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## **Financial sustainability remains biggest challenge for Councils**

35 of the 100 largest local councils in NSW will need to increase their rates, fees and charges by 80% to 200% over the next ten years<sup>1</sup> or be forced to severely cut their services if they are to restore their finances and infrastructure to prudent and responsible levels.

For another 19 councils the increases are of the order of 60% to 80%. This means that the existing policies of half of all large councils in NSW fall short of being financially sustainable.

This is the main finding of the second FiscalStar annual financial sustainability survey of councils, commissioned by Review Today and sponsored by Dexia.

The FiscalStar study is based on the latest annual financial and infrastructure data published by councils as well as additional information councils provided in response to a questionnaire. Only 3 councils (Botany Bay, Gwydir and Wellington) failed the transparency test of not providing sufficient data on their websites to enable FiscalStar to assess their sustainability.

Changes in results from FiscalStar's 2007 survey are mainly due to councils providing new data, though a refinement of the analytical methodology also played a part.

It should be stressed that the 35 councils whose existing revenue and spending policies are unsustainable are not facing insolvency. This is because councils like other tiers of government can always tax their way out of bankruptcy. But they face huge increases in rates, fees and charges over the next ten years unless the commonwealth and/or state governments come to their assistance or they drastically cut services or they allow a backlog of dilapidated infrastructure to grow worse or they accept escalating budget deficits.

The most alarming aspect is that neither the state nor federal government accepts the gravity of the crisis sinking local government. The state government seems to think that as long as a few large councils each year are allowed a significant rate hike the problem will go away. The federal government appears more interested in funding state initiatives even though local government has a narrow revenue base and collects only 3% of all taxes.

The heart of the problem is that most councils are facing a large and growing backlog of infrastructure (e.g. roads, kerbing, footpaths, street lighting, stormwater drains, buildings, retaining walls, playgrounds, picnic benches, sports ovals, parks and gardens, etc) that has

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<sup>1</sup> Assuming price inflation averages 3% per annum over the same period.

passed its use-by date and needs replacing, not just patching. If this infrastructure backlog is added to councils outstanding debt then the resulting total 'broad liabilities' of all councils that are 'unsustainable' averages about 187% of their total annual operating revenue.

For 'vulnerable' councils the 'broad liabilities' average is 95%. To be 'sustainable' a council's combined debt and infrastructure backlog generally should not exceed around 60%. With 'sustainable' councils averaging 55%, they too should be vigilant as they're living on the edge.

The 'unsustainable' and 'vulnerable' councils also have difficulties on other fronts. For instance 'unsustainable' councils typically have large operating deficits as a proportion of their own source revenues. By contrast 'sustainable' councils have large operating *surplus* ratios.

Other weaknesses of many councils is a heavy reliance on tenuous grants from other governments, little or no spare cash to meet emergencies and special needs, expenses growing well in excess of underlying costs and insufficient capital works spending to renew ageing infrastructure. This too is documented by FiscalStar.

How should councils react to these findings, given that they are based on their own data?

First they could ask themselves:

- Have we measured our infrastructure backlog correctly?
- Are we positioned to meet future infrastructure renewals as they fall due?
- Can we withstand unexpected shocks or developments (e.g. impact of climate change)?
- How will we cope with demographic pressures (e.g. population growth and ageing)?

The Department of Local Government, State Grants Commission and Australian Bureau of Statistics could also help by improving the consistency and accuracy of the council data they collect. For instance the DLG should clarify that the requirement for a council to report the total cost of bringing its degraded assets to a satisfactory condition does not mean renewing all its assets to their original condition as some councils think.

If a council is rated 'unsustainable' or 'vulnerable' and the problem is not data related, then it must start a serious dialogue with its community and the state government on how best to rectify the situation if that hasn't already been done. Denying the gravity of the situation would exacerbate the problem as the longer it's left the more intractable it becomes.

Of course the state government's decision to reduce the scope of councils to levy developer charges, to continue with rate pegging when no other state does and to tolerated cost shifting (the latest being a proposals to make councils pay more for fire services) will constrain the ability of local government to rescue itself.

Recent data collected by a Dexia international research department shows that in 2006 local government expenditure as a share of GDP was only 2.3% in Australia compared with 15.1% in Japan, 12.9% in the UK, 12.7% in the European Union and 8.5% in the USA. Although Australia is a very large country we don't entrust much power, let alone resources to our third tier of government.

And within Australia, there is a tighter rein on local government in NSW than any other state. A recent Productivity Commission report into the revenue raising capacity of local government found that:

*The rate of growth in rates revenue in New South Wales has been among the lowest of all jurisdictions over the past seven years, for which reliable data are available. New South Wales also has rate revenue per person below that of most other jurisdictions. Rate pegging in New South Wales appears to be restricting revenue raised from rates, notwithstanding scope for councils to seek variations to mandated rate increases. In addition, only partial reimbursement of concessions affects the revenue of local governments in New South Wales. The evidence suggests that the NSW Government has chosen to have a more significant constraining influence on the revenue raised by local governments than have other State governments.”*

If the NSW government is determined to further reduce the relative size of local government it would do better to circumscribe its role and operating expenses through an intergovernmental agreement than stopping councils from raising the necessary revenue to rehabilitate, renew and enhance the state’s decaying community infrastructure.

New Zealand has a much lower per capita income than NSW yet the standard of its local roads, footpaths, kerbing, public places, stormwater drains, community, recreation and other facilities puts us to shame.

Ironically, the straitjacket applied to NSW councils may ultimately backfire on the state if voters unleash their fury on MPs for not addressing local problems that councils could have fixed had they been allowed to do so. Already there are many councils whose infrastructure backlog is too big for ratepayers to fund. As more join their ranks the pressure on the state’s Treasury to come to their rescue will intensify.

Another possibility is that any revamp of federal state financial relations might address local government funding, especially for rural and remote councils. The recent Productivity Commission report advised:

*Given the differences in the scope to raise additional revenue across different classes of councils, there is a case to review the provision of Australian Government general purpose grants to local governments.*

The NSW Independent Pricing and Regulatory Tribunal has been asked by the Premier to review the inter-governmental and regulatory framework for setting council rates and charges. Perhaps this is a sign that the government is heeding the advice of the Local Government Inquiry of 2006.

Repeated opinion polls– the latest being by the Federalism Project of Griffith University – have found that Australians have more confidence in their local councils than they do in state government and most think it better for decisions to be made at the lowest level of government including councils. They also recognize that local government is under-resourced.

With local government confined to only 5% of general government end spending, its time its future was secured by formal recognition in the Australian constitution and a guaranteed share of national taxation like the states receive through the GST.

Yet councils would be unwise to stake everything on manna from heaven. Instead each council should take charge of its destiny by identifying its service and infrastructure needs and devising a long term strategy and financial plan as councils do in New Zealand. Indeed the Department of Local Government is likely to make this mandatory.

By exploring its sustainability in terms of services, infrastructure and finances, a council can develop a business case for increased funding to put to its community and the Minister for Local Government. Some councils have already done so this with success.

Also councils should rethink their community relations. Too often annual reports, ratepayer notices and websites trumpet council achievements without highlighting the real threats to their community's amenities, services and environment. Greater candour by councils about the true plight of their finances and infrastructure could bring these issues to the forefront of the public's consciousness.

Hopefully the FiscalStar report will help galvanise attention on a problem that some would prefer was kept under wraps. The report identifies local government's problems at a local level. By doing so it highlights the scale of the task each community faces.

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End Note: Professor Allan chaired and directed the NSW Local Government Inquiry of 2006. He is a former Secretary of the NSW Treasury (1985-1994) and was Chair of the NSW Premier's Council on the Cost & Quality of Government (1999-2007).

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Note: Full FiscalStar report can be downloaded from [www.reviewtoday.com.au](http://www.reviewtoday.com.au)

# The Financial Sustainability of Existing Financial and Infrastructure Policies, Largest 100 NSW Councils, 2006/07

As assessed by:



| larger NSW councils           | financial sustainability rating of existing policies<br>(a) |
|-------------------------------|---|
| <b>METROPOLITAN: INNER</b>    |   |
| Ashfield Municipal Council    | Unsustainable   |
| Botany Bay City Council       | n.a.  |
| Burwood Council               | Unsustainable   |
| Canada Bay City Council       | Unsustainable   |
| Canterbury City Council       | Sustainable   |
| Hurstville City Council       | Sustainable   |
| Kogarah Municipal Council     | Sustainable   |
| Lane Cove Municipal Council   | Sustainable   |
| Leichhardt Municipal Council  | Sustainable   |
| Manly Council                 | Vulnerable  |
| Marrickville Council          | Unsustainable   |
| Mosman Municipal Council      | Unsustainable   |
| North Sydney Council          | Sustainable   |
| Randwick City Council         | Vulnerable  |
| Rockdale City Council         | Sustainable   |
| Strathfield Municipal Council | Sustainable   |
| Sydney City Council           | Sustainable   |
| Waverley Council              | Sustainable   |
| Willoughby City Council       | Vulnerable  |
| Woolahra Municipal Council    | Sustainable   |
| <b>METROPOLITAN: OUTER</b>    |   |
| Auburn Council                | Unsustainable   |
| Bankstown City Council        | Sustainable   |
| Baulkham Hills Shire Council  | Sustainable   |
| Blacktown City Council        | Sustainable   |
| Blue Mountains City Council   | Unsustainable   |
| Camden Council                | Unsustainable   |
| Campbelltown City Council     | Vulnerable  |
| Fairfield City Council        | Sustainable   |
| Gosford City Council          | Unsustainable   |
| Hawkesbury City Council       | Unsustainable   |
| Holroyd City Council          | Sustainable   |
| Hornsby Shire Council         | Sustainable   |
| Ku-ring-gai Council           | Vulnerable  |
| Liverpool City Council        | Unsustainable   |
| Parramatta City Council       | Vulnerable  |
| Penrith City Council          | Unsustainable   |
| Pittwater Council             | Sustainable   |
| Ryde City Council             | Sustainable   |
| Sutherland Shire Council      | Sustainable   |
| Warringah Council             | Sustainable   |
| Wollondilly Shire Council     | Unsustainable   |
| Wyong Shire Council           | Vulnerable  |

| larger NSW councils             | financial sustainability rating of existing policies<br>(a) |
|---------------------------------|---|
| <b>REGIONAL: COASTAL URBAN</b>  |   |
| Ballina Shire Council           | Unsustainable   |
| Bega Valley Shire Council       | Sustainable   |
| Byron Shire Council             | Unsustainable   |
| Coffs Harbour City Council      | Vulnerable  |
| Eurobodalla Shire Council       | Vulnerable  |
| Great Lakes Council             | Unsustainable   |
| Greater Taree City Council      | Unsustainable   |
| Kempsey Shire Council           | Unsustainable   |
| Kiama Municipal Council         | Unsustainable   |
| Lake Macquarie City Council     | Sustainable   |
| Newcastle City Council          | Unsustainable   |
| Port Macquarie-Hastings Council | Unsustainable   |
| Port Stephens Council           | Vulnerable  |
| Richmond Valley Council         | Unsustainable   |
| Shellharbour City Council       | Vulnerable  |
| Shoalhaven City Council         | Sustainable   |
| Tweed Shire Council             | Unsustainable   |
| Wollongong City Council         | Unsustainable   |
| <b>REGIONAL: INLAND URBAN</b>   |   |
| Albury City Council             | Sustainable   |
| Armidale Dumaresq Council       | Unsustainable   |
| Bathurst Regional Council       | Vulnerable  |
| Broken Hill City Council        | Unsustainable   |
| Cessnock City Council           | Unsustainable   |
| Dubbo City Council              | Vulnerable  |
| Goulburn Mulwaree Council       | Sustainable   |
| Griffith City Council           | Unsustainable   |
| Lismore City Council            | Unsustainable   |
| Lithgow City Council            | Vulnerable  |
| Maitland City Council           | Sustainable   |
| Orange City Council             | Sustainable   |
| Queanbeyan City Council         | Sustainable   |
| Singleton Shire Council         | Vulnerable  |
| Tamworth Regional Council       | Vulnerable  |
| Wagga Wagga City Council        | Sustainable   |
| Wingecarribee Shire Council     | Unsustainable   |
| <b>REGIONAL: RURAL</b>          |   |
| Bellingen Shire Council         | Unsustainable   |
| Cabonne Shire Council           | Unsustainable   |
| Clarence Valley Council         | Unsustainable   |
| Cooma-Monaro Shire Council      | Sustainable   |
| Cowra Shire Council             | Sustainable   |
| Forbes Shire Council            | Sustainable   |
| Gunnedah Shire Council          | Sustainable   |
| Gwydir Shire Council            | n.a.  |
| Leeton Shire Council            | Sustainable   |
| Liverpool Plains Shire Council  | Vulnerable  |
| Inverell Shire Council          | Sustainable   |
| Mid-Western Regional Council    | Sustainable   |
| Moree Plains Shire Council      | Vulnerable  |
| Muswellbrook Shire Council      | Unsustainable   |
| Nambucca Shire Council          | Unsustainable   |
| Narrabri Shire Council          | Sustainable   |
| Parkes Shire Council            | Sustainable   |
| Temora Shire Council            | Sustainable   |
| Tumut Shire Council             | Sustainable   |
| Upper Hunter Shire Council      | Sustainable   |
| Upper Lachlan Council           | Vulnerable  |
| Wellington Council              | n.a.  |
| Young Shire Council             | Sustainable   |

Note: All assessments exclude a council's water & sewerage operations.

## Explanatory notes:

(a) Assessment of the financial sustainability of a council's existing financial and infrastructure policies is based on the council's most recent statutory financial reports, focussing on its operating deficit, debt level and infrastructure backlog – each as reported by the council. n.a. = not assessed (the full statutory financial reports for 2005/06 and 2006/07 are not on the council's website), only three councils (Botany Bay, Gwydir and Wellington) do not publish all their financials on the internet.

A council's existing financial and infrastructure policies are assessed as financially '**unsustainable**' where substantial revenue (or expenditure) adjustments over the next few years seem unavoidable. The financial solvency of such councils is not being called into question. Rather, it is continuation of a council's present revenue-raising and spending that is financially unsustainable. In the absence of increased grants funding, the substantial rates increases and/or spending cutbacks necessary if these councils are to achieve financial and infrastructure conditions that are prudent and responsible will impose a considerable cost on ratepayers and the communities they serve.

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