insurance which the ICA advise are the major classes of business.[6] The ICA's recommended FSL rates over the past five years and the current rates recommended for 2004 for the various insurance products are:

4 ibid, p8
5 Supplementary Submission No 61, Insurance Council of Australia, p3
6 ibid, p2

| Insurance Type | 1999 Levy % | 2000 Levy % | 2001 Levy % | 2002 Levy % | 2003 Levy % | 2004 Levy % |
|---|---|---|---|---|---|---|
| Fire/Industrial Special Risk/Consequential Loss | 39 | 36 | 36 | 34 | 30 | 24 |
| Contractors All Risks (excluding public liability) | 39 | 36 | 36 | 34 | 30 | 24 |
| Householders and House Owners | 19 | 19 | 19 | 18 | 17 | 14 |
| Motor | 1 | 1 | 1 | 1 | 1 | 1 |

Source: Submission No 49, NSW Treasury, p7, correspondence from ICA 12 February 2004

4.16 Although the advisory rates in 2004 have reduced for most classes of insurance, the FSL is expected to raise necessary funds for the slight increases in the fire services' budgets.

4.17 Determining FSL rates is complex. With the tax base being the insurance premium, attaching rates to the premiums a year in advance is inherently difficult because of fluctuations in premiums and the market.

4.18 Each insurer's share of the FSL is a derivative of their premiums as a percentage of total premiums from the previous year. These shares are applied to the fire service budgets and from that insurers know their contribution to each fire service for that year.

4.19 In deciding FSL rates, insurers must take account of different classes of property insurance. Insurers differentiate premium income between domestic and commercial risks when reporting to fire services. When the services provide the information back to the insurers they outline what share of each total premium amount is made up of domestic premiums and commercial premiums. These percentages are then applied to calculate the FSL rates for either domestic or commercial premiums for that year.

4.20 The amount of FSL collected for NSW Fire Brigades and the Rural Fire Service has grown over the past few years. The level of FSL collections for the past five years for both fire services is outlined below.

| Year | NSW Fire Brigade $M | Rural Fire Service $M |
|---|---|---|
| 1998-99 | 217 | 52 |
| 1999-2000 | 227 | 59 |
| 2000-01 | 239 | 67 |
| 2001-02 | 264 | 83 |
| 2002-03 | 276 | 89 |

Source: Figures for 1998-99 to 2001-02 are taken from New South Wales Budget Papers. Figure for 2002-03 was provided in correspondence to the Public Accounts Committee Secretariat from NSW Treasury on 22 January 2004.

4.21 NSW Treasury advised the Committee that the amount of FSL collected from the four insurance types is roughly spread evenly between households and commercial sectors:

> Applying the ICA recommended rates to industry premium income indicates that 6 per cent of the levy is collected from motor vehicle policies, while 48 per cent is collected from commercial insurance policies and the 46 per cent from household policies.[7]

4.22 This division between the commercial and residential sectors has varied over time. The ICA advised the financial modelling consultants that in 2003, 56 per cent of the total FSL was paid on commercial premiums and 44 per cent from residential.[8]

4.23 Section 80 of the *Fire Brigades Act 1989* requires insurance companies to state on the premium notice what proportion of the premium is attributable to the levy. However, in recent times insurance companies have not stated the levy contribution on the premium due to the uncertainty of the actual amount contributed. The Committee heard in evidence that:

> **Ms STAGNITTA:** Historically we have included a note as to how much in dollar terms that levy has been. Under legal advice we removed that from all our documentation on the basis that, although we were calculating a set percentage, we had no way of knowing whether that was the correct amount we needed to collect.[9]

## Contributions from local councils

4.24 Contributions from local councils vary between the two services. The NSW Fire Brigades receives 12.3 per cent from local councils. The exception is under section 50 (2) of the Act where a fire district includes a reserved area. In this instance, Parks Service Division is required to provide the 12.3 per cent.

4.25 Funding contributions will depend if the council is located within the Greater Sydney Area (GSA). Section 51 of the Act specifies that if a fire district is made up of more than one Local Government Area, the amount of the contribution to be paid by each area will be apportioned according to the current 5-year average of the aggregated land values of all rateable land in the Local Government Area.

4.26 In a submission from Ku-ring-gai Council, the difference contributed from various councils was examined. The amount contributed through the fire levy was $1,788,717 for Ku-ring-gai, compared to $964,343 for Blacktown. The submission stated that:

> The application showed that Ku-ring-gai pays nearly double the contribution, 5 times more per household and 19 times more per incident than that Council. This is the case even though Blacktown has 2 ½ times the population, 15 times more fires, 6 times more incidents and 2 ½ times more incidents per capita.[10]

4.27 The large difference between the two councils is based on the value of land in each council. The value of land in the Ku-ring-gai area is higher compared to land values in Blacktown.

4.28 In other parts of New South Wales, Local Government contributions to the NSW Fire Brigades reflect the estimated cost of operating the brigade in a council's area. NSW

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[7] Submission No 49, NSW Treasury, p8
[8] Professional Financial Solutions, Final Submission, *Quantitative Modelling of NSW FSL Funding Methods* p25
[9] Leanne Stagnitta, National Home Products Manager, Insurance Australia Group, Transcript of Hearing, 21 November 2003, p7
[10] Submission No 3, Ku-ring-gai Council, p3

Treasury estimates that contributions from councils outside the GSA will increase on average by around 1.1 per cent for 2003-04.[11]

4.29 For the Rural Fire Service, the Local Government contribution is 13.3 per cent. Councils bid for funds from the Rural Fire Fighting Fund (RFFF) in order to equip and operate the rural fire brigade in that area.

4.30 Under section 103 of the *Rural Fires Act 1997,* the Minister is required to prepare an estimate of the probable rural fire expenditure for the next financial year taking into account information made available by councils. For the bidding process, funds are linked to the calculation of the total size of the RFFF based on information provided to the Minister from local councils regarding their budgetary requirements.

4.31 The actual allocation of funds to local councils is based on their bids and the standards of fire cover which link the level of resources necessary to protect an area based on its fire risk.

4.32 Under section 109(3) of the *Rural Fires Act 1997,* a council can be exempt from contributing to the RFFF if the Local Government Area has negligible danger from a bushfire. If the council area is exempt, it cannot receive any payment out of the fund for rural fire fighting expenditure under section 118.

4.33 It is important to note that councils can, and many do, contribute more to the funding of local brigades. Councils can impose additional levies on ratepayers to fund brigades, by way of an increase in their general levy on ratepayers, as outlined in section 110 of the *Rural Fire Act 1997*.

### Contributions from State Government

4.34 For the NSW Fire Brigades, the State Government is required to contribute 14 per cent to the total funding allocation.

4.35 Under section 108 of the *Rural Fires Act 1997,* the State Government is required to contribute 13 per cent. The total amount of the RFFF is determined by the size of the Government contribution. When the State contribution is agreed then the total amount available for the RFFF for that year will be 7.69 times the State's contribution.

## MISCELLANEOUS CHARGES

4.36 While this revenue source is small compared to the statutory contributions, it is of relevance to NSW Fire Brigades. The fire brigades are entitled to charge for certain services under section 42 of the Act for such things as inspections, fire prevention advice, training courses, false alarms and other activities. Revenue from these sources account for less than 5 per cent of total funding for the NSW Fire Brigades. The Committee heard in evidence:

> **Mr PAUL McLEAY:** In what other circumstances do you charge for attending fires or other emergencies to which you have been called?
>
> **Mr MULLINS:** Under our Act we have the ability to charge people for attending hazardous materials spillages where there is no risk of fire. To give an example of that, if a petrol tanker rolled over and spilled petrol everywhere there is a clear risk of explosion and fire, so there is no charge for that. But if a tanker full of pesticides rolled over and spilled the

[11] Submission No 49, NSW Treasury, p8

pesticides everywhere, there is no risk of explosion or fire. Potentially we can recover our costs of response and the operations.

**Mr PAUL McLEAY:** What about false alarms?

**Mr MULLINS:** We charge the owners of premises who have automatic fire alarm systems for the third and subsequent false alarm in any six-month period. The intention of that is to encourage the building owners to service their systems and make sure they work properly, rather than revenue raising. It is an area in which we are trying to reduce the amount we collect by working with those people to make sure that the systems do what they are meant to do.

**Mr PAUL McLEAY:** Do you only charge commercial entities fees, or do you charge residential owners fees as well?

**Mr MULLINS:** Under the Building Code of Australia a block of flats, depending on the size, would be required to have a fire alarm system or sprinkler system, and they are charged the same as a commercial entity. We regularly receive requests to waive charges. We investigate each of those requests, and if they can show that they are making efforts to reduce the number of false alarms we are quite prepared to waive those charges.[12]

4.37 Under the *Fire Brigades (Charges) Regulation 2000,* false alarms are charged $250 for second and subsequent false alarms. Call outs to hazardous materials are charged various amounts depending on staff numbers and the ranks of staff in attendance as well as equipment used.

4.38 The Rural Fire Service does not charge for attending false alarms or other events, even though they do have a response requirement:

**Mr KOPERBERG:** We do respond because, in addition to being responsible for bushfire protection, we also provide fire services to some 1,200 towns and villages throughout New South Wales—those areas not covered by New South Wales Fire Brigades.[13]

## COMMONWEALTH AND OFFSHORE CONTRIBUTIONS

4.39 The NSW Fire Brigade is funded for attending fires on Commonwealth land. The Committee heard in evidence that:

**Mr MULLINS:** We have an agreement with the Federal Government by which we identify each year our responses to Federal Government property, and on that basis there is a formula by which that Government remits funds to us, or basically buys those services from us. That includes places like Federal Government airports, defence establishments, Federal Government departments, et cetera.

**Mr STEVE WHAN:** Does the Federal Government remit on the basis of services you provide?

**Mr MULLINS:** May I check on that, because it has changed over the last couple of years and there has been a lot of negotiation. In years gone by it was a lump sum, but now I believe it is based on the number of responses and the services we provide. I have had that matter clarified. It is now based on the services we provide, so it is retrospective if you like. It is about $2.5 million per year. In Western Australia, with the new levy over there, they do exactly the same: it is retrospective based on what services they provide.[14]

[12] Greg Mullins, Commissioner, NSW Fire Brigades, Transcript of Hearing, 26 November 2003, p8
[13] Phillip Koperberg, Commissioner, Rural Fire Service, Transcript of Hearing, 26 November 2003, p10
[14] Greg Mullins, Commissioner, NSW Fire Brigades, Transcript of Hearing, 26 November 2003, p8

4.40 Under both Acts, property owners who hold property and insure with a foreign insurer are still required to contribute to the funding of the fire service. Under normal arrangements, the insurer is usually liable for the payment of the FSL (including brokers and other insurance intermediaries that utilise overseas insurers). However, in situations where insurance is undertaken with a foreign insurer, provisions of the Act require the property owner to contribute directly to the fund. On this point the ICA submission noted that:

> …in the age of the internet and multinational companies it may not be possible for governments to monitor direct transactions of this nature.[15]

4.41 The extent of the use of offshore insurance to evade the FSL is unclear:

> **CHAIR:** I would like to get a better understanding of self-insurance and people who insure offshore. Can you explain the issue of offshore insurance and the extent to which it occurs? If you have any figures on how much fire services levy is lost through this offshore insurance, I would appreciate that information.
>
> **Mr BROWN:** No accurate statistics are kept by government or anybody else on how much business goes out of Australia but there is a trend when insurance markets change internationally that for some of the larger commercial businesses in particular, they place their business with the broker and that business is placed offshore because the rates are cheaper at the particular time. I cannot give you the figures of what they are or how much business goes out of Australia or how much goes with insurers that are not Australian Prudential Regulatory Authority [APRA] registered insurers here in Australia. There is a significant amount now of the larger risk in particular being reinsured in jurisdictions outside of Australia.[16]

## INSURANCE AND RISK

4.42 In general terms, insurance is purchased to offset any risk from adverse events that would result in a loss to an individual. Insurance can provide peace of mind by ensuring that losses are covered and risk is mitigated. Insurance allows individuals:

> …to substitute a small, definite cost (the premium) for a large but uncertain loss (not to exceed the amount of the insurance) under an arrangement whereby the fortunate many who escape loss will help compensate the unfortunate few who suffer loss.[17]

4.43 Any definition of insurance will include reference to risk. For the purposes of insurance, risk is defined as “uncertainty concerning loss.”[18] Insurance, therefore, is designed to handle risk, while “risk makes insurance both desirable and possible.”[19]

4.44 Predicting the likelihood of future events occurring in individual cases is not exact. If prediction was certain and an event was foreshadowed, then insurance would not be obtainable. Insurers could not adequately set premiums to cover such losses. Alternatively, if an event were never predicted to happen, insurance would not be purchased. Individuals and businesses would have no desire or compulsion to purchase insurance when there was no chance of loss.

[15] Submission No 45, Insurance Council of Australia, p6
[16] Ian Brown, Deputy Chief Executive Officer, Insurance Australia Group, Transcript of Hearing, 21 November 2003, p8
[17] Mehr, Robert I Phd & Cammack, Emerson, 1980, *Principles of Insurance*, Richard D Irwin, p30
[18] ibid, p18
[19] ibid, p19

4.45 Therefore, insurance policies are written and undertaken because of the uncertainty of events and what people do not know. As most individuals are risk adverse, people justify insurance on the grounds that they would rather outlay a small amount (premium) against facing large, uncertain losses that they may not be able to cover at some future time.

## Handling Risk

4.46 Risk can be managed or mitigated by a number of different methods.

4.47 **Avoidance** – risk will be avoided "when the reluctance to accept risk is so great it cannot be counterbalanced by the utility gained from the risky action."[20] If there is no alternative action to take, and the risk cannot be avoided, then more often than not the risk should be handled in a different manner.

4.48 **Retained** – risk can be retained:

- out of ignorance (people unaware of insuring for events not expected);
- out of inertia (delaying techniques);
- not possible to address the risk (individuals engaging in dangerous activities may not be able to obtain insurance); and
- the loss is relatively small (may not be a concern if there is no large financial burden).

4.49 **Hazard reduction** – methods may be introduced to reduce hazard. Examples include safety precautions in the workplace, such as protective goggles and equipment or through research into disease prevention.

4.50 **Reduction in loss** – "Action is possible to minimize a loss if one occurs. The chance of a loss occurring is not eliminated, but its severity is reduced."[21] In most situations methods of hazard reduction and reducing loss are simultaneous goals. For example a pedestrian crossing reduces the number of pedestrian fatalities crossing a busy road but also slows the speed of traffic in the area.

4.51 **Shifting of risk** – various methods to shift risk include:

- hedging (offsetting the risk on both sides);
- subcontracting (portions of risk are pushed onto others);
- surety bonding (where the surety must answer for the default of the principal[22]);
- incorporation; and
- insurance (placing risk onto insurers).

4.52 **Reduction in risk**– taking out insurance can reduce risk. From an individual point of view, actions such as installing a burglar alarm can reduce the risk of theft while a smoke detector can reduce the risk of a house burning.

[20] ibid, p24
[21] ibid, p26
[22] ibid, p27

## TAXATION ON INSURANCE

4.53 The Committee was informed by NSW Treasury that "Taxes on insurance remain high for policies subject to the FSL."[23] The Government has reduced the stamp duty rate on general insurance from 11.5 per cent to 10.0 per cent from 1 October 2000 and further reduced the rate to 5 per cent from 1 August 2002, giving New South Wales the lowest general insurance rate in Australia. However, insurance remains subject to three separate taxes.

4.54 The insurance premium has the following levels of taxation applied:

- FSL levy is applied to the basic insurance premium (ranging from 1-24 per cent);
- GST (10 per cent) is applied on the total of both the basic insurance premium and the FSL; and
- Stamp duty (5 per cent) applies to the sum of the basic insurance premium, the FSL and the GST.

4.55 The application of stamp duty on goods or services including Commonwealth taxes, as is the case with insurance, is not a new feature of the State's tax system. This practice has been a longstanding feature.[24]

4.56 In New South Wales, the taxes on household building and contents insurance policies can add around 32 per cent to the base premium, while for businesses, taxation can add around 43 per cent (prior to allowing for GST input tax credits).

4.57 The following table outlines a typical calculation of the charges imposed on a basic household and commercial insurance premium. The following example uses current recommended ICA FSL rates, combined with both the GST (10 per cent) and insurance stamp duty rate (5 per cent).

| | **Basic Premium $** | **FSL $** | **GST $** | **Stamp Duty $** | **Total Cost $** | **Taxes Contribution %** |
|---|---|---|---|---|---|---|
| Household | 100 | 14 | 11 | 6 | 132 | 32 |
| Commercial | 100 | 24 | 12 | 7 | 143 | 43 |

4.58 Removing the FSL from the above example would result in the tax contribution falling from 32 per cent to 16 per cent of the premium for household policies and from 43 per cent to 16 per cent for commercial policies. The following table illustrates the impact of removing the tax.

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[23] Submission No 49, NSW Treasury, p11
[24] ibid, p10

| | Basic Premium<br>$ | FSL<br>$ | GST<br>$ | Stamp Duty<br>$ | Total Cost<br>$ | Taxes Contribution<br>% |
|---|---|---|---|---|---|---|
| Household | 100 | 0 | 10 | 6 | 116 | 16 |
| Commercial | 100 | 0 | 10 | 6 | 116 | 16 |

4.59 By international standards, New South Wales is highly taxed on insurance products. In comparisons with other jurisdictions in Australia and overseas, New South Wales is rated third behind Victoria (metropolitan and non-metropolitan insurance) for both commercial and household insurance. At the low end of the scale, countries like Japan and Hong-Kong pay no insurance taxes, while Singapore and Ireland pay 2 per cent respectively.[25] The Committee heard:

> **Mr MASON:** The other problem is that the levels of tax have reached a point where the budgets of the fire services have increased, of necessity, at rates far exceeding both the CPI increase and the rates of increase in insurance premiums over recent years so that the level of taxation on insurance products—when you add in State stamp duty and GST—is at levels that we would regard as penal and which in other areas are the sorts of levels of tax that are designed to be a disincentive to people to use the goods and services they are imposed on.[26]

[25] Submission No 45, Insurance Council of Australia, Appendix A, p4

[26] Alan Mason, Executive Director, Insurance Council of Australia, Transcript of Hearing, 21 November 2003, p13

# Chapter Five - Alternative Funding Arrangements

## INTRODUCTION

5.1 This chapter examines the requirements under point 3(b) of the Terms of Reference, which asks the Committee to consider the funding approaches in Queensland and South Australia and soon to come into effect in Western Australia. The Committee is also to examine the findings of the Victorian review of fire service funding.

5.2 The first section of the chapter will outline in detail the current funding arrangements used in other jurisdictions, including

- details on contributors to the funding base;
- how the levy is collected; and
- what emergency services benefit from the current funding arrangements.

5.3 The second section examines the findings of the recent Victorian review of fire services and the views and responses of various departments and organisations.

5.4 The final section will detail some of the alternative funding suggestions provided in various submissions to this inquiry.

## ALTERNATIVE APPROACHES TO FUNDING FIRE SERVICES

5.5 Fire services provided in Australia are funded from a variety of sources across all jurisdictions. However, there are three basic models (Tasmania uses a hybrid model that has elements of the three models). Chapter 2 outlined the four basic options available to fund fire services and concluded that the most suitable options were funding from consolidated revenue and hypothecated taxes.

### Insurance-based model

5.6 This model is used in New South Wales and Victoria. Under this scheme the majority of funding is collected through insurance contributions. The insurance companies pass their statutory contributions onto the insured through the FSL on selected insurance products.

### Property-based system

5.7 The property-based model operates in Queensland, South Australia and Western Australia. The approach adopted in each jurisdiction differs, but the levy is essentially collected on the value of the property augmented by other factors such as risk, service expectation and geographical location.

5.8 In Western Australia and Queensland, the levy is collected as part of local council rates. In South Australia, Revenue SA collects the fixed property levy. Transport SA collects the mobile property levy, which is not part of the funding arrangements in the two other jurisdictions.

### Consolidated revenue

5.9 Fire and emergency services in the Northern Territory and Australian Capital Territory are funded from consolidated revenue.

## CHARACTERISTICS OF CURRENT ALTERNATIVE FUNDING SYSTEMS

5.10 This section compares the following fundamental characteristics of each jurisdiction's fire services funding arrangements:

- funding base
- funding service coverage
- collection agent
- concessions/rebates
- treatment of State/Local Government assets

5.11 The section will also analyse each jurisdiction's funding arrangements against the principles of efficiency, equity, simplicity, transparency and stability.

### Funding Base

5.12 This section will detail the funding base that operates in each jurisdiction and the various sources of contributions to the funding. That is:

- on what basis the levy is collected;
- what property types are included in the tax base;
- what property types are exempt, (for those that operate under a property system); and
- what industries or sectors of the community contribute.

5.13 As outlined in earlier chapters, New South Wales operates an insurance-based funding system, with the majority of the funds for the two fire services operating in the state coming from the insurance industry. The insurance industry contribution is passed on to consumers through the imposition of the FSL on certain insurance policy types.

5.14 The insurance contribution is supplemented by contributions from the Local Government, and a State Government contribution.

5.15 Victoria operates a similar scheme to that in New South Wales. However, unlike New South Wales, where the insurance companies fund the same percentage of the fire services' budget, the insurance industry contributes different amounts to the metropolitan and country fire services.

5.16 The FSL is imposed on selected insurance policies but there is no levy on motor vehicles.

5.17 Local Government only contributes to the funding of the Metropolitan Fire and Emergency Service Board. The level of each council's contribution depends on the value of rateable land in the area.[1] Both services receive funding from the State Government.

[1] Department of Treasury and Finance, July 2003, *A Review of Victorian Fire Services Funding Arrangements*, Melbourne, p20

5.18 The following table outlines the funding arrangements between the two fire services in Victoria.

| Statutory Contributions | Metropolitan Fire and Emergency Service Board<br>% | Country Fire Authority<br>% |
|---|---|---|
| Insurance Industry | 75.0 | 77.5 |
| Local Government | 12.5 | 0 |
| State Government | 12.5 | 22.5 |

Source: Department of Treasury and Finance, July 2003, A Review of Victorian Fire Services Funding Arrangements, Department of Treasury and Finance, p18

5.19 The property levy in Queensland collects an urban fire levy through municipal rates. Properties that are serviced solely by Rural Fire Brigades are not subject to the levy, however, the respective local councils may impose a levy in order to fund their local rural brigade.

5.20 Owners of prescribed property pay the levy and the calculation of the levy is based on three factors;

- the classification of urban districts (4 in total);
- activity or use of the land; and
- improvements to the land.

5.21 The Queensland model factors in risk-rating by establishing 16 different fire levy groups, classified according to property categories and fire risk. For example, fire group 1 includes vacant land and jetties whereas fire group 16 includes casinos and oil and fuel depots.

5.22 The property levy contributes around 73 per cent of the total funding base for the Queensland Fire and Rescue Service. The remainder of the funding comes from the Queensland Government (10 per cent), other Government funding sources (9.6 per cent), user charges (5 per cent) and the remainder through grants.

5.23 The new model introduced in Western Australia imposes an Emergency Services Levy (ESL) on fixed property owners. The levy is calculated on the “gross rental value” of the property. Western Australia uses a property valuation system based on estimates of each property’s rental yield.

5.24 In determining the calculation of the levy, the State is divided into five geographical emergency categories. Category area 1 comprises the Perth metropolitan area, which is serviced by the Career Fire and Rescue Service and SES. Further category areas spread out from category 1 as the level of service provision changes. Category areas 2, 3 and 4 include major rural cities, metropolitan fringe areas and major country towns. These categories have various levels of service provision from the Career Fire and Rescue Service stations, SES, Volunteer Fire and Rescue Service Brigades, Bush Fire Brigades and Fire and Emergency Services Authority (FESA) units. Bush Fire Brigades and FESA units service category area 5.

5.25 The levy amount is therefore calculated by combining the properties’ gross rental value with an ESL rate. Minimum and maximum caps apply for properties in categories 1 to 4 with different caps for residential and commercial properties. For properties in category area 5, a flat fee of $30 applies for all properties, including residential and commercial. All mining tenements are also charged $30.

5.26 The property levy in South Australia has an ESL levied on both fixed properties and mobile properties (including motor vehicles, motorcycles and vessels). The fixed property levy is calculated on the capital value of the property (on which the State's property valuation system is based), whilst the motor vehicle fee is charged at a flat rate.

5.27 The calculation of the levy is based on a fixed dollar amount plus a variable amount calculated on the property's capital value. The variable component is made up of three factors:

- an area factor which reflects levels of service provision (4 different areas);
- a land use factor depending on the type of the property, such as residential, commercial etc (seven different categories); and
- the levy rate adopted for the year.

5.28 Motor vehicles and vessels are charged a fixed fee, varying between different classes of vehicles.

5.29 The Tasmanian funding system collects revenue from a variety of different sources. In a system similar to New South Wales and Victoria, the Tasmanian system has an insurance levy component, which imposes a FSL on certain insurance products, contributing 24 per cent to the total fire service budget. The majority of the funds (47 per cent) come from a fire service contribution levied on property. The levy varies depending on whether the property is located in urban or rural areas. It is a fee for service based on the annual assessed value of the property and the level of fire protection provided.

5.30 The remainder of the funds are sourced from a flat fee motor vehicle levy (9 per cent of funding) and a contribution by the State Government (8 per cent).

## Funding Service Coverage

5.31 This section outlines what emergency services are covered by the funding arrangements adopted in various jurisdictions and the area size, location or population serviced by these emergency services.

5.32 In New South Wales the current arrangements provide funding to both metropolitan fire services, through the NSW Fire Brigades and to non-metropolitan or rural and regional areas through the Rural Fire Service. Both services operate in selected fire districts with most fire districts or rural fire districts (in the case of the Rural Fire Service) following council boundaries. The general rule is that NSW Fire Brigades will provide their service to towns with a minimum population of 1,000.[2]

5.33 Victoria has two fire brigades. The Metropolitan Fire and Emergency Services Board provides fire services in metropolitan Melbourne only (the Melbourne Metropolitan Fire District), which covers approximately 1,096 $km^2$ and has approximately 1.9 million people. The Country Fire Authority provides fire services to all of Victoria, other than

[2] Submission No 49, NSW Treasury, p6

the Melbourne Metropolitan Fire District, including public land. The services area coverage is around 150,182 $km^2$ with a population of 2.5 million.[3]

5.34 The Tasmanian hybrid funding system funds the Tasmanian Fire Service. The service has 235 brigades across Tasmania and is made up of 251 career firefighters and 4,866 volunteer fighters.

5.35 In Queensland, the current funding arrangements are the main source of revenue for the Queensland Fire and Rescue Service (QFRS), of which the Rural Fire Service is a division. Levies are collected from prescribed properties that must be situated within urban fire districts controlled by the QFRS and serviced by full time QFRS staff.

5.36 South Australia and Western Australia include a number of emergency agencies in their funding arrangements. In the case of South Australia, the funding system incorporates the SA Metropolitan Fire Service, the SA Country Fire Service, State Emergency Service, Surf Life Saving SA, Volunteer Marine Rescue SA, and services provided by the South Australian Police Department.

5.37 The SA Metropolitan Fire Service has fire stations across most of metropolitan Adelaide and some regional cities and towns. The Country Fire Service has brigades across most of South Australia and is predominately made up of volunteers.

5.38 Similarly in Western Australia, a number of emergency services are funded through the collection of the emergency service levy. The levy funds the operation of the Career Fire and Rescue Service, Volunteer Fire and Rescue Service, Local Governments' Bush Fire Brigades, State Emergency Service and the new multi-service FESA Units.

5.39 The Career Fire and Rescue Service has fire stations in metropolitan Perth and five regional centres – at Bunbury, Geraldton, Albany, Kalgoorlie and Northam. Based on current figures, the Volunteer Fire and Rescue Service operates in around 100 regional areas of the State.

5.40 The Local Governments' Bush Fire Brigades operate in rural and pastoral areas throughout the State, providing bushfire prevention and suppression. In areas of Perth's urban-bushland fringe some units also operate as Volunteer Fire and Rescue Service units, providing more than just fire protection.

5.41 The Northern Territory Fire and Rescue Service and the Bushfire Council provide fire protection and prevention in the Northern Territory. The Bushfire Council is a statutory body established under the *Bushfires Act* to provide advice to the Minister on bushfire control and management, rather than fighting fires. The *Bushfire Act* covers all Northern Territory land, except for the 0.5 per cent of land that is subject to control by the Northern Territory Fire and Rescue Service. Funding for both units are provided from consolidated revenue.

5.42 In the Australian Capital Territory, the ACT Fire Brigade and the ACT Bushfire Service jointly provide fire services. The ACT Bushfire Service is primarily responsible for suppressing bushfires. It operates with two departmental brigades and nine volunteer brigades across the territory. All bushfire brigades can respond to any fire emergency given that the ACT is a single fire control unit. The ACT Fire Brigades, on the other hand, is a full-time urban brigade located at seven stations throughout the ACT. Like

[3] Department of Treasury and Finance, July 2003, *A Review of Victorian Fire Services Funding Arrangements*, Department of Treasury and Finance, p8

other emergency services in the ACT, funding for the fire services comes from consolidated revenue.

## Collection Agent

5.43 In New South Wales, Victoria and Tasmania the insurance companies directly pay their contribution to the Government. This contribution is sought from policyholders through the mechanism of the FSL on insurance premiums.

5.44 Western Australia and Queensland collect their levies through local councils. In Queensland, councils collect the urban fire levy plus an administration fee based on collection numbers. The *Fire and Rescue Service Regulation 2001* sets the fees at $3.10 per collection, where collections are less than 40,000 and $2.60 per collection +$124,000, where collections are above 40,000.

5.45 Similarly, in Western Australia, councils are paid an administration charge. This annual charge is based on both the number of rates notices issued and the amount of the levy collected by each Council. In 2003-04, $2.25 million was paid to local councils to collect the levy.[4]

5.46 Council contributions are paid through rate notices in Tasmania and are collected by local councils, who are paid a 4 per cent collection fee by the State Fire Commission. In 2002-03 a collection fee of $838,000 was paid to local councils.[5]

5.47 Unlike other property-based funding systems, South Australia does not use local councils to collect the levy. Instead, the fixed property component of the levy is collected from property owners by the State revenue collection agency, Revenue SA. The Committee was advised that it cost in the order of $5.7 million to collect the levy from 530,000 property owners.[6]

5.48 Only two States collect a levy on motor vehicles. In South Australia the levy is collected through registrations for both motor vehicles and vessels and is paid to the State Government agency, Transport SA. In Tasmania the Department of Infrastructure, Energy and Resources collect the motor vehicle levy.

5.49 With regards to the Australian Capital Territory and the Northern Territory, as the levy is funded via consolidated revenue, the levy is collected through the payment of other taxes.

## Concessions/Rebates

5.50 Under the insurance based approach in New South Wales and Victoria, there are no concessions provided, as the insurance company is required to contribute to the funding of the service. In turn, they do not provide concessions to policyholders.

5.51 In Queensland, a 20 per cent discount is available for those pensioners who reside in QFRS areas and who qualify under the terms and conditions of the State Government pensioner subsidy scheme.

5.52 Western Australia provides similar rebates to seniors and pensioners on ESL to those they receive on council rates. For Seniors Card holders, a capped rebate of 25 per cent is available for ESL. Holders of pensioner concession cards, state concession

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[4] Emergency Services Levy Information Guide, 14 August 2003
[5] State Fire Commission, Annual Report 2003, p27
[6] Meeting between Public Accounts Committee and RevenueSA, 4 February 2004

cards or holders of both a Seniors Card and a Commonwealth Seniors Health Card may be entitled to a rebate of up to 50 per cent on ESL or 100 per cent deferment of payment.

5.53 Like other property-based systems, South Australia provides a concession of up to $40 for an individual's principal place of residence. Eligible community groups include holders of pensioner concession and State concession card, Veterans Affairs Gold Repatriation Health Card, recipients of Centrelink allowances such as Newstart and widows allowances and Seniors Card holders. There are no concessions provided to the mobile property levy although 90 per cent of motorists pay the minimum $24 levy.[7]

5.54 Pensioners and health cardholders receive discounts on rates and motor vehicle levies in Tasmania.

## Treatment of State/Local Government assets

5.55 Under the insurance-based system operating in New South Wales and Victoria, State-owned assets are insured under Government insurance authorities. In terms of Local Government assets, properties that are insured would pay any FSL on those properties. The financial modellers were advised by the Local Government and Shires Associations of NSW that local councils in New South Wales currently pay $2.2 million in FSL on these policies.[8]

5.56 In Queensland, Local Government buildings, complexes and parkland (whether improved or not) are subject to the urban fire levy. However Crown land, including State and Commonwealth assets, are exempt even if the land is within a designated fire district.[9]

5.57 State and Local Government land is subject to the ESL in Western Australia, as is the case in South Australia.

5.58 Under the contribution from insurance companies in Tasmania, State-owned assets are self-insured and local councils would contribute to the FSL through insurance policies. For the fire levy contribution from property, State and Local Government owned land is exempt from the duty.

## Analysis of funding arrangements in each jurisdiction

5.59 Chapter 6 will evaluate in detail the current funding arrangement operating in New South Wales. This evaluation will compare the system against the general tax principles of efficiency, equity, simplicity, stability and transparency.

5.60 This section provides a similar analysis against these principles for the funding arrangements that operate in other jurisdictions. The analysis does not include many of the factors that differ across individual jurisdictions. However, it serves as a starting point for discussions.

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[7] Meeting between Public Accounts Committee and South Australian Department of Treasury and Finance, Revenue and Economics Branch, 4 February 2004

[8] Professional Financial Solutions, Final Submission, *Quantitative Modelling of NSW FSL Funding Methods*, p82

[9] Information correct at time of accessing web site – www.fire.qld.gov.au. Information from Urban Fire Levy Scheme – Administration Procedures Manual, Version 2.0, December 2001, p3

**Comparison of Funding Arrangements to Taxation Principles**

| | Efficiency | Equity | Simplicity | Stability | Transparency |
|---|---|---|---|---|---|
| **Victoria*** | Low | Low-Medium | High | Medium-High | Low |
| **Queensland** | Medium-High | Medium-High | Medium | Medium-High | Medium |
| **Western Australia** | Medium-High | Medium-High | Medium | Medium-High | Medium |
| **South Australia** | Medium-High | Medium-High | Medium | Medium | Medium |
| **Tasmania** | Medium-High | Medium-High | Medium | High | Medium |
| **Australian Capital Territory** | High | High | High | High | Medium-High |
| **Northern Territory** | High | High | High | High | Medium-High |

* Refers to the current Victorian funding model and does not include any recommended changes following the recent review of funding arrangements.

5.61 Against the taxation principles, the insurance-based approach in Victoria ranks the lowest. Against the principle of simplicity the system ranks high because of the low administration and collection costs. On efficiency grounds the system ranks low because of the narrow tax base and the additional cost to insurance. Transparency was also rated low because an insurance system is not always precise in knowing the actual amount of revenue collected.

5.62 Under an insurance-based system, the revenue source is fairly stable and has the growth potential. Given that insurance continues to be taken out and premiums increase, there is little potential for it to decline. Finally, in terms of equity, the system suffers because of unequal contributions from various sectors, avoidance of the levy and high degrees of under and non-insurance.

5.63 A property-based approach, like that adopted in Queensland, Western Australia and South Australia, performs reasonably well against the tax principles. On efficiency the scheme has a wider tax base. Even though there are concessions which pulls the ranking down, the levy cannot be evaded so there are more contributors to the scheme, therefore improving equity. Administration and compliance costs are reasonable.

5.64 Likewise with measures of stability and transparency, this funding approach ranks higher than the insurance scheme because of the higher visibility of the levy for taxpayers and base on which the levy is collected is stable and will grow in line with economic activity. In the table, South Australia has a lower ranking on stability than the other jurisdictions. This is because the structure of the scheme and the large remissions provided could have the potential to weaken the scheme.

5.65 Finally, the consolidated revenue models in the two Territories provide the highest ranking. Funding from consolidated revenue draws from a broad base, with all taxpayers contributing through some form of taxation, it is simple to fund, grows with economic development and, provided Budgetary reporting requirements are transparent, the scheme is highly visible.

5.66 Therefore, the table above highlights the similar conclusions from Chapter 2, in that funding from consolidated revenue is the best option in providing government services. This is followed by the hypothecated revenue option, or in this case, the property levy, and following this is the insurance-based system. While the FSL is a hypothecated tax, it is only one part of the current funding arrangement.

## VICTORIAN REVIEW OF FIRE SERVICE FUNDING

5.67 On 1 November 2002 the Victorian Treasurer, the Hon John Brumby MP, announced a review of the funding arrangements for the fire services in Victoria. The Review aimed to answer the following key questions:

- What is the fairest way to charge for the cost of fire services, or how should the costs of these services be apportioned among those who benefit?
- How should the charge be collected?[10]

5.68 The Review was undertaken by the Victorian Department of Treasury and Finance. 150 submissions were received from a variety of key organisations, Government agencies, emergency service providers, peak interest groups and Local Governments.

5.69 The Review outlined four models to consider as alternatives to the current insurance system. Two of these were based on insurance and two involved introducing a property-based model. Insurance model 1 was a modified insurance model. It introduced cost recovery for self-insureds, hazardous material call-outs and avoidable false alarms. Insurance companies would be required to identify their statutory contribution on premium notices and fire services would be required to publish the amounts collected via the levy.

5.70 The second insurance model had the same characteristics as the first but included a levy on motor vehicles.

5.71 Property-based model 1 levied a uniform rate on the fixed property value for both residential and commercial properties within fire districts, therefore improving equity and efficiency. The second insurance model was similar to property model 1, except that the levy rates were based on relative fire risk.

5.72 A media release from the Office of the Treasurer, on Thursday July 31, 2003, stated that the Victorian Government will retain the current insurance-based system, with some minor modifications:

> After viewing the Report, the Government has concluded that funding fire services primarily through contributions from insurance companies remains the best way of matching contributions with benefits.[11]

5.73 The enhanced insurance system will include:

- requiring insurance companies to clearly identify and account for the fire services contribution component of insurance premiums;
- full cost recovery from the uninsured, hazardous material call-outs and avoidable false alarms – through increased direct charges; and
- refine the basis for allocating contributions between insurance companies.[12]

5.74 Emergency service providers, peak industry groups and Government agencies in New South Wales held differing views on the Victorian report. In evidence before the

[10] Department of Treasury and Finance, July 2003, *A Review of Victorian Fire Services Funding Arrangements*, Department of Treasury and Finance, p2
[11] The Hon John Brumby MP, Victorian Treasurer, Media Release, Thursday, July 31, 2003, p1
[12] ibid, p1

Committee, the IAG and ICA expressed concern about the Victorian review and the outcome:

> **Mr BROWN:** The issue that was flawed within the Victorian system is that they had not done enough work on modelling as to what the differences were and the costs incurred by people who do not have insurance or people who have insurance now.[13]

5.75 Additionally:

> **Mr MASON:** The Victorian review was disappointing from our point of view in that, notwithstanding the original indications from the Victorian Government, it was by no means thorough. The Victorian Treasury did not take up the industry's offer to do the detailed modelling and assessment of different options and testing of different people's assertions. It made some theoretical desktop assumptions, which lead to conclusions with which we do not agree. The problem with the conclusion is that it is left with what it has now because the proposals for finetuning the system still leaves the equity and under and non-insurance problems. The real problem, which is greater in Victoria than in New South Wales, is that the future projections as to where fire brigade funding needs are going in Victoria will become more and more onerous if it continues to be funded out of the insurance mechanism.[14]

5.76 NSW Treasury had a similar view, based on the agency's own analysis of the findings:

> **Mr CLARK-LEWIS:** That is right. I do not accept their findings. You could say that they are looking at a half empty glass: they see it half full and we see it half empty. It could be interesting to run this but if you look at the report and some of the analyses that we have done of insurance premiums and look at the issues that they have raised, the essential premise is that there is a fire risk embedded in premiums and therefore the fire service levy on insurance premiums is equitable because there is, on the one hand, a risk assessment done by the insurance companies and contribution. But even in their own analysis I think their conclusions were that there was a moderate relationship between costs and benefits—not a strong term: moderate—and their executives somewhere talk about a broader correlation between costs and benefits. One of the concerns I had when I looked at the work was it is done at a purely aggregate level.
>
> So they are happy if, on average, households are paying 20 per cent. Say we take, for the sake of argument, that 20 per cent of the cost of the fire service is being funded by residential properties and 20 per cent of households account for fire offence or fire costs in terms of fire claims—I would use the fire claims measure because that takes account of not only the incident but the value of the incident which I think is the best measure of benefit of the fire services—if they were the same at the aggregate level, and they are not if you look at the Victorian one, but if they were, they would be happy that that is a good match. But in fact I think the example we have given on contents insurance shows that the amount that individuals are paying will vary quite widely depending on their location, and it is varying because of risk of theft, which is completely unrelated to fire services. At the aggregate level they found a broader relationship or a moderate relationship. At the detailed level I do not think it holds up very well at all.[15]

[13] Ian Brown, Deputy Chief Executive Officer, Insurance Australia Group, Transcript of Hearing, 21 November 2003, p5

[14] Alan Mason, Executive Director, Insurance Council of Australia, Transcript of Hearing, 21 November 2003, p16

[15] Michael Clark-Lewis, Senior Director, Revenue Strategy Branch, NSW Treasury, Transcript of Hearing, 21 November 2003, p25

5.77 Conversely, there were several submissions that supported the findings of the Victorian review and the rejection of introducing a property-based levy. The NSW Fire Brigades stated in its submission that:

> The Victorian review and previous NSW reviews have identified significant strengths in models like the current NSW fire services funding model.[16]

5.78 Similarly, the NSW Fire Brigade Employees' Union stated, "The Victorian Review has much to recommend it and is endorsed by NSW firefighters."[17]

## ISSUES RAISED IN SUBMISSIONS

5.79 The Committee received 64 initial submissions from a range of Government agencies, businesses and local councils. This is in contrast to the Victorian experience. When the Victorian Treasurer announced a review of funding arrangements for the State's fire services in November 2002, a total of 150 submissions was received.

5.80 It is noted that while the vast majority of submissions to this Committee were from organisations and agencies that could be classified to varying degrees as stakeholders in the process, only a single submission was received from a member of the public. The fact that only one member of the NSW community was driven to submit their view to this inquiry may indicate a lack of public disquiet about the present system.

5.81 This view is consistent with the statement of the NSW Fire Brigades Commissioner in evidence that the Brigades received only 35 complaints in total in 2002 and very few of these were about the fire levy.[18] On the other hand NSW Treasury advised that public concern actually prompted the Government to start investigating the issue:

> **Mr CLARK-LEWIS:** We get representations from members of the public about taxes and post-GST the environment has really put the spotlight on insurance taxes. The insurance companies put on their notices the premium and their estimate of the fire service levy, GST and stamp duty and we have had quite a lot of correspondence, disproportionately on that tax, compared to most other taxes. Up until the budget that was probably the largest area that we received correspondence on.
>
> **Mr RICHARD TORBAY:** That is interesting because I remember reading information in 2000 when the joint select committee raised some issues as well. We were all surprised by how little that issue was touched upon in all the submissions. In fact, it was almost nothing.
>
> **Mr CLARK-LEWIS:** I suspect it may be a person-in-the-street issue. They are not the sorts of people who come to committees and make their concerns known, but certainly we have seen representations on the issue and, actually, that is what got us interested in this whole area. We got those representations and we thought that maybe they had a point, so we started looking at it.[19]

5.82 The submissions canvassed a variety of views and raised a number of issues, concerns and suggestions in relation to the current funding system for fire services and possible alternative funding options.

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[16] Submission No 54, NSW Fire Brigades, p2
[17] Submission No 53, NSW Fire Brigade Employees' Union (FBEU), p18
[18] Mr Greg Mullins Commissioner NSW Fire Brigades, Transcript of Hearing, 26 November 2003, p7
[19] Michael Clark-Lewis, Senior Director, Revenue Strategy Branch, NSW Treasury, Transcript of Hearing, 21 November 2003, p28

## Funding options

5.83 Most submissions to the inquiry outlined support for either retaining the current funding system or replacing it with a property-based system. Over half of the submissions supported the introduction of a property levy of some variety. A range of combinations of elements from funding schemes in other jurisdictions were recommended but there was no unified approach. Most support for a property system came from local councils and various industry groups.

5.84 The Local Government Association of NSW and the Shires Association of NSW strongly supported a property system. The Associations were supportive of a valuation based property levy augmented by a flat levy on motor vehicles. The objective of introducing this new funding system would:

> …produce a more equitable system, removing the gross contributors (being the State Government, Local Government and the Insurance industry), and reducing the gross premiums to those who are adequately insured. It may increase costs to the uninsured, underinsured and those who benefit from offshore insurance arrangements.[20]

5.85 Various other councils, such as Lockhart Shire Council, Auburn Council and Gundagai Shire Council were also supportive of the position taken by the Associations and the introduction of a property-based system.[21]

5.86 The Property Council of Australia held a similar view to that of the councils listed above. They stated:

> A property and motor vehicle based funding mechanism provides a broad based tax system to fund fire services. Property and motor vehicle owners are key users of fire services.[22]

5.87 A number of submissions raised various issues regarding the implementation of a property levy. Boorowa Council and Snowy River Shire Council suggested that a property levy should be calculated on the improved capital value of land, rather than the rateable value of land or just a flat fee.[23]

5.88 The issue of including some degree of risk rating into the calculation of the levy was also raised in several submissions. National Insurance Brokers Association, Riverina Wool Combing Pty Ltd and Woollahra Municipal Council all advocated including a risk element. This risk rating will take into account the fire potential of different buildings and the resources used to prevent or suppress a fire.[24]

5.89 Another proposal was to calculate the property levy with some regard to service levels or expectations of service. The State Chamber of Commerce and a submission from Mr William J Lea were supportive of an expectation of service model.[25]

5.90 Hornsby Shire Council also advocated this model. In particular, they proposed introducing the Queensland model:

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[20] Submission No 42, Local Government Association of NSW and Shires Association of NSW, p7

[21] Submission No 15, Lockhart Shire Council, Submission No 12, Auburn Council and Submission No 27, Gundagai Shire Council

[22] Submission No 22, Property Council of Australia, p18

[23] Submission No 30, Boorowa Council, p3 and Submission No 8, Snowy River Shire Council,p1

[24] Submission No 2, National Insurance Brokers Association, p4, Submission No 56, Riverina Wool Combing Pty Ltd, p3 and Submission No 25, Woollahra Municipal Council, p2

[25] Submission No 4, State Chamber of Commerce, p2 and Submission No 6, Mr William J Lea

> The preferred model is the Queensland one which has a flat levy on land based on service expectation; where major urban centres serviced by large permanently manned brigades pay the highest levies with lower levies applying in areas with lesser levels of service availability.[26]

5.91 Given that the provision of fire services is similar to other government services, such as police and ambulance services, the issue of funding the service from consolidated revenue was raised in a few submissions. Leeton Shire Council and the Alliance both note that the service could be funded through consolidated revenue.[27]

5.92 However, the Alliance submission notes:

> State budgets are not 'magic puddings' and it would be desirable for a clear funding source to give security to the resourcing of this essential service.[28]

5.93 The issue of self-insurance and the lack of contributions resulting from the practice were also raised in some submissions. The Nature Conservation Council of NSW and the NSW Fire Brigade both suggested that a levy or service fee could be introduced in order to ensure that individuals or companies self-insuring would be required to contribute.[29]

5.94 As stated earlier, there were a number of submissions that advocated retaining the current funding system. Most notably, these submissions were received from the those who provide the State's fire services, the NSW Fire Brigades and the Rural Fire Service and the peak bodies representing their members' interests: the Fire Brigades Employees' Union and the Rural Fire Service Association.

5.95 These agencies, which are responsible for the administration and expenditure of the funding to support their operations, argue that the current system is administratively efficient, provides stable and adequate funding and that the funding mix between insurers, Local Government and the State Government adequately reflects services and benefit levels.

5.96 The Rural Fire Service recommended a modified version of the insurance-based funding scheme:

> … that the insurance-based funding system supported by local government contributions is that the appropriate scheme, which links contribution to risk. It is recognised however that some inequities arise as a result of non-insurers or under insurers.[30]

5.97 NSW Fire Brigades questioned the argument that the current fire services funding model is substantially inequitable, citing the Victorian review's finding that the "the current system is reasonably equitable and efficient because contributions for those insured are broadly linked to benefits and encourage fire risk management."[31]

5.98 The Fire Brigades submission also stated:

> The Victorian review and previous NSW reviews have identified significant strengths in models like the current NSW fire services funding model. Strengths of the current

[26] Submission No 33, Hornsby Shire Council, p2
[27] Submission No 38, Leeton Shire Council and Submission No 46, Alliance for the Equitable Funding of Fire Services
[28] Submission No 46, Alliance for the Equitable Funding of Fire Services, p14
[29] Submission No 51, Nature Conservation Council of NSW and Submission No 54, NSW Fire Brigades, p7
[30] Submission No 55, Rural Fire Service, p2
[31] Submission No 54 NSW Fire Brigades p 2 quoting Victorian Fire Services Funding Review, Victorian Dept of Treasury and Finance, 2002 p vii

> system include stability of revenue, low administrative and compliance costs and relatively effective linking of contributions to benefits and risks.
>
> However, significant potential for refinement to the current NSW fire services funding model exists.[32]

5.99 The submission warned the Committee that:

> The reasons for and benefits of a major change may well be found to be illusory when examined in depth against the background of interstate review and experiences, and the efficiency of the current system.[33]

5.100 The NSW Rural Fire Service Association stated:

> The Association's view is that the insurance-based funding system is the appropriate scheme, because it links contribution to risk.[34]

5.101 However, the Association did concede that the current system had some inequities caused by non-insurance and under-insurance. To overcome these issues, the Association recommended that:

> Some of the inequities of the current system may be addressed while retaining an insurance-based approach. These include improving transparency and addressing the lack of contributions by some sectors, namely motor vehicle owners, non-insureds, and contributions within the residential sector (ie. building compared to contents) can be better aligned with the distribution of benefits.[35]

5.102 The NSW Fire Brigade Employees' Union were similarly supportive of retaining the current funding system. However, they believed that Local Government should be removed from the funding base, with the shortfall picked up by the insurance industry and State Government. They were also supportive of charging on non-insured properties. The Union strongly rejected any change to the current funding system stating:

> The Union will stridently resist any regressive attempt to change the current approach to fire service funding that is inequitable and/or that shifts the burden away from where it belongs – with the Insurance Industry and the State Government.[36]

## Contributors to the funding of fire services

5.103 The majority of submissions received outlined concerns over the extent of the funding base. Of most notable concern was the extent of non-insurance and under-insurance.

5.104 The Property Council of Australia submission stated:

> The current funding mechanism is simply unfair. As is, the majority of funding for fire services is sourced only from those people who take out property insurance, regardless of the fact that fire services are a public good accessed by the entire community.[37]

5.105 To this the Council added:

> Presently, people who either fail to insure, or else under insure their properties are not adequately contributing to the cost of fire services.[38]

[32] ibid pp2-3
[33] ibid p4
[34] Submission No 37, NSW Rural Fire Service Association, p5
[35] ibid, p5
[36] Submission No 53, NSW Fire Brigade Employees' Union (FBEU), p18
[37] Submission No 22, Property Council of Australia, p9

5.106 A number of submissions quoted various figures and sources relating to the extent of non-insurance and under-insurance. These figures vary considerably and range from 4.49 per cent to as high as 25 per cent. The main thrust of the arguments in submissions is that contributions should be sought from these individuals or companies. Temora Shire Council was resolute in ensuring uninsured properties contribute. The Council submission stated:

> The most evident of these deficiencies [with the current system] is the ability to avoid contribution to fire services by simply not taking out insurance. It is the belief of Council that this could be overcome by a compulsory levy if insurance is not taken out similar to the levy introduced by the Federal Government to cover private health insurance contributions.[39]

5.107 A contribution, or lack thereof, from motor vehicles was another issue raised in a number of submissions. Most submissions commented that motor vehicles now contribute significantly to the workload of fire services and as a result they should be required to make a greater contribution to the funding base. A number of submissions suggested imposing a levy on motor vehicles.

5.108 The Property Council of Australia supported a flat charge on motor vehicles, as did Woollahra Municipal Council. They recommended a levy on all registered motorised transport, similar to that introduced in South Australia. Similarly, the Group Captains Snowy River Shire supported a levy:

> …applied to all motor vehicle, boat, caravan, aircraft and any other transportation device and that this levy be collected through the registration process.[40]

5.109 Contrary to the views stated above, the NRMA Motoring and Services did not agree with a levy on motor vehicles. The NRMA believed that the incidence of vehicle fires is low compared with other occurrences and that motor vehicle ownership is already highly taxed through stamp duty.[41]

5.110 The inclusion of land owned by Governments was also raised in some submissions. Tallaganda Shire Council suggested that State Government land including property of the National Parks and Wildlife Service and NSW State Forests should be levied on the same basis as other land.[42]

5.111 Similarly, the Local Government Association of NSW and Shires Association of NSW also proposed that properties currently exempt from rates should also contribute to any new funding system. This would include State and Local Government.

5.112 The Property Council of Australia recommended that the current State Government contribution should be maintained as well as contributing on the basis of property owned, thereby contributing twice. Others do not share this view. The Department of Environment and Conservation (DEC) stated:

> The imposition of a fire services levy on DEC lands would be inappropriate considering the expenditure the Department is committing to fire suppression and prevention.[43]

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[38] ibid, p9
[39] Submission No 20, Temora Shire Council, p1
[40] Submission No 17, Group Captains Snowy River Shire, p2
[41] Submissions No 19 and 81, NRMA Motoring and Services
[42] Submission No 35, Tallaganda Shire Council, p1
[43] Submission No 43, Minister for the Environment, p4

5.113 State Forests, a public trading enterprise with statutory responsibility for preventing and suppressing fires, pointed out that in 2002-03 it contributed $16.1 million to fire suppression on its properties and it was not a major beneficiary of the fire services.[44]

## Self-providers of fire services or mitigators of fire risk

5.114 The current funding system is New South Wales does not provide any exemptions to the FSL. All individuals and businesses are required to contribute either through council rates or insurance. No recognition is made of organisations or companies who are either required under legislation or as part of their own corporate governance to provide fire-fighting services.

5.115 The NSW Minerals Council provided the following information:

> The coal mining sector has a NSW statutory requirement to fund, maintain and operate the Mines Rescue Service (MRS), as governed by the *Coal Industry Act 2001 (NSW)*.
>
> The MRS is fully funded by the NSW coal mine operators, both open cut and underground. The MRS and its associated levies are mandated by NSW legislation, and are additional to the other fire rescue services in NSW - the NSW Fire Brigades and the Rural Fire Services.[45]

5.116 These emergency services perform rescue services dealing with the mine emergencies and are required to provide their own rescue equipment. Consistent with the legislation, mining operators would not call upon either the NSW Fire Brigades or the Rural Fire Service in the case of a disaster.[46]

5.117 In addition to providing an off-site emergency services, NSW Minerals Council also contribute to the funding of the FSL through insurance. The Council, therefore, recommended that:

> Coal mining operators should incur a fire services funding levy rebate due to their compulsory maintenance of the MRS, regardless of the basis of the levy.[47]

5.118 ARIMA Ltd, an organisation representing professional risk managers, also raised the issue of corporate fire services. In its submission, ARIMA stated that:

> Any replacement scheme should recognise those organisations that go beyond just paying the FSL by including an option to apply a discount to organisations which are deemed low risk because of fire controls they have in place.[48]

5.119 Ku-ring-gai Council also addressed the possibility of exemptions or discounts from any proposed new funding arrangement. The council recommends that discounts should be provided to councils who initiate measures to reduce fire risks. Such measures would include fire breaks, hazard reductions and equipment to establish fire breaks.[49]

## Concessions or exemptions

5.120 The issue of providing concessions or exemptions from a property-based system was not largely discussed in submissions. In a submission from the Department of Community Services, the Hon Carmel Tebbutt MLC, Minister for Community Services,

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[44] Submission No 47, State Forests, p1
[45] Submission No 16, NSW Minerals Council, p4
[46] ibid, p5
[47] ibid, p6
[48] Submission No 13, ARIMA Ltd, p5
[49] Submission No 3 Ku-ring-gai Council, p2

Minister for the Ageing, Minister for Disability Services and Minister for Youth, recommended that:

> In the case of a property levy being introduced, concessions for disadvantaged people should be developed to ensure that vulnerable members of the community are not adversely affected.[50]

5.121 The Insurance Council of Australia is also supportive of concessions or rebates to pensioners. These concessions "should be in a manner similar to that which currently exists for Local Government rates."[51]

5.122 The NSW Council of Social Service also supported comprehensive concessions from a scheme for low income earners and recipients of benefits:

> Either you should be looking at a two-tier arrangement, in terms of a recognition of people's economic circumstance or you should be looking at a robust concession arrangement.[52]

5.123 The NSW Rural Fire Service raised the issue of volunteers in its submission and the possibility of rebates offered to ratepayers under a property-based approach. While the service was supportive of such a proposal, they did highlight a number of practical issues that needed addressing, such as active versus non-active members and costs associated with other emergency situations to which the service attended.[53]

5.124 The NSW Farmers Association contend that rural landowners contribute in a variety of ways to funding fire services, through insurance contributions, rates for local councils and direct support through provision of resources, equipment and volunteering for the brigades.[54]

5.125 Due to the substantial rural contribution, the Association:

> Strongly believes that this level of support should be taken into account when fire levies are being calculated, and that levy contributions should be appreciably lower in areas that support a bushfire brigade.
>
> The rate should be 50% lower in these areas, and believes that current in-kind contributions should be factored into the modelling work to determine the actual discount rate that should be applied.[55]

## Collection of Fire Service Levy

5.126 Support for local councils collecting a proposed property levy was quite strong amongst the submissions. Of those submissions advocating a property-based system, the majority of them recommended the local councils collect the levy as part of rates. If councils were to collect the levy on behalf of the State Government, some submissions suggested that they should be compensated. Sydney Harbour Regional Organisation of Councils (SHOROC), the Local Government Association of NSW and the Shires Association of NSW, and Forbes Shire Council, were some of the

[50] Submission No 59, Minister for Community Services, Minister for the Ageing, Minister for Disability Services and Minister for Youth, p1
[51] Submission No 45, Insurance Council of Australia, p17
[52] Mr Gary Moore, Chief Executive Officer, New South Wales Council of Social Service, Transcript of Evidence 7 May 2004, p33
[53] Submission No 55, NSW Rural Fire Service, p4
[54] Submission No 31, NSW Farmers Association
[55] ibid, p4

submissions recommending that local councils could collect the levy on a fee for service basis.

5.127 Councils were also concerned that including the levy on rates notices would make individuals think the levy was a further local council impost. As such, some submissions requested that the levy be identified as a State Government levy. While the collection of the levy by local councils was widely supported, Hornsby Shire Council raised the issue of debt administration and collection. The Council believed that bad debts and overdue accounts should be collected by the relevant state agency.[56]

5.128 Not all councils were supportive of collecting a property levy. Richmond Valley Council and Council of the Shire of Jerilderie both suggested that the fire brigades themselves could collect the levy:

> Richmond Valley Council believes that if a proposal to collect the fire service levy from all property owners is to replace the direct contributions from Local Government and insurance companies collection of the fire service levy, then this should be done directly by the NSW Fire Brigades and NSW Rural Fire Service, not Councils.[57]

5.129 Alternatively, the Council also suggested that the Office of State Revenue (OSR) could collect the levy. Whilst not specifically mentioning OSR, Tallaganda Shire Council and Guyra Shire Council also recommended that the State Government should be responsible for the collection and administration of the levy.

5.130 Of the submissions advocating the introduction of a motor vehicle levy, the majority argued that the Roads and Traffic Authority (RTA) should collect as part of the annual registration process. However, the Minister for Roads and Minister for Housing, the Hon Carl Scully MP, stated in a submission to the Committee that he did not support a levy on vehicle registration charges. However, if a levy was to be collected it may be more suitable to collect it through Compulsory Third Party insurance.[58]

## Extension of the Fire Service Levy to an Emergency Service Levy

5.131 The State Emergency Service (SES) and the State Emergency Service Volunteer Association (SESVA) both made submissions to this inquiry seeking their inclusion into this review. The SES strongly believes they should be funded by the insurance industry. Presently, the SES is predominantly funded from consolidated revenue.

5.132 The SES states it contributes substantially to saving the insurance industry millions of dollars every year and provide enormous benefits to the community. In its submission the SES outlines a study that measures the worth of a SES volunteer. This study found:

> An active SES volunteer is conservatively worth at least $12,500 per year to the community, and using these figures the total value of the NSW SES is estimated to be at least $87.5 million per year.[59]

5.133 The SES argues that there is a clear case for the insurance industry to contribute substantially to the funding of the SES and its activities. The Organisation asserts that the insurance industry benefits from the work of the SES in much the same way

[56] Submission No 33, Hornsby Shire Council, p3
[57] Submission No 24, Richmond Valley Council, p3
[58] Submission No 40, the Hon Carl Scully MP, Minister for Roads and Minister for Housing
[59] Submission No 48, State Emergency Service , p3

as it does from the fire services, thus justifying an extension of the funding scheme to include the SES:

> Unlike the State's Fire Services the SES receives no funding from the Insurance Industry despite the fact that much of the SES's operational activities benefit insurance companies through millions of dollars in reduced claims every year.[60]

5.134 The submission also states:

> The insurance industry has clearly benefited from the work of SES volunteers by hundreds of millions of dollars nationwide over the years but has never made any meaningful financial contribution to the operations of the SES. It is fair to say that the Insurance industry is having a free ride on the back of the SES over the years.[61]

5.135 The State Emergency Service Volunteers Association put a similar case forcibly in its submission:

> In the case of funding to SES, it is the view of the SESVA that those who benefit from the work of the SES organisation should contribute to the cost of providing it[]s services. The disparity between the way that [the] SES is funded, and the way that the RFS is funded has, in the view of the SESVA, provided a financial advantage to the RFS and retarded the growth of the SES. It has also placed the taxpayers of NSW in the position where they are paying the full cost of the SES budget while those who receive the most benefit have not been asked for any contribution, or support, to SES.[62]

5.136 A few submissions supported creating a levy that was not specifically designed to fund the fire services only, but to fund other emergency services, similar to the practice in other jurisdictions. The New South Wales Volunteer Rescue Association, Wellington Council and the Country Women's Association of New South Wales raised the possibility of funding all emergency services in a similar fashion, with a similar levy on all emergency services.

5.137 However, a number of submissions did not want to fund other emergency services in any proposed new levy. Sydney Harbour Regional Organisation of Councils (SHOROC), Eurobodalla Shire Council and the Property Council of Australia were opposed to expanding the tax base to include other emergency services.

5.138 While consideration of the inclusion of the SES in any possible future funding options was not included in this inquiry's terms of reference, the Committee notes with concern the issues raised in the SES and SESVA submissions.

5.139 The Committee acknowledges that, because this issue is outside the Committee's Terms of Reference, it is a matter for the Government to consider in further detail. The Committee suggests that SES funding be considered as part of any future studies on this issue.

[60] ibid, p2
[61] ibid p3
[62] Submission No 10, State Emergency Service Volunteers Association

# Chapter Six - Evaluating the Current Funding Arrangements

## INTRODUCTION

6.1 In this chapter, the report evaluates the current funding arrangements in NSW against the taxation policy principles described in Chapter 2. Important considerations are the principles of equity and efficiency of the current funding system.

## EFFICIENCY

### Cost to insurance

6.2 The Insurance Council of Australia (ICA) commented that the current funding system is inefficient because it:

> …distorts economic efficiency by being a significant additional cost (a deterrent) on the purchase of appropriate insurance.[1]

6.3 The Insurance Australia Group (IAG) included in its submission to this inquiry a survey conducted for NRMA Insurance Ltd for small and medium sized businesses, which states that 31 per cent of respondents (out of a total of 1,253) claim the main reason they are not adequately insured is because they want to avoid paying higher premiums. Additionally, 39 per cent of respondents claim the main reason they are not covered by applicable insurance is because it is too expensive. This indicates that some parts of the community consider that cost of insurance to be too high and therefore do not take out adequate insurance.[2]

6.4 In a similar report conducted on households, 23 per cent (out of 227) responses stated that the reason they did not have building and contents insurance was because insurance is too expensive (eg due to the high premium, insurance is too expensive). For motor vehicles, 47 per cent (out of 55) said they did not have any non-compulsory vehicle insurance because insurance is too expensive, while 38 per cent (out of 138) said that insurance was too expensive in the case of comprehensive insurance.[3]

6.5 If the cost of insurance is high and results in a reduction in the take-up of insurance, it is worth considering the reaction of individuals to any price increases for insurance. Are consumers willing to respond to price signals?

6.6 The NSW Treasury submission quotes a US study by Grace, Klein and Kleindorfer that estimated "a 10 per cent increase in the price of insurance would result in a 14 per cent reduction in the quantity of insurance demanded."[4] The figures increased for homeowner catastrophe insurance products, where "a 10 per cent price increase lead[ing] to a 28 per cent fall in quantity demanded."[5]

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[1] Submission No 45, Insurance Council of Australia, p27
[2] Submission No 11, Insurance Australia Group Ltd, Appendix 1 MJ Powling Research Consulting Business Insurance: A National Survey of Small and Medium Size Businesses, July 2001
[3] ibid, Appendix 2
[4] Submission No 49, NSW Treasury, p14
[5] ibid, p14

6.7 The issue of insurance cost structures and the impact these decisions have on businesses relocating to the State or continuing to operate, were raised by the Property Council of Australia:

> **Ms THOMAS:** Apparently [the Department of State and Regional Development] has instances where it had people threatening to leave the State, regional investors who had to get a special proviso from the Treasurer to be exempted from some of the insurance levies. They were thinking that it was so exorbitant—it had tripled in one case and they scaled back to a doubling instead. So the Department of State and Regional Development has had this issue.
>
> **Mr MORRISON:** This is new businesses coming into New South Wales?
>
> **Ms THOMAS:** This is businesses existing, suddenly found that their insurance policies have over a small period tripled, and have approached the Government and said that "without some sort of intervention we are looking at leaving the State, we cannot afford this". It has had other instances where major investors looking to locate here have examined it and come across the levy as an issue.[6]

6.8 A submission from Riverina Wool Combing expressed concern about large increases in the amount of FSL the company was required to pay as a result of steep increases in its insurance premiums following the 2001 terrorist attacks in the United States. The FSL increased from $90,000 to $240,000 between 2001 and 2003.[7] Fletcher International which operates an abattoir in Dubbo informed the Committee that the FSL in NSW amounted to $10 a head for each beast. This affected the company's ability to compete with abattoirs in other states.[8]

6.9 The Committee has heard anecdotal evidence of companies choosing to respond to such circumstances by reducing the amount of insurance coverage in order to remain competitive. This would leave such companies more exposed to the risk of catastrophe. In the case of regional industries, where they may be few alternative employers, a fire on premises without adequate insurance could have enormous flow on effects in the regional economy.

6.10 The Committee notes that increases in fire services levies of this scale are directly linked to increases in insurance premiums.

## Narrow tax base

6.11 The tax base itself is raised as an impediment to efficiency. The Property Council of Australia submission states:

> Tying fire services funding to levies on insurance policy holders creates a narrow tax base. Those caught in this tax base are subjected to higher costs by virtue of the narrowness of the base, that is, there are simply fewer people to tax so the cost is more concentrated. This is inefficient because it distorts the market.[9]

6.12 Tax policy principles suggest that an efficient tax is one that is broad based and set at a low tax rate. By spreading the tax burden across a larger number of people, the lower the individual tax burden. However, the FSL base limits the tax burden to a smaller number of taxpayers as not all property and business owners have insurance.

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[6] Cheryl Thomas, Senior Policy Advisor, Property Council of Australia, Transcript of Hearing, 21 November 2003, p36
[7] Submission No 56, Riverina Wool Combing, p1
[8] meeting with Public Accounts Committee, 3 June 2004
[9] Submission No 22, Property Council of Australia, p10

## Calculation of fire risk into the premium

6.13 A further criticism with regard to the efficiency of the funding arrangements is that the FSL is charged on the total premium. This premium also takes into account other risks. In comparison to risks such as theft, vandalism and other natural disasters, fire represents a small component of risk. Consequently, the FSL is charged on a higher premium than a premium relating directly to fire, and as such, the contribution to the fire service is higher as well:

> **Mr STEVE WHAN:** You were talking earlier about your analysis of risk with insurance policies—and obviously that is something you are an expert at—suggesting that fire risk is not very high in the components of setting your premiums at the moment. How much does fire risk come into your premium setting?
>
> …
>
> **Mr BROWN:** If you ask the question about what percentage of the risk rating is based on fire, on buildings I think it is 24 per cent of the risk rating which is attributable to fire.
>
> **Mr JOHN TURNER:** Is that the single largest component?
>
> **Mr BROWN:** No it depends on the areas because in certain other areas you have issues to do with burglary and now there is climatic change and things like that coming in as well. There are lots of other issues coming into our rating factors.[10]

6.14 The NSW Treasury submission also discussed the issue of fire risks in calculating premiums:

> If premiums vary substantially for non-fire risk factors, then the levy is not ensuring those with greater risk of fire are making appropriately larger fire services levy contributions. In fact, the evidence points to the fire services funding burden being disproportionately borne by those in areas with relatively greater rates of theft.[11]

## Accuracy of FSL collection

6.15 The nature of determining the fire service level of funding a year in advance can result in significant over and under collections. Where an insurer under collects, they are required to pay the difference into the fund. Alternatively, if the insurer over collects the insurers retain the extra funds. The system therefore distorts efficiency for both the insurer and insureds.

6.16 The Property Council of Australia submission stated in relation to this point:

> Insurance companies move through cycles where they over collect from customers to fund the levy (and make a profit which they retain) or under collect from customers (and make a loss which they bear).[12]

6.17 The submission went on further to say:

> The imprecise nature of this collection mechanism actively discourages insurance companies from reporting the fire levy component to customers.[13]

6.18 However the Committee was not presented with any evidence that showed that insurance companies regularly over-collected FSL from policy holders.

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[10] Ian Brown, Deputy Chief Executive Officer, Insurance Australia Group, Transcript of Hearing, 21 November 2003, p10
[11] Submission No 49, NSW Treasury, p17
[12] Submission No 22, Property Council of Australia, p13
[13] ibid, p13

## Attitude to insurance

6.19 While the arguments outlined above suggest the high costs for insurance are a disincentive to take out insurance and may account for some individuals and companies not entering into insurance arrangements, there are other possible reasons. Issues such as perceptions of fire risk, attitude to insurance and even past experiences with insurance companies or processing a claim may be alternative reasons why people chose not to insure or underinsure their property.

6.20 The household survey referred to above reported that 15 per cent (out of 53 respondents) stated that the reason they had a lack of confidence in the adequacy of home insurance was because a previous claim payment was inadequate, 15 per cent said they did not trust insurance companies while 9 per cent said they did not understand insurance.[14]

6.21 For motor vehicles, the reasons cited for a lack of confidence in their motor vehicle insurance was that 25 per cent (out of 65) thought a previous claim payment was inadequate, 8 per cent did not trust insurance companies and 5 per cent did not understand insurance.[15]

6.22 The survey results did mention that avoiding the high cost of premiums was a reason for lacking confidence in the adequacy of the insurance. However, for both household insurance and motor vehicle insurance, this rated behind the reasons listed above and accounted for only around 6 to 8 per cent of respondents.[16]

6.23 The IAG submission also referred to a regular quarterly survey by the *State Chamber of Commerce (NSW) and NRMA Insurance Local Business & Regional Affairs Survey* of outer-metropolitan and regional businesses in Australia. The January 2003 survey asked questions of the 613 respondents about state taxation and business insurance. 31 per cent of the respondents stated that insurance service taxes imposed the greatest financial burden on business (behind payroll tax at 32 per cent).

6.24 The survey also asked businesses what they would do if insurance premiums were reduced through a drop in taxes and charges. 60 per cent of respondents would leave their current insurance policies in place, 13 per cent would take out more insurance on items not currently insured and 12 per cent would take out insurance on items currently uninsured. These results suggest that decisions to take out insurance and provide adequate insurance are based on more than just the costs involved.

# EQUITY

6.25 On equity grounds, the current funding system in NSW ranks poorly. One submission commented:

> The current levy system founded upon insurance premiums is highly inequitable, with the bulk of fires services funding being borne by only those property owners who adequately insure.[17]

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[14] Submission No 11, Insurance AustraliaGroup, Appendix 2, MJ Powling Research Consulting, *Home and Motor Vehicle Insurance: A Survey of Australian Households* October 2001

[15] ibid Appendix 2

[16] Submission No 11, Insurance Australia Group Ltd

[17] Submission No 38, Leeton Shire Council, p1

6.26 Individuals who do not insure their property or under insure place a greater tax burden on a select group of the community who choose to fully insure their properties and contents. Non-insurers are provided fire services at no cost and essentially 'free ride' on the provision of the fire service. Similarly, under insurers contribute only partially to the provision of the service but receive the full benefit.

6.27 The tax burden on those insuring is set artificially high. They are effectively paying a higher amount than they should, due to the narrow funding base.

6.28 The extent of non-insurance, and to a lesser extent under-insurance, is highlighted in figures produced by both the ICA and the IAG.

## Extent of non-insurance

6.29 The Committee notes that it is extremely difficult to obtain reliable data on the extent of non-insurance as such exercises attempt to measure the gaps in a complex and diverse market through sample surveys and statistical analyses. The Insurance Council of Australia publication of October 2002 *Report on Non-Insurance/Under-Insurance in the Home and Small Business Portfolio* is derived from Australian Bureau of Statistics surveys undertaken every five years and other statistical sources.[18] It estimates that 25.25 per cent of households were uninsured in 1998-99. For owner-occupiers, the figure was 4.49 per cent, while for tenants the figure was 68 per cent for the same period. These figures have declined from the previous survey of 1993-94 and the corresponding figures are shown in the following table.

| | **1993-94 (% of 6,616,800)** | **1998-99 (% of 7,122,800)** |
|---|---|---|
| % of uninsured households | 31.0 | 25.25 |
| Owner occupiers uninsured | 6.17 | 4.49 |
| Owner occupiers contents uninsured | 20.0 (approx) | 15.18 |
| Tenants uninsured | 75.0 | 68.0 |
| Small business uninsured | 20.0 (approx) | 17.0 |

Source: Insurance Council of Australia, Report on Non-Insurance/Under Insurance in the Home and Small Business Portfolio, October 2002

6.30 Figures for small businesses show that 1 in 6 businesses had no insurance. The ICA report quoted figures that small businesses employ in excess of 2.5 million people and represent approximately 28 per cent of GDP.

6.31 Similarly, figures from the NRMA October 2001 household insurance survey of 1,212 people showed that 1 in 6 households in Australia do not have buildings and contents insurance. Additionally, the survey also found that 1 in 5 passenger vehicles was not comprehensively insured.[19]

6.32 CommInsure stated in its submission that, based on a survey conducted by Research International, released on 9 October 2003, for general insurance products between June 2001 to June 2003:

[18] Insurance Council of Australia, *Report on Non-Insurance/Under Insurance in the Home and Small Business Portfolio*, October 2002, p10
[19] MJ Powling Research Consulting, *Home and Motor Vehicle Insurance: A Survey of Australian Households,* pp4-5

- Home building insurance dropped from 49 to 45 per cent;
- Home contents insurance fell from 62 to 58 per cent; and
- Motor insurance declined from 71 to 68 per cent over the same two-year period.[20]

6.33 Based on figures from the Sydney hailstorm in 1999, 68.7 per cent of buildings were insured whilst 8 per cent were not. In 23.3 per cent of cases, it was not possible to determine whether the building was insured or not. The ICA report determines that if the level of insurance/non-insurance distribution remained the same, the overall level of non-insurance would have been 10.4 per cent (these figures only apply to building insurance, not contents).[21]

6.34 The ICA suggests the reason for the level of non-insurance was due to a "high percentage of older inner urban households which fell into the lower income quintiles."[22]

6.35 In addition to hearing figures quoted on levels of non-insurance, the Committee also heard anecdotal evidence about insurance following major fires.

> **Mr GLEDHILL:** I do not have figures or anything like that. However, I am aware of the last major fire down south that burned from Boorowa almost to Moss Vale. Moss Vale was on alert. A large number of people could not afford to put up fences after those fires. I had no trouble putting up fences because my fences were insured. Those who were not able to re-fence their properties had to be underinsured. I pay a levy on my policy so that I am able to get money to re-fence my property. Money that came from Sydney was given to people who never had their fences or their stock insured to enable them to put up fences and to repurchase stock. I cannot give you figures on that but I assume that an insurance company would be able to do so.[23]

6.36 The figures quoted above from the ICA for levels of non-insurance relate to national non-insurance only. The ICA report, however, also presents non-insurance data for New South Wales. The table below shows the percentage of non-insurance in New South Wales compared to the total number of households. Figures show the level of non-insurance has fallen from the 1993 levels across the geographical areas. The ICA report states the fall in rural non-insurance probably reflects improvements in the rural economy between 1993 and 1998.

| | **CAPITAL CITY** | | | **OTHER URBAN** | | | **RURAL** | | |
|---|---|---|---|---|---|---|---|---|---|
| | 1988 | 1993 | 1998 | 1988 | 1993 | 1998 | 1988 | 1993 | 1998 |
| % of Market | N/A | 62.45 | 61.68 | N/A | 30.25 | 30.96 | N/A | 7.29 | 7.35 |
| % Non-Insured | 29.4 | 31.85 | 28.29 | 24.0 | 28.62 | 25.14 | 41.0 | 36.67 | 25.54 |

Source: Insurance Council of Australia, Report on Non-Insurance/Under Insurance in the Home and Small Business Portfolio, October 2002, p27

6.37 The two tables below show that tenants across all income groups still represent the highest contribution to non-insurance, despite the level of non-insurance falling

[20] Submission No 21, CommInsure, p6
[21] Insurance Council of Australia, October 2002, *Report on Non-Insurance/Under Insurance in the Home and Small Business Portfolio*, p26
[22] ibid, p26
[23] Robert Gledhill, Vice President, Shires Association of New South Wales, Transcript of Hearing, 26 November 2003, p33

across most income ranging quintiles (Quintile 1 – poorest to Quintile 5 – richest). The figures also show the decline in overall number of renters.

**Average Rates of Ownership/Non-Insurance (NSW)**

| | | 1988/1989 | 1993/1994 | 1998/1999 |
|---|---|---|---|---|
| Ownership % (adds to 100) | Owner | 45.2 | 41.5 | 41.19 |
| | Purchaser | 25.4 | 24.8 | 28.84 |
| | Tenant | 29.4 | 33.7 | 29.97 |
| Non-insured % (adds to 100) | Owner | 10.9 | 9.9 | 8.3 |
| | Purchaser | 7.6 | 7.5 | 5.3 |
| | Tenant | 73.7 | 74.8 | 73.7 |

Source: Insurance Council of Australia, Report on Non-Insurance/Under Insurance in the Home and Small Business Portfolio, October 2002, p28

**NSW Households by Income, Ownership and Non-insurance**

| | | | Quintile 1 | Quintile 2 | Quintile 3 | Quintile 4 | Quintile 5 |
|---|---|---|---|---|---|---|---|
| Ownership % | Owner | 93/94 | 54.9 | 49.9 | 38.6 | 29.8 | 34.0 |
| | | 98/99 | 57.1 | 54.06 | 31.8 | 28.40 | 34.49 |
| | Purchaser | 93/94 | 5.2 | 12.5 | 27.7 | 35.5 | 42.8 |
| | | 98/99 | 9.9 | 9.89 | 33.9 | 45.85 | 45.57 |
| | Tenant | 93/94 | 39.9 | 37.6 | 33.7 | 34.7 | 23.2 |
| | | 98/99 | 33.8 | 35.96 | 34.3 | 25.75 | 19.92 |
| Non-insured % | Owner | 93/94 | 15.4 | 14.9 | 13.2 | 6.3 | 1.8 |
| | | 98/99 | 12.8 | 8.04 | 6.68 | 6.9 | 4.38 |
| | Purchaser | 93/94 | 8.9 | 8.9 | 9.4 | 5.1 | 6.0 |
| | | 98/99 | 10.59 | 7.86 | 6.68 | 3.77 | 2.33 |
| | Tenant | 93/94 | 86.0 | 82.6 | 77.6 | 65.8 | 55.0 |
| | | 98/99 | 86.11 | 75.95 | 76.93 | 66.82 | 60.12 |

Source: Insurance Council of Australia, Report on Non-Insurance/Under Insurance in the Home and Small Business Portfolio, October 2002, p27

6.38 One of the aims of the financial modelling work commissioned from to support this inquiry was to develop an understanding of the level of non-insurance and under-insurance in New South Wales. The consultants, Professional Financial Solutions, matched information on the land value of all properties in New South Wales to information on building and contents insurance. The consultants were able to show that, of those residential properties covered by any type of insurance policy, 11 per cent had no building insurance and 24 per cent had no contents insurance.[24]

6.39 The Committee heard evidence that not everyone is convinced with the figures quoted in relation to levels of non-insurance:.

> **Mr MULLINS:** Finally, the claim that up to 25 per cent of households are not insured also needs to be challenged and rigorously researched if it is seen as a reason for change.

[24] Professional Financial Solutions, Final Submission, *Quantitative Modelling for NSW FSL Funding Methods*, p63

> The Victorian review estimated non-insurance for households at only 6 per cent, and taking into account leased or rented properties, buildings and contents, the non-insurance rate was estimated at only 10 to 11 per cent. Clearly that area needs closer scrutiny.[25]

## Extent of under-insurance

6.40 ICA figures for household under-insurance shows that for 1999, 7.5 per cent of household buildings are insured for less than 70 per cent of their replacement value, while 20 per cent of household buildings are insured for between 70 per cent and 90 per cent of their replacement cost.

6.41 Figures for contents insurance show that the level of under-insurance remains fairly high at the less than 70 per cent of replacement value category.

6.42 Compared to the last survey of 1994, the figures in the less than 70 per cent of replacement value category in the case of contents insurance has improved the most. The following table outlines the level of under-insurance for both buildings and contents for 1994 and 1999.

| Risk | < 70% of replacement value | | > 70% but < 90% of replacement value | |
|---|---|---|---|---|
| | 1994 % | 1999 % | 1994 % | 1999 % |
| Buildings | 12 | 7.5 | 22 | 20 |
| Contents | 42 | 35 | 10 | 10 |

Source: Insurance Council of Australia, Report on Non-Insurance/Under Insurance in the Home and Small Business Portfolio, October 2002

6.43 Figures from the NRMA publication *Business Insurance: A National Survey of Small and Medium Size Businesses,* show that 47 per cent of business do not have relevant cover or insurance classified as adequate.[26]

6.44 Insurance Disaster Response Organisation (IDRO) figures on under-insurance for households regularly find that, on average, contents insurance falls short of the true cost of replacement by 30 per cent, with buildings insurance in a similar range. Figures for the older population and low-income earners show under-insurance for these groups to be at around 40 per cent of true replacement costs for buildings.[27]

6.45 While figures presented above quote levels of non-insurance and under insurance for both households and small businesses, the actual extent of commercial property insurance is not clear. The Property Council of Australia's submission stated:

> In the main, non-insurance and under-insurance occurs among households, that is, residential property owners and occupiers. Commercial property owners, on the other hand, tend to insure their properties and contents at appropriate levels.[28]

[25] Gregory Mullins, Commissioner, NSW Fire Brigades, Transcript of Hearing, 26 November 2003, p2
[26] cited in Submission NO 11 Insurance Australia Group p 12
[27] Submission No 46, Alliance for the Equitable Funding of Fire Services in NSW, p6
[28] Submission No 22, Property Council of Australia, p9

## Inequity of Local Government contributions

6.46 The 1994 Robson review discussed the inequities of the current funding system from the view of local councils. Under the current system some NSW Fire Brigades fire districts may cover more than one council and therefore receive contributions from multiple councils. Differences between council contributions arise due to the number of ratepayers in the area and the value of land.[29] For 2002-03 council contributions for Sutherland Shire Council was $2,339,806, for South Sydney City Council $1,249,867, Lane Cove Municipal Council was $510,719 and Hunters Hill Municipal Council was $311,940. These councils, however, all belong to the same fire district of Sydney.[30]

## Inequity between industry sectors

6.47 Other areas of inequity discussed by the Robson review were the areas of transport and hazardous materials. In the area of transport, the review found that the FSL contribution from the transport sector was too low considering the large number of fire callouts. The submission from the NSW Fire Brigades stated that:

> A large and growing portion of NSWFB (5.7% in 2002-03) workload, as well as that of the RFS is in relation to motor vehicle (accidents and rescues) and hazmat incidents.[31]

6.48 This figure was later updated in evidence to "closer to 8 per cent."[32]

6.49 Woollahra Municipal Council also raised the issue of perceived inequities in the transport sector. In supporting a levy on motor vehicles the Council stated:

> It also supported the introduction of a levy on all registered motorised transport to broaden the base from which the funding requirements are recovered to include a well known source of cost and risk.[33]

6.50 As noted earlier, only 1 per cent of premiums for comprehensive insurance for motor vehicles are attributed to the FSL. This suggests a lack of equity, given the growing share of workloads for the fire services and the high fire risk.

6.51 Contributions from hazardous material callouts were also considered very low and the ability to charge for calls outside a fire district were not adequate. Due to the extreme danger and nature of the work involved, the Robson review found that funding contributions should be increased.[34]

## Avoidance of the FSL

6.52 Finally, the Robson review found that insurers' ability to avoid or evade the FSL was quite high. The use of deductibles, netting of premiums and use of off shore insurance markets was contributing to lowering the base and placing a greater burden on others.[35]

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[29] Robson, K, September 1994, *Review of Funding Arrangements for the Fire Service of New South Wales*, pp43-44
[30] NSW Fire Brigades Annual Report 2002/03, Appendix 4, pp121-122
[31] Submission No 54, NSW Fire Brigades, p8
[32] Gregory Mullins, Commissioner, NSW Fire Brigades, Transcript of Hearing, 26 November 2003, p4
[33] Submission No 25, Woollahra Municipal Council, p1
[34] Robson op cit p 28
[35] ibid p

6.53 The issue of deductibles and offshore insurance is an area of concern for both the insurance industry and the fire services. For the insurance industry it represents a loss of business and additional pressure on companies and products to fund the FSL:

> **Mr MASON:** The other problem relates to the business, commercial and industrial area and the way that insurance premiums are calculated. There are far more opportunities for businesses to reduce premiums and reduce risk than there are for the average household. That could be by having deductibles or self-insured amounts on the policies and by layering the policy. As we know, many people insure overseas because there are other taxes and imposts that they can avoid through that mechanism. So you have all those distortions as well. We therefore do not think that trying to rely on it purely with the fire risk is feasible or that it will achieve the best outcome.[36]

6.54 For the fire services, these avoidance measures result in a reduction in funding sources and heavy reliance on a narrow tax base:

> **Mr MULLINS:** We really have no way at present of knowing whether all companies that insure offshore or who do not insure are remitting the required moneys to the fire services in New South Wales. That could be a much larger issue than the elderly and disadvantaged who do not insure their homes. Deductibles, which are like an excess, are another issue. Many companies say to a huge industrial company, "You take the first $100 million of risk and we will insure the rest." What happens to the self-insurance of that $100 million? Nothing is remitted to the fire services for that. I would suggest that we are talking about the small end of town. It is probably the big end of town where the money is not coming in.[37]

## SIMPLICITY

6.55 From an administrative perspective, the funding arrangements for fire services are administratively efficient and inexpensive. This view is outlined in several submissions. With no exemptions to the tax base, and a relatively easy collection method, via insurance policies and rate notices, the tax has low administration and compliance costs and raises the required amount of funds annually.

6.56 The NSW Fire Brigades submission stated:

> The current model, while perceived by some as inequitable in terms of inputs – is certainly efficient. The NSWFB is able to collect over $400 million in revenue at a cost of around $250,000 (Accounts Receivable function).[38]

6.57 The NSW Treasury submission stated:

> The FSL is simple to administer as it is paid by insurance companies and they are few in number (around 250 companies are registered to operate in NSW).[39]

6.58 However, the submission went on further to acknowledge that:

> There are costs for insurance companies in determining how to recover the cost of the levy through their insurance policies…that it is not necessarily easy for insurance companies to determine the correct amount to recover from policy holders, as this will depend on the amount of business they write in a year and the premiums charged.[40]

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[36] Alan Mason, Executive Director, Insurance Council of Australia, Transcript of Hearing, 21 November 2003, p18
[37] Gregory Mullins, Commissioner, NSW Fire Brigades, Transcript of Hearing, 26 November 2003, p6-7
[38] Submission No 54, NSW Fire Brigades, p11
[39] Submission No 49, NSW Treasury, p19
[40] ibid, p19

6.59 The Insurance Council of Australia has advised that while the direct costs of developing the advisory rates for FSL each year are only around $5,000, each registered insurance company in New South Wales must seek their own actuarial advice about the level of fees to impose and then make systems changes. These costs are in the order of $20,000 per year. Brokers and insurance agents responsible for collecting FSL are likely to face similar charges.[41] Based on the fact that more than 120 insurance groups currently remit FSL to the NSW Fire Brigades each year, this indicates that total annual administrative costs would be in the order of $2.4 million.[42]

## STABILITY OR FLEXIBILITY

6.60 Revenue sources should have growth potential and move in line with economic activity. Due to the nature of the current funding arrangement and the heavy reliance on insurance, the revenue source is relatively stable:

> The NSWFB points out that while aspects of the current funding system are unpopular with stakeholders, the system is inherently stable, administratively efficient and cost-effective, and ensures that the fire services have adequate funding.[43]

6.61 The current funding mechanism adequately raises the required level of funds each year. The Robson review comments that the system raised the required amount of revenue without a great amount of difficulty.[44] This view is possibly not so valid since the introduction of the GST. NSW Treasury noted:

> The introduction of the GST has heightened public awareness of taxes on insurance, as the various taxes are often listed separately on insurance premium notices.[45]

6.62 Collecting the majority of the funding contribution from insurance provides a rather stable source of revenue. Levels of under-insurance and non-insurance aside, the inherent risk adverse nature of individuals and businesses will mean that insurance will continue to be taken up and will provide a stable source of revenue.[46]

6.63 The only reason that may place pressure on insurance contributions is if premiums were to continue to substantially increase and people could no longer afford to have insurance. However, the increases in premiums would need to be very severe to result in individuals and businesses moving away from insurance.

## TRANSPARENCY

6.64 Transparency was identified in a number of submissions as an area where the current funding arrangements, in particular the FSL, were particularly lacking.

6.65 Under section 80 of the *Fire Brigades Act 1989,* insurance companies are required to separately identify the amount of FSL collected in insurance premium notices. However, due to the imprecise nature of the amount of FSL that is actually collected

[41] Mr Allan Hansell, Manager for NSW and the ACT Insurance Council of Australia, Transcript of Evidence 7 May 2004, p13
[42] Number of companies remitting FSL advised by Submission No 61, Insurance Council of Australia, p5
[43] Submission No 54, NSW Fire Brigades, 5
[44] Robson, K, September 1994, *Review of Funding Arrangements for the Fire Service of New South Wales*, p24
[45] Submission No 49, NSW Treasury, p10
[46] ibid, p14

once the financial years are concluded, many insurance companies no longer identify the FSL amount. On this point the ICA has noted:

> Those who pay the FSL are never given any justification for the precise amount levied upon them nor how it relates to either the fire risk that they represent or the fire services available to them.[47]

6.66 In addition to the transparency of the FSL, the NSW Treasury submission also raised the transparency of the funding component from local councils. Local councils collect their funding contribution through council rates although this is not included in rates notices and most rate payers would be unaware of the proportion of rates being used to this purpose.[48]

## SUMMARY

6.67 In comparing the current funding arrangements in New South Wales to the taxation principles, the current system performs less well than the alternatives. In Chapter Two, the Committee examined four ways of funding fire services and concluded that consolidated revenue or hypothecated taxes were the best mechanisms.

6.68 In Chapter Five, the Committee examined the three ways of funding the fire services currently used in Australia, through:

- consolidated revenue,
- an insurance-based scheme and
- a property-based levy.

6.69 As the Committee considers that fiscal constraints preclude the use of consolidated revenue to fund fire services in New South Wales, the following discussion focuses on comparing the current insurance-based scheme to a property-based system.

6.70 The table below compares the results for the current scheme to a theoretical system which would replace the current levy on insurance companies with a simple levy on the value of property held. It also assumes that property-based system would replace the Local Government contribution as has occurred in Western Australia and that local councils collect the levy.

6.71 The table also identifies the key issues affecting performance in each aspect.

[47] Submission No 45, Insurance Council of Australia, p28
[48] Submission No 49, NSW Treasury, p20

| Taxation Principle and Summary of Issues | NSW Insurance Based scheme | A theoretical property-based system on residential, commercial and Local Government properties |
|---|---|---|
| **Efficiency** | Low | Medium-High |
| **Summary of Issues** | Narrow tax base – only those with insurance contribute<br>Increases cost of insurance and may discourage prudent insurance<br>Cost of insurance has limited relationship to risk of fire and use of fire services | Broadens tax base as related to all properties and potential users of fire services.<br>Property-based levy has relationship to ability to pay |
| **Equity** | Low-Medium | Medium-High |
| **Summary of Issues** | Only those with insurance contribute and contribute more than they should<br>Local Government contributions are not related to cost of fire services in all cases | All property owners contribute in proportion to the value of property.<br>Unless type of land use in considered, there is no relationship to risk of fire |
| **Simplicity** | High | Medium |
| **Summary of Issues** | Low administration and compliance costs. Flat rate on insurance policies is simple to administer. | Calculations could be complex and require updating<br>Increased number of collectors (if local councils used to collect)<br>Inclusion of concessions complicates model |
| **Stability** | Medium-High | High |
| **Summary of Issues** | Demand for insurance is relatively stable | Demand for property ownership is very stable |
| **Transparency** | Low | Medium |
| **Summary of Issues** | Amount of FSL not always stated on insurance policies<br>Ratepayers probably unaware are contributing through council rates | Property owners would be more aware of their contributions<br>Taxpayer contribution to Local and State Government contributions may still be unclear |

6.72 This shows that, on a theoretical basis, a property-based levy would provide a better way of funding fire services than the current arrangements. The two options available to the Committee would be to develop a property-based levy that meets these criteria or to address the weaknesses identified in the current arrangements through administrative improvements.

6.73 In the next chapter, the Committee considers whether it would be practical to develop a property-based system that meets these theoretical objectives. Issues related to the design of such a property-based system and the impacts on various sectors of the community are assessed.

# Chapter Seven - Modelling the Impact of Alternative Funding Arrangements

## INTRODUCTION

7.1 This chapter describes the financial modelling work commissioned from Professional Financial Solutions (PFS) for the Committee. This project compared the impact of the current insurance-based arrangements to introducing a property-based levy for funding fire services. The Executive Summary of the PFS final submission *Quantitative Modelling of NSW FSL Funding Methods* is at Appendix Six. The full submission is available from the Committee's website.[1]

7.2 This financial modelling is consistent with the Terms of Reference 3 which asks the Committee to:

> e. undertake modelling of the impact of the proposed funding arrangements on taxpayers to assist in determining proposed funding arrangements.

7.3 The chapter describes:

- the process of developing the model;
- the results of the modelling work;
- public responses to the interim PFS submission; and
- the final PFS submission to the Committee.

## FINANCIAL MODELLING PROCESS

### The Consultants

7.4 The Insurance Council of Australia contracted the assistance of actuarial consultants, Professional Financial Solutions (PFS) to develop a financial model to examine alternative funding options on the basis of a limited invitation to tender. PFS was selected by a panel consisting of representatives of the insurance industry, the Office of Emergency Services and NSW Treasury.[2]

7.5 The initial funding for the project was provided by the Insurance Council of Australia. NSW Treasury provided some additional funds at a later date.[3]

7.6 The Committee is confident that PFS acted with independence and professionalism in conducting this work on its behalf. The consultants met the Committee several times, both formally and informally, during the course of the project to discuss its progress. On a day to day basis, the parameters of the project were developed in consultation with an informal working group consisting of representatives of NSW Treasury, the ICA and the Committee secretariat.

[1] Throughout this chapter, all references are to the PFS Final Submission of April 2004 rather than the Interim Submission March 2004. Some figures vary between the two versions of the submission.
[2] Allen Hansell, Manager for NSW and ACT, Insurance Council of Australia, Transcript of Evidence 7 May 2004, p9
[3] Mr Doug Drysdale, Principal, Professional Financial Solutions, Transcript of Evidence 7 May 2004, p3

7.7 PFS also developed the project in a transparent way by consulting widely to seek data. Throughout their submission, the consultants have explained the assumptions on which the model is based. Interested groups have had the opportunity to comment on the interim submission to the Committee and to attend a public forum on 29 March 2004 where the consultants explained their work. The consultants also undertook additional analysis at the request of the Property Council of Australia and the Local Government and Shires Associations of NSW.[4]

7.8 The Committee is also assured that PFS handled private information obtained as part of the project in accordance with privacy agreements and that this information will be destroyed at its completion.[5]

## Background to the model

7.9 PFS was asked to develop a model which would determine the expected revenue generated under various scenarios for a property levy. The brief included estimating the number of individual properties with insurance which would contribute more or contribute less under proposed arrangements than they do currently.[6]

7.10 The model provides information about the amount contributions made by types of property in each geographic region. The model also estimates the amount State and Local Governments would contribute if a property-based levy were charged on their properties.

7.11 The model works by matching data about insurance policies to the value of properties. The Valuer General provided the value of each valued property, as well as the allocated value of each strata block, to determine a value for each rateable property at 1 July 2003. The table below summarises this information and shows the total value and average value of land in New South Wales both within the Greater Metropolitan Region (GMR) and the non-Metropolitan region.[7]

7.12 The table shows that land values are much higher in the GMR than outside it and that the number of residential properties is over ten times the number of commercial properties.

[4] Professional Financial Solutions, Final Submission, *Quantitative Modelling of NSW FSL Funding Methods* pp 44-45

[5] Mr Doug Drysdale, Principal, Professional Financial Solutions, Transcript of Evidence 7 May 2004, p4

[6] Professional Financial Solutions, Final Submission, *Quantitative Modelling of NSW FSL Funding Methods* p15

[7] For the purpose of the modelling work GMR was defined in relation to the local government areas in the Sydney, Wollongong and Newcastle, consistent with a definition developed by the Department of Infrastructure, Planning and Natural Resources. PFS included a table listing the local government areas in the GMR in Appendix 2 of their submission

**Land Values in NSW 1 July 2003**

| GMR | Residential | Commercial | Rural | Vacant | Total |
|---|---|---|---|---|---|
| Total Land Value(m) | $441,957 | $71,176 | $23,758 | $10,716 | $547,607 |
| No. of Properties | 1,680,351 | 171,980 | 58,086 | 38,078 | 1,948,495 |
| Average Value | $263,015 | $413,862 | $409,010 | $281,428 | $281,041 |
| **Non- GMR** | **Residential** | **Commercial** | **Rural** | **Vacant** | **Total** |
| Total Land Value (m) | $50,739 | $6,788 | $44,795 | $3,002 | $105,324 |
| No. of Properties | 551,067 | 40,688 | 238,415 | 12,888 | 843,058 |
| Average Value | $92,075 | $166,838 | $187,887 | $232,913 | $124,931 |
| **All Regions** | **Residential** | **Commercial** | **Rural** | **Vacant** | **Total** |
| Total Land Value (m) | $492,697 | $77,964 | $68,553 | $13,718 | $652,932 |
| No. of Properties | 2,231,418 | 212,668 | 296,501 | 50,966 | 2,791,553 |
| Average Value | $220,800 | $366,601 | $231,206 | $269,160 | $233,896 |

Source: Professional Financial Solutions Final Submission *Quantitative Modelling of NSW FSL Funding Methods* p56

7.13 The Committee called for information from insurance companies regarding details of their commercial and household insurance policies on which FSL was paid. The insurance data was used in the model to determine the current number of insurance policies, the total value insured and the amount of FSL collected through insurance policies.

7.14 The two data sets were matched in order to identify individual properties with insurance policies. However, the matching process was complicated because of various data quality issues and different formatting practices between insurance companies. The consultants provide details of the steps taken to manipulate the data in their submission. Eventually PFS was able to match insurance records for over 900,000 properties in the following categories:

| | Number of Matches | % of number of properties |
|---|---|---|
| **Residential** | 836,240 | 37.5% |
| **Commercial** | 26,159 | 12.3% |
| **Rural** | 34,293 | 11.6% |
| **Vacant Land** | 5,898 | 11.6% |
| **Total** | **902,590** | **32.3%** |

Source: derived from Professional Financial Solutions Final Submission *Quantitative Modelling of NSW FSL Funding Methods* p68 and p56

7.15 This table shows that, while around a third of properties were matched with insurance records, the vast majority of these were from the residential sector. There was limited information available about the amount of FSL collected on commercial properties. PFS received 2.7 million insurance records which the Insurance Council estimated covered 80 per cent of the residential market but only around 30 per cent of the commercial market.[8]

[8] cited in Professional Financial Solutions Final Submission *Quantitative Modelling of NSW FSL Funding Methods* p58

7.16 It is also not clear how representative the matched commercial sample is of the sector. There were 314,000 commercial insurance records with an average FSL of $173 but the 23,000 matched records had an average levy of $565.[9] Therefore the PFS database only relates to $14 million of FSL, or between 6 and 8 per cent of the FSL paid on commercial insurance policies.[10]

7.17 This limitation on the matched data arose because of the complex nature of commercial insurance products. Residential house and contents insurance relates to a particular property. As noted in chapter four, the insurance industry generally imposes FSL on commercial insurance in the categories of:

- Fire, Industrial Special Risk, consequential loss; and
- Contractors All Risk (excluding public liability).[11]

7.18 Some of these policies are not linked to business premises. Policies can cover multiple addresses. The consultants were also not provided with complete information on ISR policies.[12]

7.19 With these limitations, the matching process enabled the contractors to demonstrate the current amount of FSL paid in the three sectors as shown in the table below.

| | Average FSL paid ($) | Mean FSL paid ($) |
|---|---|---|
| **Greater Metropolitan Region** | | |
| Residential properties | 112 | 101 |
| Commercial properties | 789 | 234 |
| Rural properties | 127 | 112 |
| **Non-Greater Metropolitan Region** | | |
| Residential properties | 86 | 81 |
| Commercial properties | 272 | 107 |
| Rural properties | 108 | 92 |

Source: Professional Financial Solutions Final Submission *Quantitative Modelling of NSW FSL Funding Methods* pp84-85

## Levy design factors

7.20 The consultants estimated the amount of revenue required to be raised through a levy at $412 million. This was based on the amount currently raised from insurance companies, initial estimates of the costs of administering a new scheme and the amount of stamp duty and GST revenue projected to be foregone by the State Government if the FSL was no longer imposed on insurance policies.[13]

7.21 In designing the options for a property-based levy, a number of decisions were made about the types of property that should be included. For instance, the 19 different property types included in the Valuer General's database were simplified to four basic

[9] ibid p61
[10] ibid p62
[11] Supplementary Submission No 61 Insurance Council of Australia, p2, Submission No 49, NSW Treasury, p49
[12] cited in Professional Financial Solutions op cit p62
[13] ibid p22

types of commercial, residential, rural and vacant. It was decided to treat rural and vacant land in the same way as residential for the sake of simplicity of modelling. A decision was also made to exempt mining properties because some of these provided their own Mines Rescue Service.[14]

7.22 The simplest form of a levy would be a flat fee. Based on the existing ratios of contributions through FSL on insurance the consultants estimated this would be $72 for residential and $1,085 per commercial properties.[15] However this approach would not account of other factors such as equity, access to fire services and fire risk, ability to pay or potential use of fire services.

7.23 In the options developed PFS established:

- **Base fees** a minimum fee for each sector to reflect universality of service provision.
- Levies on the value of property **(ad valorem levies**) as a proxy for the owner's ability to pay and the level of benefit which could be derived from fire services.
- **Second level ad valorem levies** in the commercial sector - it was considered that for properties above $500,000 in value a second higher ad valorem levy could be imposed to reflect the tendency of larger businesses to have additional insurance. This reduced the impact of a levy on smaller commercial properties
- **Maximum levies** were developed to reduce the effect of the ad valorem levies in both sectors. These were set at $175 for residential and $200,000 or commercial properties.[16]

## Scenarios

7.24 The Committee asked the modellers to investigate options for funding fire services through a levy based on a consideration of the inquiry's Terms of Reference 4 that new arrangements should:

> a) ensure, to the maximum extent possible, that all those that benefit from the provision of fire services contribute to funding the fire services;
>
> b) broadly match funding contributions to the level of service provided to the taxpayer and/or the risk of fire affecting each taxpayer;

7.25 The Committee asked PFS to develop three different scenarios for funding. These were based on principles that the commercial and residential sectors in the metropolitan and non-metropolitan areas should contribute to fire services in proportion to:

- the level of benefit received from fire services;
- the amount of use made of fire services; and
- the level of service available in the area.

7.26 The ratios derived under these three options could also be applied at an aggregate level to modify an insurance system or introduce a hybrid scheme based on both property values and insurance.

[14] ibid p24. The number of these properties was reduced in the final report as only some of the mining properties provided their own service.
[15] ibid p26
[16] ibid pp23-27

7.27 Of necessity, these options were based on a range of assumptions and generalisations which simplify a complex situation. For instance, in order to identify the amount of benefit received from fire services, the model used as a proxy the value of insurance payments for fire related loss in the commercial and residential sectors. The most recent data available indicates that over 70 per cent of such claims were from the commercial sector.[17] The modellers indicated that they had reservations about the reliability of this data:

> **CHAIR:** Should the Committee recommend replacing the current funding system with the property system, questions will arise as to why each sector contributes the amount that they do if we look at some of the scenarios that you have given. You attempted to define this initially on use, service and beneficiaries. Can you explain why you chose to step back from this approach in the final submission?
>
> **Mr DRYSDALE:** I think under the - we tried to get a beneficiaries model based on the amount that was actually being paid in fire claims for the different sectors and we have had - the data there actually indicated that commercial in the last couple of years was I think something like 70, almost 70 per cent of all claims, which it just seemed an incredibly high figure given it was only I think 8 per cent of all properties are commercial. If you go back into earlier years the data was different and the data was not based on the whole of the insurance market. The only data we could get was based on, for some years, 60 per cent and some years 30 per cent of the markets. You were having to gross up figures and then compare them.[18]

7.28 The Committee notes that the NSW Fire Brigades and the Rural Fire Service query the basis of all of these scenarios.[19]

## RESULTS

7.29 PFS developed three scenarios and provided results. These three scenarios did not provide entirely satisfactory outcomes. Far too many in certain groups would contribute far greater rates to fire services than they do under the current scheme. For instance, because there is a high level of cost per property to provide fire services in the non-metropolitan area despite the lesser availability of fire services, under the "User Pays" scenario the costs of a property levy would be very high for non-metropolitan property owners. Only 4.7 per cent of non-metropolitan residential property owners would contribute less. However under the Service level scenario non-metropolitan property owners faced much lower costs because the lower rates of the levy were compounded by lower property values. 98.8% would be contributing less under this scenario.[20]

7.30 PFS then developed a fourth option called the "combined option" because it combined some features of the other three and attempted to reduce the apparently high costs for low value commercial properties by imposing an initial ad valorem rate at the same level as for residential properties. This levy is described below:

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[17] Professional Financial Solutions op cit p28
[18] Doug Drysdale, Principal, Professional Financial Solutions, Transcript of Evidence 7 May 2004, p6
[19] Submission No 87, NSW Fire Brigades and NSW Rural Fire Service Joint submission
[20] Professional Financial Solutions Final Submission *Quantitative Modelling of NSW FSL Funding Methods* pp8-9

| Property Type | Base Levy | Ad valorem Rate 1 (per $1,000 of LV) | Ad valorem Rate 2 (per $1,000 of LV) |
|---|---|---|---|
| Residential – GMR | $50 | $0.13 | Nil |
| Commercial – GMR | $50 | $0.13 | $5.55 |
| Residential – Non-GMR | $30 | $0.13 | Nil |
| Commercial – Non-GMR | $30 | $0.13 | $5.55 |

Source: Professional Financial Solutions, Final Submission, *Quantitative Modelling of NSW FSL Funding Methods* p8

7.31 The results of the individual comparisons are shown below:

| Property Type | Share of Revenue | % Cont. Less | Av. Contribution Reduction | Av. Additional Contribution |
|---|---|---|---|---|
| Residential – GMR | 35.9% | 75.1% | $36 | $17 |
| Commercial – GMR | 53.0% | 60.0% | $532 | $2,910 |
| Residential – Non-GMR | 8.7% | 96.9% | $45 | $16 |
| Commercial – Non-GMR | 2.4% | 85.8% | $239 | $418 |

Source: Professional Financial Solutions, Final Submission, *Quantitative Modelling of NSW FSL Funding Methods* p9

7.32 Under this example, a residential property owner with land valued at the average in the metropolitan area of $263,000 would pay a total of $84 (the $50 base fee plus $34 in ad valorem levy). Although most commercial property owners would contribute less, those with properties above $500,000 in value would face increased costs of more than $2,000.

## RESPONSES TO THE MODELLING

7.33 The Committee sought public comment on the interim submission from Professional Financial Solutions and held a public meeting in Parliament House on 29 March 2004. The Committee received 23 submissions in response to the interim submission.[21]

7.34 Submissions from Local Government were concerned that the modellers did not address how Local Government contributions to the fire services were calculated and appeared to indicate that local councils would be expected to maintain their direct contributions as well as pay a levy on their property.[22] The Woollahra Municipal Council and the Vaucluse Progress Association submissions were particularly concerned with the current basis of determining Local Government contributions to the fire services based on land value as this is not linked to risk of fire.[23] There was also concern that the estimated administrative costs of $2 per transaction might be too low although the Hornsby Shire Council considered that this might be adequate for ongoing costs but not for introducing the system.[24]

[21] These are submissions No 66 to 83 and 86 and 87 listed in Appendix 2. These are available from the Committee's website.
[22] Submission No 76 Local Government and Shires Associations of NSW, p1, Submission No 77, Parkes Shire Council p1
[23] Submission No 66 Vaucluse Progress Association p1, Submission No 74 Woollahra Municipal Council pp1-2
[24] Submission No 78, Hornsby Shire Council, p3

7.35 The Fire Services expressed the following concerns about the modelling work including:

a. The statistical validity of the data – particularly

- the exclusion of residential units from the model and
- the low number of matched records in the commercial sector.

b. The assumptions supporting the three scenarios for attributing costs between the different sectors including:

- the 56:44 ratio between the commercial and residential sectors. The services argue this does not reflect the balance of risk between the sectors rather the relative level of insurance held by the sectors, This should not be transferred to a new system;
- the indirect benefits flowing from fire services such as education and fire prevention that were not addressed in the user pays and beneficiary pays scenarios;
- using insurance claims as a proxy to measure the benefits of fire services rather than actual fire service delivery; and
- the 100:60 service standard ratio between the metropolitan and non-metropolitan areas was not well justified.

c. The amount of funds required –

- the report did not include consideration of bad debts and transition costs and underestimated the cost of administering scheme;
- the report only covered the costs of operating the services without recognising the costs of maintaining equipment owned by local councils which is used by the RFS.[25]

7.36 State Forests considered its properties should be exempt from any property levy as the organisation currently contributes $16 million a year to fire suppression.[26] A submission from the Department of Housing indicated that the modellers had not included its residential property holdings in the calculations. The Department estimates the cost to the agency of a levy as described in the PFS report on its property holdings at $10 million annually. Of this, $7 million would be due to the base levy of $55 being applied to public housing properties. The Department does not recover market based rents from its clients who are predominantly low income earners and the socially disadvantaged, and it does not receive community service obligation funding from Treasury. Thus it would find it difficult to absorb the additional cost of a levy on its properties.[27] Other submissions commented that a property levy was not related to risk of fire.[28]

7.37 Some submissions supported the introduction a new levy. The Insurance Council of Australia (ICA) noted that the model understated the number of people who would

[25] Submission No 87, NSW Fire Brigades and NSW Rural Fire Service Joint submission, pp1-4
[26] Submission No 75, State Forests, pp1-2
[27] Submission No 88, Department of Housing, pp2-3
[28] Submission No 67, David Lewis Northbridge Consulting, p1, Submission No 68, Council of the Shire of Jerilderie, p1

contribute less as it neither included information on tenants nor on residents in strata units who would face lower costs for contents insurance. The ICA considered that commercial tenants would also face considerably lower insurance costs.[29]

7.38 A submission from Riverina Wool Combing commented that the company was liable for $236,000 in FSL in 2003 but under the combined option, they would only pay $1,726.82.[30]

7.39 Following examination of the various models, the Property Council of Australia revised its earlier positions, with a representative expressing the following:

> **Mr MORRISON:** We are very happy to continue working with the modellers and with the community to try to find a solution but, to be frank, we are teetering on the edge in terms of our support for reform, because currently we are seeing currently massive increases for business, but we will talk about that in a moment.[31]

7.40 Mr Morrison went to comment

> **Mr MORRISON:** It also assesses risk on a variety of non- fire-related elements which I think is what has been shown is the fire-related element is becoming a less and less important - or other issues are becoming increasingly important in the assessment of the insurance risk. I mean, I do not think - certainly the current system has got many flaws. Moving to a property based system theoretically should be a cleaner, simpler, more equitable system. I think what the modelling has highlighted is a big disjuncture in that theoretical case which needs to be resolved. If it is not resolved then, really, I think you are going to have a lot of business concern about that and if it is resolved then it is probably going to take complicating the model somewhat to resolve it.[32]

7.41 The Property Council was particularly concerned about projections of the large increases in direct costs for high value commercial properties. Some building owners reported increased costs of 2,000 per cent. The Council proposed a range of alternative funding scenarios to reduce this impact.[33]

7.42 The consultants' assumptions about the reduction in direct State Government contributions of $31 million to compensate for reduced stamp duty and GST income was commented on unfavourably in a number of submissions.[34]

## FINAL SUBMISSION

7.43 As a result of these comments, PFS produced a final submission to the Committee. This included updated information and an additional option designed to minimise the effect of a levy on owners of high value commercial properties. It did this by increasing the base levy for non-metropolitan properties, increasing the first ad valorem rate for commercial properties and by including a levy on motor vehicles of

[29] Submission No 80 Insurance Council of Australia, pp1-3
[30] Submission No 69, Riverina Wool Combing Pty Ltd
[31] Mr Ken Morrison, Executive Director, Property Council of Australia, Transcript of Evidence, 7 May 2004, p17
[32] ibid p21
[33] Submission No 83 Property Council, pp5-6
[34] Submission No 76 Local Government and Shires Associations of NSW, p2, Submission No 83 Property Council, p5, Submission No 74 Woollahra Municipal Council, Submission No 68, Council of the Shire of Jerilderie, p1

$13.50 to raise 15 per cent of the levy.[35] The tables below show the levy structure and results of modelling this option:

| Property Type | Base Levy | Ad valorem Rate 1 (per $1,000 of LV) | Ad valorem Rate 2 (per $1,000 of LV) |
|---|---|---|---|
| Residential – GMR | $55 | $0.11 | Nil |
| Commercial – GMR | $80 | $0.20 | $2.97 |
| Residential – Non-GMR | $55 | $0.11 | Nil |
| Commercial – Non-GMR | $80 | $0.20 | $2.97 |

Source: Professional Financial Solutions, Final Submission *Quantitative Modelling of NSW FSL Funding Methods* p12

| Property Type | Share of Revenue | % Cont. Less | Av. Contribution Reduction | Av. Additional Contribution |
|---|---|---|---|---|
| Residential – GMR | 42.3% | 76.2% | $36 | $15 |
| Commercial – GMR | 39.7% | 49.6% | $693 | $1,251 |
| Residential – Non-GMR | 15.5% | 81.5% | $28 | $12 |
| Commercial – Non-GMR | 2.5% | 52.2% | $326 | $100 |

Source: Professional Financial Solutions, Final Submission *Quantitative Modelling of NSW FSL Funding Methods* p12

7.44 This demonstrates that the average additional contribution by commercial property owners is less than half the increase under the previous option.

7.45 The final report also included a simple three tiered levy for non-commercial properties at different values as shown in the table.

| Land Value Range | 0 to $200,000 | $200,001 to $400,000 | Above $400,000 |
|---|---|---|---|
| **Levy** | $60 | $85 | $145 |

Source: Professional Financial Solutions, Final Submission *Quantitative Modelling of NSW FSL Funding Methods* p51

7.46 The Committee notes that this would be simple to administer and appears to have little effect on the number of property owners who would contribute less under the option.[36]

[35] Professional Financial Solutions, Final Submission *Quantitative Modelling of NSW FSL Funding Methods* p48

[36] ibid pp51-52

# Chapter Eight - The Current System or a Property-Based Levy?

8.1 This chapter discusses the unresolved issues arising from the financial modelling of the property-based levy. It compares this to the theoretical discussion showing that such a scheme would be more advantageous than the current insurance-based arrangements. Options for addressing the problems of the current scheme are also canvassed.

8.2 The chapter contains the Committee's findings and recommendations about current and future funding arrangements for fire services in New South Wales.

8.3 The role of the State and Local Governments in funding fire services and impact of replacing current arrangements with a property-based levy on these groups are also addressed. These considerations are required under point 3 c. and d. of the Terms of Reference, which state:

> c. consider the implications of any changed fire service funding arrangements for the role of local governments in funding and facilitating the provision of fire services, particularly in rural NSW;
>
> d. consider how the State government's contribution to funding the fire services should be determined within any new funding framework.

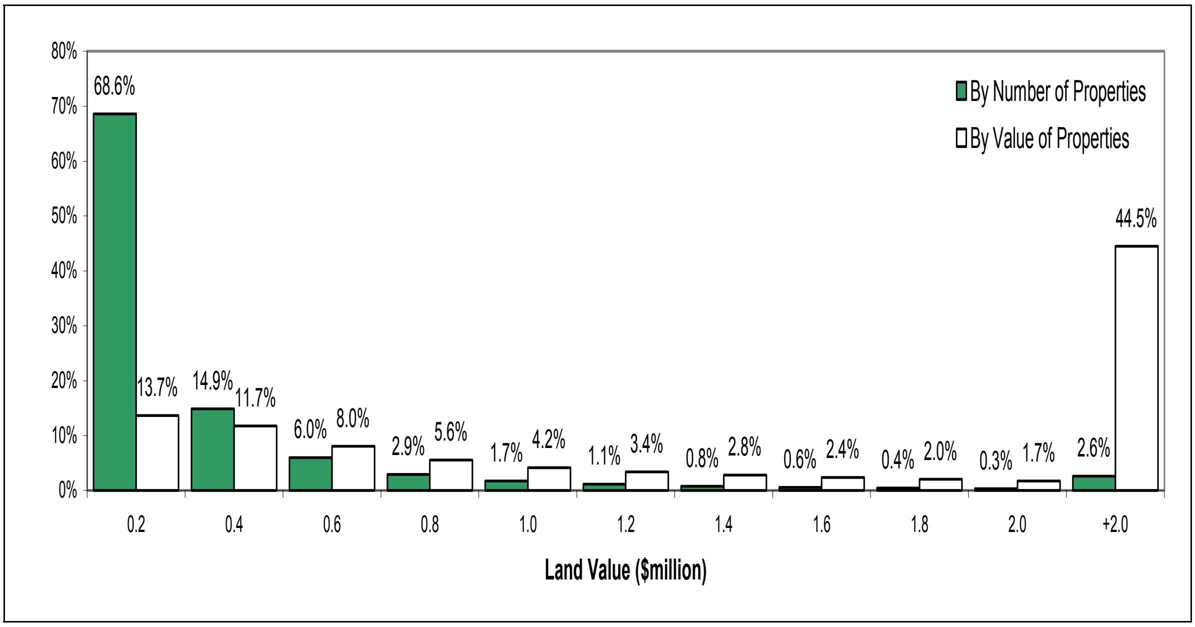
## UNRESOLVED ISSUES

### Impact on commercial sector

8.4 The Committee notes that despite the scale of this project and the thoroughness of the consultants in undertaking the work, there were significant limitations to the available data and, therefore, on the conclusions drawn as a result. Importantly, the consultants were only able to match insurance records with properties for around 11 per cent of the commercial properties. As noted above this sample does not seem to be representative of the level of FSL applied to commercial policies.

8.5 This issue is complicated by the distribution of commercial property values. There is a high number of low value commercial properties but a very small number of very high value properties which would bear a large proportion of the cost of any ad valorem charges. The chart overleaf shows that 2.6 per cent of commercial properties, or around 5,500 by number, are valued at 44.5 per cent of the total value of commercial properties.

8.6 The modellers also could not obtain detailed information about the level of FSL currently paid by commercial tenants compared to the amount paid by building owners. This means that the total levy currently paid for commercial properties is uncertain and cannot be compared to any replacement property levy in a meaningful way.




Source: Professional Financial Solutions, Final Submission *Quantitative Modelling of NSW FSL Funding Methods* p43

8.7 Correspondence from Property Council states that:

> One of our large members has advised that they own and occupy a major Sydney CBD commercial office block comprising 34,000 square metres. Under the existing insurance based FSL they paid $19,331 in FSL on consequential loss of rent and material damage policies in 2003. As the sole tenant of this property they paid another $10,000 in FSL on their contents insurance in 2003. They suggest, however, that if the building was multi-tenanted and the tenants had to procure their own insurance then a figure of $30,000 would more likely have been paid.
>
> Consequently, the owner to tenant FSL contribution ratio for this building is currently 2:1 for a single tenant and 2:3 if multi-tenanted.[1]

8.8 This conflicts with the view of the Insurance Council of Australia::

> **Mr MASON:** Property owners currently pay a fire service levy if they insure on their buildings, but also on the insurances on the machinery, plant and stock, on the industrial special risk policies, business interruption policies, goods in transit policies, motor vehicle policies, and tenants also pay all of the above, except a FSL on the building insurance, but we presume a lot of that is already passed through either in rent or in outgoings under lease agreements.
>
> Our manager in South Australia has advised us that when the fire services levy was reformed in South Australia, they showed there that tenants could contribute anything up to 13 times the contribution that the landlord was paying for FSL on the building.
>
> We do think that there is significant capacity for any increased cost to be passed through without tenants necessarily being unduly penalised. We think that the savings they are going to get in their areas could well offset this.[2]

8.9 The Property Council advises that, in the example provided above, the two best funding scenarios developed by PFS would lead to increases in FSL liability for the building of at least 200 per cent. The Council provided the following table to support this statement:

---

[1] Correspondence from Ken Morrison, Executive Director, Property Council of Australia, 24 May 2004
[2] Alan Mason, Executive Director, Insurance Council of Australia, Transcript of Hearing, 7 May 2004, p10

| | Single tenant | Multi-tenanted |
|---|---|---|
| **Current insurance based system** | | |
| Owner's FSL | $19,331 | $19,331 |
| Tenant's FSL | $10,000 | $30,000 |
| Total FSL | $29,331 | $49,331 |
| **Combined scenario total FSL** | $185,365 | $185,365 |
| FSL % increase | 618% | 371% |
| **Additional scenario total FSL** | $103,205 | $103,205 |
| FSL % increase | 344% | 206% |

Source: Correspondence from Ken Morrison, Executive Director, Property Council of Australia, 24 May 2004

8.10 The Property Council also pointed out that there may be difficulty in passing these increased costs on to tenants in the short term:

> **CHAIR:** And is it your understanding that most commercial leases would interpret this impost as an outgoing and that would be directed directly to the tenant?
>
> **Mr MORRISON:** Yes. It depends on whether it is a net or gross lease. So if it is - some leases are structured and this again depends on the industry so industrial, retail, office will be a bit different but say about 75 per cent of leases in the office sector are net so that outgoings - this would be considered to be an outgoing and it would be passed straight through to the tenant Where it is a gross lease those costs are sort of hidden within the rental structure. That is more common in retail areas. Some industrial areas it is a bit more common so with those then it takes time, I guess, for those lease arrangements to sort of equilibrium with the new cost built in but, certainly even under that structure, then yes, they would be built into rents.[3]

8.11 The Committee has been advised that the insurance industry is currently surveying commercial clients to seek improved information about the amount of levy paid on insurance by commercial property owners and tenants.[4]

## Conclusions

8.12 The Committee finds that the current insurance-based scheme is flawed with a number of problems of inefficiency and potential inequity, however on balance the current scheme continues to perform better in a number of critical areas than the potential replacement.

8.13 As discussed in Chapter Six, a property-based levy theoretically appears to perform better against the majority of taxation principles than the current insurance-based arrangements for funding fire services in New South Wales. A levy on property would meet the four criteria for funding arrangements in this inquiry's Terms of Reference which provide:

> The Committee's proposed funding arrangements should
>
> a) ensure, to the maximum extent possible, that all those that benefit from the provision of fire services contribute to funding the fire services;
>
> b) broadly match funding contributions to the level of service provided to the taxpayer and/or the risk of fire affecting each taxpayer;

[3] Ken Morrison, New South Wales Executive Director, Property Council of Australia, Transcript of Hearing, 7 May 2004, p17

[4] Correspondence to the secretariat from Allan Hansell, Insurance Council of Australia, 3 August 2004

c) be difficult to avoid through changed taxpayer behaviour; and

d) provide a stable base for funding fire services.

8.14 On the basis of the modelling work, the Committee notes that, in the residential sector, a levy based on land value is likely to lead to the majority of property owners contributing less to the fire services and it a more equitable and transparent way of funding fire services. It is the modellers' view that the link to property value broadly reflects the different level of service availability between urban and rural areas. The Committee notes that the modelling work shows that replacing the current insurance based arrangements with a property-based system would broaden the base of the contributions to the fire services in the residential sector. As noted in Chapter Five, residential insurance is not related to fire risks as much as risk of theft. As noted by NCOSS, disadvantaged people who do not take out insurance tend to live in areas where insurance is high because of crime factors. Any reduction in the price of insurance may encourage increased insurance by these groups.

8.15 Unlike an insurance-based scheme, a property-based levy would be difficult to avoid and would provide a stable base for funding fire services.

8.16 However, in the commercial sector, a property levy would narrow the base of those contributing funds to fire services. Such a system only meets the final two criteria for assessing the suitability of arrangements: being difficult to avoid and providing a stable source of funding. This would overcome problems with the current insurance-based scheme of avoidance through business practices such as self-insurance.

8.17 However, on the basis of the evidence before it, the Committee is unable to draw any firm conclusions about the impacts of a change on the commercial sector. More work is needed to ensure the commercial sector is not unfairly disadvantaged by any change to the current system. The Committee concludes that while there are some marginal benefits for the majority of property owners in the residential sector, these are outweighed by the level of uncertainty regarding about the impacts of replacing the current system on other groups.

## OPTIONS FOR IMPROVING THE CURRENT SYSTEM

8.18 The Committee notes that there are a number of options for improving the current arrangements.

8.19 In its submission the New South Wales Rural Fire Service suggests these changes to the current funding model:

- Increase the range of insurance policies that contribute to the fire services levy ie broadening the base of those contributing;
- Link non-fire related emergency responses to categories of insurance and associated contributions;
- Providing incentives to encourage entities or individuals to insure;
- Establish direct contribution to fire services from non-insured, but who wish to contribute; and
- Introduce compulsory emergency service insurance.[5]

[5] Submission No 55, NSW Rural Fire Service, pp3-4

8.20 Similarly, New South Wales Fire Brigades did not support changing the current funding approach. The organisation is supportive of some minor changes to the current funding model to reduce the impacts of current problems with the scheme. The submission suggested reducing the compounding tax effect on insurance by making the taxes non cumulative and calculating the Fire Service Levy as part of the premium.[6]

8.21 NSW Fire Brigades also suggested improving transparency of the scheme by establishing a Fire Services Trust Fund so that the Fire Service Levy collected from premiums would be paid directly into this account to improve transparency.

8.22 The Fire Brigades suggested that base of those contributing could be widened by:

- improving enforcement of collection of FSL from overseas insurance companies providing insurance in NSW;
- developing strategies to promote universal insurance;
- introducing a fire service fee for companies that partly or fully self-insure; and
- imposing a levy on motor vehicle registration.[7]

8.23 The submission also stated that the scheme could be improved administratively by reviewing the weighting of insurance policies and by refining the method of setting the insurance companies' contributions.

8.24 The Committee notes that the NSW Fire Brigades Employees' Union recommended removing Local Government from contributing to fire services at all.[8] Ku-ring-Gai Council recommended that the following changes to the current funding arrangements occur in relation to calculating Local Government contributions to the fire services:

- reduced weighting on average property values to 50 percent;
- the remaining 50 percent of calculation to be based on user pays principles;
- discounts to be provided to councils who demonstrate spending on activities to reduce the risk of fire incidents; and
- annual increases are not to exceed the rate of pegging amount.[9]

8.25 The NSW Fire Brigades submission recommended improving the relationship between the service and Local Government to provide earlier notice to Local Government of the level of contribution required each year to assist in planning. It also suggested implementing a purchaser/provider model with Local Government.[10]

8.26 The Committee sees merit in some of these suggested administrative improvements.

## Reducing compounding tax effect on insurance

8.27 As noted in chapter 4, insurance policies are subject to GST of 10 per cent and stamp duty of 5 per cent. These taxes are applied to the whole premium and the FSL imposed by the insurance company. The application of FSL to policies at the advisory rates would impose additional costs of 16 per cent to residential policies and 27% to

[6] Submission No 54 NSW Fire Brigades, p 6
[7] ibid p3
[8] Submission No 53 and transcript of evidence 26 Nov -p
[9] Submission No 3, Ku-ring-gai Council p 2
[10] Submission No 54 NSW Fire Brigades p3

commercial policies (before GST input credits are claimed). This can deter individuals from insuring prudently.

8.28 The application of GST is a matter for the Commonwealth to determine. However policy holders could also make savings if the state tax of stamp duty was applied to policies before the GST was included. NSW Treasury's submission was opposed to this option. Prior to the introduction of the GST, stamp duty was imposed after Commonwealth taxes and this policy has continued. Furthermore, taxation on insurance was not included as one of the state taxes to be reduced by the introduction of the GST.[11]

8.29 Another option would be excluding the FSL from inclusion in the total premium subject to GST and stamp duty. The Committee understands that this is not possible in the current insurance-based scheme. The FSL is essentially a surcharge voluntarily applied by insurance companies to premiums to recover their obligations rather than a tax on individual insurance policies. In order for the FSL to be exempt, it would require identification of the FSL as a tax on the insurance policy.

## Weightings on policies

8.30 The Committee considers that if the weightings on types of insurance used in calculating the liability on individual insurance companies are no longer appropriate, these should be reviewed and updated to reflect the pattern of activity by fire services. The legislation provides that the Minister is able to alter these weightings if at least two thirds of the insurance companies liable to contribute under the scheme agree and the Commissioner recommends the change.[12]

8.31 The example provided by the NSW Fire Brigades was that the weighting of 2.5 per cent of premiums for motor vehicles may be outdated. On the basis of the number of insurance policies on motor vehicles, NSW Treasury estimated that only about 6 per cent of the total amount of FSL raised from premiums was from motor vehicles.[13]

8.32 In Chapter Three, the Committee noted that in 2002-03, around 21 per cent of the incidents attended by the Rural Fire Service were either motor vehicle fires or accidents.[14] Around 15 per cent of the fire and explosion incidents attended by the NSW Fire Brigades in the same year involved motor vehicles, although this forms a much smaller proportion of the total number of incidents attended by the Fire Brigades.[15]

8.33 The Committee notes that it is quite complicated to determine the actual proportion of the fire services' time used for motor vehicle incidents. Simply counting the number of incidents does not reflect the total effort involved in these incidents. In evidence the Committee was told that about 8 per cent of the Fire Brigades workload related to motor vehicle and hazardous material incidents.[16]

8.34 In designing a property-based levy, Professional Financial Solutions attempted to determine the proportion of the fire services' effort expended on attending incidents

[11] Submission No 49, NSW Treasury, p10
[12] s55(5) *Fire Brigades Act 1989* and s112(5) *Rural Fires Act 1997*
[13] Submission No 49, NSW Treasury, p8
[14] see table following paragraph 3.13
[15] see table following paragraph 3.8
[16] Gregory Mullins, Commissioner, NSW Fire Brigades. Transcript of Hearing, 26 November 2003, p4

involving motor vehicles. However the consultants were unable to obtain enough information the number of personnel used and length of time spent on these activities. The table below shows the consultants' conclusions :

| | Incidents attributable to motor vehicles (including False Alarms) | incidents attributable to motor vehicles (excluding False Alarms) |
|---|---|---|
| **Individual Results** | | |
| NSW Rural Fire Service | 21.2 | 22.8 |
| NSW Fire Brigades | 8.5 | 15.3 |
| **Consolidated Result** | | |
| By Budget | 11.5 | 17.1 |
| By number of incidents | 10.3 | 16.9 |

Source: Professional Financial Solutions Final Submission *Quantitative Modelling of NSW FSL Funding Methods*, p47

8.35 This indicates that it might be reasonable to increase the weighting on these policies to increase the proportion of funding raised from motor vehicle insurance.

## FSL rate imposed on Motor Vehicle policies

8.36 On the grounds of equity, those that use fire services should contribute in proportion to the use of the service. Related to the obligation on insurance companies, is the fact that some insurance companies do not choose to impose FSL on motor vehicle insurance policies and recover their contribution to the fire services from other types of insurance.

8.37 The Committee considers that, if insurers do not currently collect FSL in proportion to the amount of use by motor vehicles, either the rate on these policies should be increased or a levy should be imposed through motor vehicle registration. As there is no current levy on vehicle registrations, in the interest of administrative simplicity, the Committee would prefer insurers to increase the rate on current insurance policies.

8.38 This is a matter for individual insurance companies as they apply the rates of FSL on individual policies as advised by the Insurance Council of Australia. However it would be reasonable, if the weighting applied to premium income is increased following a review, that the costs of this were recovered directly from motor vehicle policies.

## Broadening the type of insurance

8.39 The Committee notes that the Rural Fire Service also recommended broadening the insurance to cover public liability insurance:

> **Mr KOPERBERG:**…. We also recognise that public liability insurance carried by a range of householders, landowners, public authorities and so on is not subject to any levy. However, most major emergencies that require a massive resource from emergency services occur on lands the owners or managers of which invariably carry public liability insurance. However, there is no mechanism for levying that particular stream of income. [17]

8.40 The Insurance Council of Australia, however, was very strongly opposed to broadening the range of insurance policies used to calculate insurance companies' liability. In

[17] Phil Koperberg, Commission, NSW Rural Fire Service, Transcript of Hearing, 26 November 2003, p4

particular the Council commented that it was inappropriate to include public liability insurance as Governments had been working in recent years to maintain the affordability of public liability insurance. If insurance companies passed these costs on to policy holders through FSL the Council argued this:

> …would only hurt those groups that these Governments have been trying so hard to help – including not for profit groups and small businesses. While the Rural Fire Services is a champion of volunteerism it appears this proposition will only serve to set back volunteer efforts in the community by placing public liability insurance beyond their reach.[18]

8.41 The Council also commented:

> During the drought we do not think there is much value in increasing FLS payments associated with crop peril insurance. The market for crop peril insurance is so small that increases to the FLS rate in it would need to be significant to warrant the justification of collection.[19]

8.42 The Committee sees little benefit in extending the type of insurance beyond those which may directly benefit from normal activities of the fire services.

## Offshore insurance

8.43 As noted in Chapter Six, the Committee was unable to obtain any reliable information about the extent of offshore insurance. There is a concern that not all groups that purchase insurance overseas are remitting FSL to the NSW Government. This is causing a disproportionate share of the fire services funding burden to fall on those groups insuring prudently.

8.44 The Committee considers that it is essential for there to be arrangements in place to audit the amount of premiums undertaken overseas and to ensure that FSL is paid in New South Wales on these premiums. The Committee however did not receive reliable information on how this could be enforced.

8.45 The Committee considers it appropriate that the Government review the extent of offshore insurance by commercial policy holders and options for monitoring of FSL remissions from offshore insurance to enhance compliance with legislative requirements.

## Incentives for insurance

8.46 While strategies to encourage all groups to undertake insurance would broaden the base of those contributing to the fire services, these would also be a matter for the insurance companies to pursue, rather than the Government.

8.47 The Committee does not see that there are any feasible options for offering incentives for those taking out insurance available to the State Government.

## Fire services contributions for those without insurance

8.48 The Committee notes that other emergency services such as ambulance services require those who use the service to contribute in some way and may require individuals to pay for the use of the service. The Committee believes that it would be reasonable to consider such a scheme for the use of fire services so that those who

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[18] Submission No 61, Insurance Council of Australia, p7
[19] ibid p7

chose not to insure their properties could contribute a reasonable amount to the fire services in order to avoid paying for the cost of attending a fire should it be required.

8.49 However, as noted in Chapter Two, the Committee does not consider it publicly acceptable nor economically feasible to charge all property owners for attendance at a fire should they be uninsured. In particular, those in the residential sector who are least likely to hold insurance are also least likely to be able to afford a voluntary contribution to fire services.

8.50 There may be more of a need for contributory scheme in the commercial sector where companies may choose to self-insure and may be more able to afford direct contributions to the fire services.

8.51 However it is difficult to determine on what basis such contributions would be made other than on a type of property levy as described in Chapter Seven. Such a scheme would require the development of a new administratively expensive scheme for what is likely to be less than a quarter of households and a minority of businesses.

## User charges

8.52 As noted in Chapter Two, NSW Fire Brigades derives up to 5 per cent of its income from charges for miscellaneous activities such as attending repeated false alarms or hazardous materials incidents. In 2002-03 for instance, the Fire Brigades attended more than 45,000 false alarms and 12,000 hazardous conditions incidents.[20] The *Fire Brigades (Charges) Regulation 2000* enables the Fire Brigades to charge $250 for responding to false alarms.

8.53 The Committee notes the view of the NSW Fire Brigades that, in the case of false alarms, the charges are more in the nature of a deterrent and are used to encourage people to maintain their fire alarm systems appropriately. Such fees are often waived.[21] The Committee sees this as an appropriate mechanism for improving the operation of fire alarms.

8.54 However in the case of hazardous materials, user charging is related to the cost of the clean up activities. The regulation provides maximum hourly rates for the attendance of personnel and equipment ranging from $91.30 for each hour of attendance by a chief superintendent or above to $48.40 for each firefighter. The attendance of a standard pumper is only $108.90 per hour.[22] These maximum rates may not cover the direct costs to the fire service of attending these incidents.

8.55 The Committee notes that only $20,000 was raised from these activities in 2002-03. It considers that these fees should be reviewed by the Government in consultation with relevant stakeholders in order to determine whether they reflect the actual direct costs of this work.

## Improving Transparency

8.56 The Committee notes that the current scheme lacks transparency because policy holders are not informed how much levy is imposed on policies even though this is a legislative requirement. The Committee believes that, despite the administrative complexity of determining the precise proportion of an insurance company's liability

[20] see table following paragraph 3.8
[21] Greg Mullins, Commissioner, NSW Fire Brigades, Transcript of Hearing 26 November 2003, p8
[22] *Fire Brigades (Charges) Regulation 2000,* clause 4

that should be imposed on each policy holder, insurers should comply with the legal requirements to inform policy holders of this amount.

8.57 Another factor contributing to a lack of transparency of the scheme is that there is no mechanism for companies to report how much FSL is collected from policy holders. The Committee notes that the system is complex to administer as insurance payments fall due at different times and premium income varies from year to year. For this reason, establishing a separate trust fund for the payment of FSL directly from premiums to the fund does not seem justified. This would be cumbersome and more expensive to administer than the current arrangements of companies making quarterly payments.

8.58 A more feasible option would be for insurers to report annually to the Government on the amount of FSL collected from policy holders. Members of the public could then be informed of the amount they are contributing individually, the amount collected by companies and the amount companies are meant to contribute to the fire services.

## Local Government contributions

8.59 Local Government operates in an environment of extreme fiscal constraint. Councils have little control over the amount they are required to contribute to fire services as their budget is determined by others.

8.60 The Committee acknowledges that the unpredictable nature of councils' statutory contribution to fire services can place budgetary pressure on some councils. In recognition of this, councils are able to request the Minister to take into account increases in the fire service levy if they seek a special variation to their general rates income under the "rates cap". As an alternative, councils could be involved in formal service delivery agreements as customers of the fire services. While this would improve planning, the NSW Fire Brigades consider that the costs for councils are likely to be higher under this approach.[23]

## PART 1

## FINDING A

A1 The Committee finds that the current insurance-based scheme for funding fire services has provided the essential fire services with a stable and administratively simple revenue source.

A2 However, the current system is flawed because it is not universal and not all who benefit from fire services contribute to funding them. Anyone can choose not to contribute by not taking out insurance at prudent levels.

A3 In the residential sector, there is likely to be a proportion of individuals who do not insure at prudent levels but the Committee was unable to conclusively determine the scope or value of this non-insurance and under-insurance.

A4 In the commercial sector, some organisations choose to self-insure or use deductibles. Some may choose to insure overseas and not remit FSL to the NSW Treasury as they are legally required to do.

[23] Submission No 54 NSW Fire Brigades, p11

A5 The weighting applied to the types of insurance policies used to determine the percentage of levy required from each insurance company has not been updated for some time and may not reflect the pattern of fire services activity.

A6 The amount of Fire Services Levy (FSL) levy raised from individual policies has limited connection to the benefit derived from fire services by individuals.

A7 The FSL charged on motor vehicle insurance is not in proportion to the level of fire services used.

A8 The Fire Services may not recover adequate funds to cover the costs of certain services such as attendance at false alarms or fire safety inspections.

A9 The scheme is not transparent as individual policy holders are not always informed of the amount of FSL imposed on insurance policies.

A10 There is no clear mechanism used by insurance companies to report the amount of FSL collected. In certain years, insurance companies may collect more FSL from policy holders than their liability to the fire services. In other years they may under-collect. The Committee does not find that insurance companies consistently over-collect their liability from policy holders.

A11 Local Government contributions are not always in accordance with the use of fire services in the area and it can be difficult for councils to budget for their contributions at short notice when their ability to increase rates is limited by rate pegging. They also have limited information about the level of service available in the area in the future.

**RECOMMENDATION 1** On the current evidence, the Committee recommends that the Government retain the current insurance-based system having regard to the improvements recommended below.

**RECOMMENDATION 2**: The current funding arrangements be improved by adopting the following measures:

**RECOMMENDATION 2.1** The Insurance Council of Australia increase the advisory rate of FSL imposed on motor vehicle insurance to reflect the proportion of use made of fire services by motor vehicles without increasing the total amount collected from policy holders.

**RECOMMENDATION 2.2** The Minister in consultation with relevant stakeholders review the types of insurance and weightings listed in the legislation as the basis for calculating the contribution required from insurance companies to determine whether they reflect the pattern of activity of fire services.

**RECOMMENDATION 2.3** The Government review the extent of offshore insurance by commercial policy holders and options for monitoring of FSL remissions from offshore insurance to enhance compliance with legislative requirements.

**RECOMMENDATION 2.4** Insurance companies notify individual insurance policy holders of the amount of FSL paid on policies.

**RECOMMENDATION 2.5:** The Government review the charges payable for services rendered by the NSW Fire Brigades to ensure they remain appropriate.

**RECOMMENDATION 2.6:** The insurance industry report annually on the amount of FSL collected from policy holders.

**RECOMMENDATION 3:** The Committee recommends continued investigation of funding arrangements which eliminate the flaws acknowledged in the current system.

## PART 2

# DISCUSSION OF A PROPERTY-BASED LEVY

8.61 If the Government does pursue options for alternative funding arrangements for fire services, this section discusses how such a scheme could be implemented.

8.62 The Government should ensure that such a change is justified for both the residential sector and commercial sectors. There are a number of unresolved issues which warrant further investigation prior to any change to the current scheme. The Committee considers that the first step would be to conduct further research into the extent of FSL paid on commercial insurance by commercial tenants.

8.63 There are a number of other aspects that the Government should consider in designing a property-based system.

## Risk Rating factor

8.64 The property-based system designed by the modellers does not consider the impact of risks of fire. The Committee notes that, unlike in South Australia and Western Australia where improvements to land value such as buildings or landscaping are included in the value of property, there is less direct connection between the value of land in NSW and fire risk.

8.65 The development of a risk rating factor may be appropriate as a way of reducing the impacts on the high value commercial properties and would reflect the diversity of uses within the commercial property sector.

8.66 The Committee is particularly concerned that, under a simple property-based levy, high risk industries with low land values would face much lower costs and would not therefore be contributing in proportion to their use of fire services.

8.67 The Property Council suggested:

> **Ms THOMAS:** I think part of the difficulty of what is occurring here is the vast range of difference between commercial property, whereas residential we can all envisage it is a house, whereas in commercial the size can vary greatly and the nature of the use can vary greatly and the modelling does not actually capture that. Risk would go some way to doing that but the rates would need to be varied as well, the ad valorem rates.
>
> **Mr WHAN**: How would you propose assessing risk on commercial properties or how would you propose that the new system assess risk?
>
> **Ms THOMAS**: Well, we would start by looking at potentially different property types, so you have got the industrial, you have got the retail, so dividing - at the moment we have got commercial properties as one big group. We need to actually differentiate the nature of those properties a great deal. Risk can be done in one category and then you might want to look at regions. I understand in Queensland they have got quite a complicated system, variety of regions. You might want to have a melding of the two. We anticipate that this is complicating the model to an extent but it is getting a better model. You cannot eliminate risk entirely from the equation because it is so fundamental to the use.[24]

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[24] Cheryl Thomas Senior Policy Officer, Property Council of Australia, Ken Morrison, New South Wales Executive Director, Property Council of Australia, Transcript of Hearing, 7 May 2004, p20

8.68 The Committee considers that a simple cost effective risk rating system to augment a property-based levy could be investigated for the commercial sector and used in conjunction with a property levy.

## Residential tenants

8.69 In the residential sector, the modelling work indicates that the funding required from each property is quite low and most property owners would be making lower contributions to the fire services.

8.70 The New South Wales Council of Social Service informed the Committee that if a property levy is introduced, property owners may attempt to pass this cost on to tenants in increased rent. Under current arrangements tenants have limited power to contest rental increases.[25]

8.71 The Committee notes that the consultants estimated the estimated levy in this sector is a maximum of $175 which amounts to $3.00 a week. Most residential properties would be liable for less than this amount and the majority of owners would benefit from a reduction in insurance on the building.

8.72 The Committee also notes that residential tenants who have insurance on contents would be major beneficiaries of a changed system by reduced costs for insurance.

## Concessions

8.73 The Committee notes that other States with property-based fire services levies also have a range of concessions for pensioners and concession card holders. The New South Wales Council of Social Service recommended the need to build in a robust concession scheme for those on low incomes, not just those receiving benefits.[26]

8.74 The effect of including concessions in a property-based system would be a narrowing of the base of those liable to contribute to fire services and an increase in the costs of a levy for other property owners. PFS estimated the cost of providing 50 per cent concession from a property levy to the more than 500,000 householders currently receiving a pensioner concession on rates to be at least $10 million and up to $17 million.[27]

8.75 Local Government was also concerned that they would end up bearing some of the costs of concessions as they do under the concession scheme for council rates.[28]

8.76 Given that insurance companies currently give no concessions on insurance, those low income property owners who insure should benefit from this removal of FSL. However, as noted in chapter four, low income groups are less likely to have insurance. The high cost of insurance can deter people from insuring their property prudently. A change to a property levy would reduce the price of insurance and may encourage more people who may be deterred from insuring by its high price to change their view:

[25] Gary Moore, CEO, NCOSS, Transcript of Evidence, 7 May 2004, p33
[26] Gary Moore, CEO, NCOSS, Transcript of Evidence, 7 May 2004, p32
[27] Professional Financial Solutions Final Submission *Quantitative Modelling of NSW FSL Funding Methods* p10
[28] Shaun McBride, Senior Policy Officer, Economics and Development, Local Government and Shires Association, Transcript of Evidence, 7 May 2004, p40

**Mr McLEAY:** Do you find that the people you represent have expressed a view that they do not purchase insurance at the moment because there is a fire service levy on it and therefore it makes it unaffordable?

**Mr MOORE:** Can I say what evidence that we have from quantitative and qualitative work in this area suggests - and I guess this is one of the geographic issues about ratings and about risk and about the price of policies - we have an unfortunate, I guess, connection at times between disadvantaged communities and higher rate insurance premiums. I do not want to discuss that necessarily that connection or not but what it means is that often people who are more stretched financially, lower income households, potentially would be paying higher premiums for which the levy goes on top because of the risk rating arrangements in the insurance industry and that is a very difficult circumstance because in a sense it perpetuates inequality, in our view.[29]

8.77 According to the financial modelling, the cost of a property levy for the residential sector is likely to be the same or lower than the existing FSL contribution. Therefore the Committee does not consider there should be any concessions from the scheme at this stage.

## Updating the scheme

8.78 The Fire Services have expressed concern that a property levy system would not provide sufficient flexibility in generating income.[30] The Committee sees this as a minor issue, as under current arrangements, the amount required is annually updated in accordance with the budgetary needs of the fire services. Similar administrative arrangements could be established for any replacement funding scheme. Such a system would be flexible, robust and transparent.

## FINDING B

B1 The Committee finds that the majority of submissions to the inquiry supported introducing new arrangements and there is a perception in the submissions that a levy based on unimproved capital value (land value) would be the most efficient, equitable and transparent way of funding fire services.

B2 The Committee finds that detailed financial modelling shows that, in the residential sector, replacing the current insurance-based arrangements with a property-based system would broaden the base of the contributions to the fire services in this sector. However the majority of property owners currently holding insurance would be contributing only marginally less to fire services through a property levy than they currently do.

B3 In the commercial sector, a property-based system would narrow the base of those contributing funds to fire services. A significant number of property owners would be contributing a great deal more than they currently do. Further research is needed to ascertain the true impacts of this approach.

B4 Unlike South Australia and Western Australia, where improvements to land are included in property valuations, there is less connection between the NSW system of property valuation and fire risk. In the commercial sector, it would be appropriate for risks of fire to be considered as an additional basis of calculating contributions to the fire services.

B5 The Committee does not consider it efficient to introduce a new, administratively complex system for the residential sector alone.

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[29] Gary Moore, CEO, NCOSS, Transcript of Evidence, 7 May 2004, p34
[30] Submission No 87, NSW Fire Brigades and NSW Rural Fire Service Joint submission

B6 The Committee considers that it would be equitable for a levy to be imposed on motor vehicle registrations in proportion to their use of services by the two fire services and reduce the amount raised from a levy on real property by the same amount. This could be administered through the vehicle registration system.

**RECOMMENDATION 4.1** The Government should commission further research to ascertain as far as possible the impacts of introducing a property-based levy for funding fire services on the commercial property sector.

**RECOMMENDATION 4.2:** In relation to commercial properties only, the Government should explore a simple system of fire risk factors or property use factors to identify those commercial properties most at risk of fire to use in conjunction with a levy on land value.

**RECOMMENDATION 4.3:** In order to distribute the burden of funding fire services more equitably, there should also be a levy on motor vehicles to raise funds in proportion to this sector's use of fire services without increasing the total amount of funds to be raised. This should be collected by the Roads and Traffic Authority.

**RECOMMENDATION 4.4:** The property-based system should be reviewed annually to reflect the amount of revenue required to fund the fire services and changes in property values.

## IMPACT ON LOCAL GOVERNMENT FUNDING AND SERVICE PROVISION

8.79 As described in Chapter Three, Local Government is statutorily required to provide 12.3 per cent of the funding for the NSW Fire Brigades and 13.3 per cent of the funding for the Rural Fire Service.

8.80 The option of a property-based funding system would mean that local councils were removed from contributing to the fire services through rates notices. Instead, Local Governments would be required to contribute to funding fire services based on the value of its property holdings, as would other property owners.

8.81 Generally, local councils seemed to favour contributing to the fire service based on the value of council property. To do so would ensure that all property owners were contributing on a similar basis.

> **CHAIR:** Do you think the Council should pay a levy if it goes to a rate base on their land?
>
> **Mr TOZER:** I would think we would have to pay a levy.
>
> **Mr TICKNER:** Provided that we are not contributing the 13.3 per cent as well. That is the main concern for us.[31]

8.82 Similar views were expressed in other evidence:

> **CHAIR:** With your proposed property levy would you advocate that the levy should be put on council-owned property and buildings as well as State Government-owned buildings?
>
> **Mr STEWART:** Yes, I believe that would be equitable.
>
> **CHAIR:** A levy on every piece of land?
>
> **Mr STEWART:** Yes.
>
> **Mr HART:** The risk is the same, no matter who is the owner or the tenant of the land.[32]

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[31] Leonard Tozer, Café Proprietor, Mayor, Gundagai Shire Council, and Graeme Tickner, General Manager, Gundagai Shire Council, Transcript of Hearing, 27 November 2003,p14

[32] Leslie Hart, Mayor, Tallaganda Shire Council and Alan Stewart, General Manager, Tallaganda Shire Council, Transcript of Hearing, 27 November 2003, p27

8.83 The financial modelling did not assess the way Local Government contributions were calculated. It assumed that if direct contributions were removed there would be an equivalent saving to the ratepayer.

8.84 The Committee notes that the amount contributed by different local councils varies in accordance with the cost of the local fire services in the area and, for councils in the Greater Sydney Area in accordance with a rolling average of land value over the past five years. As noted in previous chapters this is a source of inequity. It is also not transparent and the majority of ratepayers are probably unaware of the amount they are contributing to fire services through rates.

8.85 The NSW Fire Brigade Employees' Union suggested that, as local councils no longer have a direct role in managing the Fire Brigades, they should no longer be required to contribute directly:

> **Mr READ:** It is, we believe a minor adjustment. I took on board the views of Commissioner Koperberg. By removing the local government funding contribution, of course, you also remove that weight and burden from ratepayers in New South Wales. We are proposing that that gap be made up instead by the State Government and insurance companies. The continued role of local government has no real basis. Certainly in the case of the New South Wales Fire Brigades, prior to 1990 where there was a Board of Fire Commissioners, local government was represented on that board and is no longer. Local government has little, if any, role in the operation of the New South Wales Fire Brigades, and we see no role for local government to be involved in its funding.[33]

8.86 The Committee considers that, given the increasing professionalism of the Rural Fire Service and the decreasing role of Local Government in managing these operations, similar arguments would apply to this service as well.

8.87 The final version of the PFS submission report includes an estimate of the actual costs of removing the Local Government contribution averaged over all sectors. This increased the amount of revenue required by a levy of 15.5 % per cent.[34] This would be offset by lower local council rates which would vary in accordance with the difference between the individual local council's contribution under the current system and under a property levy.

8.88 Another area of major concern under a property-based approach is the collection of the levy. The option favoured by NSW Treasury would be for local councils to collect the levy on behalf of the state, through rate notices.

> The simplest way of administering the levy on fixed property would be through local government rate collections with the levy separately identified on rates notices and independent of rate setting arrangements. The existing administrative structures at the local government level would provide for a low cost mechanism for collecting the levy but there would be some variability in rate collections between localities as the timing of rate payments differs between councils.[35]

8.89 Of those supporting the use of local councils in collecting the levy, the majority wish to see the levy appear on rate notices as a clearly identifiable contribution to the State Government. One Council told the Committee:

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[33] Mr Chris Read, State Secretary, NSW Fire Brigade Employees' Union, Transcript of Evidence 26 November 2003, p13

[34] Professional Financial Solutions Final Submission *Quantitative Modelling of NSW FSL Funding Methods* p45

[35] Submission No 49, NSW Treasury, p26

**CHAIR:** In saying that, does a separate item mean that the levy would be sent out on a different mail-out or piece of paper, or would that be incorporated as a separate line item to your existing rate notices?

**Mr GENTNER:** Our preference would be as a separate item completely, but in the worst-case scenario as a separate item on the rate notice. But we would like to see it completely divorced from the rate notices.[36]

8.90 Identifying the levy on rate notices as a State Government charge would be simple to introduce and would ensure that taxpayers are aware of the charges they are required to pay and would improve transparency. As discussed earlier, there is no obligation for councils to inform ratepayers how much the levy is on their property. By clearly identifying the new property levy, ratepayers know how much they are contributing. The Department of Local Government has informed the Committee that local councils are not currently able to make collect levies except for the services they provide.[37] Special legislation would be required to enable local councils to collect this levy as agents for the State Government.

8.91 Councils, however, did not seem to favour being responsible for the collection of bad debts. Under the current rating mechanism councils are responsible for collecting their own debt and have options available to them to recover that debt.

8.92 However, given that the property levy is a state charge, the council may not have the same ability to recover the debt from property owners. The Committee was advised that in Western Australia councils chose to take responsibility for recovering these debts because it was administratively convenient.[38] This is unlikely to be the case in New South Wales.

8.93 Collecting the levy through council rates would possibly require the additional expense of administration or collection costs. In property-based funding jurisdictions, councils are paid an administration charge based on either the number of rate notices collected in the councils, as is done in Queensland or on the number of rate notices and the amount of ESL collected, as in Western Australia.

8.94 The actual amount of the administration charge varies amongst councils and other Government bodies. NSW Treasury suggested that they would like to see local councils paid around $2 to $3 per household, or less if possible.[39]

8.95 Others, such as the Local Government Association of NSW and the Shires Association of NSW suggested that councils should be paid a commission in the range of 4 per cent to 5 per cent.[40]

8.96 The actual commission per rate notice should be set at a level that covers the cost of the local council billing ratepayers (including postage), collecting the levy and administration charges.

8.97 Contributing as any other property owner would see Local Governments transferring their existing fire fighting assets to the Rural Fire Service. While the exact cost of

[36] Karl Gentner, General Manager, Jerilderie Shire Council, Transcript of Hearing, 27 November 2003, p19
[37] Submission No 79, Department of Local Government
[38] Meeting between Committee and Western Australian Local Government Association, 2 February 2004
[39] Michael Clark-Lewis, Senior Director, Revenue Strategy Branch, NSW Treasury, Transcript of Hearing, 21 November 2003, p29
[40] Submission No 42, Local Government Association of NSW and the Shires Association of NSW, p35

transferring the assets from Local Governments is not known, the Committee heard in evidence that:

> **Mr STEVE WHAN:** You gave evidence earlier about the cost of maintaining the fleet and equipment that is currently with local governments and the possibility of transferring it. Do you have an estimate of the recurrent cost of that fleet? Is it included in the $70 million in local government contributions or is it additional?
>
> **Mr KOPERBERG:** We have based our figures on a depreciated value of the assets. In addition to the $455 million worth of vehicles and the $524 million worth of real estate, $247 million in ancillary equipment was provided over the past nine years. That makes an estimated total of $1.2 billion, or in that order. It is vested in local government. Land tenures on which stations are sited vary right across the spectrum of land tenures. No future local government involvement would almost undoubtedly lead to a transfer of those assets. It would seem rather strange were a different funding system to be responsible for the provision of the assets and yet they were vested in an entity with no financial responsibility for the maintenance of them and what have you.
>
> So it stands to reason that New South Wales, the State, would be faced with a significant financial impost in bringing all those assets across to the State, but of far greater significance is the very real possibility that those who no longer contribute to the scheme will play no part in what was traditionally, historically and conventionally their responsibility in looking after that and maintaining it because it does not have that responsibility anymore. We have not done an estimate on how much that would cost but a figure in the order of $20 million would not be unreasonable.[41]

8.98 This view was raised in later public hearings and the Committee heard evidence suggesting that:

> **Mr STEVE WHAN:** But if the Rural Fire Service, I think as you said in your submission, took control of the ownership of the assets and infrastructure, they would certainly incur a fairly substantial cost, which I acknowledge that councils are currently taking on.
>
> **Mr TAYLOR:** The firefighting fund reimburses councils for the expenses they have met in maintaining the fire equipment. So in the full equation the Government is already meeting those costs of maintaining the assets that are devoted to firefighting. So I would suggest it is not going to change.[42]

8.99 Questions have been raised throughout this inquiry discussing the extent of service provision if local councils were removed from the funding mix under a property levy. The concern revolves around the notion that if Local Government was removed from direct statutory contributions, councils may also opt out of other service arrangements. In its submission the Rural Fire Service pointed out that a major risk of changing the funding arrangements was that councils would no longer make voluntary contributions of money and resources:

> Over and above the statutory contribution to the Rural Fire Fighting Fund, councils provide financial assistance directly to brigades at an estimated cost of $20M per annum. This does not include the support provided by councils through the utilisation of council owned infrastructure etc.
>
> The potential of councils withdrawing from direct and indirect financial support to the brigades could have a negative impact on the NSW Rural Fire Service Brigades at a local level.

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[41] Phillip Koperberg, Commissioner, Rural Fire Service, Transcript of Hearing, 26 November 2003, p11

[42] Warren Taylor, Deputy Director, Strategic Services, Local Government and Shires Association of New South Wales, Transcript of Hearing, 26 November 2003, p38

Councils will seek the transfer of assets currently vested in them (including approximately 3,500 fire fighting vehicles and 2000 brigade stations and other facilities) to the State Government and the financial consequences of this would be significant as well as the upkeep requirements.

It is very important that the strong culture of local government involvement (as a land management agency) in the day-to-day management of volunteer brigades, is not adversely affected by funding changes, which effectively disenfranchises local councils' support.[43]

8.100 This issue was also raised in evidence before the Committee:

**CHAIR:** The Committee has been told that many councils contribute more than they are required to for their local fire services, especially rural fire services, which are an integral part of many communities. Do you think that by removing the levy, local councils may lower voluntary contributions and, therefore, lower service levels?

**Mr SMITH:** No, not in the slightest. I believe that the community's commitment, especially from local government to their rural fire services, is very high and that is why I spoke earlier about the service delivery processes, which are often not in direct fire-type contributions; they could be the use of buildings. They are often the use of plant and equipment, which I do not believe would diminish in any way, shape or form. I might add that New South Wales Fire Brigades has not been that close to local government for many years, but whenever there is a requirement—from my experience in my area—for local government commitment to the New South Wales Fire Brigades, whatever they have asked for, they have got, without any qualms.[44]

8.101 The Committee was told in South Australia that in rural areas there was no lessening of voluntary or in-kind support after formal links between the fire services and Local Governments were removed.[45] The Committee trusts that in New South Wales Local Government would continue to work with and provide voluntary support to the fire services despite no longer contributing a fixed proportion of the services' funding.

## FINDING C LOCAL GOVERNMENT ROLE AND CONTRIBUTIONS

C1 The Committee finds that the current arrangements for determining local council contributions to fire services are disproportionate in some cases and not transparent to ratepayers. If the insurance-based system is changed, Local Government contributions to fire services should be based on the value of council land. This would mean that the direct contributions from councils would be lower.

C2 The most administratively efficient means of collecting a property-based levy would be through the council rates billing system although the levy should be separately identified as a contribution to the NSW fire services.

**RECOMMENDATION 5.1:**Under a property-based system, Local Government should no longer be required to maintain direct contributions to the funding of fire services, but instead councils should pay a levy based on the value of their land.

**RECOMMENDATION 5.2:**The levy for a property-based system should be collected by councils at the same time as collecting rates. Such a levy should be clearly identified as a NSW fire services levy.

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[43] Submission No 55 Rural Fire Service p3
[44] Alan Smith, Executive Member, Local Government Association of New South Wales, Transcript of Hearing, 26 November 2003, p39-40
[45] Meeting between Committee and Emergency Services Administration Unit, 4 February 2004

**RECOMMENDATION 5.3:** Local councils should be paid a suitable amount per collection. This amount should be set at a rate that adequately covers the administrative costs of collecting the levy and should be determined in consultation with the Local Government and Shires Associations.

## STATE GOVERNMENT CONTRIBUTION

8.102 As discussed in Chapter 4, the State Government currently provides 14 per cent of the total statutory funding contribution to the NSW Fire Brigades and 13 per cent to the Rural Fire Service. For 2003-04, these estimates are approximately $55 million and $16 million respectively.

8.103 The majority of submissions to the inquiry are in favour of the State Government maintaining a funding presence for the provision of fire services. However, the extent and the coverage of that contribution differs, and is constrained by the Terms of Reference requiring a "cost neutral" outcome.

8.104 The NSW Treasury submission stated that the State Government should maintain their funding contribution under any reform to fire service funding, but that contributions based on the value of property holdings would see a decline in contribution levels[46]. On the issue of property holdings it said:

> If the State's contribution is to be maintained, then it may not be cost effective to directly charge all Government properties for the levy. There would be administrative costs in valuing all Government property and there would be a number of difficulties in valuing some State assets, for example, heritage assets. The increase in administrative costs to regularly revalue State assets could outweigh the benefits derived, especially if the State is to continue contributing on the existing basis consistent with the objective of revenue neutrality. Nonetheless, it would be appropriate to directly charge Government owned commercial businesses to ensure they are not put at a competitive advantage vis-a-vis private sector competitors.[47]

8.105 Other submissions suggested that the State should contribute on the basis of their property holdings. The Property Council of Australia said that the Government should continue to maintain current funding levels as well as contribute on the basis of property owned.[48] This view was also expressed in evidence before the Committee:

> **Ms GLADYS BEREJIKLIAN:** Can you please explain under your proposed model how you would treat currently non-rateable land? How do you propose to incorporate that in your model?
>
> **Mr McBRIDE:** Most of it would need to be valued, as has happened in Western Australia and so on. When we talk about buildings, they might be schools, churches or hospitals. At present, although they are unrateable, they would still be paying fire levies through their insurance. They would mostly be insured buildings. They would need to be encapsulated in the levy process. That would involve an exercise of running a valuation on those properties, which is certainly not beyond the capabilities of the Valuer-General.
>
> **Ms GLADYS BEREJIKLIAN:** So you are saying that the State Government, over and above what it pays currently, should pay the levy for those properties that are currently non-rateable, is that right?
>
> **Mr McBRIDE:** If they were Government-owned properties, yes.

[46] Submission No 49, NSW Treasury, p26
[47] ibid, p26
[48] Submission No 22, Property Council of Australia, p17

8.106 On equity grounds, the Government should be required to contribute on the value of their assets, given that the same level of protection is provided to these assets as privately held assets. The same level of fire risk is prevalent as is the same level of benefit derived. A further consideration in the case of State-owned commercial enterprises is competitive neutrality. If a property levy was introduced, these enterprises should be contributing to fire services on the same terms as their commercial competitors. PFS was able to estimate the cost of these entities contributing to fire services on the basis of property values separately to the rest of the State Government.[49]

8.107 However the Committee understands that State Government properties may not be appropriately valued or be easily identified. As noted in Chapter 7 the Department of Housing has advised that PFS did not consider the impact of a levy on its almost 140,000 residential properties. The Department estimates the introduction of a property levy as described in the PFS report would impose an annual net cost of $9.8 million on the Department.[50]

8.108 The additional contribution to fire services can be viewed as the contribution required by the Government to provide this public service or good to the community. In addition to a property owner, the State derives a collective benefit from contributing to fire services, as outlined in Chapter Two.

8.109 While the consensus is that the Government should continue to contribute, the actual extent of that contribution is crucial. The concept of revenue neutrality and the Government expressing a view that funding levels should remain the same, means that the actual amount of funding directly provided to the fire services would decline.

8.110 This is due to the decline in revenue receipts from removing the FSL from insurance premiums and as a consequence the amount of GST and stamp duty collected on premiums will decline. This loss in revenue, estimated by the modellers to be around $31 million[51], would need to be recouped through any alternative funding system to meet the requirements under the Terms of Reference:

> **CHAIR:** With the introduction of this property levy, and the removal of the FSL, on my basic mathematics, we would see a reduction in stamp duty. How would this proposed model maintain the cost-neutral aspect of our terms of reference? How could that work?
>
> **Mr CLARK-LEWIS:** If you want to be absolutely cost neutral you would estimate the amount of tax on tax you would forego, and you might factor that into the model. In doing that, you would maintain essentially the status quo but the Government would continue to get that amount of money and taxpayers would effectively still be paying. No-one will be worse off doing that and you would preserve the neutrality for both taxpayers and the State Government.
>
> **Mr PAUL McLEAY:** Would that mean that you could not then hypothecate the percentage? If it was to be broad-based property this could not be a hypothecated funding situation because then all you are doing is taking money out of consolidated revenue and putting it into the fire service?

[49] Professional Financial Solutions Final Submission *Quantitative Modelling of NSW FSL Funding Methods* p40
[50] Submission No 88, Department of Housing, pp2-4
[51] Professional Financial Solutions Final Submission *Quantitative Modelling of NSW FSL Funding Methods,* p22

**Mr CLARK-LEWIS:** I think you could address that issue by reducing the contribution by the amount of the tax on tax but only to maintain the status quo and the level of neutrality.[52]

8.111 Therefore, the budgetary impact of any proposed new funding arrangement would be zero for the Government. The level of fire service funding minus the tax on tax revenue would represent the net contribution to fire services. In essence, fire services would be receiving less under any new funding arrangement than what occurs now.

8.112 The revenue received from the tax on tax practice is not directly hypothecated to fire services, but goes into consolidated revenue. The Committee does not consider that this is an effective approach for funding fire services.

8.113 If the Government wanted to maintain its current funding levels in dollar terms, rather than percentage terms, the Government contribution would fall to just under 8 per cent. The percentage fall in the contribution would be incorporated into any proposed alternative funding arrangement, such as a property levy.

8.114 On this point, the ICA submission noted that:

> The NSW State Government should not pay less than its current percentage contributions to the fire services budgets were FSL to be abolished. ICA believes that any move away from FSL should not be taken as an opportunity to shift that proportion of the cost of fire services incurred by the State Government onto property owners.[53]

8.115 At a later hearing, the ICA noted that the State Government may not face a lower level of stamp duty income if the FSL were abolished:

> **Mr MASON:** We have another couple of points just to raise. In looking at the model previously we were attempting, or the modellers were, to provide a cost neutral outcome to the State Government and in particular built in to the model was an attempt to recompense the State for the loss of GST revenue and stamp duty revenue.
>
> On further reflection, we formed the view that the State does not lose any GST revenue, as the GST revenue in the first place does not go directly to the State.
>
> Secondly, if people spend less money on the fire service levy now they will have more disposable income to spend on other GST taxable supplies, or they will buy more insurance, which will increase their level of insurance, which is obviously one of our objectives, and therefore pay more GST generally on that, so we believe that $10 million could be excluded from the final modelling.
>
> Our experience when the State Government reduced stamp duty insurance from 10 to five percent last year, the revenue did not reduce by 50 per cent. The revenue to the Office of State Revenue reduced by 8.6 per cent, so the reduction in costs contributes to an increase in the take-up of insurance and therefore we think that the Government will not necessarily lose that money straight off.[54]

## FINDING D STATE GOVERNMENT CONTRIBUTION

D1 The Committee finds that there are strong arguments for the State Government to continue to contribute the same proportion of funding to the fire services if a property-based system was introduced. There may be additional net costs to the Government because of reduced stamp duty collections from lower insurance costs but this is by no means certain and these funds would not be provided to the fire services.

[52] Michael Clark-Lewis, Senior Director, Revenue Strategy Branch, NSW Treasury, Transcript of Hearing, 21 November 2003, p27

[53] Submission No 45, Insurance Council of Australia, p25

[54] Alan Mason, Executive Director, Insurance Council of Australia, Transcript of Hearing, 7 May 2004, p11

**RECOMMENDATION 6.1:** The State Government contribution should be maintained at 14 per cent for the NSW Fire Brigades and 13 per cent for the Rural Fire Service.

**RECOMMENDATION 6.2:** The Valuer-General should value all State Government properties and provide these values to the Government within a suitable timeframe following any decision to alter the funding of fire services. Once these values are provided, the State may be required to contribute through a levy rather than a direct contribution.

# Chapter Nine - Transitional Issues

## INTRODUCTION

9.1 This chapter addresses the Terms of Reference in relation to implementation of recommended changes to the funding scheme. These state:

> The report should:
>
> b. provide detailed information on how the recommended arrangements would apply to facilitate their possible implementation in 2004-05
>
> c. identify any administrative and compliance issues associated with the current and recommended funding arrangements, including transitional issues and the earliest practical commencement date for the proposed reforms.

9.2 Changes to the funding arrangements will raise issues such as:

- timing of implementation – administration considerations
- need for transitional arrangements;
- nature of transition;
- implementation costs; and
- savings to individuals and businesses.

9.3 These issues were addressed in other jurisdictions when changing over from one funding system to another. Where possible, reference to other jurisdictions has been made and how the matter was addressed.

## TIMING OF IMPLEMENTATION – ADMINISTRATION CONSIDERATIONS

9.4 The Committee does not believe it is feasible to introduce new arrangements in the immediate future.

9.5 In considering the timing of a new funding system, consideration should be given to both the operational and administrative issues and the need to inform the public awareness campaign.

9.6 If a property-based system was introduced, with a levy collected through local council rates and the FSL removed from insurance policies, the views of both the insurance industry and local councils must be considered.

### Insurance Industry View

9.7 The Committee heard from a representative of the Insurance Council of Australia:

> **Mr MASON:** Last but not least, if the Government did go forward and made changes to the system, our member companies have advised us that they would probably need a lead time of at least three months to make any necessary changes to their systems to deliver that.[1]

9.8 This time is required for insurance companies to update and test their computer systems in order to handle the new funding arrangements.

[1] Alan Mason, Executive Director, Insurance Council of Australia, Transcript of Hearing, 21 November 2003, p14

9.9 In order to gain some experience concerning the changeover between funding systems, the Public Accounts Committee Secretariat spoke to the Perth office of the ICA (8 January 2004). The Secretariat was told that insurance companies were given a minimum of six months to update software and administration arrangements to comply with the new funding system.

9.10 From the Western Australian experience, insurance companies found six months to be a satisfactory timeframe. For national insurance companies, the change was relatively easy given other states operate a property system. For insurance companies that solely conduct their operations in Western Australia the changeover was a little more difficult, but the timeframe was still achieved.

9.11 In educating the public, all insurance policyholders were sent an information package 12 months prior to the changeover. This information package outlined details of the changeover and what to expect.

9.12 The Western Australian ICA office indicated that the introduction period and the public education that preceded the new funding system resulted in little or no public complaints. The Fire and Emergency Services Authority informed the Committee that there were far fewer complaints from the public than expected. FESA established a community information line and estimating that it would receive 100,000 calls but only 2,000 calls were received.[2]

### Local Government View

9.13 Any announcement of a changed funding system must also be considered in the context of the ratepayer. Discussions between the Public Accounts Committee Secretariat and the Western Australian Local Government Association (12 January 2004) stated that despite the great amount of state publicity prior to the introduction of the new levy, from a Local Government role, ratepayers were probably aware of the change and the impact on their rates by March/April 2003 with an implementation date of 1 July 2003. Ratepayers were all provided with an information package in their rate notices around July/August/September 2002.

9.14 In order to address the administrative changes, local councils in Western Australia required approximately 12 months to implement the change, update and test software and train staff. If they were to do this again, the Association thought that it would have been beneficial to have longer to implement the new system, but the change was managed within the timeframes given.

### Additional View

9.15 The Committee heard evidence that suggested a property levy should also be collected on motor vehicles. It was proposed that the RTA should collect the levy through motor vehicle registration.

9.16 In evidence before the Committee, the RTA stated that:

> **Mr ALLEN:** The initial set-up would be about $200,000 and it would be about 6 to 12 months to get that done.[3]

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[2] Meeting between Western Australian Fire and Emergency Services Authority and Committee, 2 February 2004

[3] David Allen, Acting General Manager, Driver and Vehicle Strategy, Roads and Traffic Authority, Transcript of Hearing, 26 November 2003, p27

**Collective Considerations**

9.17 From a practical view, any announcement regarding a new funding system should be made as early as practical. The longer the public is educated that a new funding system is to come into operation the smoother will be the transition.

9.18 While the Western Australian system may have provided information packages at least 12 months prior to implementation, the changes proposed to the funding system were discussed at least three years earlier.

9.19 While it is not recommended that such a long period be announced in New South Wales prior to introducing any new system, it is important that the public are given a reasonable timeframe between the announcement of a new scheme and the introduction of the scheme.

9.20 However, given the Committee's recommendation that additional work be undertaken prior to a Government decision to implement any new scheme, it is clearly not feasible to introduce a new system in the immediate future.

9.21 Implementation of a new system would require at least three months for implementing administrative changes and notifying the public.

### FINDING E – TRANSITIONAL ARRANGEMENTS

E1 Should the Government choose to implement a property-based levy, the Committee does not believe it is feasible to introduce the new arrangements in the immediate future..

E2 In order to assist the transition, the Committee finds that early notice to the public and the administrators of the scheme would be required.

**RECOMMENDATION 7.1:** The Government should publicly announce any change to the current funding arrangements in such a way that there is adequate notice to the public of these changes.

## NEED FOR TRANSITIONAL ARRANGEMENTS

9.22 Any changes to the current funding arrangements, which alter the timing and nature of the funding receipts, will involve some financial cost. This financial cost should be minimised for the taxpayer, by ensuring they are not contributing more tax under the transition to a new system. From the perspective of the Government any new system should comply with the Terms of Reference which require the report to:

> 2a. present recommendations on future funding arrangements that meet the current and prospective needs of the fire services and would be as near as possible to cost neutral.

9.23 The current insurance-based system collects remittances from insurance companies three months in advance: in July, October, January and April. Council rates are paid two months in arrears: in September, December, March and June. If a property system were introduced and collected through rate notices, the funding would be:

> …received around two months later than they would under the insurance-based system, although total collections in a given year would be unchanged.[4]

[4] Submission No 49, NSW Treasury, p29

9.24 In order for the funding of fire services to remain unchanged and in order to cause no disruption, a funding shortfall due to timing delays must be met. According to the NSW Treasury submission:

> While not large in the context of the FSL, this net cost could be avoided by taking this cost into account when determining the property levy rates. This need not impose any additional cost on taxpayers as the cost of the advance payment of the insurance levy would have been reflected in insurance company costs and passed on to policyholders.[5]

9.25 The ICA has also raised the issue of timing of payments, in particular council rates. Given that council rates are paid in arrears, the ICA felt that:

> It is not until well into the financial year, possibly in the third quarter, that accrued receipts will match the required level of contributions to the fire services. This means that if the transition gap is not covered permanently in the first (transition) year, the gap would recur at the start of the next financial year and possibly in subsequent years as well.[6]

9.26 The ICA solution was to either use bridging funds to cover the cost or to have a single additional payment in the transition year. This additional payment:

> …would allow council receipts to be shifted to the right until they coincide with the timing of fire services' contributions requirements.[7]

9.27 According to the ICA, the additional payment could either be achieved via:

- consolidated revenue grant;
- increased receipts in the first year sufficient to cover 100 per cent of the councils' contributions PLUS the transitional gap; or
- funds from insurers (recovered from policy holders).[8]

9.28 Funding from consolidated revenue meets the taxation principles of efficiency, equity and simplicity. Funding from general revenue means that all taxpayers contribute, there is no distortion to taxpayer behaviour and no significant administrative or compliance requirements. However, funding from consolidated revenue is an additional cost to the Government and would contravene the Terms of Reference.

9.29 Option 2 would ensure that all taxpayers contributed to the funding gap and there was no additional financial cost to the Government. However, the funding required to cover the gap may result in no saving to the taxpayer following the introduction of the new funding scheme and may result in additional costs. In the first year of operation the scheme should not impose any significantly higher costs on taxpayers than what is required to ensure that fire service funding levels are maintained.

9.30 There is the added concern of complexity to this option. Increasing the contribution for the first year may confuse taxpayers and prevent a smooth transition to a new funding scheme where the level of contribution changes from year 1 to year 2. Ideally, any new scheme should attempt to maintain a constant level of taxpayer contributions for the first few years.

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[5] ibid, p29
[6] Submission No 45, Insurance Council of Australia, p20
[7] ibid, p20
[8] ibid, p20

9.31 The final option suggested by the ICA would be to recover the cost from insurance policies. This option is the least desirable as the inequities identified under the current insurance-based scheme were essentially maintained. Again, taxpayers who choose to insure their property and businesses would be called upon to fund the transition gap. The narrow base would again lead to higher costs for individuals and businesses with insurance.

9.32 While the options presented by the ICA all have significant drawbacks, the Committee understands that the funding for fire services must be maintained and any gap between removing the current system and replacing it with a new scheme must be funded.

9.33 The option that results in lower costs to the taxpayer, minimises changes to taxpayer behaviour and is reasonably simple in terms of administration and compliance should be adopted.

9.34 Therefore, the option to fund the transitional gap from consolidated revenue is considered the most suitable.

## NATURE OF TRANSITION

9.35 As outlined earlier, any transition between two different funding systems must ensure that taxpayers are not contributing more than they would under current arrangements or paying for a service twice. Acceptance of a new scheme is highly dependant on ensuring that the majority of taxpayers are not worse off under the new arrangements.

9.36 While the previous section discussed the concept of a transitional year between the two different funding schemes, there is nothing precluding the Government from providing the total funding requirements for both fire services for a year, between the cessation of collection the FSL and introducing the property levy. This would alleviate the need to operate two systems concurrently and ensure that policyholders were not contributing more in this transitional year than non-policy holders.

9.37 In practical terms however, this option would not be possible. Such an option would cost the Government an additional $442 million in 2004-05 (this includes only the FSL amount and the Local Government contribution). Given fiscal constraints and other vital government services this funding could be allocated towards, this option is not considered viable.

9.38 The alternative, according to NSW Treasury, is to run the two systems concurrently. The agency's submission stated that:

> To smooth the changeover to the new system, there is merit in operating a transitional year where the insurance levy is still collected on all policies taken out during the year, but at half the current rate, and the property levy is collected for the first time on all properties but also at half the rate.[9]

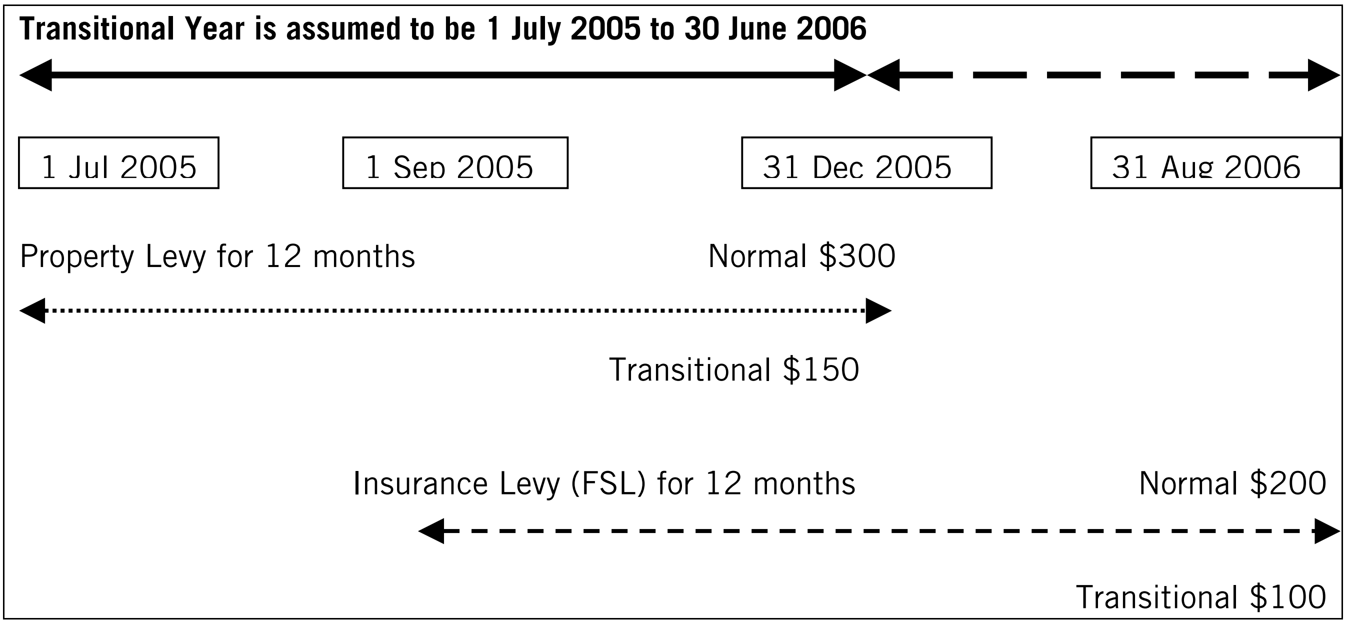
9.39 For example, if the transitional year was operating from 1 July 2005 to 30 June 2006, during this time, the normal property levy should be $300 for the full 12 months. However, this proposal would have the property levy set at $150. During this transitional year an insurance policy is renewed for the period 1 March 2005 to 28 February 2006. Under normal arrangements the FSL contribution would be $200, but the Treasury proposal sets the amount at $100.

[9] Submission No 49, NSW Treasury, p28

9.40 In the absence of a transitional arrangement and the only contribution being the property levy, the total amount payable should be $300. However, for policyholders in the transitional year, the total amount of their contribution is $250. For non-policyholders in the transitional year the total contribution is $150.

9.41 This arrangement is demonstrated in the timeline of an indicative transitional year below.

**Timeline of indicative Transitional Arrangements**




9.42 Under this option the policyholder is better off by $50 in the transitional year than when the full amount of the levy is imposed. For year 2 the policyholder returns to paying $300.

9.43 The non-policyholder in the transitional year would be required to pay $150 compared to no contribution under the current funding arrangement. However, comparing the policyholder to the non-policy holder, results in the policyholder contributing and extra $100 in the transitional year.

9.44 This model still generates the bulk of the funding through individuals who choose to insure. However, the equity concerns between the two taxpayers improves when moving from the transitional year into year 2.[10]

9.45 If the option to run both systems concurrently in the transitional year is recommended, a derivative of the option proposed by NSW Treasury is to apply the FSL in the transitional year at a pro rata rate. As such, in the example explained earlier the FSL contribution should only be three twelfths of the total amount, which equates to $50. Under this proposal the total amount contributed by the policyholder in the transitional year would be $200.

9.46 While the policyholder is still contributing more compared to the non-policyholder, the contribution covers only the period within the transitional year, not any part of year 2.

[10] Correspondence from NSW Treasury, 20 January 2004

9.47 According to a discussion between the Public Accounts Committee Secretariat and NSW Treasury (15 January 2004), this option is not favoured because NSW Treasury believes people will alter their insurance behaviour to take advantage of the removal of the FSL for the period outside the transition year. While this is always a possibility, the extent to which this practice will occur is unknown as it assumes that people are extremely price sensitive and are wiling to forgo insurance for a specific period of time. The number of policyholders that may take advantage of such a situation is only considered to be minor.

9.48 Another difficulty perceived by NSW Treasury is that it would be complicated to work out on an individual basis what every policyholder should be entitled to. Working out contributions for every day included in the transition year is thought to be an extra burden for insurance companies.

9.49 The running of the two funding systems concurrently is not universally supported:

> **Mr STEVE WHAN:** Your recommendation 23 is that any funding shortfall resulting from the transition or as a result of budget supplementation to New South Wales Fire Brigades or fire services should be funded by the New South Wales Government from Consolidated Revenue. You are saying there that you believe the levy should not rise in the future?
>
> **Mr MORRISON:** No. Because of the current way the insurance levy operates, there is forward funding and back funding of the fire services, which causes essentially what the property owner pays currently just to be an estimate of what is going to be needed for fire services. If you reform the system, one of the options would be to continue running with some form of insurance as well as a property tax, concurrently, so that the insurance could perform that back funding function. We would not want to see those two, we would not want to see double taxation effectively, by having an insurance levy and a property levy running concurrently. I do not know what the numbers would be but we do not think they would be substantial. We think the Government should step in and cover them.[11]

9.50 In Western Australia, similar transitional arrangements were in place. The ESL property levy commenced from 1 July 2003. Insurance policies continued to have the FSL placed on premiums up to 31 December 2003. For the period 1 January 2004 onwards, there was no FSL placed on the premium. For the six month overlap period, properties subject to FSL (categories 1, 2 and 3) had their rates reduced.

9.51 For category areas 1 and 2, rates were reduced by 35 per cent, while category area 3 properties had rates reduced by approximately 25 per cent. Rates were not reduced by 50 per cent as the contribution from the insurance companies only covered career fire fighters, whereas the ESL covered a full year contribution for voluntary emergency services. Category areas 4 and 5 did not have their rates reduced.[12]

9.52 According to the ICA submission:

> The West Australian transition funding arrangement effectively is an extension of the existing FSL scheme to which insureds have already contributed in advance. In the transition period, contributions will be recovered from insureds in proportion to the time remaining under the transition arrangement. For instance, insureds with renewals in the

[11] Ken Morrison, Executive Director New South Wales Policy, Property Council of Australia, Transcript of Hearing, 21 November 2003, p37
[12] Emergency Services Levy Information Guide, 14 August 2003

first month of the transition period will pay 12/12ths of the full recovery amount, while insureds with renewals in the final month will pay 1/12th of the full amount.[13]

9.53 The introduction of a similar option in New South Wales would operate differently, given that the requirement is that the FSL funds the fire service for the current year only, not the current year and following year, as in Western Australia. As such, policies in New South Wales would require insureds to contribute on the basis of the period covered in the transition year.

**FINDING E3** A transition to a new scheme presents significant costs and administrative challenges. Special arrangements to ensure stability of revenue for the fire services and to minimise the costs to the public during the transition are required.

**RECOMMENDATION 7.2:** If a property-based system is introduced, there should be a transitional period where both the old and new funding systems operate concurrently. During this period, the property levy should be paid at half the required rate, as well as any insurance policy that is renewed during the transitional period, up to and including the last day of the transitional period. Any part of the annual premium that spans the end of the transitional period should be charged FSL.

## IMPLEMENTATION COSTS

9.54 Implementing any new funding system will involve some cost. This section is dealing with implementation costs, rather than administration costs. Implementation costs will only be incurred at the initial establishment of a new funding system.

9.55 As outlined earlier, if a property levy was collected on motor vehicles through the registration process, than the RTA suggest that:

> **Mr ALLEN:** Again, I am not an information technology [IT] expert, but we have done some initial costings. It would cost in the order of $200,000 to do the IT systems.[14]

9.56 No evidence was provided to the Committee concerning the implementation costs for the insurance industry. However, in Western Australia insurance companies were not given any extra funding to meet the financial costs of updating their systems. Rather, insurance companies were required to absorb all costs. Any initial costs for insurance companies would be later recovered when savings from removing the FSL on insurance policies were realised.

9.57 Implementation costs for local councils have not been identified either. Though, given the large number of councils across the state, it is conceivable that initial set up costs may be substantial. The Committee was told that the Western Australian Government provided financial assistance and training to Local Government to implement the new administrative arrangements.[15]

9.58 According to the Fire and Emergency Services Authority of Western Australia Replacement Funding Arrangements - Operating Manual, local councils were allocated $0.25 million in 2003-04 as a commencement fee:

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[13] Submission No 45, Insurance Council of Australia, p22

[14] David Allen, Acting General Manager, Driver and Vehicle Strategy, Roads and Traffic Authority, Transcript of Hearing, 26 November 2003, p27

[15] Meeting between Western Australian Local Government Association and the Committee 2 February 2004

> The 'Commencement Fee' will be based on the number of ESL Notices issues, with a minimum payment of $1,000 and a maximum payment of $5,000 to each Local Government.[16]

**RECOMMENDATION 7.3:** If local councils are used to collect a levy through rates, it would be appropriate for funding to be provided to implement the new arrangements.

## SAVINGS TO INDIVIDUALS AND TAXPAYERS

9.59 Under a proposed property levy, taxpayers should expect to realise savings through the removal of the FSL on insurance policies and the reduction in council rates from removing the Local Government contribution, notwithstanding any increases in premiums or council rates. Any change to the current funding arrangement would only be introduced on the basis that the Committee was convinced there were savings to the taxpayer.

9.60 In their submission, the ICA noted:

> In the transition arrangements in Queensland, South Australia and Western Australia, the State Governments legislated to ensure that insurers passed through the full benefits of abolishing FSL.[17]

9.61 In Western Australia the *Fire and Emergency Services Legislation (Emergency Services Levy) Amendment Act 2002*, states that sufficient information must be provided from insurance companies to satisfy the Minister that premiums have been reduced or refunds processed (Division 3 - clause 14). Additionally, the Minister must present a report to both Houses of Parliament within 18 months after the new levy commences reporting on the arrangements outlined above (Division 3 – clause 15). On 22 June 2004, the Western Australian Emergency Services Minister tabled an independent audit report on the cost of insurance since the levy on policies was removed. This report found that insurance companies had passed savings on to policy holders. On average, premiums had reduced and that consumers had responded by increasing the amount of insurance cover they had.[18]

9.62 Similar provisions were written into South Australian legislation following the introduction of the Emergency Services Levy. Under Schedule 2 of the *Emergency Services Funding Act 1998* insurers were required to reimburse policyholders for any paid liability occurring after 30 June 1999, unless the amount was less than $10. Any amounts under $10 were to be paid into the Community Emergency Services Fund (clause 4).

9.63 Additionally, a report from the Commissioner for Consumer Affairs must be presented to the Minister, on or before 30 September 2000, outlining the effect on insurance premiums for 1999-2000, in particular the savings from the removal of the FSL. Within six days of receiving the report, the Minister was required to table it in both Houses of Parliament (clause 4A).

[16] Fire and Emergency Services Authority of Western Australia, 19 May 2003, *Replacement Funding Options – Operating Manual*, p26

[17] Submission No 45, Insurance Council of Australia, p20

[18] Sigma Plus Consulting *Emergency Services Levy: Insurance Compliance Review: Final Report* , tabled 22 June 2004

9.64 Ensuring that savings were passed onto taxpayers was raised in a number of submissions and throughout the public hearings. Eurobodalla Shire Council raised the point in its submission, stating:

> Mechanisms would need to put in place to ensure that these savings are passed on and not absorbed by premium increases. The Australian Competition and Consumer Commission (ACCC) and the NSW Department of Fair Trading would have an enforcement role.[19]

9.65 In evidence before the Committee, the IAG stated:

> **CHAIR:** To finish off Mr Torbay's question, would APRA or the ACCC monitor you if that levy were taken off and you decided to pass on—
>
> **Mr BROWN:** The ACCC certainly would. It would show up in the statistics that we give to APRA on a quarterly basis. They would see it straightaway.
>
> **Ms STAGNITTA:** The West Australian Government has proactively implemented a process of auditing insurance companies to ensure that, as the fire levy was being wound down, it was calculated correctly and the savings were being passed on.[20]

9.66 Similar sentiments were stated by the ICA:

> **Mr MASON:** The greatest assurance we could give the Committee is that if you make a change to the legislative requirements and the audit requirements, the willingness of the industry to meet the changes would be there; you could place huge confidence in the fact that consumers will realise the benefits.[21]

9.67 The question was also asked in relation to local council rates of the Fire Brigade Employees' Union:

> **Ms GLADYS BEREJIKLIAN:** You expressed concern that, if the system was changed, the savings that insurance companies made might not be passed on to policy-holders, and how would we guarantee that those savings would be passed on. Given you are now recommending that local government be taken out of that equation, how do you propose that guarantees be put in place to ensure that rates reflected the lifting of the burden from local government?
>
> **Mr READ:** I would imagine there is a far more simple legislative action available to Parliament.
>
> **Ms GLADYS BEREJIKLIAN:** So you would suggest legislating?
>
> **Mr READ:** To do just that, yes. That would be a far easier thing to do.
>
> **Ms GLADYS BEREJIKLIAN:** So you say we should legislate to guarantee that the savings would be passed on to ratepayers?
>
> **Mr READ:** Yes. I stand to be corrected here, but I would imagine it could be done by ministerial direction. Rate reduction proposals should enjoy a fairly easy passage through Parliament.[22]

9.68 The view of at least one local council was similar to that of the Union:

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[19] Submission No 36, Eurobodalla Shire Council, p5

[20] Ian Brown, Deputy Chief Executive Officer, and Leanne Stagnitta, National Home Products Manager, Insurance Australia Group, Transcript of Hearing, 21 November 2003, p6

[21] Alan Mason, Executive Director, Insurance Council of Australia, Transcript of Hearing, 21 November 2003, p14

[22] Christopher Read, State Secretary, New South Wales Fire Brigade Employees' Union, Transcript of Hearing, 26 November 2003, p19

> **Mr STEVE WHAN:** A number of witnesses we have had so far have talked about how they would expect that if we introduced a property-based system that local government would then reduce its rates commensurate with the amount of money which it is currently putting into the fire service levy. Would that be your understanding as well?
>
> **Mr GLEDHILL:** That would be a fair comment, but that will be up to each council to make that decision themselves. We could not speak for all councils but, speaking for my own council, yes, I would assume we would, the same as we would expect insurance premiums to fall.[23]

9.69 The overwhelming evidence presented to the Committee suggests there is strong support from both the insurance industry and local councils to ensure that removing the fire service funding contribution from both insurance policies and rates is passed on.

9.70 To ensure that taxpayers are confident that any new funding system delivers savings and is a financial benefit to them, it would be in the interests of transparency and accountability, that when legislating for a new funding system, requirements are established to ensure the realisation of savings and the financial benefits any new system delivers.

**FINDING E4** Unless compliance and reporting mechanisms are in place there are also risks that savings from reduced contributions are not passed on to the public by insurance companies and Local Government.

**RECOMMENDATION 7.4:** In establishing legislation for the introduction of any new funding arrangement, provision should be made that:

- Insurers are to provide a report to the Minister and or Treasurer (depending on who is responsible for overseeing any new funding arrangements) outlining the reduction in premiums due to the abolition of the FSL, average savings to policyholders and refunds provided to policyholders in relation to policies that span the implementation date;
- Upon receipt of the report, the Minister/Treasurer is to present the report to the Auditor General for certification;
- Upon certification from the Auditor General the Minister/Treasurer is to table this report before both Houses of Parliament; and
- These arrangements should be reviewed after five years to determine whether they continue to be required.

**RECOMMENDATION 7.5:** The Department of Local Government is to present a report to the Minister/Treasurer on behalf of all local councils, for the applicable financial year, detailing the expected savings from each council of removing the annual fire service contribution. This report will be publicly presented prior to the commencement of a new funding system. Six months after the end of the applicable financial year, the Department of Local Government is to present an updated report to the Minister/Treasurer outlining the actual savings per local council from removing the annual fire service contribution. The Minister should take the report into account when determining the rate pegging setting for the following year.

[23] Robert Gledhill, Vice President, Shires Association of New South Wales, Transcript of Hearing, 26 November 2003, p37

9.71 In addition to legislation, policyholders should also be given avenues to question and dispute savings from the abolition of the FSL. If policyholders are not satisfied that the adjusted premium is correctly reflective of the removal of the FSL, they should be able to raise this matter with relevant authorities.

9.72 Policyholders should be given access to the ICA as a first point of reference for any disputes regarding their premiums. Following on from that the matter should be directed to a consumer advocate body, such as the NSW Department of Fair Trading. It is important to note though, that the complaints mechanism is only for the removal of the FSL, not issues regarding general premium increases.

9.73 The ICA has suggested that such customer complaints could be referred to a committee for resolution. They suggest this committee could consist of representatives of the council and the Office of Fair Trading.[24]

**RECOMMENDATION 7.6:** Mechanisms should be established for policyholders to query or dispute the impact of savings from the abolition of the FSL. In the first instance, policyholders should be able to direct their concerns to the ICA. Disputes should be referred to a joint Government-industry committee for resolution.

[24] Correspondence form Allan Hansell Manager for NSW and the ACT, Insurance Council of Australia, 21 May 2004

# Chapter Ten - Extraordinary Costs Associated with Funding Major Bushfires

## INTRODUCTION

10.1 As part of this inquiry, the Committee was asked to assess the best way to manage the financial impact of bushfires. Point 5 of the Terms of Reference state:

> The report should also consider the appropriate funding arrangements for meeting the extraordinary costs associated with fighting major bushfires. In particular, the Committee should examine the possible development of a fire fighting reserve - funded by a fire service levy - to assist in meeting future extraordinary costs associated with major bushfires.

10.2 Over the past several years New South Wales has been subject to a number of large bushfires that have resulted in major damage to both property and the environment. According to NSW Treasury, these catastrophes often "have significant budgetary impacts for NSWFB and RFS."[1]

10.3 This chapter describes:

- the extraordinary costs of recent major bushfires;
- the arrangements for Natural Disaster Relief Funding and the level of funding received as a result of these bushfires; and
- the implications of introducing a fire fighting reserve fund.

## ESTABLISHMENT OF A FIRE FIGHTING RESERVE FUND

10.4 The NSW Treasury submission outlined the extraordinary costs for major recent events and the cost to the brigades for these events. These costs are detailed below.

| Year | Event | Cost to Fire Brigades ($'000) | Cost to Rural Fire Service ($'000) | Total Cost ($'000) |
|---|---|---|---|---|
| 1993-94 | Jan 94 Bushfire | 2,600 | 7,137 | 9,737 |
| 1994-95 | | | 2,413 | 2,413 |
| 1995-96 | | | 124 | 124 |
| 1996-97 | | | 112 | 112 |
| 1997-98 | Thredbo + bushfires | 1,300 | 13,194 | 14,494 |
| 1998-99 | Sydney Hailstorm | 8,623 | | 8,623 |
| | Bushfires | | 4,467 | 4,467 |
| 1999-2000 | Newcastle Disease | 486 | 1,247 | 1,733 |
| 2000-01 | Bushfires | | 6,014 | 6,014 |
| 2001-02 | Christmas 2001 Bushfires | 6,861 | 63,830 | 70,691 |
| 2002-03 | Summer 2002 Bushfires | 6,196 | 120,899 | 127,095 |
| | | **26,066** | **219,437** | **242,503** |

Source: Submission No 49, NSW Treasury, p30

[1] Submission No 49, NSW Treasury, p30

10.5 The NSW Treasury submission raised the establishment of a reserve to “assist in dealing with the spikes this causes in funding the fire services.”[2] The fund would be established with funding of $60 million, collected through higher FSL contributions. The submission states:

> A contribution of $20 million in 2003-04 would represent an increase in the FSL by an average of around 5 per cent.[3]

10.6 Under this proposal the $20 million per year would be collected for three years until the $60 million level was reached. If a property levy were to be implemented, NSW Treasury recommends not introducing the reserve immediately, but rather deferring it “until the new property levy is fully implemented.”[4]

10.7 While NSW Treasury is supportive of introducing the reserve fund, other submissions have opposed the introduction or suggested alternatives. The ICA submission “opposes any suggestion that additional funds be raised via a further impost on those who take out insurance.”[5] It went on to say that:

> Should the Government decide that it would like to develop a fire-fighting ‘reserve’ fund, this could be built up, over time, through any new property-based levy through systematic collection over and above the fire services budgetary requirements.[6]

10.8 Other submissions, such as those from the Property Council of Australia, IAG, Rural Fire Service and the New South Wales Fire Brigade Employees’ Union have all rejected the need to introduce such a funding reserve. The Property Council of Australia did not support such a move, stating:

> To build in contingency stakeholders would have to pay higher levies to generate the necessary ‘fat’. Building in this fat deliberately is distortionary.[7]

10.9 Similar views were outlined by the New South Wales Fire Brigade Employees’ Union:

> In recent heavy fire seasons, additional financial burdens have affected the fire services. However, these burdens have come from the ad hoc nature of public policy making in the area (eg. the somewhat panicked utilisation of the Erickson Air-Crane Helitankers). Rather than make the funding system match this level of adhocracy, the decision-making processes should be more systematic and build contingency for large-scale bushfires into the regular policy making and funding processes.[8]

10.10 The view of the Rural Fire Service was not concerned with aspects of efficiency or budgeting but possible implications for funding received under the Natural Disaster Relief Arrangements. The Service’s submission stated:

> Any proposal for the establishment of a ‘Fire Fighting Reserve Fund’ could jeopardise the current cost sharing arrangements between governments under the Natural Disaster Relief arrangement for large scale emergency events.[9]

10.11 The arrangements for Natural Disaster Relief are discussed below.

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[2] ibid, p30
[3] ibid, p30
[4] ibid, p30
[5] Submission No 45, Insurance Council of Australia, p31
[6] ibid, p31
[7] Submission No 22, Property Council of Australia, p23
[8] Submission No 53, NSW Fire Brigade Employees’ Union, p17
[9] Submission No 55, NSW Rural Fire Service, p4

## NATURAL DISASTER RELIEF ARRANGEMENTS

10.12 The Commonwealth Department of Transport and Regional Services administer the Natural Disaster Relief Arrangements (NDRA). The funding arrangements:

> …provide assistance to States and Territories aimed at alleviating the financial burden associated with the provision of natural disaster relief payments and infrastructure restoration.[10]

10.13 Funding provided is not complete compensation but is part reimbursement once a State or Territory exceeds a determined expenditure threshold.

10.14 NDRA will apply to any one of, or a combination of, the following natural disasters:

- bushfires;
- cyclones;
- earthquakes;
- floods;
- storms;
- stormsurge (large amounts of water following a hurricane, similar to lfash flooding); and/or
- landslides (consequential upon an eligible event).11

10.15 Relief measures provided to the States and Territories under NDRA are:

- A personal hardship and distress payment (PHD) – for emergency food, clothing, accommodation, essential repairs to houses and replacement of essential items of furniture and personal effects; or
- Restoration or replacement of an essential public asset – or restoring the asset to its pre-disaster standard. Expenditure must occur within a period of less than two years after the end of the financial year in which the disaster occurred; or
- A concessional-interest loan – loans are provided by the State to a farmer or small business operator who lost assets, had the assets significantly damaged or cannot access commercial finance but has long-term viability; or
- A concessional-interest loan – loans provided to needy individuals or non-profit bodies who had assets significantly damaged and who cannot access commercial finance; or
- Provision of interest subsidies (grants) – by a State for loans advanced by authorised deposit taking institutions to a farmer or small business operator who had their assets significantly damaged; or
- Psychological counselling – for distress suffered by individuals or communities; or
- Other acts of relief and restoration.12

[10] www.dotars.gov.au/ndr/index.htm - accessed 8 October 2003
[11] ibid
[12] Natural Disaster Relief Arrangements, Determination of Terms and Conditions by the Minister for Regional Services, Territories and Local Government, Wilson Tuckey MP, Former Minister for Regional Services, Territories and Local Government, 28 June 2002, www.dotars.gov.au/ndr/terms.htm

10.16 It is important to note that the eligible measures outlined above can be made in the form of goods as an alternative to cash payments.

10.17 Commonwealth funding is normally provided after a natural disaster and is calculated on the following basis:

- Half of State and Territory outlays following a natural disaster for PHD where the disaster expenditure exceeds the small disaster threshold (currently $200,000) for each disaster;
- Half of State and Territory expenditure on eligible relief measures above a specified threshold amount (0.225 per cent of State and Territory revenue) up to a second threshold (1.75 times the first threshold). Above the second threshold the Commonwealth will reimburse three quarters of any further expenditure.[13]

10.18 Disaster thresholds vary across jurisdictions:

> **Mr RHEESE:** The current base amount for New South Wales is $79,740,000. That is what we call the first threshold. Above that rate the Commonwealth reimburses 50 per cent of State expenditure. Up until the State expenditure hits the second threshold which is $139,545,000 at which time the Commonwealth provides a 75 per cent reimbursement.[14]

10.19 There are a number of general conditions attached to receiving assistance through NDRA. Examples of some of the conditions include that the States and Territories are required to recognise the assistance of the Commonwealth, ensure disaster mitigation strategies are in place and participate in risk management studies. However, the main criterion for the purposes of establishing the fire fighting reserve fund is the condition that:

> 3.1 In adopting eligible measures, the State must observe the general intention that:
>
> - assistance is not to supplant, or operate as a disincentive for, self-help by way of either commercial insurance or appropriate strategies of disaster mitigation; and
> - so far a practicable, assistance is to be designed to achieve an efficient allocation of resources.[15]

## IMPLICATIONS OF INTRODUCING A FIRE FIGHTING RESERVE FUND

10.20 As outlined earlier, there are opposing views on the impacts of introducing a reserve to meet the extraordinary costs associated with bushfires. The tax policy issues of establishing the reserve seems secondary to whether the creation of the reserve will cause financial concerns in receiving Commonwealth funding under the Natural Disaster Relief Arrangements.

10.21 As the central agency responsible for administering the State's financial arrangements, the views of NSW Treasury are important to note. The view of NSW Treasury when asked whether the reserve could create financial problems for the State was:

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[13] http://www.dotars.gov.au/ndr/index.htm - accessed 8 October 2003

[14] Kevin Rheese, Director, Natural Disaster Management, Commonwealth Department of Transport and Regional Services, Transcript of Hearing, 27 November 2003, p29

[15] Natural Disaster Relief Arrangements, Determination of Terms and Conditions by the Minister for Regional Services, Territories and Local Government, Wilson Tuckey MP, Former Minister for Regional Services, Territories and Local Government, 28 June 2002, www.dotars.gov.au/ndr/terms.htm

> **Mr CLARK-LEWIS:** No, our understanding is that it is entirely a matter for State Government how it goes about funding its services and there would be no conflict of those arrangements. It is not my area but I have spoken to the people who work there and they do not see any problem.[16]

10.22 The view of the NSW Fire Brigades was more cautious. Their main argument is that the creation of this fund could result in New South Wales not having access to disaster funding which can provide significant assistance to the State rather than the State bearing the costs:

> **Mr MULLINS:** I admit to a bit of nervousness in the suggestion that in a new levy system there would be this emergency fund because the very people who are making such suggestions [about arson] may say, "Well, New South Wales does not require assistance in disasters anymore".[17]

10.23 However, a representative of the Commonwealth Department of Transport and Regional Services considered that any such fund would not compromise the State's access to natural disaster funding should the issue arise:

> **CHAIR:** The terms of reference ask this Committee to consider whether a firefighting reserve fund could be introduced in order to provide funds to meet the extraordinary costs associated with major emergencies, such as the recent bush fires. The Committee has heard evidence that if such a fund were established it may mean that the State would not have access to natural disaster funds. Is that assertion correct?
>
> **Mr RHEESE:** No.
>
> **CHAIR:** Why?
>
> **Mr RHEESE:** There are no provisions in the determination about excluding a State on the basis of how it raises revenue, if you like. Again Commonwealth assistance kicks in after pre-determined thresholds are reached, and then there are known proportions that the Commonwealth will reimburse. Those thresholds are calculated at a rate of 0.225 per cent of gross public sector revenue. So, if you like, there is an automatic mechanism there where if the State chooses to collect its revenue by levy, taxes whatever, then that is automatically factored in the calculation of the threshold amounts at which Commonwealth assistance will come in.[18]

10.24 The Department went on further to add:

> **CHAIR:** Your department lists as a principal objective of the natural disaster relief arrangements to ensure that disaster relief assistance does not operate as an disincentive to effectively plan, mitigate and allocate sufficient resources for disasters, or to discourage individuals or businesses taking out appropriate insurance to protect their assets and home. Is the establishment of a firefighting reserve fund consistent with that objective?
>
> **Mr RHEESE:** I believe so.[19]

10.25 From the evidence presented to the Committee, the establishment of a fire fighting reserve does not contravene the Natural Disaster Relief Arrangements and will not

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[16] Michael Clark-Lewis, Senior Director, Revenue Strategy Branch, NSW Treasury, Transcript of Hearing, 21 November 2003, p27

[17] Gregory Mullins, Commissioner, NSW Fire Brigades, Transcript of Hearing, 26 November 2003, p13

[18] Kevin Rheese, Director, Natural Disaster Management, Commonwealth Department of Transport and Regional Services, Transcript of Hearing, 27 November 2003, p30

[19] ibid, p30

prevent NSW from accessing Commonwealth funding under the arrangements when the situation arises.

10.26 However, the establishment of the reserve through the FSL is not considered optimal. There are no beneficial tax policy principles on which to collect the levy. The reserve is simply to smooth out budgetary fluctuations in providing extraordinary funding following natural disasters. The regularity of providing this funding does not necessitate the creation of the reserve.

10.27 Over-collecting revenue to put aside in a trust would question the transparency of the levy and may call on other sectors to collect more from levies and duties to put aside in trusts. If the State can access Commonwealth funding following a natural disaster, there is no need to create a specific reserve.

## FINDING E BUSHFIRE RESERVE FUND

The Committee finds there is no administrative need to establish a separate fund for fighting major bushfires.

**RECOMMENDATION 8:** The Committee does not support the creation of a fire fighting reserve fund under current or any future funding arrangements for fire services.

# Appendix 1 – List of Submissions

1. The Vaucluse Progress Association
2. National Insurance Brokers Association of Australia
3. Ku-ring-gai Council
4. State Chamber of Commerce
5. The Council of Sutherland Shire
6. Mr William J Lea
7. Mulwaree Shire Council
8. Snowy River Shire Council
9. Gloucester Shire Council
10. The NSW State Emergency Services Volunteers Association
11. Insurance Australia Group Limited
12. Auburn Council
13. ARIMA Ltd
14. Wollongong City Council
15. Lockhart Shire Council
16. NSW Mineral Council
17. Snowy River Group Captains
18. Merriwa Shire Council
19. NRMA Motoring and Services
20. Temora Shire Council
21. CommInsure
22. Property Council of Australia
23. Greater Taree City Council
24. Richmond Valley Council
25. Woollahra Municipal council
26. SHOROC Regional Organisation of Councils
27. Gundagai Shire Council
28. Hume Shire Council
29. Wellington Council
30. Boorowa Council
31. NSW Farmers' Association
32. Council of the Shire of Jerilderie
33. Hornsby Shire Council

34. Rous Water Centre
35. Tallaganda Shire Council
36. Eurobodalla Shire Council
37. NSW Rural Fire Service Association
38. Leeton Shire Council
39. Northern Sydney Regional Organisation of Council's
40. Minister for Roads
41. Guyra Shire Council
42. Local Government Association of NSW and Shires Association of NSW
43. Minister for Environment
44. Forbes Shire Council
45. Insurance Council of Australia
46. Alliance Members
47. State Forests
48. State Emergency Service (SES)
49. NSW Treasury
50. Kogarah Council
51. Nature Conservation Council of NSW Inc.
52. NSW Volunteer Rescue Association
53. NSW Fire Brigade Employees' Union (FBEU)
54. NSW Fire Brigade (NSWFB)
55. NSW Rural Fire Service
56. Riverina Wool Combing Pty Ltd
57. Sydney Catchment Authority
58. Department of Local Government
59. Minister for Community Services
60. Country Women's Association of NSW
61. Insurance Council of Australia (Additional Submission)
62. Confidential
63. Gundagai Shire Council
64. Department of Local Government
65. Professional Financial Solutions
66. The Vaucluse Progress Association
67. Northbridge Financial Consulting

68. Council of the Shire of Jerilderie
69. Riverina Wool Combing Pty Ltd
70. Lockhart Shire Council
71. Confidential
72. Insurance Australia Group
73. ARIMA Ltd
74. Woollahra Municipal Council
75. State Forests of NSW
76. Local Government Association of NSW and Shires Association of NSW
77. Parkes Shire Council
78. Hornsby Shire Council
79. Department of Local Government
80. Insurance Council of Australia Ltd
81. NRMA Motoring and Services
82. Kempsey Shire Council
83. Property Council of Australia
84. Carrathool Shire Council
85. Scone Shire Council
86. Penrith City Council
87. NSW Fire Brigades and Rural Fire Service
88. Department of Housing

# Appendix 2 – List of Witnesses

## Friday 21 November 2003

| | |
|---|---|
| Ian Brown | Deputy Chief Executive Officer<br>Insurance Australia Group |
| Leanne Stagnitta | National Manager Home Products<br>Insurance Australia Group |
| Graham Adams | General Manager, Product and Underwriting<br>Insurance Australia Group |
| Allan Mason | Executive Director<br>Insurance Council of Australia |
| Allan Hansell | Manager NSW and ACT<br>Insurance Council of Australia |
| Michael Clark-Lewis | Senior Director, Revenue Strategy Branch<br>NSW Treasury |
| Julian Carter | Senior Economist<br>NSW Treasury |
| Ken Morrison | Executive Director – NSW Policy<br>Property Council of Australia |
| Cheryl Thomas | NSW Policy Adviser<br>Property Council of Australia |
| Ross Jones | Executive Director<br>Northern Sydney Regional Organisation of Councils |
| Nick Tobin | Director of Corporate Services, Willoughby City Council<br>Northern Sydney Regional Organisation of Councils |
| Roy Newsome | Group Manager Corporate Services, Ryde City Council<br>Northern Sydney Regional Organisation of Councils |

## Wednesday 26 November 2003

| | |
|---|---|
| Greg Mullins AFSM | Commissioner<br>NSW Fire Brigades |
| Phil Koperberg AO AFSM | Commissioner<br>NSW Rural Fire Service |

| | |
|---|---|
| Christopher Read | State Secretary<br>NSW Fire Brigade Employees' Union |
| Michael Wright | Senior Industrial Officer<br>NSW Fire Brigade Employees' Union |
| Steve Yorke | President<br>NSW Rural Fire Service Association |
| Keith Jordan | Executive Officer<br>NSW Rural Fire Service Association |
| Don Luscomb | Secretary and Treasurer<br>NSW Rural Fire Service Association |
| David Allen | Acting General Manger, Driver and Vehicle Safety<br>Roads and Traffic Authority |
| Vicki Sharp | Unit Manager, Projects<br>Registration Policy |
| Fiona McCredie | Policy Manager<br>NSW Farmers' Association |
| Robert Gledhill | Shires Association Executive<br>Local Government Association of NSW and<br>Shires Association of NSW |
| Alan Smith | Local Government Association Executive<br>Local Government Association of NSW and<br>Shires Association of NSW |
| Shaun McBride | Policy Officer, Economics and Development<br>Local Government Association of NSW and<br>Shires Association of NSW |
| Warren Taylor | Deputy Director of Strategic Services<br>Local Government Association of NSW and<br>Shires Association of NSW |
| Hugh McMaster | Government and Commercial Relations Manager<br>NSW Road Transport Association |
| Susan Streeter | Deputy Executive Director<br>NSW Mineral Council |
| Alan Finlay | Manager, Public Policy<br>NRMA Motoring and Services |

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|---|---|
| Grahame Gibbs | Director, Performance Management and Compliance<br>Department of Local Government |

## Thursday 27 November 2003 (Queanbeyan)

| | |
|---|---|
| Viv Straw | Acting General Manager<br>Snowy River Shire Council |
| Dave Glasson | Group Captain<br>Snowy River Shire Rural Fire Service |
| Darval Dickson | Group Captain<br>Snowy River Shire Rural Fire Service |
| Cr Len Tozer | Mayor<br>Gundagai Shire Council |
| Graham Tickner | General Manager<br>Gundagai Shire Council |
| Charles Gentner | General Manager<br>Jerilderie Shire Council |
| Alan Stewart | General Manager<br>Tallaganda Shire Council |
| Cr Leslie Hart | Mayor<br>Tallaganda Shire Council |
| Kevin Rheese | Director, Natural Disaster Management<br>Department of Transport and Regional Services |

## Wednesday 5 May 2004

| | |
|---|---|
| Greg Mullins AFSM | Commissioner<br>NSW Fire Brigades |
| Phil Koperberg AO AFSM | Commissioner<br>NSW Rural Fire Service |

## Friday 7 May 2004

| | |
|---|---|
| Doug Drysdale | Principal<br>Professional Financial Solutions |

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|---|---|
| Thach Huynh | Associate<br>Professional Financial Solutions |
| Ken Morrison | Executive Director – NSW Policy<br>Property Council of Australia |
| Cheryl Thomas | NSW Policy Adviser<br>Property Council of Australia |
| Alan Mason | Executive Director<br>Insurance Council of Australia |
| Allan Hansell | Manager NSW and ACT<br>Insurance Council of Australia |
| Tim Banks | Director<br>ARIMA Ltd |
| Jason Hall | Special Interest Group Coordinator<br>ARIMA Ltd |
| Chris Michie | Special Interest Group Associate<br>ARIMA Ltd |
| Sean O'Brien | Special Interest Group Associate<br>ARIMA Ltd |
| Garry Moore | Director<br>Council of Social Service in NSW (NCOSS) |
| Alan Smith | Local Government Associate Executive<br>Local Government Association of NSW and the Shires Association of NSW |
| Shaun McBride | Policy Officer, Economics and Development<br>Local Government Association of NSW and the Shires Association of NSW |
| Warren Taylor | Acting Director Strategic Services<br>Local Government Association of NSW and the Shires Association of NSW |

# Appendix 3 – Interstate Consultations

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|---|---|---|
| **Date** | 2 February 2004 | |
| **Organisation** | **Western Australian Fire and Emergency Services Authority (FESA)** | |
| **Attendees** | Mr Bob Mitchell | CEO |
| | Mr Lindsay Cuneo | FESA Director Funding Project |
| | Mr Frank Pasquale | FESA Management Accountant |
| **Organisation** | **Western Australian Local Government Authority (WALGA)** | |
| **Attendees** | Ricky Burges | CEO |
| | Mr Bruce Wittber | Policy Manager Governance |
| **Date** | 3 February 2004 | |
| **Organisation** | **Office of the Western Australian Auditor-General** | |
| **Attendees** | Des Pearson, | Auditor-General |
| | Peter McCann | Performance Review Division |
| | Paul Refferath, | Compliance Division |
| **Date** | 4 February 2004 | |
| **Organisation** | **South Australian Department of Treasury and Finance** | |
| **Attendees** | Robert Schwarz | Assistant Under Treasurer (Revenue and Economics) |
| | Kathy Moore | Director Revenue, Revenue and Economics Branch |
| | Damon Hall | Revenue and Economics Branch |
| **Organisation** | **Revenue SA (South Australian State Tax Office)** | |
| **Attendees** | Mr Emilio Fantasia | Assistant Commissioner, Revenue Business Services |
| | Mr Glenn Lodge | Director Property Revenue Services |
| | Kathy Moore | Director Revenue, Revenue and Economics Branch |
| **Organisation** | **South Australian Emergency Services Administration Unit (ESAU)** | |
| **Attendees** | Vince Monterola | Chief Executive ESAU |
| | Rex Mathews | Fund Manager, Strategic and Financial Services |
| | Kym Pennifold | Director, Strategic and Financial Services Unit |
| **Date** | 5 February 2004 | |
| **Organisation** | **South Australian Parliament's Economic and Finance Committee** | |
| **Attendees** | Hon Graham Gunn MP | Member for Stuart |
| | Karlene Maywald MP | Member for Chaffey |
| | Michael O'Brien MP | Member for Napier |
| | Jack Snelling MP | Member for Playford |
| | Paul Collett | Secretary to Committee |
| | Kylie Coulson | Research Officer |

# Appendix 4 – Interstate Comparison[1]

| Jurisdiction | New South Wales |
|---|---|
| **Funding Arrangements** | An insurance-based system that provided 73.7 per cent of funding for the NSW Fire Brigades and the Rural Fire Service.<br>NSW Fire Brigades receive 12.3 per cent of budget from local councils and 14 per cent from the State Budget.<br>Rural Fire Service received 13.3 per cent of budget from local councils and 13 per cent from the State Budget. |
| **Base** | Insurance Council of Australia (ICA) provides recommended fire service levy rates on the following insurance types: Commercial; Residential; Fire, Industrial Special Risk (ISR); and Motor vehicles. |
| **Exemptions/Discounts** | None |
| **Collecting Agent** | Fire service levy is paid directly to insurance companies who pass funds to fire services. Local council and State contributions are paid directly to fire services. |
| **Jurisdiction** | **Victoria** |
| **Funding Arrangements** | An insurance-based system that funds the Metropolitan Fire and Emergency Services Board and the Country Fire Authority.<br>Metropolitan Fire and Emergency Services Board Fire Service receive 75 per cent of funding from levy on insurance premiums, 12.5 per cent from Local councils and 12.5 per cent from State Budget.<br>Country Fire Authority receives 77.5 per cent of funding from levy on insurance premiums and 22.5 per cent from the State Budget. |
| **Base** | Insurance Council of Australia (ICA) provides recommended fire service levy rates on the following insurance types: Fire, ISR or CL commercial property; Contractors - all risks (construction and engineering); and Residential (house and contents). |
| **Exemptions/Discounts** | None |
| **Collecting Agent** | Fire service levy is paid to insurance companies who pass funds directly to fire services. Local council and State contributions are paid directly to fire services. |
| **Jurisdiction** | **Queensland** |
| **Funding Arrangements** | Majority of funding for the Queensland Fire and Rescue Service (QFRS) is collected through an urban fire levy, collected through municipal rates. Remainder is collected through State and Commonwealth charges and smaller fees and levies. |
| **Base** | Owners of prescribed properties pay the fire levy. Prescribed properties must be situated within urban fire districts controlled by the QFRS, serviced by full time QFRS staff and is imposed on real property, vacant land, council parkland and council buildings.<br>The amount of the levy depends on three factors:1. Classification of urban districts – 4 classes depending on service level, 2. Activity or use of the land, improvements to the land and 3 Commercial properties are subject to fire risk categories – 16 in total. |
| **Exemptions/Discounts** | Fire levies are not liable for properties that are serviced solely by the Rural Fire Brigades although local councils may choose to impose a levy to fund the Rural Fire Brigade operating in that area.20 per cent pensioner discount is available for pensioners, who reside in QFRS areas, and who qualify under the terms and conditions of the State Government pensioner subsidy scheme.<br>Land owned by the Commonwealth, Crown or State land is not liable for the levy. |
| **Collecting Agent** | Local councils collect the Urban fire levy on behalf of the State Government. Councils are paid an administration fee. Current regulation defines the collection fee as: $3.10 |

[1] Source: derived from Submission No 49, NSW Treasury, Appendix 2

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| | per collection- where collections are less than 40,000 and $2.60 per collection +$124,000 – where collections are above 40,000. |
| **Jurisdiction** | Western Australia |
| **Funding Arrangements** | Emergency Services Levy (ESL) collected through a property levy. The levy funds the Career Fire and Rescue Service, Volunteer Fire and Rescue Service; Local Governments' Bush Fire Brigades, State Emergency Service; and the new multi-service FESA Units.<br>All property owners are required to pay the levy, including State Government, Local Governments and not-for-profit organisations.<br>Commonwealth property is exempt from the levy as they contribute through a separate arrangement. |
| **Base** | The State is divided into 5 service categories according to the type of emergency service available.<br>Category area 1 comprises of the Perth metropolitan area, which is serviced by the Career Fire and Rescue Service and SES.<br>Further category areas spread out from category 1 as the level of service provision changes, category 5 being serviced by Bush Fire Brigades.<br>The amount of the levy is calculated by multiplying the ESL rate (varies according to category, but only for categories 1-4) by the gross rental value of the property. Properties in category 5 and leviable mining tenements are charged a fixed amount of $30 per rate notice.<br>Minimum ESL charge for all property types= $30.<br>Maximum residential, farming property or vacant land ESL charge = $175.<br>Multiple residential property = $175 multiplied by the number of dwellings.<br>Maximum commercial, industrial or miscellaneous property (eg. private schools, churches) ESL charge = $100,000. |
| **Exemptions/Discounts** | Seniors and pensioners who qualify for a rebate on their Council rates will receive the same level of rebate on their ESL charge. |
| **Collecting Agent** | Local councils collect the ESL on rate notices for the State Government. Local Governments will be paid an annual administration fee. A total of $2.25 million will be paid in 2003-04.<br>Both the number of rates notices issued and the amount of levy collected determine the amount received by each Council. |
| **Jurisdiction** | South Australia |
| **Funding Arrangements** | Emergency Service Levy (ESL) collected through a property levy, including a levy on motor vehicles. The levy funds the SA Metropolitan Fire Service, Country Fire Service, State Emergency Service, Surf Life Saving SA, Volunteer Marine Rescue SA; and Emergency Services provided by the South Australian Police Department.<br>The levy is applied to all property, including private schools, churches, charities and private hospitals. State and Local Governments also contribute, based on the land their own property. Commonwealth Crown land is exempt, however the Commonwealth provides assistance for the protection of their own land. |

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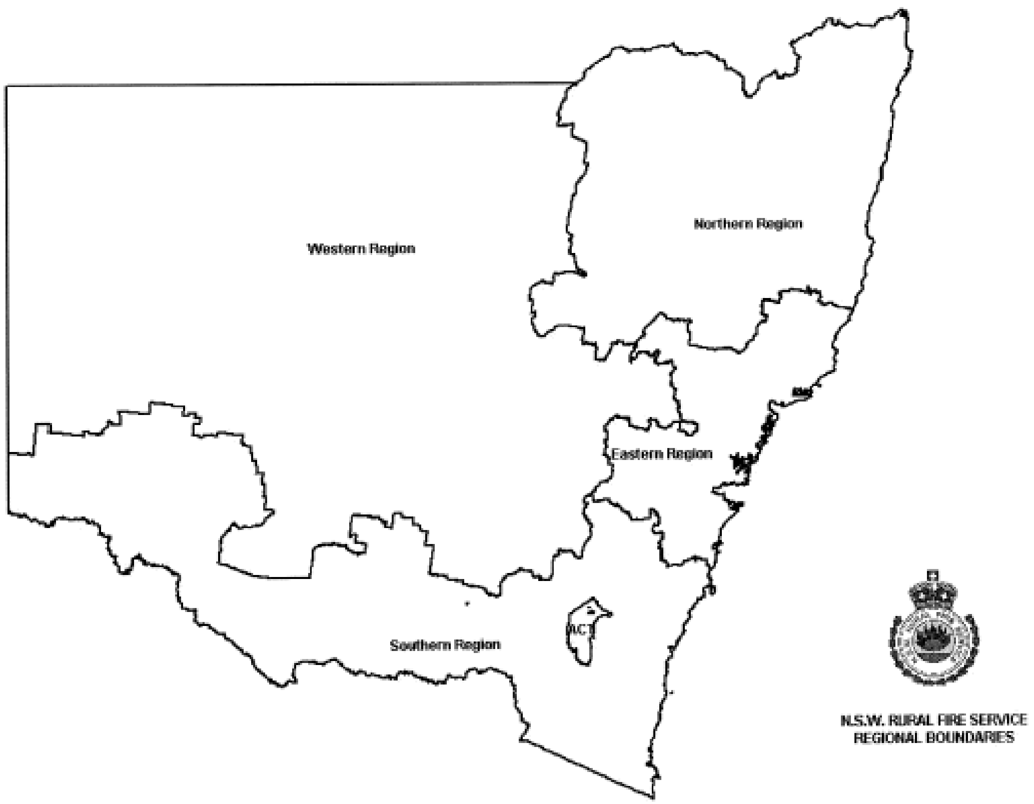
| **Base** | Levy is calculated in accordance with ownership as of 1 July each year. The fixed property levy is based on the capital value of the property, while mobile properties are charged at a flat rate.<br>The gross fixed property levy is made up of a fixed dollar amount plus a variable component based on the property's capital value. The capital value is multiplied by three determining factors:<br>Area factor, one of four areas reflecting varying levels of emergency service provision;<br>Land use factor, one of seven different categories, depending on the classification of the land, eg. residential, commercial etc.; and<br>The applicable levy rate for that year.<br>Remissions, concessions and any payments made are subtracted from the gross levy calculation to determine the payable levy amount.<br>Motor vehicles and vessels are charged a fixed fee, varying between different classes of vehicles. |
| **Exemptions/Discounts** | Concessions of up to $40 are available for individuals principal place of residence, including pensioner concession card holders, recipients of Centrelink allowances, Seniors card holders and Veterans Affairs Gold Repatriation Health Card. |
| **Collecting Agent** | Fixed property component is collected via notifications from RevenueSA. The collection of the levy on mobile property (cars, motorbikes etc) occurs through Transport SA's Customer Service Centres. All funds are placed in the Community Emergency Services Fund, for distribution by the Minister for Emergency Services. |
| **Jurisdiction** | Tasmania |
| **Funding Arrangements** | Funding for the Tasmanian Fire Service (TFS) comes from these sources:<br>Fire Service Contribution - 47 per cent.<br>Insurance Fire Levy - 24 per cent.<br>Motor Vehicle Fire Levy - 9 per cent<br>State Budget - 8 percent.<br>Smaller contributions are generated through fire prevention charges, sundry income and contributions from the Commonwealth. |
| **Base** | The Fire Service contribution varies throughout the State depending on whether the property is located in urban or country areas. The contribution is a fee for service based on the assessed annual value of properties and the level of fire protection provided.<br>The Insurance Fire Levy. Rate is levied on the following various insurance types: Marine cargo insurance; Aviation hull insurance; and Other prescribed classes of insurance.<br>Motor Vehicle Fire Levy is levied at a flat rate per vehicle.<br>The Treasurer determines an appropriate State contribution. |
| **Exemptions/Discounts** | Pensioners and health cardholders receive discounts on rates and motor vehicle levies. The motor vehicle levy for pensioners is $8.<br>Motor cycles are excluded from the vehicle fire levy. |
| **Collecting Agent** | Insurance companies are responsible for collecting the insurance fire levy, the Department of Infrastructure, Energy and Resources collects the motor vehicle fire levy and local councils collect the fire service contribution through council rates. Local councils are paid a four percent collection fee from the State Fire Commission. |
| **Jurisdiction** | Northern Territory |
| | Northern Territory Fire and Rescue Service is funded from consolidated revenue. |
| **Jurisdiction** | Australian Capital Territory |
| | ACT Fire and Emergency Services is funded from consolidated revenue. |

# Appendix 5 – Regional Boundaries for the NSW Rural Fire Service




Source: Submission No 55, NSW Rural Fire Service, Appendix A

# Appendix 6 – Executive Summary of *Quantitative Modelling of NSW FSL Funding Methods* by Professional Financial Solutions