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## An Assessment of Pensioner Rebates in New South Wales

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**Abstract:** The problem of cost-shifting from higher tiers of government to local councils in Australia is widely recognized and has been investigated by several official inquiries. However, it has thus far been difficult to gather reliable estimates of the magnitude of the problem. Quite apart from the taxing definitional and data problems associated with the phenomenon, these difficulties have been compounded by the fact that very few attempts have been made to measure the impact of specific instances of cost-shifting in Australian local government, especially the spatial impact of cost-shifting. In an attempt to remedy this neglect, this paper seeks to measure the spatial effects of pensioner concession rebates on local councils in New South Wales.

**Keywords:** Cost-shifting; local government; pensioner concession rebates; spatial effects.

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## Introduction

It is now widely recognized that Australian local government is afflicted by a severe financial crisis perhaps most vividly illustrated by the worsening local infrastructure backlog. While the causes of this crisis are manifold and not fully understood, consensus exists that cost-shifting from state and federal governments to local councils represents an important source of the problem. Cost-shifting occurs where higher tiers of government legally oblige municipal authorities to assume new responsibilities or extend existing functions without fully funding the expenditure involved and where higher levels of government place constraints on the revenue-raising capacities of local councils.

The problem of cost-shifting has been investigated by several official inquiries. For example, the Commonwealth House of Representatives Standing Committee on Economics, Finance and Public Administration Report ['Hawker Report'] (2003), entitled *Rates and Taxes: A Fair Share for Responsible Local Government*, examined cost-shifting from a national perspective and made various recommendations to alleviate the problem. The Hawker Report (2003, 25) found that 'the majority of cost shifting was from state to local government, but there was also evidence of cost shifting by the federal government'. However, it observed that 'assessment of the true extent of cost shifting from other spheres of government to local government is extremely complex' and since 'there is no clear definition of cost shifting', it was impossible to provide an accurate calculation of its extent in Australia (p.26).

In addition to the Hawker Report, two state-based local government inquiries have also included cost-shifting as an integral part of their efforts. For instance, the South Australian Financial Sustainability Review Board's (2005, 13) *Rising to the Challenge* Report concluded that compliance costs imposed by the government in that state 'are substantial and growing'. However, 'while there is some evidence of true cost shifting, not all that is claimed to be cost shifting by some within local government qualifies as such'. In a similar vein, the Independent Inquiry into the Financial Sustainability of NSW Local

Government (2006, 13) produced a comprehensive Final Report entitled *Are Councils Sustainable?* On the basis of research that it had commissioned, the Independent Inquiry (2006, 11) found that ‘the total burden of “cost shifting” may be costing NSW local government about \$340 million per annum’ [emphasis added]. Both the ongoing Queensland Local Government Association (LGAQ) (2006) *Size, Shape and Sustainability* (SSS) project and the current Western Australian Local Government Association (WALGA) (2006) *Systemic Sustainability Study: In Your Hands - Shaping the Future of Local Government in Western Australia* Inquiry seem likely to reach analogous conclusions for their respective state systems.

There is thus clear evidence that cost-shifting represents a significant source of the financial predicament confronting Australian local government. However, it seems equally clear that the magnitude of cost-shifting is uncertain and the difficulties involved in estimating the impact of cost-shifting in monetary terms are formidable.

One way of approaching the problem is to focus on specific and incontrovertible examples of cost-shifting that are amenable to measurement and are not beset by definitional problems and a blurring of responsibility between the different levels of government. Moreover, this approach would consider a specific dimension of the impact of a given instance of cost-shifting rather than its aggregate impact. A case in question is the spatial impact of the provision of pensioner rate concessions by local authorities in NSW under the *Local Government Act 1993*. In terms of this legislation, a person meeting the definition of an eligible pensioner can claim various rebates on the rateable charges levied on their principal place of abode. These rebates are constant across New South Wales local government jurisdictions, regardless of the differential abilities to pay of both beneficiaries and local councils. The present paper attempts to provide a tangible estimate of the uneven spatial impact of this form of cost-shifting on different councils with different fiscal capacities and different demographic characteristics.

The paper itself is divided into four main parts. Section 2 considers the main types of cost-shifting in Australian local government, provides a working definition of cost-shifting and locates pensioner rate concessions within this conceptual framework. Section 3 examines the spatial impact of the pensioner rate concession on different councils across New South Wales. Section 4 outlines various caveats that should be taken into account in assessing the perspicacity of the estimates of the spatial effects of the concession on different councils, thereby emphasising the difficulties involved in the analysis of the impact of cost-shifting, even at a well-defined, unambiguous micro-level. The paper ends with some brief comments on the policy implications of the analysis in the concluding section 5.

## **Cost-Shifting and NSW Pensioner Rate Concessions**

In *Australian Local Government Economics*, Dollery *et al.* (2006, 238-9) contend that cost-shifting in the Australian municipal milieu has four broad components:

- **Grant Funding** – Local government grants have been reduced in real terms and ‘this is compounded by the fact that grants have failed to keep pace with changing responsibilities’.
- **Service Gaps** – Local government has had to fill ‘the gap left by state and federal governments either withdrawing services or their failure to implement/provide services required by the community’. Moreover, ‘local government has been required to “pick-up” services as a result of the direct transfer of “ownership” of infrastructure from another sphere of government’.
- **Agency Fees** - Fees imposed by higher levels of government have increased as ‘state and Commonwealth agencies have sought to recover a range of costs by increasing fees, licence contributions and other charges imposed on councils’.
- **Legislative Requirements** – Australian local councils have faced ‘major increases in accountability and compliance requirements without adequate recognition of the attending costs’. Furthermore, ‘legislation

has required councils to provide concessions and rebates, with no compensation payment'; 'services have formally referred to, and/or have been assigned to local government through legislative and other state and/or federal instruments, without corresponding funding'; local councils have been required to be 'the sole provider of essential/important local services'; new services that 'have no historical funding precedent have been mandated'; and fees and charges that 'local government is permitted to apply, for services prescribed under state legislation or regulation, are have little if any correlation to the cost of proving the service'.

The legal authority for the mandate for compulsory rate concessions in New South Wales can be found in the *Local Government Act 1993* (as amended), together with its associated regulations. The Act requires councils to reduce the rates payable by eligible pensioners, who occupy the dwelling for which a concession is sought as their sole or principal place of living.

Under section 575 (3) of the *Local Government Act 1993*, eligible pensioners are able to claim the following mandatory annual concessions on their rates and these amounts have remained unchanged since 1989:

- 50% of the total ordinary rates and charges for domestic waste management services payable up to a maximum of \$250;
- 50% on water rates payable up to a maximum of \$87.50; and
- 50% on sewerage rates or charges payable up to a maximum of \$87.50.

An eligible pensioner, as defined in section 18 of the *Local Government (Rates and Charges) Regulation 1999*, embraces the following categories of person:

- A person who receives a pension, benefit or allowance under Chapter 2 of the Social Security Act 1991 of the Commonwealth Government and who holds a pensioner concession card issued by or on behalf of the Commonwealth Government;

- A person who receives a service pension under Part III of the Veterans' Entitlements Act 1986 of the Commonwealth and holds a pensioner concession card issued by or on behalf of the Commonwealth Government;
- A person who receives a pension from the Commonwealth Department of Veterans' Affairs as the widow or widower of a member of the Australian Defence or Peacekeeping Forces, or the unmarried or widowed mother of a deceased unmarried member of either of those Forces (people in both of these categories are eligible only if they would also be eligible for a pensioner concession card from Centrelink).
- A person who receives a general rate of pension adjusted for extreme disablement under section 22(4) of the Veterans' Entitlements Act 1986 of the Commonwealth, or a special rate of pension under section 24 of that Act.

The process of implementing the legislative requirements for pensioner concessions involves eligible pensioners being required to complete an application form (designed by the New South Wales Department of Local Government), and to provide proof of their eligibility in the form of their Commonwealth-issued pensioner or veteran's card. Councils annually seek confirmation of the eligibility of all pensioners from the federal government agency Centrelink. Centrelink is the primary organisation that holds all the required details of those individuals who are 'eligible' pensioners. On the basis of this information, local authorities raise their rate notices with the amount levied, less the amount of the pensioner concession. The municipal authority must then submit an independently audited return to the New South Wales Department of Local Government in order to be reimbursed for the state's 55% share of the rebate. The balance of the rebate (i.e. 45%) must be financed by the council out of its general revenue.

In the present context, we define an unfunded mandate as a non-optional requirement on local councils dictated by a higher level of government to do something (or refrain from doing something) that the local authority would

ordinarily choose not to do (or would ordinarily do), which is not accompanied by sufficient funds to cover the cost of implementing or meeting the requirement. The provision of pensioner rate concessions by local authorities meets this definition of an unfunded mandate since it is mandatory (i.e. non-optional) for councils to provide the rebate under the *Local Government Act 1993* (i.e. state government legislation) and sufficient (i.e. 100%) funding is not provided to cover the cost of the requirement (i.e. the rebate). In addition, the pensioner rate concession falls under the 'legislative requirements' class of cost-shifting identified by Dollery *et al.* (2006).

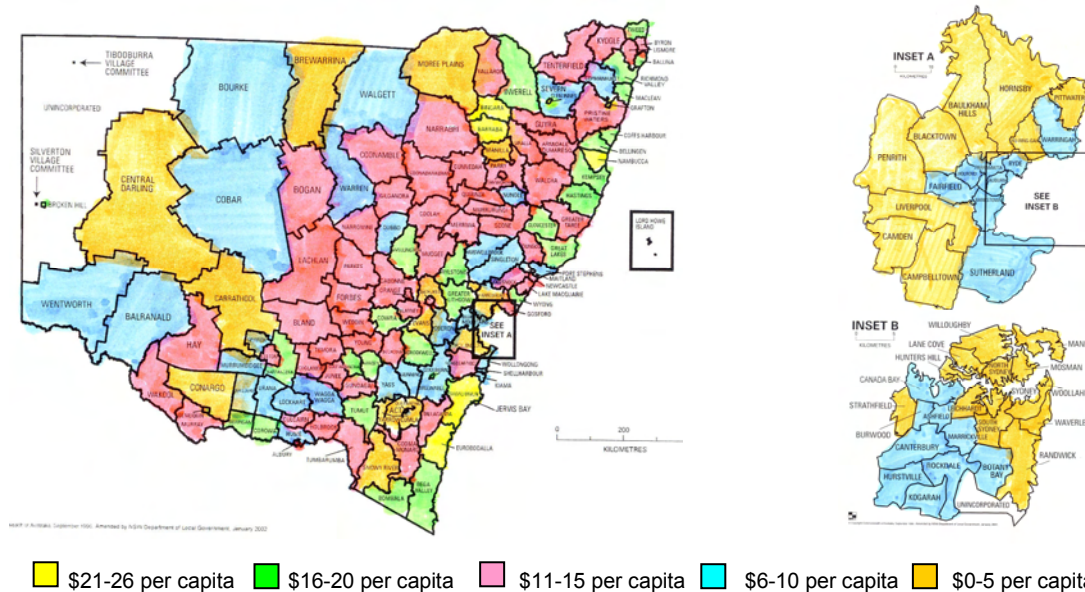
## **Spatial Variation in the Impact of the Concession**

By their very nature, pensioner rate concessions represent a redistribution function of government. In essence, they are designed to redistribute state income away from the median beneficiaries of state and local government expenditure to defined categories of pensioners due to their perceived relatively low levels of income. Redistributive arrangements along these lines are open to various criticisms on both efficiency and equity grounds (see, for instance, Bailey 1999; Dollery *et al.* 2006).

However, given the major focus of this paper on the spatial impact of pensioner rate concessions on different local government jurisdictions across New South Wales, the major objection to the provision of pensioner rate rebates to eligible pensioners primarily relates to the decreasing and uneven capacity of municipal authorities to fund the concessions. It can be demonstrated that the fiscal burden resulting from the payment of pensioner rebates falls unevenly among different localities. Figure 1 indicates the net amount of the rate rebate per capita (after deducting the state government's 55% contribution) for each council and shows that the higher levels of pensioner rebates are concentrated in coastal areas and in a number of rural inland areas and that much lower levels per capita are experienced in the affluent inner-city metropolitan areas. For instance, Glen Innes Municipal Council recorded the highest net pensioner rebate per capita at \$25.76,



closely followed by Bingara (\$24.63), Barraba (\$23.30), Eurobodalla (\$22.75), and Shoalhaven (\$21.79). At the other end of the spectrum, Conargo recorded the lowest net pensioner rebate per capita at \$0.60 closely followed by Sydney City (\$1.47), Woollahra (\$2.52), North Sydney (\$2.58) and South Sydney (\$2.65).



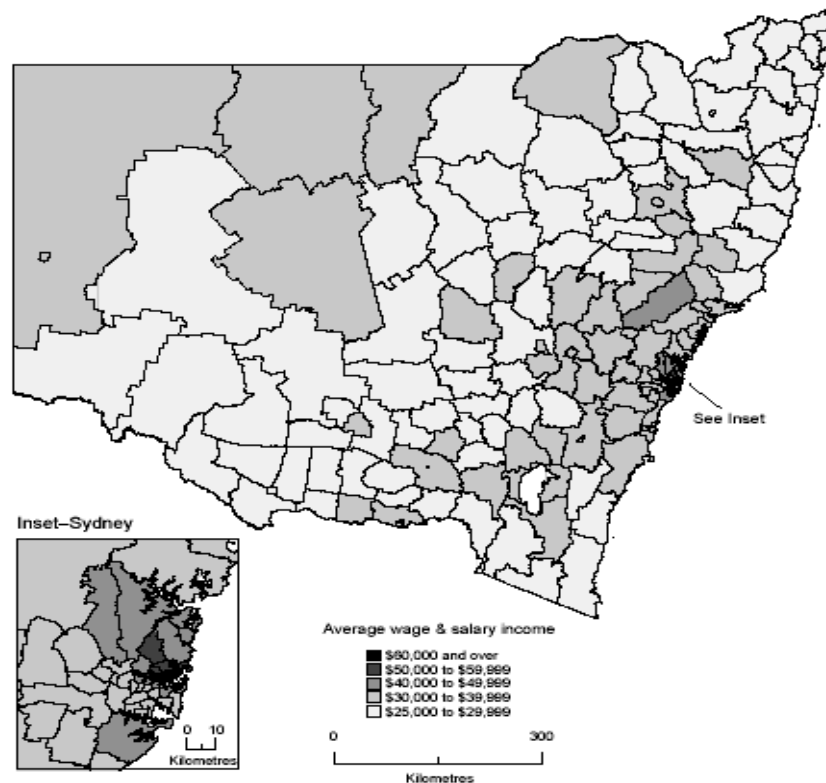
**Figure 1: Pensioner rate rebate per capita**

Source: Adapted from ABS 2003; NSW DLG 2004; NSW LGGC 2005; and NSW DLG 2005.

Given the spatial differentiation by council jurisdiction in the burden of providing the pensioner rate concessions, a review of the capacity of these communities to fund the concession is required. Figure 2 provides a pictorial representation of average wage and salary income across New South Wales by local government area.

Figure 2 indicates that the lowest wage and salary income jurisdiction occurs in Bingara at an average of \$25,317, followed by Wentworth (\$25,828), Wakool (\$25,479), Wedin (\$26,325) and Barraba (\$26,351). On the other hand, Canada Bay recorded the highest average wage and salary income in the state at \$89,351, followed by Mosman (\$77,943), Woollahra (\$63,513), North Sydney (\$60,503) and Ku-ring-gai (\$59,241).





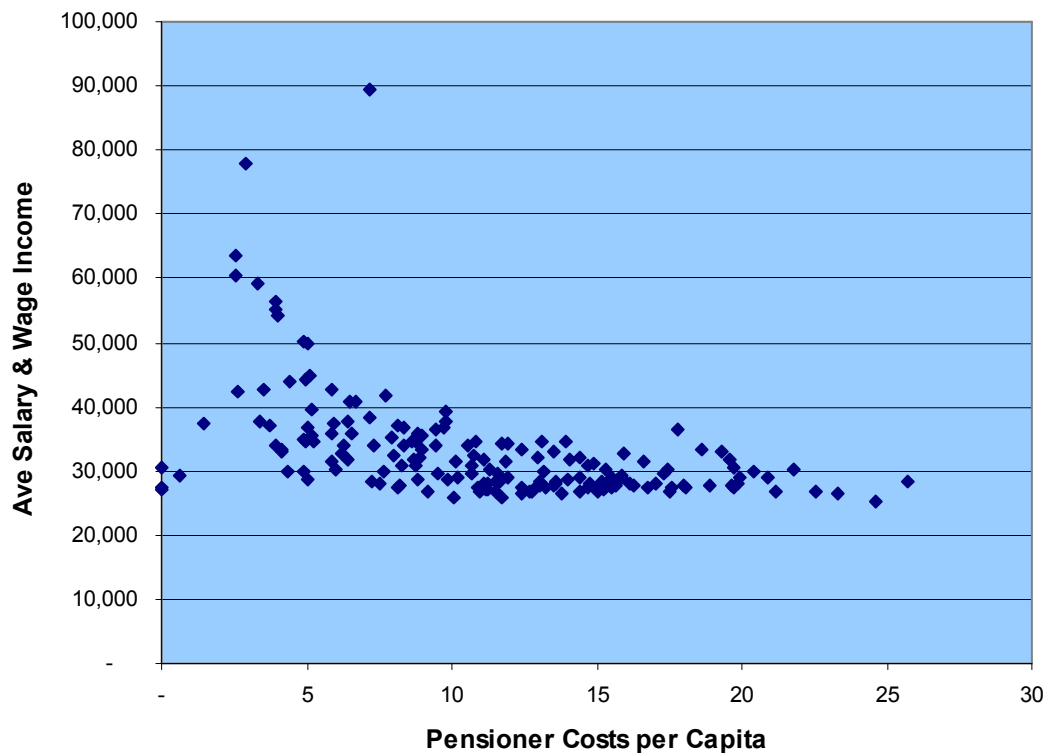
**Figure 2: Average wage and salary income in N.S.W. in 2000-01**

Source: ABS 2003, 4.

What is arresting from these observations is that there are a number of councils that appear to have both the lowest average wage and salary income and the greatest amount of net pensioner rebate expenditure per capita (i.e. Bingara and Barraba). Conversely, two councils have the highest average wage and salary income and the lowest magnitude of net pensioner rebates provided per capita (Woollahra and North Sydney).

Given the spatially unequal distribution of eligible pensioners between localities and the varying capacity of individual authorities to finance the rebate, it would appear that the central government is in the best position to fund the costs of these welfare payments, since councils with the most pensioners are also likely to have the lowest capacity to pay – a point explored further at the end of the paper. In order to clarify the relationship between income (i.e. ability to pay) and the provision of the rate rebate (i.e. magnitude of the cost-shift), both factors are plotted in Figure 3. Figure 3

indicates that there appears to be a strong inverse relationship between average wage and salary income and the net cost of pensioner rate concessions provide by municipal authorities in New South Wales.



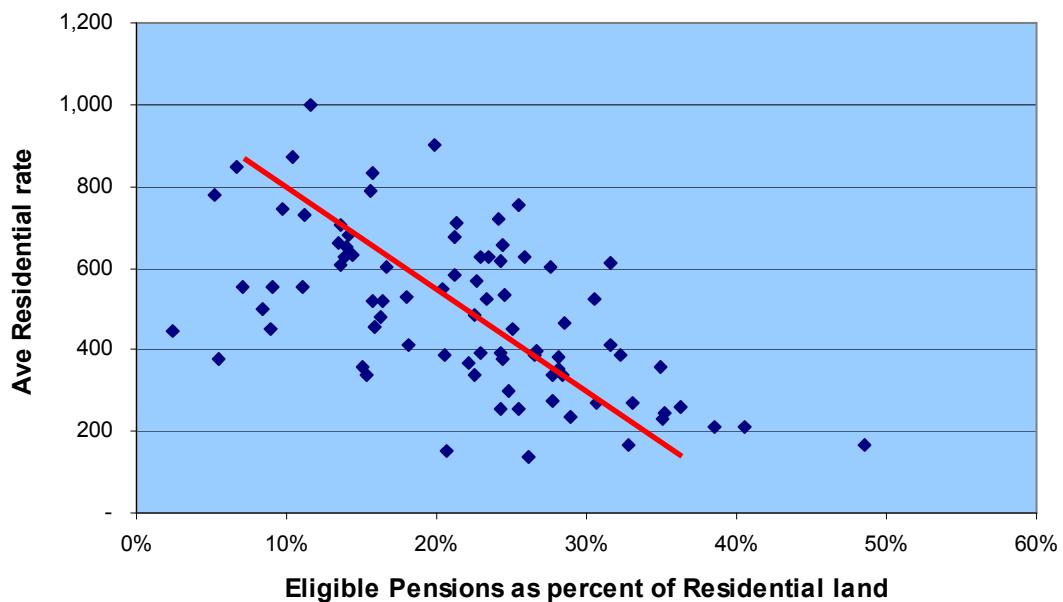
**Figure 3: Comparison between average wage and salary income and the net amount of pensioner rebates provided per council**

*Source:* Adapted from ABS 2003; NSW DLG 2004; NSW LGGC 2005; and NSW DLG 2005.

Figure 3 would thus allow us to form the preliminary conclusion that those municipal authorities with the greatest number of eligible pensioners, and thus those that have the greatest cost of providing pensioner rate concessions, also have residents with the lowest income and therefore the least ability to pay for the rebate.

Before reaching this conclusion, it is worth comparing the average rates paid by urban residents with the percentage of eligible pensioners owning residential land. This will provide an indication of a municipal authority's ability to generate 'own source' taxation income to fund the cost of providing the

pensioner rate concessions. Figure 4 shows that there is a negative relationship between the percentage of eligible pensioners as a proportion of total residential landowners and the average residential rates paid in each council. The 'line of best fit' clearly indicates that the lower the numbers of eligible pensioners who own residential land, the higher are the rates payable on this land. This would appear to indicate that those municipal authorities with a high number of pensioners may be constrained with their ability raise their own taxation to cover the costs of providing local government services than those councils who have a lower level of eligible pensioners residing within their boundaries.

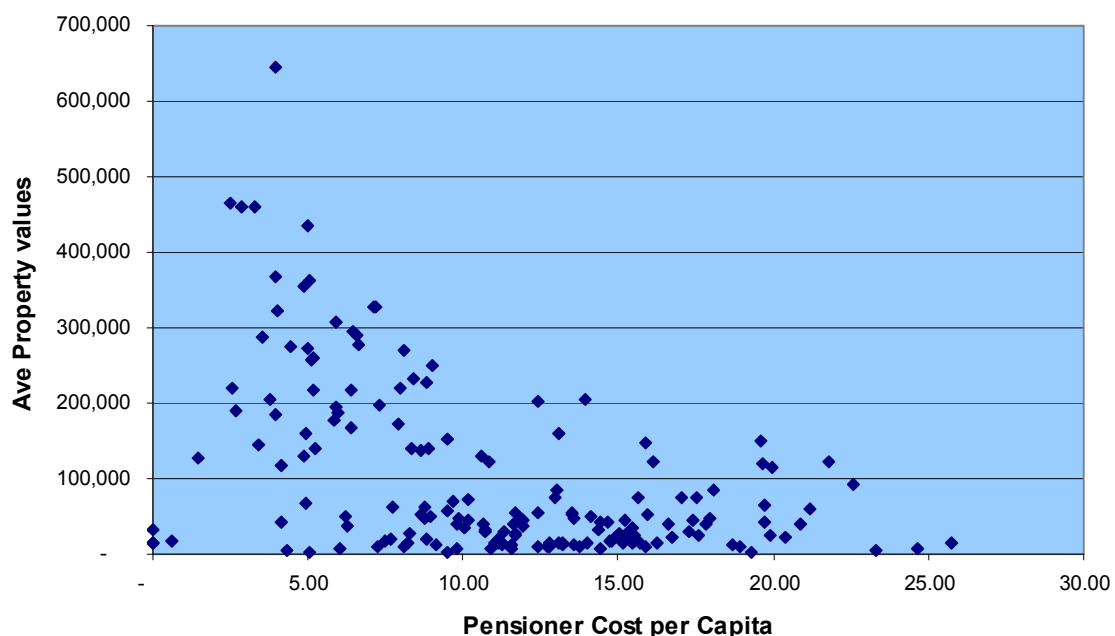


**Figure 4: Comparison of average residential rates and the percentage of eligible pensioners per council**

*Source:* Adapted using data in ABS 2003; NSW DLG 2004; NSW LGGC 2005; and NSW DLG 2005.

A final question that must be asked is whether councils are being 'over-generous' in underrating their older constituents on grounds of equity considerations rather than on their ability to pay. In other words, are these eligible pensioners 'income poor' but simultaneously 'asset rich'?

Figure 5 investigates this possibility by comparing the net cost per capita of providing pensioner rate rebates with the average value of residential land in each municipality. Figure 5 indicates that, in general, those councils with the higher costs per capita of providing pensioner rebates also have the lowest average residential property values. It can thus be concluded that not only do those municipalities that are providing the highest pensioner rate concessions per capita have the lowest average income, but their residents also consequently pay the lowest rates and their properties are generally valued at lower levels.



**Figure 5: Comparison of average residential property values and the percentage of eligible pensioners per council**

*Source:* Adapted using data in ABS 2003; NSW DLG 2004; NSW LGGC 2005; and NSW DLG 2005.

In addition to the New South Wales state government's 55% contribution to the cost of providing pensioner rate rebates, the New South Wales Local Government Grants Commission also considers the relative differential in the rebate when determining their annual allocation of the Financial Assistance Grant. The Commission aims to reduce the uneven impact of providing pensioner concessions across the state by incorporating this in the allocation

of the grants to each council. Table 1 displays the formula used by the Commission to determine how much each council should receive as a pensioner rebate allowance.

**Table 1: Calculation of the Pensioner Rebate Allowance**

<p><b>Pensioner Rebate Allowance = <math>R_c \times N_c \times (P_c - P_s)</math></b></p> <p>Where:  <math>R_c</math> = the standard rebate per property for the council  <math>N_c</math> = the number of residential properties  <math>P_c</math> = the proportion of eligible pensioner assessments for the council  <math>P_s</math> = the proportion of eligible pensioner assessments for ALL councils</p> <p>The standardised rebate for the council (<math>R_c</math>) is:  <math>R_c = 0.25 \times T_c \times t_s</math></p> <p>Where:  <math>T_c</math> = the average value per residential property in the council  <math>t_s</math> = the standard tax rate (rate-in-the-dollar) for residential property  The maximum value for <math>R_c</math> is set at \$125</p>
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Source: NOLG 2003, 94.

It should be stressed that the notional pensioner rebate allowance, as assessed by the Local Government Grants Commission, is allocated on a relative basis. Put differently, it is provided to those municipal authorities that have relatively more pensioners than the average and does not consider the aging of the population and the absolute increase in the number of eligible pensioners in general. It should also be noted that the notional pensioner rebate allowance (shown in Appendix 1) is calculated in accordance with the formula outlined in Table 1. However, the actual rebate provided to individual councils is discounted by a factor in excess of 50% as a result of the actual financial assistance grants available for distribution to councils usually being around 50% of what the New South Wales Local Government Grants Commission assesses as being required to achieve horizontal equity among local authorities.

It should be recognised that the cost of the concession is inequitably spatially distributed. Those who qualify for rebates are disproportionately represented in low income areas - areas that already have a high demand for council services, but a limited revenue raising capacity. Given the restricted revenue

base of local government, it thus seems unreasonable that it should be required to fund this form of pensioner assistance.

Lurking in the background of this analysis are two related issues: A general ageing of the Australian population and the shift of the population to coastal areas. In the first place, we must consider the characteristics of residents forming the intra-migratory wave from inland towns and farms and the various capital cities to regional coastal centre.

According to the Gurran *et al.* (2006, 1), 'many non metropolitan coastal communities are characterized by high levels of unemployment, lower than average household incomes and greater levels of socio-economic disadvantage, along with higher numbers of seniors than other parts of Australia', despite the fact that the majority of recent so-called 'sea-changers' are younger than 50 years of age.

Gurran *et al.* (2006) also found that the strongest motivation for lower income groups was 'housing affordability' and that coastal areas are over-represented in terms of low-income households (around 3.4% higher on average). Although we are unable to determine what proportion of these persons are pensioners, it would seem reasonable to assume that they would be well represented in the low-income group. The Gurran *et al.* (2006) findings are confirmed by Murphy (2006, 31) who argued that 'coastal growth now runs the risk of "killing the goose that laid the golden egg"', as sea-changers tire of the potent mix of increased house prices, over-development and 'large number of income-support recipients and other low-income earners settling on the coast'. In fact, Murphy contends that these factors may drive growth to the so-called 'tree-change' areas inland. Although it remains speculation at this stage, it is nonetheless conceivable that inland towns may also become target settlement areas as for low-income groups, thereby spatially diversifying the problem of pensioner rebates.

When viewed in the context of our work on per capita pension rebate expenses, it would thus seem that some coastal local authorities are accruing a burden of pensioner rebates due to the relatively recent growth in coastal populations because of the characteristics of the group migrating to these areas. Rather than attracting relatively wealthy residents, it seems that the sea-change phenomenon consists largely of migrants of below-average household wealth, who may well be eligible for pensioner concessions on various municipal rates and charges, including pensioner concessions.

Taking a longer term view, it would appear that the problem is likely to worsen rather than ease. The 'Baby Boom' generation is yet to reach retirement age. However, this process will begin over the next few years. In this regard, Gurran *et al.* (2006, 2) suggest that many of this demographic category intend to relocate to the coast in their retirement. While not all will receive a public pension, and thus be eligible for council pensioner rebates, a sizeable proportion will nevertheless meet the criteria for eligibility, and this is likely to place further strain on the finances of those councils in coastal areas. Further compounding this problem, the now universally acknowledged infrastructure crisis in local government is exacerbated in coastal locations, where the population is growing and the present infrastructure is straining under this demographic pressure. Councils are thus likely to be 'squeezed' both on the revenue and expenditure fronts.

### **Some Caveats to the Empirical Analysis**

Most data employed in this analysis were obtained from the Local Government Grants Commission. It must be stressed that the Commission advised caution on the use of this data and observed that 'the material contained in this data file is based upon information provided to the New South Wales Department of Local Government or the New South Wales Local Government Grants Commission by councils and drawn from a variety of sources' and 'while every effort has been made to ensure the accuracy of the information in this data file, the Department and the Grants Commission



expressly disclaims any liability to any person in respect of anything done or not done as a result of the contents of the data provided' (LGGC 2005, 2).

According to the Department of Local Government (NSW DLG 2005, 28), some factors affecting the use of average rate per assessment include the level of reliance on other revenue sources; rate-pegging legislation limiting overall revenue; rating mix relativities between rating categories; the mix of residential, farmland and business properties; revaluation of a council area; the mix of rates and charges; any special variations granted; the level of services provided in an area; the council's rating structure and policy; and the amount of abandonment for pensioner rebates and other 'write-offs'.

The pensioner rebate grants are based on actual amounts paid by the New South Wales Department of Local Government during 2003/04. This is reliant on the individual councils submitting a claim form to the Department for reimbursement of 55% of the amount abandoned. Inaccuracies can occur with the data if a claim is not submitted to the Department (thereby under-estimating the amount of pensioner grant provided in any one year), or if a claim could relate to a previous year (thus over-estimating the amount of grant received in the current year).

The estimates for wage and salary earners have been compiled by the Australian Taxation Office (ATO) from their Individual Income Tax Return Database for the Australian Bureau of Statistics. Therefore the information is based on the designation of residents and self-assessed income of individuals. It should also be noted that, while wage and salary income represents a majority of household income, other sources of income, such as business income, superannuation, investments and government pensions, benefits or allowances, are not included. Since the Australian Taxation Office's income tax return is designed to obtain an individuals total income from various sources over a financial year, and not the employment status of a person at a particular point in time, wage and salary earners have been defined as 'persons aged 15 years and over who have submitted an individual

income tax return and for whom wage and salary income was the principal (or main) source of income for the financial year'. Wage and salary income, as reported on the income tax return, includes gross income as shown on the 'PAYG payment summary - individual non-business' as well as allowances, commissions, bonuses, tips, gratuities, consultation fees, honoraria and other payments for services. Allowances and other earnings may include car, travel or transport allowances, allowances for tools, clothing or laundry and dirt, risk, meal or entertainment allowances. The data to define and compile counts of wage and salary earners have been sourced from questions 1 and 2 on the individual income tax return (ABS 2003).

## Concluding Remarks

The debate on cost-shifting in Australian local government has been devilled not only by the difficulties in identifying cost-shifting, but also by problems in measuring cost-shifting. One method of overcoming these impediments resides in adopting a micro-level approach to the problem and selecting specific and unambiguous cases of cost-shifting and then computing the relative impact of cost-shifting on different types of local councils. This paper has followed this *modus operandi* by examining the differential spatial impact of pensioner rate concessions on local councils in New South Wales. We have established that substantial differences exist between different categories of local government. In general, the burden of this form of redistribution falls most acutely on municipal jurisdictions with the lowest ability to meet this impost in terms of both average earnings and rateable capacity. Moreover, although the New South Wales Local Government Grants Commission does take into account the financial circumstances of individual councils in its grant calculations, severe constraints on the magnitude of actual grants paid to councils means that grant compensation for rate concessions falls far short of their real cost.

In this paper we have been concerned with the spatially uneven impact of the pensioner rate concession on different councils across New South Wales, and

thus will not dwell on generic efficiency and equity criticisms of these concessions that exist in the literature on fiscal federalism (see, for instance, Bailey 1999; Dollery *et al.* 2006). However, suffice it to note in conclusion that, for designated recipients of pensioner rebates who are not in fact able pay their full rates bill, other possibilities apart from the present New South Wales council-administered and part-funded pensioner rate concession exist.

Two specific alternatives seem feasible. Firstly, the standard theory of fiscal federalism prescribes that macro-economic measures, including person-specific equity objectives involved in income redistribution, should be carried out by the central government and not the lower tiers of government (Oates 1972). This prescription is already embodied in most Australian income redistribution programs, like unemployment benefits and the age pension. Accordingly, the Commonwealth government should assume responsibility for pensioner rate concession programs, and not the present combination of state and local government, evident in all Australian state and territory jurisdictions.

A second alternative approach derives from the presumption that pensioner rate concessions are regressive. Following this assumption, it can be argued that the eligible categories of pensioner in New South Wales should fund their own rate concessions through the capital gain they may reap on the sale of their home. Put differently, they could deduct the amount of the rate concession they received during the ownership of their residence from the capital gain accrued on the disposal of their residence, either upon their death or on their transfer to another location. This is generally referred to as a 'reverse mortgage'. Under this funding arrangement, the pensioner would be lent money on the argument that while they may be 'income poor', they may simultaneously be 'asset rich'.

Indeed, the intergenerational equity of the present New South Wales pensioner rebate system can be questioned since a pensioner can receive rate rebates on a property subsequently sold with a capital gain which enables the pensioner (or their beneficiaries) to benefit at the expense of ratepayers

generally. It can thus be argued that there should be no pensioner rate rebates, or at least that they should be limited, and that pensioners or persons experiencing genuine hardship in paying rates should be specifically able to defer part or all of their rates until the ratepayer ceases to occupy the property, upon transfer or death, at which time these rates would fall due.

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