RATING METHODOLOGY REVIEW

June 2022

CITY OF ADELAIDE

ACKNOWLEDGEMENT OF COUNTRY

The City of Adelaide acknowledges that we are located on the traditional Country of the Kaurna people of the Adelaide Plains and pays respect to Elders past, present and emerging.

We recognise and respect their cultural heritage, beliefs and relationship with the land. We also extend that respect to visitors of other Aboriginal Language Groups and other First Nations.

DOCUMENT PROPERTIES

Contact for enquiries and proposed changes

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BACKGROUND

At its meeting on 5 February 2022, the Audit and Risk Committee (ARC) resolved that Council reassess the valuation methodology report from 2017 to include reviewing all options available in relation to valuations for the purposes of future rate determinations.

The context behind the decision of ARC was a discussion regarding the understanding of why Annual Assessed Value (AAV) is the chose methodology for rating at City of Adelaide, different from all other South Australian councils. Further to understand the operations available in terms of rating methodology under legislation for Council to ensure the most appropriate rating methodology is applied.

2017 REVIEW

The report referred to by the ARC resolution was prepared by John Comrie and presented to Council in 2017. The report was a Review of Rating and Revenue. In summary the report provided the following findings with regards to rates:

- There is no single rating system that best suits or is preferred by all ratepayers.
- Rating system is a choice of Council that should consider relevant public finance criteria of each rating option to ensure the decision is objective and able to be defended.
- Rating systems are a form of tax that must consider equity of benefits received by and capacity to pay of different classes of ratepayers
- Two other options available outside of AAV being Capital Value and Site Value. Capital Value and AAV are both a better indicator of capacity to pay compared to site value.
- CoA does not levy a minimum rate or fixed charge, unlike all other SA Councils

The findings and elements of the report that were assessing revenues outside of rates have not been reviewed as a purpose of this report.

RATING CONSIDERATIONS

There are various elements to consider when looking at rating which are defined as:
Rate Revenue Level - Council must determine how much rate revenue to raise.
Rate Revenue mix - The LG Act requires councils to have regard to equity in determining their basis of rating. Equity considerations need to have regard to both benefits received and capacity to pay.
Rate Valuation base – Council must determine whether to base rating on the site, annual or capital value of properties.
Rate Charges – Council can determine to apply a fixed or minimum rate but can't apply both and don't have to apply either.
Differential Rates – Council can choose to apply rates based on different land uses and/or localities. Typically, a higher rate is set for non-residential rate payers based on the capacity to pay.
Separate Rates & Service Charges – Council can set rates based on specified services provided. Commonly used for Water Management schemes, Areas of higher service provision e.g. Rundle Mall Levy.

RATES REVENUE LEVEL

Council is free to determine what level of rate revenue they raise annually.

Unlike eastern states, there is no cap applied in South Australia under current legislation. Though it is important to note the introduction of the Rates Oversight Scheme introduced as a part of the recent LG reform which will ensure that rate revenues are being raised appropriately.

In the 2017 review, Mr Comrie noted that "*It is in the best long-term interests of both a council's ratepayers and the council itself that the council exercise its rating powers responsibly, strategically and accountably*". Administrative simplicity and economic efficiency are key considerations to ensure rate revenue levels are raised appropriately.

There is a clear desire from Council, through the last nine years of rating decisions, that the rate revenue level is kept to a level that will ensure rates are not a core source of income and the dependency on increasing rate revenues to fund new services is reduced with the expansion of other revenue streams.

The Council resolution on 15 December 2020 seeks to ensure that rate revenue levels grow in the future as a result of growth through new developments only, rather than seeking higher rates from existing rate payers.

RATES REVENUE MIX

The 2017 review noted the intent of Council to raise approximately 20% of its rates revenue from the residential sector and the 80% balance from non-residential properties.

This intent is typically derived from the 'capacity to pay' element of the taxation system. The value of a property used for the purposes of rating represents the capacity to pay of each ratepayer. Whereby higher values suggest greater capacity and as such rates are levied in the same weighting.

City of Adelaide current valuation mix is 71% Non-Residential vs 29% Residential which has moved slightly from the 80/20 basis from some years ago.

As a result, movement in the rates revenue mix would expect to move with the movement in valuations.

In 2016/17 the rates revenue mix was 20.6% Residential vs 79.4% Non-residential which is clearly aligned to the 80/20 valuation mix. Table 1 below was included in the review with 2017 figures and has been updated for the purpose of this report. Table 1 shows how the mix is now moved to be 24.9% Residential vs 75.1% Non-residential, not quite aligned with the 71/29 valuation mix.

Impacting this is the Council decision to retain the rate in the dollar over the last nine consecutive years. The changes in valuations over that time have driven the amount of revenue derived from residential to non-residential to be slightly skewed from the desirable 71/29 mix. As Council continues to set rates based on RID instead of rate revenue, this mix will continue to skew away from the intent to align valuation mix to rate revenue mix.

Table 1: CoA Assessments, Rates Revenue and Average Rates by Property Class 2022

Differentiating Factor	No. of Rateable Assessments	% of Rateable Assessments	Rates Revenue ($000's)	% of Rates Revenue	Average Rates / Property
Residential	16,722	62.3%	$29,443	24.9%	$1,761
Commercial	9,732	36.2%	$73,860	72.5%	$7,589
Industrial	110	0.5%	$484	0.4%	$4,400
Vacant Land	44	0.2%	$260	0.2%	$5,909
Other	254	0.8%	$2,356	2.0%	$9,276
Total	**26,862**	**100%**	**$118,423**	**100%**	**$4,409**

RATES VALUATION BASE

Council must determine the basis for valuation utilised for rating. The legislation provides for three alternatives summarised by the 2017 report as follows:

Site Value:

- More economically efficient than capital value as a rating base, no need for assessment of capital built as it doesn't recognise structural improvements.
- Are not generally as good an indicator of capacity to pay as capital values
- Relative rates can become disproportionate which would increase the rates burden to certain property types.

Capital Value:

- Recognises the value of land including structural improvements
- reasonable indicator of relative capacity to pay between different ratepayers
- Utilised by many agencies

Annual Assessed Value:

- Typically reasonably correlated with capital values (and as a guide are generally about 5% of capital values)
- reasonable indicator of relative capacity to pay between different ratepayers.
- work well in localities where strong rental markets for different types of properties exist
- often cause confusion though for ratepayers and are therefore not administratively simple
- Not popular in circumstances where the majority of properties are occupied by their owners

The 2017 review resolved that *"There is no compelling justification for CoA to switch valuation bases"* and formalised the recommendation that CoA continue to set rates based on each property's assessed annual value.

RATES CHARGES

Council can apply a fixed or minimum rate to each ratepayer as a mechanism to achieve equity from a benefit principle perspective. That is, each ratepayer receives benefits from Council and a fixed or minimum rate ensures that each ratepayer contributes a set amount regardless of the value of their property.

This service charge is then usually complemented with a variable rate in the dollar that then recognises the value of the property applied to whatever valuation base is chosen.

The 2017 review noted that because a council uses capital value or assessed annual value it has already determined that capacity to pay and as such a minimum rate would not be justifiable. This is based on the fact that minimum rates set a value threshold "*for which the minimum applies have the amount they pay determined purely based on their property value. Arguably this may mean that too much emphasis is being given to 'capacity to pay' relative to 'benefits received' considerations. At least equally importantly it means owners of the lowest valued properties, i.e. those to which the minimum applies, are effectively paying a higher ad valorem rate."*

By contrast a fixed rate, would support Councils capacity to pay and benefit principle and Mr Comrie's recommendation was for *"CoA remain open to considering the introduction of a modest fixed charge in future but on the basis of available evidence not do so at this time."* For the purposes of this report, the fixed rate modelling has not been reviewed again, however the analysis included in section 6 of the 2017 report still remain valid as a demonstration of impact.

DIFFERENTIAL RATES

Council can apply differential rate based on land use and location but cannot apply it based on availability or levels of service. Differential rates must be set objectively based on:

- perceptions of differences in capacity to pay relative to property value between properties with different land uses or in different localities; and / or
- the costs to a council generated by or in servicing properties affected by the differential, or
- the policy objectives of a council.

Differential arrangements are commonplace and have not changed materially over time as such they are generally accepted as a capacity to pay. Council's policy has chosen three differential rates based on land use: Non-Residential, Residential and Vacant Land. Consideration could be given to variations of land use.

SERVICE CHARGES AND SEPARATE RATES

The CoA currently levies a separate which is applicable to an area defined by resolution of Council as the Rundle Mall Precinct. Setting such fees presents equity issues in terms of whether a separate rate is justified. When applied appropriately, these charges and rates must be measured directly against the activity by which they are raised in order to ensure value and equity of the additional rate is achieved and justified.

The 2017 review provided a recommendation for the CoA to consider further separate rates in support of its significant retail precincts.

CAPITAL CITY COMPARISON

City of Adelaide by comparison to all other South Australian Council is the only Council to use Assessed Annual Value, while a majority of other SA Council's utilise Capital Value and other regional areas adopting site value.

The key point of difference and support for the AAV methodology is the high level of occupier/rented premises in the CBD. As mentioned above, AAV is a simple function of Capital Value and as a result a change in methodology cannot be justified other than its simplicity of administration.

Its is of more relevance to compare CoA to other capital cities in Australia. This comparison was provided in the 2017 Review and updated below with the information in Table 2.

Table 2: Capital City Valuation Methodology Comparison

City	Valuation Base	Minimum Rate / Fixed Charge	Differential Rates
Adelaide	AAV	Nil	Yes
Brisbane	Site Value	Yes	Yes
Melbourne	AAV	Nil	Yes
Perth	AAV*	Yes	Yes
Sydney	Site Value	Yes	Yes
Darwin	Site Value	Yes	Yes
Hobart	AAV	Nil	No

City of Perth recently conducted a rating methodology review and resolved to retain an AAV methodology referred to as Gross Rental Values (GRV).

2017 REVIEW RECOMMENDATIONS

The final report provided 13 recommendations, some of which related to rating and others to revenue given the scope of the report.

Details on how each recommendation has been addressed is provided below:

Recommendation	Action – Current Recommendation
1. CoA continue to set rates based on each property's assessed annual value.	Recommend to continue to use the Assessed Annual Value
2. CoA remain open to considering the introduction of a modest fixed charge in future but on the basis of available evidence not do so at this time.	Council's Rating Policy undertook significant review and change with public consultation in 2021. Council is committed to review it Rating Policy on an annual basis and confirmation of this element can be considered as a part of the review.
3. Consideration be given to introducing a waste service charge relative to overall equity and administrative considerations.	Review of this particular charge has not yet been undertaken. Council needs to consider this as a part of a broader overall strategic approach to waste in the City and consideration of these other factors may impact the appetite to want to introduce such a charge.
4. Council consider introducing a separate rate to support the promotion of retail activity in all significant retail precincts.	Consideration has been given, since the review, to introduce a separate rate for the East End, however Council did not support. Recent conversations regarding separate rates for Mainstreet Precincts also did not favour such a rate. Opportunities in this area will be assessed when deemed appropriate.
5. CoA monitor the development of the application of value capture by the State and other local governments in SA and elsewhere and consider applying the concept in future where it considers it has merit.	The concept of Value Capture has not moved since 2017 and in fact has been overshadowed by rates capping and rates oversight scheme. Continued review of State developments and legislative changes will be undertaken and reported to the Audit and Risk Committee where relevant.
6. COA review the basis of determining its • residential rate relative to its rate for other classes of property and whether it is appropriate to continue to set rates based on residential properties generating 20% of total rate revenue, • Vacant land rate relative to other differential rates and whether it would be practical and effective to charge a higher vacant land rate to encourage development	The concept of setting rates based on 20% relative to other property classes has been assessed with Table 1 in this report. With the holding of the Rate in the Dollar the alignment between value and rate revenue has skewed slightly. Council's Rating Policy undertook significant review and change with public consultation in 2021. Included in this review was an additional differential rate for Vacant Land equivalent to 100% of the non residential rate. This was put in place to encourage development of land and prevent land banking.
7. The merits of providing pensioner and self-funded retiree remissions be reviewed, with a view to potentially discontinuing these concessions	Council's Rating Policy undertook significant review and change with public consultation in 2021. Included in this review was the removal of the pensioner concessions given the concessions offered via State Government.
8. That COA's rating policy be reviewed in the light of Council's response to the conclusions and recommendations set out in this report.	Council's Rating Policy undertook significant review and change with public consultation in 2021.

Recommendation	Action – Current Recommendation
9. Council develop a policy regarding the pursuit of commercial income that encourages a cautious approach that has regard to social considerations and risk consideration. Commercial opportunities should not be disregarded but rates are likely to be an appropriate source of revenue to fund much of CoA's aggregate service costs on an ongoing basis.	Council has resolved to focus on commercial incomes to remove the burden of reliance on rate income. In development is a Finance Strategy to be considered by Audit and Risk Committee to agree the principles applied to non-rates revenues and its contribution to the overall financial position of Council.
10. It is recommended that in the absence of reasons to the contrary CoA generally base its charges for private goods on comparable market prices or in the absence thereof the full long-run cost of provision to ratepayers	Council reviews its fees and charges annually which includes a market assessment of prices. Recently, Council has resolved to hold amendments to fees and charges in support of businesses and community.
11. Council have regard to expected trends in the development of driverless cars and the likely financial impact thereof in its long-term financial planning considerations.	Council reviews its businesses and services for impact of all market and community trends through insights. Any variations to services are considered and will be factored into long term financial planning where relevant.
12. Council review the basis of the financial indicator target ranges it has set and base the annual update of its long-term financial plan and annual budget and business plan revenue and expenditure decisions on achievement of these targets, and	Council recently reviewed its Treasury Policy in November 2020 and again in February 2022 to assess its financial indicators and treasury management. These ratios are included in all Budget Review and annual reporting to ensure Council has full visibility and understanding of the financial implications of its decision making.
13. The annual achievement of financial results consistent with soundly based financial indicator target ranges be recognised as a key strategic policy objective by CoA.	These financial indicator ranges exist within the Treasury Policy. The creation of a financial policy is being considered as a part of the development of the finance strategy document. This is a key future consideration of the Audit and Risk Committee.

CONCLUSION

It is determined that there are elements of the 2017 Rate and Revenue review are still relevant and a majority of the recommendations have been addressed since.

It is recommended that the continued use of AAV as the representative method for value and capacity to pay be retained until a future review.