Submission

LOCAL GOVERNMENT RATING SYSTEM REVIEW

Victorian Farmers Federation

November 2019

The Victorian Farmers Federation

The Victorian Farmers Federation (VFF) is the only recognised consistent voice on issues affecting rural Victoria.

Victoria is home to 25 per cent of the nation's farms. They attract neither government export subsidies nor tariff support. Despite farming on only three per cent of Australia's available agricultural land, Victorians produce 30 per cent of the nation's agricultural product. The VFF represents the interests of our state's dairy, livestock, grains, horticulture, flowers, chicken meat, pigs and egg producers.

The VFF consists of a nine person Board of Directors, with seven elected members and two appointed directors, a member representative General Council to set policy and eight commodity groups representing dairy, grains, livestock, horticulture, chicken meat, pigs, flowers and egg industries.

Farmers are elected by their peers to direct each of the commodity groups and are supported by Melbourne-based and regionally located staff.

Each VFF member is represented locally by one of the 200 VFF branches across the state and through their commodity representatives at local, district, state and national levels. The VFF also represents farmers' views on hundreds of industry and government forums.

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Foreword

The VFF welcomes the opportunity to provide this submission to the Local Government Rating System Review and acknowledges the Victorian Government's commitment to initiating this review into the rating system to identify changes that will improve its fairness and equity.

The VFF has long campaigned for a fair and equitable rating system and the current review has come as a result of the organisation's strong advocacy for Victoria's farmers and rural communities.

As a proud membership based and democratic organisation the VFF has actively engaged its members throughout the drafting of this submission. This process has highlighted the enormous diversity in Victoria's agricultural sector and how local government rates affect different communities and farm businesses.

Introduction

Local government rates are a tax. By principle, taxation should be fair and equitable. Unfortunately the current local government rating system is anything but fair and equitable for all rural ratepayers, but in particular farm businesses.

The present system presumes that the higher the land valuation the greater capacity the owner has to pay. In practice however there is a great divide between land valuations, capacity to pay and what is actually paid.

Victoria's rating system has created the situation whereby rural ratepayers pay more in rates as a percentage of the value of their property than ratepayers in metropolitan Melbourne. What's more, rural ratepayers receive and have access to fewer services from local government than ratepayers in the city.

This distortive burden on agriculture is further compounded by the degree of variation in municipal rates from shire to shire and the clear discrepancies that fundamentally exist between the abilities for metropolitan councils to generate rate income, against the capacity of rural and regional councils.

It is the long held belief and concern of the VFF that local government rates derived from farmland ratepayers are inequitable. As farm businesses have become increasingly aggregated, the rating burden faced by individual farmers has been compounded. The local government rating system does not accurately capture a farm ratepayer's capacity to pay, nor the benefits they receive.

In farming businesses there are three factors of production; land, labour and capital. The benefit derived from each of these factors is compounded by changes to seasonal conditions, none of which are captured in the current rating strategies of rural and regional councils.

The current model of using land valuations for striking rates, places undue financial stress on farming businesses as the value attributed to farm land does not reflect farm businesses' revenue generation nor capacity to pay.

It is the long term position of the VFF that rates on farmland (excluding the farmhouse and curtilage) be abolished. However, in moving towards this goal, the VFF believes the principles of a fair and equitable rating system must be:

- Equity across councils; rates should be comparable for similar properties across all councils.

- Predictability; there should be a reasonable degree of stability in the level of rates burden between years for each ratepayer category.

The VFF also believes that there should be an appropriate balance between the commonly used taxation principles: efficiency; benefit; capacity to pay; horizontal/vertical equity; simplicity and sustainability.

Fundamentally the VFF believes that as a wealth tax, the local government rating system has failed and is producing inequitable outcomes for farmers and other rural ratepayers, and provides an unsustainable footing for the funding of local government.

That is why the VFF supports a comprehensive overhaul of the rating system through an equalised funding model where the state government redistributes rates to local government on the basis of equity and need.

Moreover, the VFF also supports the following mechanisms; the use of differential rates to create fairness between farm and other ratepayers; house and curtilage to be separated from farmland and rated accordingly; introduction of minimum and maximum rates; the use of valuation averaging to remove variability and unpredictability from the rates system.

Whilst it is the VFF's preference for these mechanisms to be adopted alongside that of an equalised funding model, it is recognised that such wholesale change would take significant time and effort to implement. Consideration should therefore be given to rapidly implementing these mechanisms to immediately bring about a degree of fairness and equity for farm ratepayers, while moving towards an equalised funding model.

Recommendations

Recommendation 1 – Equalised funding system

The Victorian Government implement a local government equalisation funding system where the State would set a general rate for all property and redistribute funds collected from rates on the basis of equity and need.

Recommendation 2 – Minimum and maximum rates

The Local Government Act be amended to allow councils to apply minimum and maximum rates (by property class). It is proposed that the Act define a maximum total amount that a council can raise from minimum rates at 50% of general rates.

Recommendation 3 - Compulsory differential rates

The Act be amended to require a council to use differential rates (including a compulsory differential rates for farmland) to establish a fair and equitable distribution of the rate burden for each class of land and that the rate burden for each class be maintained for at least four years; and that farm differential rates only be offered to commercial farm businesses.

Recommendation 4 – Valuation averaging

Valuation averaging be introduced for all councils in Victoria. Under this system, all councils would strike rates based on a moving average valuation calculated for each property over the past 5 years. The actual valuations returned each year by the Valuer-General would remain the same but the valuation basis for the rate strike would be changed.

Recommendation 5 - Introduce house and curtilage valuation for farm land

The house and curtilage for farmers should be charged a municipal rate similar to that of all other homes in the local government area. Farmland should be separated into a separate assessment which councils having the ability to rate land at the farm differential rate – or exempt the farm land from rates.

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Section 1
The existing rating system

1.1 Inequities of rating

The VFF believes there are five major inequities associated with the local government rating system:

- Farmers in general pay more in rates than residents in urban areas.
- Rating structures rarely account for the ability to pay and farmers' ability to pay rates fluctuates to a far greater degree than wage and salary earners.
- Farmers in general use few of the services they pay for through rates and are provided in urban areas.
- Land is a farmers' working capital and is taxed disproportionately compared with the working capital owned by other people and businesses.
- Victoria's rating system produces vast inequalities between metropolitan and regional ratepayers which compounds pressures faced by farm ratepayers.

Farmers consistently pay more in rates than residents in urban areas.

Based on analysis of the 2019-20 local government draft budgets, the VFF has determined that farmers pay an average $2,741 per assessment in rates. This is compared to an average of $1,325 per residential rate assessment, $3,145 per commercial rate assessment and $3,636 per industrial rate assessment.

The use of statistics for rural assessments underestimates the rate burden faced by farmers. These statistics are distorted by the inclusion of multiple assessments (where one farm consists of separate areas of land which are rated separately) and small areas of land that are not commercial farms. It is important to recognise the reality that farmers pay multiple assessments across their land holdings, whereas the average residential and commercial business ratepayer typically pays rates on just one property. In the Ararat Shire for example there are 1718 farm assessments. However, ABS data indicates 457 farm businesses in the shire. Nevertheless, farmers are still paying more than twice the residential rate, while often benefiting from fewer services.

To provide a sense of the disparity in the distribution of rates, the highest average farm rate is $9,265 per assessment in the City of Whittlesea, while the average resident will pay $1,699. The City of Whittlesea is also one of only 3 councils of the 58 councils analysed by the VFF that did not have a distinct commercial or industrial rate.

Comparatively, the lowest average farm rate was $1,331 in Indigo Shire, for farm assessments of less than 40ha. In Indigo Shire, there are two farm rates; one for properties larger than 40ha and one for properties less than 40ha. For properties greater than 40ha, which represents a more typical commercial farm, the average farm rate per assessment is $1,739, while the average resident will pay $1,108 and the average business $2,077.

Rating structures rarely account for ability to pay; farmers' ability to pay rates fluctuates to a greater degree than wage and salary earners' incomes.

It is relevant to compare the positions of a farmer and a wage or salary earner. Both ratepayers may earn $70,000 per year, but the farmer might be required to pay $10,000 in rates compared to $1,200 for the wage or salary earner. In this case the farmer is required to spend 14% of their income on rates as opposed to 1.7% for the wage or salary earner.

Farmers' incomes fluctuate because they are more exposed to factors beyond their control including seasonal variability such as rainfall, natural disasters and changes in international commodity markets. These factors have little impact on land values, but have a significant impact on famers' incomes and ability to pay.

Famers in general use fewer services provided in urban areas.

The justification for the existing rating system that rates levied on land are spent on servicing that land has little relevance today as it did in the past. Although some arguments in favour of rates suggest local government provides infrastructure and services that increase the value of surrounding land, the reality is that farmers are not serviced to the extent sufficient to warrant the wide difference in rural and urban rate burdens. Even though roads are important to servicing rural properties, rural councils are finding it more difficult to adequately fund upgrades and maintenance.

The 'ability to pay' concept is an important and well established framework on which taxes are levied. On the other hand, the 'ability to use' services and infrastructure provided is rarely taken into consideration. In general farmers have little demand for, use and lack of access to facilities and services such as rubbish collection, health and welfare, libraries, parks, gardens, street lighting, footpaths which are provided in towns to enhance the quality of living for residents.

Land is a farmer's working capital and is taxed disproportionately compared with the working capital owned by other businesses.

Land used for the purpose of primary production is working capital. Farming generally utilises a large amount of 'unimproved' land, and as a result municipal rates are a tax on a means of production. For example, about 70% of a woolgrower's working capital is land.

Conversely, the proportion of working capital that consists of land could be extremely small in the case of businesses in a local town. From this viewpoint, it is inequitable that 70% of a farmer's working capital should be taxed whereas another businessperson may be taxed on, say, only 30% of their capital.

The VFF has analysed the inequity of rates paid by farm and other businesses as a percentage of turnover which is set out in the following Table. It is important to also consider that farmers report that rates represent anywhere between 1% to 20% of their total cost of production. These percentages of course vary considerably across individual farms and seasonal conditions.

Table 1: Farm and other business turnovers rate burden comparison

LGA	Other Business Turnover	Farm Business Turnover	Commercial Rates Paid	Farm Rates Paid	Farm rates as a percentage of turnover	Commercial rates as a percentage of turnover
Ararat	$1,031,354,000	$238,174,000	$983,600	$6,085,800	2.56	0.10
Ballarat	$11,627,540,000	$182,829,000	$21,394,287	$1,672,288	0.91	0.18
Bass Coast	$2,535,496,000	$187,843,000	$2,150,000	$3,013,000	1.60	0.08
Baw Baw	$3,458,142,000	$653,024,000	$4,975,000	$8,463,000	1.30	0.14
Bendigo	$11,965,943,000	$403,523,000	$22,253,000	$2,828,000	0.70	0.19
Buloke	$345,339,000	$218,621,000	$629,000	$8,208,000	3.75	0.18
Campaspe	$4,619,194,000	$627,800,000	$3,570,000	$7,830,000	1.25	0.08
Colac Otway	$2,247,881,000	$413,047,000	$2,180,000	$5,775,000	1.40	0.10
Corangamite	$1,402,713,000	$673,324,000	$577,000	$10,234,000	1.52	0.04
East Gippsland	$3,438,925,000	$572,994,000	$5,744,000	$4,702,000	0.82	0.17
Golden Plains	$814,153,000	$245,053,000	$43,949	$3,299,155	1.35	0.01
Hepburn	$851,363,000	$163,408,000	$2,373,000	$1,832,000	1.12	0.28
Hindmarsh	$448,364,000	$335,309,000	$248,000	$5,163,000	1.54	0.06
Indigo	$1,490,622,000	$165,618,000	$806,000	$2,470,000	1.49	0.05
Macedon Ranges	$3,114,634,000	$183,762,000	$2,187,000	$2,260,000	1.23	0.07
Melton	$6,219,872,000	$91,657,000	$10,685,000	$1,858,000	2.03	0.17
Mitchell	$2,358,183,000	$154,541,000	$279,000	$2,784,000	1.80	0.01
Moira	$2,652,304,000	$620,936,000	$2,049,000	$4,844,000	0.78	0.08
Moorabool	$1,618,907,000	$258,328,000	$1,921,000	$3,049,000	1.18	0.12
Mornington Peninsula	$12,760,906,000	$442,108,000	$141,000	$1,783,000	0.40	0.001
Moyne	$1,517,186,000	$658,072,000	$206,000	$8,696,000	1.32	0.01
Murrindindi	$782,378,000	$238,516,000	$904,000	$6,389,000	2.68	0.12
Northern Grampians	$1,091,634,000	$199,980,000	$923,000	$4,500,000	2.25	0.08
Pyrenees	$290,461,000	$184,525,000	$119,500	$4,054,000	2.20	0.04
South Gippsland	$2,483,201,000	$651,490,000	$1,381,000	$10,673,000	1.64	0.06
Strathbogie	$599,575,000	$315,347,000	$893,000	$7,555,000	2.40	0.15
Wangaratta	$2,539,204,000	$286,818,000	$2,914,000	$6,108,000	2.13	0.11
Wellington	$4,660,646,000	$806,773,000	$12,249,000	$9,922,000	1.23	0.26
Wodonga	$5,330,003,000	$86,441,000	$4,274,000	$966,000	1.12	0.08

Source: Victorian Local Government Draft Budgets 2019-20 / REMPLAN Economy profiles
www.economyprofile.com.au

The income a farmer derives from their land is often reinvested into their business creating improvements to the land such as sheds or drainage. These improvements theoretically increase the value of the land and therefore the rates paid by the farmer. Farm commodity prices and farm gate returns have not kept pace with cost of living increases over recent decades, resulting in farmers having 'to get bigger or get out'. Farmers need to own more land to scale up their production to keep pace with increasing costs, yet they inevitably pay more rates that are disproportionate to their increase in production.

The inequity is further compounded by farmers' needing to own more land to scale up their production and grow their business, yet inevitably paying more rates that are disproportionate to their increase in production.

The value of farm land does not necessarily reflect the income potential of the land; agricultural land is not always valued on the basis of productivity. For example, peri-urban land may be valued according to future development potential, while coastal land may be valued for aesthetic reasons rather than productive. This particularly has a detrimental impact on farm business at the edges of metropolitan Melbourne and disincentivises agricultural production in this region which in turn reduces the third party benefits derived from productive farmland (amenity, weed and pest control etc.).

Inequity between metropolitan and rural ratepayers compounds pressure on farm ratepayers

Whilst much of the discussion around the rating system focusses on the inequity between ratepayers in the same local government area, there is great inequity between rates paid by rural and metropolitan ratepayers. This further compounds the inequities faced by farmers, especially those who make up the predominant rating base in individual council areas.

In its submission to the Rural Rating Enquiry (1978) the VFF's predecessor organisation the Victoria Graziers Association showed that based on 1975-1976 information from 77 shires, the average rate paid by rural ratepayers was $252 compared to $78 paid by non-rural ratepayers. This inequity continues to persist.

Even though property values in metropolitan Melbourne are higher than those in rural Victoria, the average rates paid per assessment is similar across metropolitan and regional Victoria. For example the average rate per assessment in the rural local government areas of Ararat and Alpine Shires respectively are $1,823 and $1,717, whilst the average per assessment in the Cities of Hobsons Bay and Yarra is $1,779 and $1,652.

However, the inequity between rural and metropolitan ratepayers is revealed when comparing properties of the same value. For example, the rate bill on a property in Kerang (Gannawarra Shire) valued at $300,000 is $2,400 whilst a similarly valued property in Toorak (Stonnington) only pays $390.

The total rates paid by Victorians represent roughly 2.8% of the State's total personal income. In the Gannawarra Shire rates represent 5.3% of personal income as opposed to 1.4% in Stonnington. This example illustrates the failure of the rating system as a form of wealth tax where $300,000 of measured wealth is taxed at a different rate.

Metropolitan councils draw on 2% of their communities' personal income where more than 4% or rural incomes are dedicated to rates. No rural local government pays less than the 2.8% state average whilst five local government areas draw on more than 7% of their communities' incomes through rates. Smaller rural councils face a greater rate burden in terms of the incomes that people earn. Rates bills therefore have a much larger impact on these households. The inequity for the farmer is all the more stark when comparing the rates they pay compared to someone living in metropolitan Melbourne.

1.2 Fiscal capacity of Local Government

Regional Victoria is split across 48 local government areas which have a variety of different circumstances. Populations in each vary from less than 3,000 residents to over 230,000 with some experiencing rapid population growth and others in decline. Geographical and economic factors also mean that some councils contain large urban areas, some are more rural in character.

The introduction of the State Government's cap on council rate increases and the Commonwealth's freeze on Financial Assistance Grants from 2013-14 to 2016 have placed additional burdens on the capacity of Local Government to evenly distribute the rate burden. Changes have also occurred to the funding councils receive for some jointly funded responsibilities (for instance, libraries, school crossing supervisors and health services). Whilst other grants have been introduced which partly offset these changes, many rural and regional councils have experienced a decline in their overall revenue from grants in recent years.

Rural councils are heavily dependent on grant income as a percentage of their total income, whereas grants make up a small percentage of metropolitan council's budgets. The dependence on grant income means rural councils have less capacity for local decision making and control. There are also equity considerations in that all councils receive grants, but not all councils need grants. The principle allowing local governments to receive minimum Financial Assistance Grants seems to be contrary to fiscal equalisation. The minimum grants received by relatively sustainable metropolitan councils ought to be distributed to disadvantaged rural councils where the funds would have greater impact.

The recent Victorian Parliamentary Inquiry into the Sustainability of Rural Local Government cited the Auditor General's findings that rural councils are financially unable to continue providing the extent of services they do. "Looking at adjusted underlying results (a measure of a council's ability to generate a surplus from its ordinary course of business), the Auditor General has assessed regional councils as a whole as medium risk. In relation to individual councils:

- of 10 regional city councils, four were assessed as high risk and three were medium risk
- of 19 large shire councils, five were assessed as high risk and nine were medium risk
- of 19 small shire councils, eight were assessed as high risk and seven were medium risk."

The Auditor General noted:

A longer term negative trend in this indicator will have an adverse impact on the services that these councils are able to offer to their communities. It is important that councils can generate positive surpluses, and councils' ability to do so will assist them in the longer term to generate sufficient funds to keep delivering the service levels that their communities expect. Councils' sustainability challenges can also be seen in relation to infrastructure. Many regional councils are spending less on asset investment than is required. This creates an asset renewal gap (the difference between expenditure and the amount required to maintain infrastructure to an acceptable standard).

1.3 Equity cannot be achieved through the current rating system

There are relatively few ways that councils can raise revenue. Rates and charges on property are by far the most significant source of revenue that councils can raise directly, accounting for 70.1% of their revenue when grants from other levels of government are excluded (72.6% for regional councils).

Rural councils are more dependent on rates and charges, as they do not have access to the many streams of revenue that metropolitan, peri-urban and large regional cities may have, such as parking fees and developer contributions. For example, the City of Melbourne collects $95 million from parking fines. Conversely, rates and charges can account for as much as 90 per cent of non-grant revenue in some rural municipalities.

Most problems with the current rating system arise from the large and sudden shifts that often occur in individual rate bills and the relative shares of council costs borne by different ratepayer categories. These sudden and large changes in rate bills cause considerable community angst and the shift in rate burden distribution bears no relationship to the benefits enjoyed by the ratepayer groups impacted.

The large and sudden valuation shifts can be brought on by broader economic and property market conditions but also by very localised factors. This is particularly true for farm land where there are often limited sales evidence in a valuation year or localised demand pushes property prices well above market.

The current differential rating structure provides some useful policy tools for councils to respond to this issue but does not address these more localised (and often extreme) shifts. The only measures available to councils seeking to 'cushion' or transition the impact of such changes are rebates however, these result in 'lost' revenue under the rate cap total revenue calculation.

The other problem with the current rating system is the inequity of rates across councils for similar properties. Many farm businesses own land in adjoining/similar councils and yet pay vastly different rates in the dollar for the same benefit received. All councils have different cost bases reflecting the number and level of services delivered to its community and the assets used to deliver those services. However, the cost base of each council has been established over many years based on local council decisions and has effectively been locked in by rate capping. There is also state-wide inconsistency of rating practices across councils.

Section 2
Recommendations

2.1 Equalisation funding system

Recommendation:

The Victorian Government implement a local government equalisation funding system where the State would set a general rate for all property and redistribute funds collected from rates the basis of equity and need.

To address the inequity between councils, the VFF recommends that the Local Government Rating System Review and the State Government investigate the implementation of an equalisation funding system as follows:

- The State Government would establish a general rate in the dollar on the basis of the state-wide valuation of property and the state-wide population or the state-wide number of rate assessments.
- The State Government could establish a different general rate according to council type (metro, interface, regional, rural).
- The State Government would redistribute the revenue on the basis of equity and need similar to the allocation of Financial Assistance Grants and that this function should be performed by the Victorian Grants Commission.

A key concern of the VFF is the inequity in the rates paid for similarly valued properties between municipalities. In particular the VFF is concerned by the inequiry between disadvantaged rural councils compared to metropolitan councils. Ratepayers in rural and regional councils also have lower incomes and therefore pay a higher percentage of their income towards rates as shown in the following Table.

Table 2. Household income consumed by rates in selected LGAs

Type of council	Average household income $	Percentage of household income consumed by rates %
Rural	42,659	4.3
Regional	64,270	2.8
Interface	60,632	3.0
Metropolitan	79,622	2.3

Source: Victorian Local Government Draft Budgets 2019-20 / 2016 ABS Census

The VFF believes the inequity in rates paid by farmers and other ratepayers cannot be genuinely dealt with without addressing with the inequity between rural and metropolitan councils.

All councils have different cost bases reflecting the distinct make-up of their individual communities and the consequent number and level of services consumed and the assets utilised. However, the cost base of each council has been established over many years based on local council decisions and then locked in with the introduction of rate capping. It is therefore possible that two councils which are largely similar in size, location and make-up can have completely different cost bases resulting in inequity of rating between those councils as shown in the following Table.

Table 3. Rates paid on $10 million property in similar LGAs

Council	Assessments	Rates on $10M Farm property
	No.	$
Buloke	6,259	63,140
Yarriambiack	6,939	39,110
Hindmarsh	5,124	47,180
West Wimmera	4,729	26,420

Source: Victorian Local Government Draft Budgets 2019-20

The difference is even more striking when comparisons between councils which are largely dissimilar are considered as shown in the following Table.

Table 4. Rates paid on $10 million property in dissimilar LGAs

Council	Assessments	Rates on $10M Farm property
	No.	$
Buloke	6,259	63,140
Shepparton	31,210	45,647
Ballarat	53,728	28,090
Wyndham	88,898	20,820

Source: Victorian Local Government Draft Budgets 2019-20

As part of an equalised funding system, consideration should be given to tying rate revenue to the delivery of a standard set of core services, standard costs and levels for each service and a standard allowance for administration and overheads. That standard set of services would be classified according to council type (metropolitan, rural, regional etc.). Councils wishing to deliver services over and above the standard set of core services would need to generate additional revenue to cover the cost of those services on a user pays basis or through alternative revenue sources.

2.2 Minimum and maximum rates

Recommendation:

The Local Government Act be amended to allow councils to apply minimum and maximum rates (by property class). It is proposed that the Act define a maximum total amount that a council can raise from minimum rates at 50% of general rates.

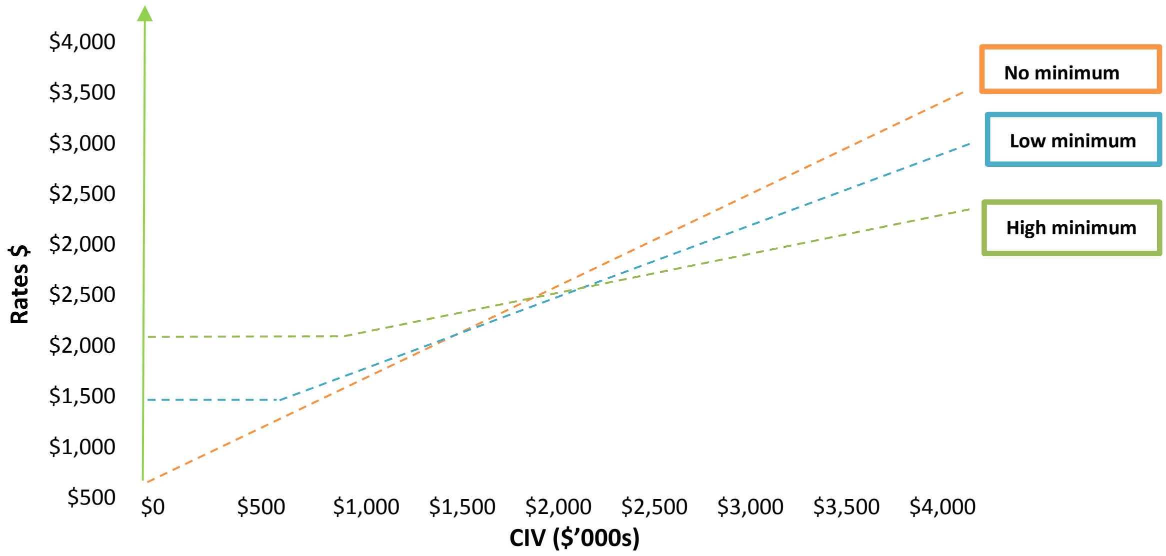
Under the Local Government Act 1958, councils were able to levy a minimum rate where all properties with a valuation equal to or less than an agreed minimum property valuation would pay the same fixed amount of rates. Above this property minimum valuation, rates would be calculated based on the property valuation. Under the 1958 Act there was no cap on the total amount that could be raised from minimum rates. Typically, this approach was justified using the ‘benefit’ principle; that the benefit of council services is generally flat across the valuation spectrum (i.e. ratepayers generally don’t get more benefit from council expenditure and services as their property value goes up).

By 1989, there were a number of councils throughout Victoria that had increased their minimum rates to a level whereby over 50% of total rates were being raised from the minimum rate. This had a levelling effect on the rating profile and led to a much more regressive taxation system (i.e. it benefited higher value properties and disadvantaged lower value properties). Minimum rates were abolished and replaced with the option for a municipal charge (for CIV rating councils only) as part of the 1989 review of the Act.

In New South Wales a council can levy a minimum rate with the minimum set by regulation (currently $526). In Queensland, councils can set a minimum rate for each category with no statutory limits on the level of the minimum rate. In South Australia and Tasmania, councils can use a minimum rate rather than a fixed rate, but the minimum can only apply to a maximum of 35% of properties in the category before the rate in the dollar cuts in. In Western Australia, a minimum rate can be used but cannot apply to more than 50% of properties if set above $200 without Ministerial approval.

Many of the services provided by council have transitioned away from being property based services and are now more broadly ‘people based’. Given this shift, it is appropriate that a minimum rate be set in a way that generates equity across ratepayers and ratepayer categories. In looking at rural and regional councils, farmers are generally paying the highest burden of rates within a council region. With minimum rates in place, the income generated from the general rate can be decreased, providing ratepayers with relief of this payment.

The following graph provides a conceptual illustration of three different rating profiles (no minimum, low minimum rate, high minimum rate).



Whilst the above is only a conceptual illustration, it shows (depending on the distribution of assessments across the valuation spectrum) how a minimum rate has the potential to substantially flatten a council's rating profile, thereby dampening the effect of the variable general rate component.

The introduction of a minimum rate should act as a mechanism to dampen the effects of substantial changes in property valuations between years. The notion of a minimum rate bill is also consistent with the community idea that all properties should make a contribution towards a council's cost structure. The additional flexibility of setting the minimum rate by category also allows a council to use valuation banding with a declining rate in the dollar as valuation increases. This again reflects, to some extent, the benefit principle where increasing property values do not necessarily result in the increased use of or benefit from services.

The reintroduction of minimum rates would make the requirement for the municipal charge redundant. The municipal charge is difficult for many ratepayers to understand and is not used in other jurisdictions where minimum rates or base charges are used to reflect the benefit principle.

However, the VFF believes that **in the event that minimum and maximum rates are not adopted, all councils should be required to levy a municipal charge** with the minimum amount a council can raise to be set at 20% of total rates and charges with a maximum of 50%. The VFF does not support the removal or reduction in the current municipal charge without its replacement by a minimum rate.

Where minimum rates not accepted, the municipal charge should be a feature of all local government rating strategies as it provides local governments a clear opportunity to levy a fair and equitable charge across their constituents to recover some of the fixed costs of a council. However, the current maximum of 20 percent is too restrictive. In New South Wales, South Australia and Tasmania councils are able to levy a flat charge up to a maximum of 50 percent of total rates and charges. In Western Australia and Queensland, there is no maximum.

2.3 Compulsory differential rates

Recommendation:

The Local Government Act be amended to require a council to use differential rates (including a compulsory differential rate for farmland) to establish a fair and equitable distribution of the rate burden for each class of land and that the rate burden for each class be maintained for at least four years; and that farm differential rates only be offered to commercial farm businesses.

Of the 79 Victorian councils, 63 have a farm rate category or equivalent. However, farm differentials are not consistently applied across the state. Eight councils have farm rates equal to 100% indicating that they have not used differential rates to address the equity and fairness of the rate burden distribution across ratepayer categories. There are also vast differences between councils which have used farm differential rates with three councils having a farm differential less than 50%, 24 councils with a farm differential between 50% and 75% and the remainder greater than 75%.

VFF analysis has confirmed that farms often pay more in rates than other commercial businesses and farm differentials are not being sufficiently used by local government to address this equity issue. The Table below demonstrates the operation of differentials and the impact they have on the rate burden distribution.

Table 5. Average commercial and farm rate assessments

Council	Commercial differential %	Farm differential %	Average rate commercial assessment $	Average rate farm assessment $
Alpine Shire	143%	73%	na	na
Ararat Rural City Council	125%	55%	2,981	3,542
Ballarat City Council	272%	72%	9,143	2,138
Bass Coast Shire	100%	80%	2,327	3,071
Baw Baw Shire	120%	90%	3,171	3,664
Benella Rural City	140%	65%	3,816	2,551
Buloke Shire Council	100%	82%	1,385	2,846
Campaspe Shire Council	116%	90%	3,210	2,092
Cardinia Shire Council	145%	75%	3,826	2,898
Casey Council	100%	100%	na	na
Central Goldfields Shire Council	152%	95%	3,320	1,817
City of Whittlesea	100%	60%	na	9,265
Colac-Otway Shire Council	165%	75%	3,344	2,001
Corangamite Shire Council	100%	90%	1,168	3,536
East Gippsland Shire Council	143%	82%	2,798	1,738
Gannawarra Shire Council	103%	68%	1,794	2,906
Glenelg Shire Council	100%	100%	1,522	2,658

Golden Plains Shire Council	100%	90%	1,022	2,594
Greater Bendigo City Council	185%	85%	9,039	2,463
Greater Geelong City Council	240%	80%	5,182	3,733
Hepburn Shire Council	116%	65%	2,828	1,642
Hindmarsh Shire Council	90%	90%	754	2,494
Horsham Shire	95%	67%	3,129	2,664
Hume City Council	100%	100%	na	na
Indigo Shire Council	135%	75%	2,077	1,739
Latrobe City Shire	100%	75%	na	2,411
Loddon Shire Council	100%	88%	na	1,666
Macedon Ranges Shire Council	120%	80%	1,951	2,198
Mansfield Shire Council	137%	66%	2,277	2,048
Melton Council	160%	72%	4,295	3,366
Mildura Rural City Council	120%	76%	5,576	2,704
Mitchell Shire Council	240%	80%	2,197	5,720
Moira Shire Council	140%	100%	2,119	2,230
Moorabool Shire Council	155%	78%	3,455	2,298
Mornington Peninsula Shire	140%	35%	2,311	1,544
Mount Alexander Shire Council	130%	100%	2,668	2,031
Moyne Shire Council	100%	100%	1,000	1,782
Murrindindi Shire Council	125%	70%	2,022	2,514
Nillumbik Shire Council	58%	43%	2,742	3,578
North. Grampians Shire Council	100%	47%	2,208	2,028
Pyrenees Shire Council	110%	79%	1,245	2,679
Shepparton Council	205%	90%	7,620	2,622
Shire of Yarra Ranges	151%	71%	3,566	2,690
South Gippsland Shire	105%	70%	2,134	3,239
South. Grampians Shire Council	100%	80%	1,858	3,070
Strathbogie Shire Council	120%	80%	2,890	3,383
Surf Coast Shire Council	190%	75%	3,290	2,077
Swan Hill Rural City Council	125%	77%	3,849	2,823
Towong Shire Council	95%	90%	716	2,425
Wangaratta Rural City Council	138%	65%	4,266	2,352
Warrnambool City Council	172%	62%	5,172	2,470
Wellington Shire Council	100%	80%	7,699	2,962
West Wimmera Shire	100%	100%	na	na
Wodonga City Council	140%	75%	5,953	3,401
Wyndham City Council	140%	80%	5,535	4,629
Yarriambiack Shire	100%	62%	800	2,730

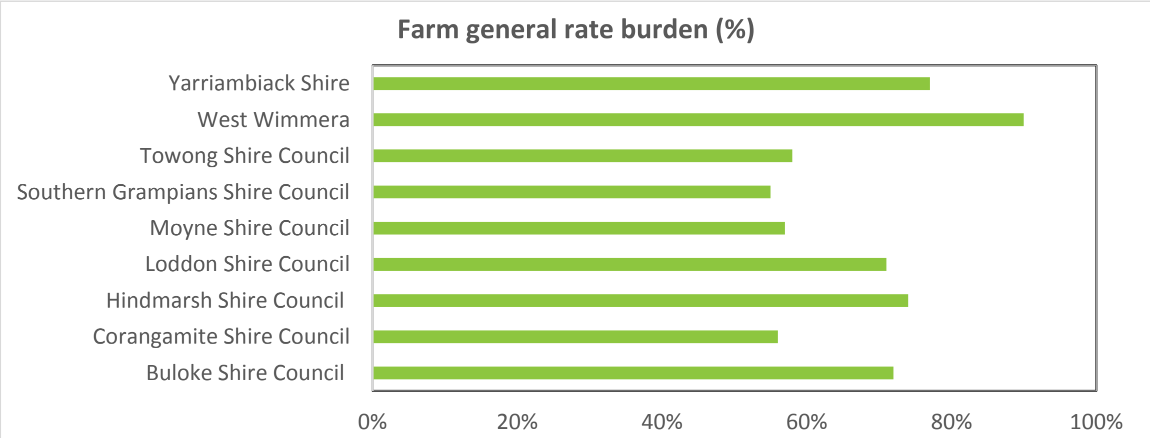
Source: Local Government Draft Budgets 2019-20.

This data uses the number of assessments as opposed to the number of businesses. It must be acknowledged that most individual farm businesses have multiple rate assessments. Therefore, the inequity between commercial and farm rates is significantly greater than what is represented here. However the inequity between farm and other businesses is nevertheless illustrated in the data.

A number of councils such as Ballarat, Bendigo, Mildura and Swan Hill have effectively used differential rates to equitably distribute the rate burden between commercial businesses and farm businesses. Councils that have failed to do this include Glenelg, Hindmarsh, Hume and Moyne.

There is also a high level of dependence on rates from farms in some municipalities, including some of the municipalities with the largest financial sustainability challenges. The following Graph shows those councils where total general rates from farms represents 50% or more of total general rates.

Table 6. Farm general rate burden



Source: Local Government Draft Budget 2019-20.

Differential rates were introduced as a tool for councils to address equity issues arising from the land valuation method of determining rates. The fundamental principle should be that as the value of farmland increases, the differential rate is adjusted to reduce the rate in the dollar so that the rate burden paid by the farm sector remains stable. However, in practice this is rarely the case.

All councils must be required to use differential rates to establish a fair and equitable distribution of the rate burden for each category of land. Once established the rate burden for each category should be maintained for at least four years.

In determining farm rates it is imperative that councils strike the rates on the basis of commercial farm operations being undertaken on the property. Councils are given broad scope in how they may apply differential rates. This has led to inconsistent definitions of land use which leads to non-commercial farm properties enjoying the same rates as those of working farms, or commercial farms not receiving the reduced rate that they should.

For example some councils like Murrindindi and Mitchell Shires strike separate rural rates for properties with an area greater or less than 40ha. Alpine Shire’s farm rates policy requires property to be no less than 8ha in area compared to 2ha in the Mornington Peninsula Shire. Macedon Ranges Shire sets an agricultural land differential for properties in ‘which the owner or occupier is regarded as a Primary Producer by the Australian Taxation Office’.

In setting a mandatory farm rate, the VFF recommends that the farm rate only apply to properties that fall within the definition of 'farm land' under Section 2(1) of the *Valuation of Land Act 1960* which states:

"Farm land" means any rateable land -

(a) that is not less than 2 hectares in area; and

(b) is used primarily for grazing (including agistment), dairying, pig-farming, poultry-farming, fish-farming, tree farming, bee-keeping, viticulture, horticulture, fruit-growing or the growing of crops of any kind or for any combination of those activities; and

(c) that is used by a business

(i) that has a significant and substantial commercial purpose or character; and

(ii) that seeks to make a profit on a continuous or repetitive basis from its activities on the land, and

(iii) that is making a profit from its activities on the land, or that has a reasonable prospect of making a profit from its activities on the land if it continues to operate in the way that it is operating.

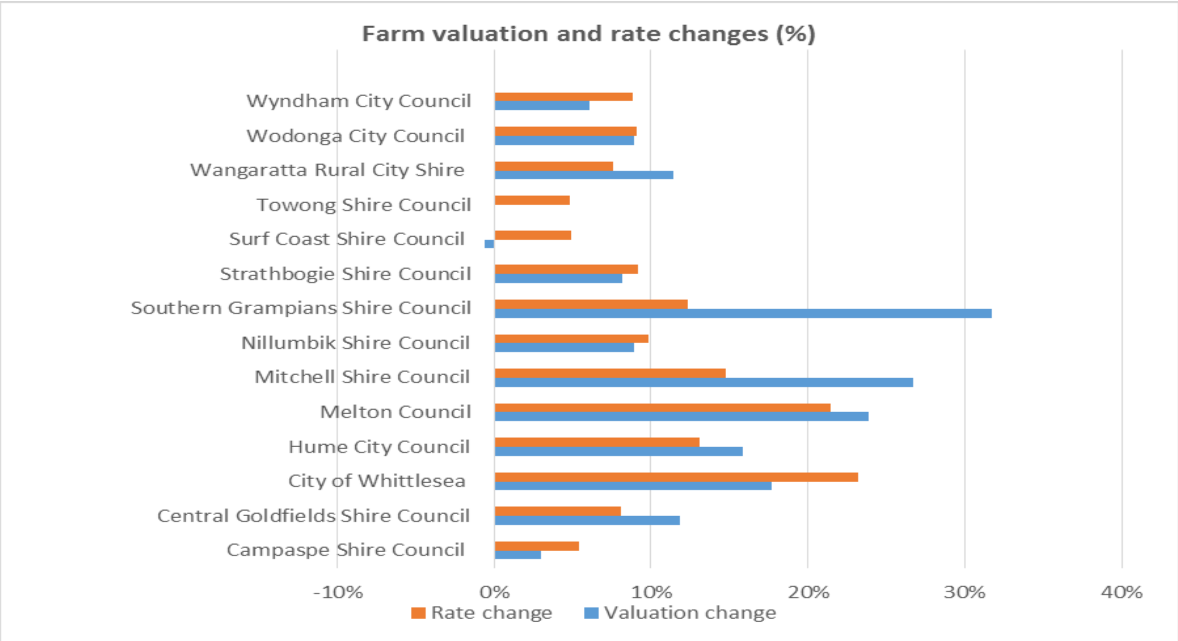
2.4 Valuation averaging

Recommendation:

Valuation averaging be introduced for all councils in Victoria. Under this system, all councils would strike rates based on a moving average valuation calculated for each property over the past 5 years. The actual valuations returned each year by the Valuer-General would remain the same but the valuation basis for the rate strike would be changed.

The key concern of most ratepayers in regard to the current rating system is the large and sudden shifts in the individual rates bills that occur. The following Graph shows the shifts that occurred in average farm valuations from 2018 to 2019 for a range of councils and the subsequent change in average rates compared to the rate cap of 2.5%.

Table 7. Farm valuation and rate changes



Despite each Council's total 'rate take' remaining within the State-mandated 2.5% rate cap, the increases and decreases in valuations were substantially different to this. Valuations changes between 2018 and 2019 ranged from -4% to +32% across the State which translated into rate changes from -19% to 23%. With the much-publicised rate cap in place, public expectations are that their rate bill will only change by a maximum of 2.5%.

For some people, presented with 50% plus rate bill increases, this is confusing and causes significant anger and dissatisfaction. Furthermore, at any reasonable level, where there is no substantive change to the service level, use or value the person gets, such a rate increase is clearly unreasonable.

Such volatility undermines community confidence in a council's key taxation source, being rates and charges. Valuations change continuously by prevailing market and economic conditions and have no relationship to capacity to pay, fairness and levels of council service provided. It is unreasonable for a council to continuously vary the amount it taxes property owners/occupiers by percentages in the order of how valuations can change from year to year. Similarly, to rely solely (arguments regarding flat charges, differentials and rebates aside) on the yearly valuation as the sole driver of the ratepayer contribution to councils' tax base is unreasonable.

Property valuations should continue to be applied but with the 'smoothing' effect of a five year valuation averaging system put in place. There is precedence for this measure with valuation averaging (as an option) already in place in Queensland. This measure would substantially reduce the year-on-year volatility that characterises the current rating system and thereby increase community confidence in it. Changes in the relative valuations of properties (individually, in a class and in a particular area) will still flow through under an averaging system though less suddenly and with less 'rates shock'.

2.5 Separation of house and curtilage from farm land

Recommendation:

The house and curtilage for farmers should be charged a municipal rate similar to that of all other homes in the local government area. Farmland should be separated into a separate assessment which councils having the ability to rate land at the farm differential rate – or exempt the farm land from rates.

The VFF believes the current model for collecting property taxes to fund local government is flawed. An inequitable burden is placed on farm business owners under the current model, which does not adequately consider the capacity of farmers to pay for their rates and greatly contributes to the ongoing concerns about the sustainability in the funding models for local government.

For a farmer, land is the major income producing asset. In the non-farm sector however, land is simply the location of income-producing assets in any given enterprise. The municipal funding system is inequitable in its different treatment of income-producing assets in the farm and non-farm sectors. In the non-farm sector, income producing assets are not subject to an annual ad valorem tax, whereas in the farm sector, the primary income producing asset (i.e. land) is subject to such a tax. This imposes a distortive burden on agriculture. Farm land is a means of production and its value bears little relationship to farmers' wealth or their capacity to pay.

Separating house and curtilage from farmland would create greater equity for farmers and other ratepayers by recognising the distinction between the home and the business. In terms of the benefit principle, the house and curtilage mechanism allows for separate rating based on the services received by the property – that is councils' people orientated services for the home and the limited services received by and for the farm property.

Aside from councils being required to set a separate differential rate for farmland that takes into account the benefit principal and farmers' capacity to pay, councils should also be given the ability to exempt farmland as part of their rating strategies.

It is important to note that the VFF makes this recommendation only on the basis that there be no change to the current system for collecting State Land Tax in which land used for primary production and the principal place of residence is exempt.