



SYSTEMIC
SUSTAINABILITY
STUDY

- In Your Hands
- Shaping the future of Local Government
in Western Australia
- Final Report

Sponsored by



WESTERN AUSTRALIAN
LOCAL GOVERNMENT
ASSOCIATION

December 2006

Cr W (Bill) Mitchell JP
President
WA Local Government Association

Dear President,

It is with great pleasure that I present, on behalf of my colleagues Fiona MacKenzie and George McCullagh, the final report of the Systemic Sustainability Study. This study represents an impressive endeavour of the Local Government sector to chart its own future as it grapples with some serious challenges.

This Final Report is focused on strategies and actions that the leadership of local Government can consider as practical responses to the range of challenges facing communities and their Councils. I do not believe that the Association or any individual Local Government will be threatened by any of our recommendations especially as implementation and change of the scale as is now required can only occur if communities, Councils and WALGA determine to support and champion the actions, directions or investments proposed.

The terms of reference presented us with the challenge of building a well informed agenda for change and rejuvenation.

The Panel's role has brought with it a strong sense of responsibility and obligation – especially as we came to better understand the pressures and drivers of activity in Local Government today and to appreciate the passion and commitment the industry has for its task and the communities it serves.

We were greatly assisted in our work and deliberations by a range of well thought out submissions and contributions from across Local Government in Western Australia. These insights were very important in helping us penetrate some of the 'noise and static' which seems to dominate discussion and popular remedies for the industry, and to build a better and more complete understanding of the diverse and valued role Local Government plays.

Regards,



Professor Greg Craven
Chair,
Systemic Sustainability Study

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Executive Summary

This study represents a significant investment by Local Government in Western Australia in its own future. The big idea is to strengthen Local Government to ensure it remains vibrant, sustainable and well equipped for the task of meeting community needs well into the 21st century.

The vision is to establish a framework that enhances the best aspects of the Local Government system and to provide strategies to address the many challenges facing Councils, Councillors and their management teams, now and into the future.

An Industry Plan is proposed as a key process by which the Industry can consider and further develop the detailed recommendations in this document into a program for change and rejuvenation across the sector.

While our research discusses a large number of issues, we believe that the key challenges to Local Government are to provide a joined up approach to a five-point plan and framework for the future:

- Leadership in the process of change by Councils, Councillors, senior management and WALGA;
- Securing better revenue outcomes for the industry from government and from the sector itself;
- Strengthening practice and technique in all authorities to improve financial and planning disciplines using a best practice approach;
- Strengthening the focus by government and the industry on new models for efficient service delivery at regional and zone levels; and
- Securing talent and investing in expertise to ensure Councillors, Management and Staff are well equipped for the challenges of 21st century Local Government.

A more confident and strategic relationship with State and Commonwealth governments will be an important foundation for the change program ahead.

In the detail of this report, and in our earlier consultancies, there is a wealth of information and experience the industry can apply to its future. The detailed recommendations in this document provide focus for investment and resourcing by government and the industry.

To enhance the best elements that exist within the Local Government sector, we recommend 'Best Practice' frameworks rather than the less certain approaches associated with regulatory change or industry codes of conduct.

We recommend that WALGA host an industry summit early in 2007 to formalise the sector's position on each of the recommendations and to consider implementation proposals which may be developed by an implementation Task Force to be established by WALGA.

The task force will need to engage State and Commonwealth government stakeholders and may consider their participation as members of the task force in due course.

Given the scale of the 41 recommendations that we have made there is a significant scope for the State Government to provide funding support for implementation, especially in initiatives for capacity building and in strengthening financial incentives for change.

While the exact magnitude and duration of funding for the changes should be determined by the sector, we believe it is substantially larger than the funds available through the existing Connecting Local Government Initiatives program. We have made some specific, short-term recommendations in relation to the focus of this fund but believe a separate and more substantial investment by State Government is required. We note the magnitude of the task parallels the Size, Shape and Sustainability project being undertaken in Queensland where \$25 million has been provided by the State Government.

The document also contains a range of strategies to enhance the performance of Local Government in this state. Many of these will require focus and investment by individual Councils or participation in agreed industry funding initiatives.

A summary of all 41 recommendations is included in Chapter 9, presented in a format that may adapt well to the documentation of an industry plan. In the body of the report there are numerous other observations on culture, technique, expertise and challenges for the industry.

The Panel did not set out to build a list of prospective amalgamation targets. Indeed our approach is leading us in a different direction - towards better performance of underlying financial instruments, strengthening industry capability and by challenging some policy settings and management practices adversely impacting the industry as a whole.

Later in this document we develop views on prospective efficiencies available to Councils. In the main these attach to mechanisms which provide the future services, skills and capabilities Local Government needs on a regional basis. In time, these models may evolve into genuine regional governance arrangements.

Chapter 1 Introduction

In January 2006, the Western Australian Local Government Association (WALGA) commissioned this review of the Systemic Sustainability of Local Government – positioned as an industry-led assessment of the condition and prospects for Local Government in this state.

An independent Panel was established to provide direction for this review and to provide WALGA with advice, strategies and a plan for the future of the industry for its further consideration and development with Local Government in Western Australia.¹

The Systemic Sustainability Study was undertaken as a three-stage process:

1. A program of research, consultancy advice and industry submissions was used to inform our assessment of Local Government sustainability. An interim report: In Your Hands: Shaping the future of Local Government in Western Australia was presented at the WALGA's annual conference in August 2006. This report provided observations and a point of view drawn from consultancies conducted between March and July 2006 and also from a number of thoughtful submissions and representations made to the review.
2. A series of industry dialogues was conducted in October and November throughout the State. This engagement process provided an opportunity to explore and road test the issues raised in the interim report and to focus on the strategies and actions the industry has available to it in moving forward. Input from these discussions was also invaluable in shaping our final report.
3. The recommendations we now make conclude this study. Our advice to WALGA builds from the strengths and challenges facing the system of Local Government in this state and endeavour to take a systemic view of the future for the industry.

This Final Report is focused on strategies and actions that the leadership of local Government can consider as practical responses to the range of challenges facing communities and their Councils. Some of our recommendations will provide endorsement or support for initiatives already underway in the industry – other advice may necessarily confront current practice and policy settings.

The vision is to establish a framework that enhances the best aspects of the Local Government system and to provide strategies to address the many challenges facing Councils, Councillors and their management teams, now and into the future.

The big idea is to strengthen Local Government to ensure it remains vibrant, sustainable and well equipped for the task of meeting community needs well into the 21st century.

¹ Panel membership and formal terms of reference are set out at Appendix 1.

Councils and WALGA will not be threatened by many of our recommendations—especially as implementation and change of the scale as is now required can only occur if communities, Councils and WALGA determine to support and champion the actions, directions or investments proposed.

The Panel has remained focussed on a systemic view of Local Government, using in the main the information base the industry uses for day-to-day management and in reporting to its own communities and funders. We are clear that Individual authorities are not on trial and will not be the subject of specific recommendations

The dialogue process has acknowledged that there is a set of related issues impacting the better performance of Local Government. These are in most cases statewide challenges beyond the scope and capacity of individual authorities to address. As a consequence we propose an industry plan for recovery and rejuvenation. This is envisaged as a 10-year program. A successful plan will require investment by the industry and its State and Commonwealth partners to address a suite of systemic or ‘inconvenient truths’ as essential preconditions for change.

The Panel did not set out to build a list of prospective amalgamation targets. Indeed our approach is leading us in a different direction – towards better performance of underlying financial instruments, strengthening industry capability and by challenging some policy settings and management practices adversely impacting the industry as a whole.

Later in this document we develop views on prospective efficiencies available to Councils. In the main these attach to mechanisms which provide the future services, skills and capabilities Local Government needs on a regional basis. In time these models may evolve into genuine regional governance arrangements once the performance of various revenue instruments available to local authorities is improved and the inconsistent nature of information used for management and policy purposes is addressed.

A precondition for success is leadership. Our view is that WALGA, Councils and industry management can use the plan and its associated processes to demonstrate to all that the industry is competently driving its own agenda for change and revitalisation. We see this as an essential precondition to any campaign directed to governments at State and Commonwealth level to better resource the future contribution Local Government makes to the Western Australian community.

The opportunity now available to WALGA and its member Councils is to consider the recommendations outlined in this report and to actively work with the sector and governments to fund an industry action plan capable of being implemented:

- At the level of individual Councils;
- Between Councils and WALGA; and
- Between WALGA and other governments and stakeholders.

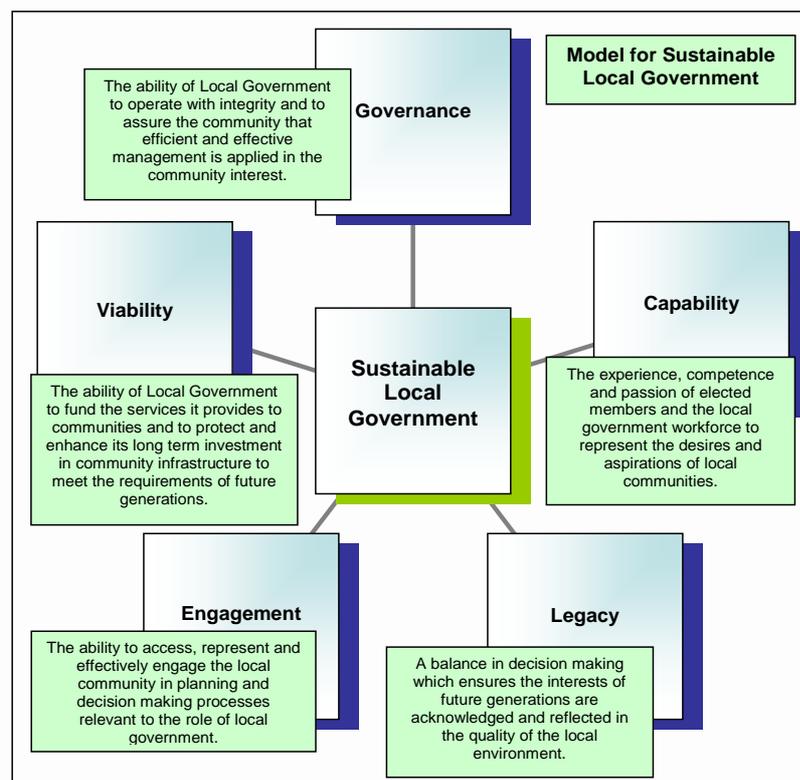
A Sustainability Context for Local Government in Western Australia

The study was conducted at a time when reform and structural change for Local Government was underway or contemplated in most Australian jurisdictions. A national industry context shaped by heightened community expectations and intense fiscal pressure has exposed most Councils to the significant challenge of maintaining current levels of community infrastructure and the daily task of ensuring the provision of valued services to communities and citizens.

In Western Australia, the review also took place against a backdrop of unprecedented growth in the State economy – bringing with it significant short and long-term infrastructure, capacity and service expectation challenges for every Council in the State. Recent ABS data shows Western Australia’s Gross State Product (GSP) grew at 4.9 per cent in 2005–06 or almost twice the national rate of 2.8 per cent over the same period. The State’s domestic economy recorded 10.9 per cent growth over the year, higher than any other Australian State or Territory.

In 2004 the Local Government Act of 1995 was amended to reflect the Western Australian Government’s Sustainability Strategy (2003). In part, the amendments required Councils to apply “*best endeavours to meet the needs of current and future generations through integration of environmental protection, social advancement and economic prosperity*”.

The Panel has explored a framework to better inform practical ways in which the idea of sustainability can be applied by individual authorities and at the level of the industry in its Western Australian setting.



Chapter 2 Interim Findings and Dialogue Feedback

An Interim Report: *In Your Hands – Shaping the Future of Local Government in Western Australia* was released at Local Government Week in August 2006.

In October and November the Panel conducted a series of industry dialogues throughout the state to consider the findings of that document. These discussions were wide-ranging and provided us with very important feedback about the interim report's findings and potential remedies to the challenges confronting Local Government. The following framework illustrates the range of issues considered or discussed in this aspect of the process.

Governance

Findings	Dialogue Feedback	Panel Commentary
<ul style="list-style-type: none"> ○ Compliance requirements are onerous and attach in the main to the impacts of a growing range of State Government legislation. ○ The capacity of Local Government to develop its own distinctive role is impeded by the effort and resources required to meet minimum governance standards and regulatory requirements. 	<ul style="list-style-type: none"> ○ The role of Local Government is increasingly shaped as administrative and regulatory rather than proactive and creative. There is often little scope to focus on the development of local communities. ○ The community often sees little value or benefit in regulatory roles – and does not always differentiate between roles of the three levels of government. ○ Most new legislative requirements or obligations for Local Government are not accompanied by explicit funding or resourcing. 	<ul style="list-style-type: none"> ○ Strong and effective engagement and influence with other levels of government in shaping policy settings and legislative outcomes is a critical success factor for a more sustainable Local Government sector. ○ At individual Council level there may be value in ensuring that CEOs in particular have scope and sufficient resources available to them to ensure adequate focus on strategic or priority issues for the Council and the community its represents.
<ul style="list-style-type: none"> ○ Increasing community expectations bring a requirement for increasing professionalism. ○ Councils are complex organisations with wider responsibilities. This is not always reflected in the legislative, governance and managerial approaches adopted. 	<ul style="list-style-type: none"> ○ Communities (particularly in rural and regional Western Australia) place high expectations on their Councils to ensure adequate services and representation of local interests. ○ The industry has an exposure from time to time where conflictual or corrupt practice is determined. Most see the industry as working hard at promoting and securing the interests of the communities it represents. 	<ul style="list-style-type: none"> ○ The industry is not immune from supply and demand pressures and community appetite for best-in-class services. ○ The industry has to continue to adapt its management and governance frameworks and practices to focus on achieving more contemporary outcomes or results. ○ Systemic issues in respect of funding and capability threaten quality and reliability in services.
<ul style="list-style-type: none"> ○ A complex and diverse industry across Western Australia. ○ Local Government - with a total workforce of over 14,000 and with non-financial assets of \$12.3B requires competent and well 	<ul style="list-style-type: none"> ○ The exposure of some Councils and many Councillors to the growing complexity and technical aspects of decision making is acknowledged – most favour greater investment in Councillor training and development. Others 	<ul style="list-style-type: none"> ○ Continued investment in the development of Councillors and staff to meet the challenges of governance and leadership in this sector is essential.

qualified political and managerial leadership and talent to secure a sustainable future.	support better compensation and the recognition that Council leadership requires more than sessional involvement for success.	
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Financial Sustainability

Findings	Dialogue Feedback	Panel Commentary
<ul style="list-style-type: none"> 83 Western Australian Councils were assessed as financially unsustainable when an 'own source' methodology was applied. 	<ul style="list-style-type: none"> Some Councils applied the Access methodology with better (and worse) outcomes for their individual Council. Some disputed the validity of a methodology that removed some capital items from the assessment arguing that Local Government is not viable without embedded subsidies or grants. Many emphasised the progressive decline in the proportion of funds from other government as the key issue to be addressed in ensuring financial sustainability. Many observed that the lack of consistency in reporting and industry information between Councils presents a significant exposure for planning for the future of Local Government. 	<ul style="list-style-type: none"> The underlying risk to the sustainability of the industry arising from its financial framework and practices remains.
<ul style="list-style-type: none"> A 4.5% deficit in the operating surplus ratio of WA Councils was reported. 	<ul style="list-style-type: none"> Some Councils felt the responsibility was with other levels of government for this shortfall, while other Councils promoted long-term plans to better manage year-to-year investments and expenditures against available resources. 	<ul style="list-style-type: none"> Significant, systemic changes to Local Government financial practices and decision making are required. Better fiscal outcomes from State and Federal partners are required.
<ul style="list-style-type: none"> A \$1.7B infrastructure backlog was reported. 	<ul style="list-style-type: none"> The exposure the Industry has was generally acknowledged – some saw the progressive decline in the proportion of funds from other government as the key issue to be addressed while others highlighted capacity and expertise issues. 	<ul style="list-style-type: none"> A detailed commentary on this issue is provided later in this document as a key industry initiative for a proposed Industry Plan.
<ul style="list-style-type: none"> A theme in the interim report was a need for the industry to focus on improved asset management. 	<ul style="list-style-type: none"> Proactive asset management can extend the life and service levels of Local Government infrastructure, improving the sustainability and quality of services provided by Local Government. 	<ul style="list-style-type: none"> There is a critical need for Local Government to strengthen its asset management capabilities. The measures proposed include better technical expertise, use of more consistent processes and methodologies and greater disclosure to

		<p>communities and funding partners of the challenge faced and the remedies being applied.</p> <ul style="list-style-type: none"> ○ A detailed commentary on this issue is provided later in this document as a key industry initiative for a proposed Industry Plan.
<ul style="list-style-type: none"> ○ Variation in the approaches to depreciation may mask the full exposure of the industry to asset related management challenges. 	<ul style="list-style-type: none"> ○ Some favour clearer regulatory guidance for all – others recommend either a best-practice or code-based approach for interpretation at Council level. 	<ul style="list-style-type: none"> ○ A detailed commentary on this issue is provided later in this document as a key industry initiative for a proposed Industry Plan.

Capability

Findings	Dialogue Feedback	Panel Commentary
<ul style="list-style-type: none"> ○ Councillor competency is not uniform. 	<ul style="list-style-type: none"> ○ Better induction level and continuing training and development opportunities for elected members were consistently supported . 	<ul style="list-style-type: none"> ○ A detailed commentary on this issue is provided later in this document as a key industry initiative for a proposed Industry Plan.
<ul style="list-style-type: none"> ○ There are critical labour shortages in key technical and professional areas central to the current role of Local Government. 	<ul style="list-style-type: none"> ○ The industry faces significant challenges in the recruitment and retention of staff – especially in the context of the strong WA economy. ○ Predation of staff between authorities is endemic. ○ Labour market competition for specialist skills has reduced the competitiveness of Local Government as an employer. ○ Some Local Governments have begun recruiting internationally. ○ Graduate and entry level recruitment is spasmodic and driven locally. ○ Greater focus on Local Government requirements from University and TAFE providers is warranted, with the objective of developing graduates and future employees with skills and competencies appropriate to Local Government. 	<ul style="list-style-type: none"> ○ There is considerable scope for whole-of-industry initiatives. ○ A detailed commentary on this issue is provided later in this document as a key industry initiative for a proposed Industry Plan.
<ul style="list-style-type: none"> ○ The Local Government workforce is ageing. 	<ul style="list-style-type: none"> ○ Authorities reported a number of strategies to attract and retain staff. ○ A range of measures was proposed including greater use of pooled staff and strengthening the network of Local Government alumni, who in retirement, may find sessional or part-time work 	<ul style="list-style-type: none"> ○ There is a strong case for sustained investment in the attraction of new talent to the industry at intake and graduate levels. The industry should encourage consideration of industry cadetships, a graduate pool scheme with a

	attractive.	single, whole-of-state employer and related measures.
<p>Significant population growth is occurring across the state however many authorities are challenged to continue their operations in communities where populations have been in decline for some time.</p> <p>Western Australia's population profile is ageing, as are the populations of other Australian states and most western countries. Statewide, those aged over 65 are projected to rise from 11.5 per cent of the population in 2004 to around 17.0 per cent of the population in 2025, and 18.5 per cent by 2031.</p>	<ul style="list-style-type: none"> Industry experience reflects the extremes of this shift – some authorities described the challenges of rapid growth and associated infrastructure challenges – others manage against the reality that population loss has occurred and seems likely to continue. 	<ul style="list-style-type: none"> There may be a limit on the size of a community that can sustain the full range of services and competencies required in 21st Century Local Government.

Engagement

Findings	Dialogue Feedback	Panel Commentary
<p>A definition of community of interest was developed in our interim report:</p> <ul style="list-style-type: none"> <i>A real or perceived sense of community or belonging to a locality that comes from a critical mass of people having common interests in similar social, economic, environmental, recreational, historical attachment or other matters of common interest.</i> 	<ul style="list-style-type: none"> Dialogue participants consistently stressed the importance of strong connections and trust between Local Government and the community. Most observed changes in community preference and expectations in relation to services. Some participants favoured a reduction in the number of Councillors, particularly in smaller Councils – and more general adoption of the whole-of-council – whole-of-community frameworks for decision making – moving away from ward-based models. Some stressed the importance of convenience, access and quality as key requirements for services – others were concerned to prevent the 'leakage' or loss of local critical mass in services (notably from State Government). 	<p>In the final report the Panel has further developed the service context of community of interest and explored the growing importance of activity of interest as an organisational principle for Local Government in the future.</p>

Legacy

Findings	Dialogue Feedback	Panel Commentary
<ul style="list-style-type: none"> There is a substantial infrastructure backlog (see section on Financial Sustainability). 	<ul style="list-style-type: none"> A number of authorities emphasised the need for long-run capital plans for use in decision making and budget prioritisation against long-term obligations and priorities. Building community confidence in the planning process was seen as a critical success factor. 	<ul style="list-style-type: none"> There is considerable scope for whole-of-industry initiatives. A detailed commentary on this issue is provided later in this document as a key industry initiative for a proposed Industry Plan.
<ul style="list-style-type: none"> The industry does not always apply strategic considerations to annual budgeting and related program decision making. 	<ul style="list-style-type: none"> Confident and balanced advice from Local Government Officers to Councils is essential to ensure strategic focus is maintained on economic, social and environmental dimensions of good government. 	<ul style="list-style-type: none"> There is considerable scope for industry-wide guidance and templates to be developed to assist Councillors and Officers when executing their duties.
<ul style="list-style-type: none"> Financial and asset plans. 	<ul style="list-style-type: none"> Some financial decisions, contractual undertakings and processes such as rate setting and development of infrastructure assets are conducted without a thorough understanding of their costs or impacts on other services. 	<ul style="list-style-type: none"> There is a need to incorporate whole-of-life costing into Local Government decision making and tie these decisions in with long-term asset management plans and comprehensive financial plans.

General Comments

During the engagement process Councils and staff raised many valid questions regarding the findings of the interim report and the significance of the findings. We welcomed this debate and challenge – it is clearly a great characteristic of the industry. We have endeavoured to address themes from the dialogue process in detail in the balance of this document.

- We observed a great diversity of views. Authorities experiencing rapid population growth presented with distinct infrastructure and service challenges. Other Councils where a decline of 4–5% of the resident population over the past few years is evident, presented practical observations on the challenge of funding and providing services to the communities they continue to serve.
- We were encouraged to find that systemic change was seen as essential – although there were clearly diverse views on where initial focus or investment should occur.
- The dialogue process consistently put the view that Local Government is well supported in the communities it serves, especially in rural and remote communities. Most had a confident view of the role Local Government is set to play conditional on the development of a more complete funding framework for the industry.

“There is little reason suggested to focus on the metropolitan area where the factors impacting on Local Government are less of an issue and do not demonstrate an impact on the sustainability of (most) Local Governments. The focus should be on the rural and isolated areas. It should be on how the community-based Councils can be supported to remain viable while they are needed by their communities.”

WESROC submission page 3.

- For others the presence of a Local Government provides an organisational focus and identity for communities – particularly in settings where business and government services have reduced over time or where population growth has declined or slowed.
- Localised innovation in service provision was consistently demonstrated – driven in the main by a chronic shortfall of funds.
- Performance experience was mixed in resource sharing and inter-Council pooling of plant, personnel and roles. A smaller number of communities indicated they are reluctant to allow ‘leakage’ of economic benefit to neighbouring or regional centres – especially where consolidation of staffing roles may see families leave local communities. Some authorities are actively planning to take advantage of their geographic positioning, regional role or skill base as a service hub to neighbouring Councils.
- Others indicated that a growing range of core Local Government services or functions are routinely supplied on a sourced basis – reflecting difficulties in attracting specialist staff and with the attendant risk that quality and competence issues may inevitably emerge. Services requiring professional/technical expertise are increasingly met by from other authorities, consultants and bureau style services.
- Most authorities cite cost shifting and the growing compliance roles determined by over 400 pieces of state legislation as significant drivers of cost and sustainability challenges facing Councils across the state.
- Many observed that the leadership role that Councils can play in developing local communities and economies is increasingly constrained by the growing administrative burden of compliance activities of little value or relevance to local communities.

Approach Used To Inform Financial Sustainability

We welcomed debate around the methodology we applied when considering the systemic financial sustainability of the industry in Western Australia. In context, we have been at pains to say that financial sustainability is only one element in any assessment of sustainability.

We accepted advice from Access Economics to the effect that:

“A Councils annual operating financial performance is sustainable only if the Council avoids both excessive borrowing and operating deficits over the medium- to long-term. Practically, this means a Council is sustainable if its operating deficit is less than 10% of own-source revenue.” (Access Economics, p VII and XIII).

The findings from this analysis are that just over one in every two Councils in Western Australia require a substantial (i.e. greater than 10%) further increase in

their own-source revenue to eliminate their underlying operating deficits. This assessment is made after taking into account each Councils additional revenue-raising capacity on the one hand and the costs likely to be imposed if they are to address any infrastructure backlog on the other.

Methodology

While our report did not identify individual authorities as unsustainable, a number of authorities have subsequently applied the methodology using their own data. In some cases this has resulted in better (and worse) self-assessment outcomes for authorities. Some have argued that this reduces confidence in our observation in August that some 83 Western Australian Local Governments were financially unsustainable. Others tell us that the methodology provides the industry with a confronting but realistic fiscal wake up call and that infrastructure backlog is likely to be larger and more challenging than described by our consultants.

We have been happy to defend the methodology. On advice from the WALGGC² we also applied a series of qualifications to the data applied to the model – these are clearly stated in our report.

We observe that the methodology is not dissimilar to that which a credit agency would use. We also had strong encouragement from WALGA to replicate some aspects of this methodology against interstate experience reported during 2005. This has helped to provide the industry in Western Australia with insights as to how it compares with peers in NSW and South Australia.

Access Economics have been clear and transparent in their advice to us. We also note that where assumptions are made these are fully documented or qualified. An appropriate conservative bias is evident in the treatment of variables or where estimates are drawn.

The methodology was used to obtain a macro perspective of the condition of the industry – we did not set out to build a list of prospective amalgamation targets. Indeed our approach is leading us in a different direction – towards better performance of underlying financial instruments and policy settings.

Focus on Own Source Revenue

Others have been concerned that the focus on own-source revenue is inappropriate – noting the important and inextricable role that various forms of grant or subsidy plays in funding Local Government services. In fact the methodology includes key aspects of these funding sources in the following manner:

- For the local roads grant component of Financial Assistance Grants (which may or may not be counted as capital grants by Councils), treating all these grants as operating grants;
- For 'Roads to Recovery' grants from the Commonwealth, apportioning these grants between 'operating' and 'capital' grants for each Council in proportion to the maintenance and renewal component of roads

² This was a requirement of the WALGGC in releasing the data for our use.

expenditure as recorded in the WALGA's annual Roads Survey publication; and

- For all other grants labelled by Councils as 'capital' grants received from other government, treating all these grants as capital grants.

What the methodology seeks to do is to clearly separate capital funds (with the exceptions allowed above) from masking the operating role of authorities. This is a well-accepted management and accounting principle and goes with our theme that a sustainable local authority routinely applies good governance, fiduciary and prudential standards to its operations.

The model also has a useful performance assumption embedded in it – that being 10% off the pace was a 'gap' that could be closed over a ten year period using own-source revenue provided a range of financial disciplines and management practices were sensitively applied – without deep fiscal or political push back from communities. The 10% threshold was based on 10 year's worth of annual increases in rates and other charges at one percentage point per annum above the no-policy-change increase. Even for councils currently with relatively high revenue-raising effort, an additional one percentage point annual increase in own-source revenue above the no-policy-change increase may be tolerable. Increases beyond this could reasonably be described as 'substantial', and therefore constitute evidence that a Councils present policies are unsustainable. Hence, we do not consider increases at the higher rates observed over the past four years – which have been at 2½ percentage points above what we consider to be the no-policy-change increase – to be sustainable.

Strategic Value

At a strategic level the methodology provides a lever for better and more equitable revenue outcomes for the sector as a whole from the Commonwealth Government. However observations of recent Commonwealth policy settings around national programs (such as the National Water Initiative) reveal that the Commonwealth will increasingly expect their program partners in Special Purpose Programs to demonstrate rigour and sound operating frameworks in order to attract Commonwealth assistance on a continuing basis. Our view, developed later in the report, is that Western Australian Local Government has some particular exposures in the integrity and coherence of its information base and that an industry-wide determination to strengthen performance in order to shape and inform better policy and funding outcomes is required.

Data Integrity

We believe that the findings understate the overall condition of the industry – while some have been quick to let us know that the data is wrong for their Council – we have also had clear signals from others that their position is in fact worse than we have identified.

We note that the underlying information is that used by Councils to tell the community it is doing the right thing with public funds.

The information is also applied by bodies such as the WALGC to inform its grant funding.

We only really had two choices. We could have said that the data was suspect in certain respects, been super cautious and not drawn any conclusions – or we could use the data in the manner described. The second option was preferred.

Confidence in Panel Conclusions

Of far greater concern are the Councils that we have put in the sustainable category on the basis (unknown to us) of deficiencies in their data which has overstated their expenses or understated their revenues. This may be due to abnormal or one-off items as well as errors on a Councils part.

We are reasonably confident that Access Economics endeavoured to understate rather than overstate Councils financial performance as the cumulative view of the underlying operating deficit facing most Western Australian authorities was assembled.

Within this distribution some Councils may be incorrectly assigned to the unsustainable category due to abnormal items in the year under review (2004–05) or reporting errors on a Councils part. These are undoubtedly offset by Councils that (unjustifiably) find themselves in the sustainable category.

Way Forward

We believe that the Local Government sector in Western Australia is confronted with a series of significant challenges to its sustainability, not all of which have a financial context. While the severity and immediate significance of many of these issues can be ignored in the short term, we believe that they will not go away. Many of the issues highlighted in the interim report will become more pressing in the future as the economic, capacity, skills demographic and service challenges continue.

The remainder of this document sets out the central challenges currently confronting Local Government sustainability and presents a set of strategies and actions to secure a more sustainable and equitable future for Local Government.

PANEL RECOMMENDATIONS

1. That WALGA develop a comprehensive engagement process to enable industry consideration of this report and its recommendations leading towards an industry-wide action plan.
2. A Local Government Summit is recommended for the early part of 2007 to debate and consider the basis for further industry investment and Council implementation of priority recommendations and actions.

Chapter 3 Local Government in the Australian Political System

Australia's Federal System and Local Government

Australia has developed its own distinctive federal form – characterised since federation in 1901 by a consistent trend of centralising power and revenue collection powers with the Commonwealth.

The consequence is a substantial vertical fiscal imbalance where a shortfall of revenue from one level of government is made up for by grants funded from the surplus revenue in another sphere. Australia's federation has a very high level of vertical fiscal imbalance compared to other federations throughout the world.

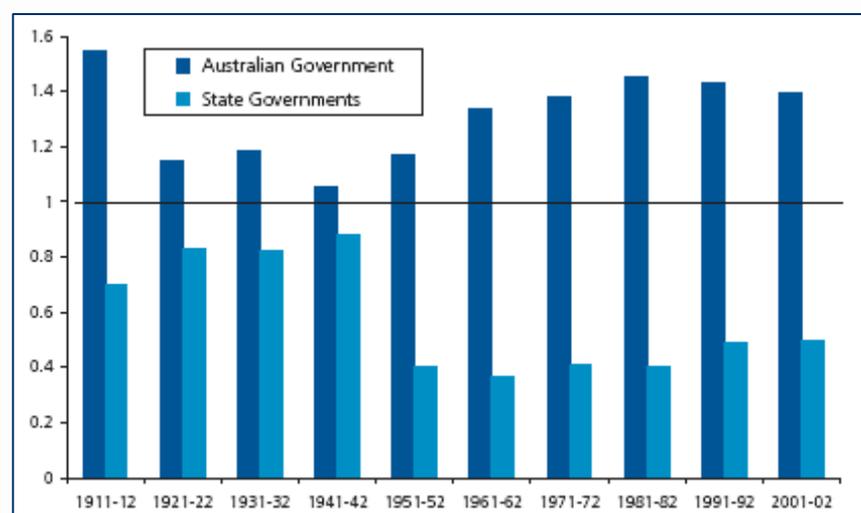
The positioning of Australian Local Government in jurisdictional roles, determined by State legislation and with revenue sourced from State and Commonwealth sources along with own-source rates and charges, provides significant scope for role and funding tensions between the three levels of government.

"The issue of Vertical Fiscal Inequality cannot be ignored as it is fundamental to the sustainability of Local Government particularly in rural and remote WA."

Town of Bassendean submission p.8.

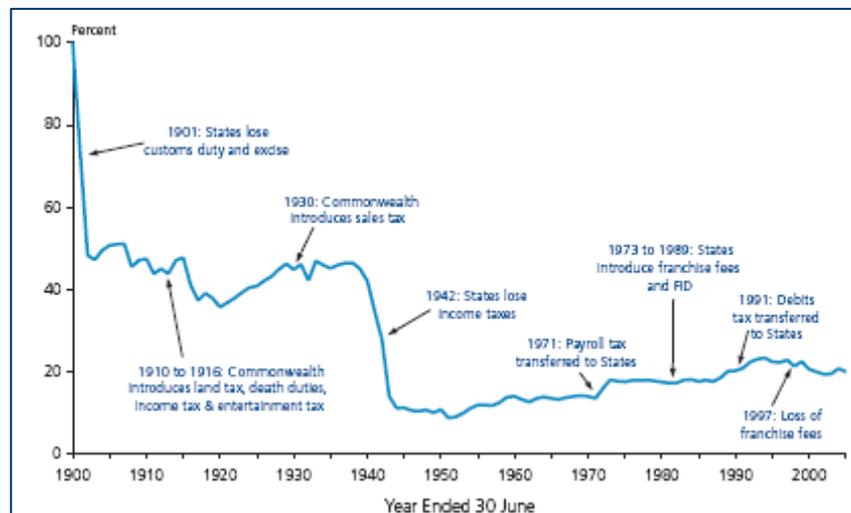
The high degree of vertical fiscal imbalance largely reflects the erosion of the States' revenue powers since federation. The history and extent of this imbalance is shown in figures 3.1 and 3.2.

FIGURE 3.1: COMPARISON OF VERTICAL FISCAL IMBALANCE (OWN-SOURCE REVENUE / RETAINED REVENUE)³



³ E. Ahmad and B. Searle, *On the Implementation of Transfers to Subnational Governments*, International Monetary Fund Working Paper WP/05/130, <http://www.imf.org/external/pubs/ft/wp/2005/wp05130.pdf>.

FIGURE 3.2: STATE OWN-SOURCE REVENUES AS A PERCENTAGE OF ALL STATE/AUSTRALIAN GOVERNMENT REVENUES⁴



The history of Local Governments own-source revenue as a percentage of all federal revenues follows the same path.

A 2001 review conducted by the Commonwealth Grants Commission confirmed total Commonwealth and State transfers to Local Government comprised a much smaller portion of total Local Government revenue (19%) than was the case in 1974-75 (25%).⁵

Since 1997-98 Councils around Australia have lost the equivalent of \$170 million in financial assistance grants from the Commonwealth reflecting policy shifts away from a funding model shaped by population growth in favour of an approach adjusted against an inflationary indicator.

In Western Australia alone, the estimate of equivalent funding foregone is about \$16.7million⁶.

In addition, a net fiscal subsidy of approximately \$4 billion is provided to the Commonwealth from the Western Australian economy.

We note the focus currently applied by The Australian Local Government Association to the principle of achieving explicit constitutional recognition and for an improved and defined share of the national revenue pool for Local Government purposes through Financial Assistance Grants (FAGs) and Specific Purpose Payments (SPP). The underlying principle is a more adequate sharing of benefits between different spheres of government especially where a local

⁴ Department of Treasury and Finance, 'Discussion paper on Commonwealth-State Relations: An economic and financial assessment of how Western Australia fairs' March 2006. pp 25.

⁵ Commonwealth Grants Commission, *Equality in Diversity*, Australian Government Publishing Service, Canberra 1995.

⁶ Western Australian Minister for Local Government and Regional Development, 'Commonwealth starving Local Governments of their fair share of funding', Press Release, August 4, 2006, <http://www.mediastatements.wa.gov.au>.

community directly contributes to infrastructure, such as the road network, and where the major beneficiaries are industries such as mining and tourism. These situations result in inequitable funding of the local road network and can perpetuate under-investment in its maintenance.

We are sceptical that an ideal or entirely equitable allocation of funds between the three levels of government will eventuate. The Commonwealth's preference for Specific Purpose Payments (SPPs) will present periodic opportunities for the industry to campaign for assistance to address infrastructure and capability challenges – although funds secured from this source seem likely to be accompanied by more onerous conditions placed on Local Government by the Commonwealth in relation to improvements in asset management and Council efficiency.

A prudent course for Local Government appears to be to continue to ensure that those revenue sources available to it and which it controls are used to best strategic effect and community benefit.

PANEL RECOMMENDATIONS

3. WALGA develop and commit to a 10-year industry plan (Big Ideas for a Big State) shaped around a range of best-practice reforms in the Local Government sector as a foundation for future campaigns to improve the systemic fiscal imbalance faced by Local Government.

4. WALGA should continue to press for changes to the escalation methodology for FAGs to a new formula tailored to Local Government cost movements (perhaps involving a combination of the Australian Bureau of Statistics (ABS) Wage Cost Index and Construction Cost Index coupled with population growth).

5. That the Industry Plan strengthen the information base used to inform and influence policy, legislation and revenue frameworks at State and Federal level and that the document provide guidance and secure resources to assist individual Councils to improve their performance in a more systemic manner. Investment by the State and Federal Government and Councils in the processes described in the plan is recommended.

Our theme advice is that we are confident however that Local Government's presence and influence can grow, provided it is able to demonstrate strong community support for its role and achievements and consistent, efficient performance in the services it provides.

Chapter 4 A changing community and the strategic direction and role of Local Government

Overview

Local Government has periodically demonstrated a capacity to make 'step changes' in its role and functions. Generally this has been in response to new legislative requirements rather than proactively leading change to address changing economic and social conditions in Western Australia.

In the 20th century, changes in the nature of the economy, changes in legislative requirements and various reviews have impacted across the sector. While some boundary rationalisations have proceeded in the metropolitan area (notably in the 1940s and 1990s) much of rural and regional Western Australia has a boundary framework shaped one hundred years ago.

A small number of voluntary amalgamations have occurred. Our observation is that the industry has a history and culture that regards boundary adjustments as predatory. Council and community resistance to enforced change is deeply embedded and is resisted accordingly.

Local Government in Western Australia dates back to 1838 with the enactment of the Towns' Improvement Act. This statute authorised the establishment of Town and Country Trusts for the purpose of building roads. Boundaries were drawn as new settlements occurred in isolated areas and as development spread, new 'authorities' were established between existing ones. The precursor to today's Local Government system was established in 1871 with the passage of the Municipalities Act and the Road Districts Act. By the end of that year there were eight municipalities and 21 road boards. By 1910 there were 147 authorities across Western Australia. Since 1901, the social and economic nature of Western Australia has changed dramatically as evidenced in the following table summarising changes in the distribution of the population.

TABLE 4.1 – CHANGES IN WESTERN AUSTRALIA POPULATION DISTRIBUTION 1901 & 2001⁷

	1901 POPULATION DISTRIBUTION (%)	2001 POPULATION DISTRIBUTION (%)
Capital City	32	64
Rural	61	17
Coastal	7	19

A significant driver of this change attaches to changes in agricultural practice and improvements to transport, communication and business practice. As an illustration the average total area of a farm holding in the central wheatbelt has

⁷ B. Salt, *The Big Shift*, Hardie Grant Publishing, 2005, p 64.

increased from 1,404 hectares in 1961 to 3,571 hectares in 2001, an increase of almost 250%. The number of farms have fallen accordingly from 22,000 in 1971 to 12,778 in 2001.

The paradox is that while significant change has occurred, and is still occurring in our communities (urban and rural), the number of local authorities serving communities has remained extraordinarily constant since the early 1900s and in fact has grown by only 2.08% since 1991. Elsewhere in Australia there have been substantial reductions in the numbers of Authorities servicing State populations with the number of authorities decreasing by 27% across the nation since 1991.

**TABLE 4.2 LOCAL GOVERNMENT AUTHORITIES IN WESTERN AUSTRALIA
1910–2004⁸**

1910	1991 ^a	2004-05 ^b	% change 1991-2004
147	138	144	2.08%

The sweeping structural reform that has occurred in the rest of Australia has not happened in Western Australia. The total number of Local Governments has gone from 147 in 1909 to 142 in 2006. Since 1945 only 18 Councils have been abolished, while a number of new ones have been created. The newly created Councils include: Tammin in 1948, Mandurah in 1949, Kwinana in 1953, Coorow in 1962, Exmouth in 1963, Jerramungup in 1982, Ngaanyatjarraku in 1993, Cambridge, Victoria Park and Vincent in 1993, and Joondalup in 1998.

In WA, during the 1991–96 census period, there was a net movement to the largest centres in the inland regions from other inland areas. Unlike the Eastern States, WA has few inland regional centres and has a small and dispersed non-metropolitan rural population. This exacerbates the problems associated with representing and delivering services to communities experiencing population decline.

There is another challenge associated with the rural population decline – the increasing exodus of younger people. This trend is reflected in the ages of people engaged in rural work with fewer young people entering agriculture to take the place of ageing workers and the attraction of wages and conditions in the resource sector. “In the early 1950s almost 11% of persons employed in agriculture nationally were under 20. 21% of males and 15% of females employed in agriculture were aged 20 to 29. By the mid 1990s these proportions had fallen to 16% and 11% respectively”⁹.

⁸ K. Sproats, *Inquiry into Local Government structure in inner and eastern Sydney*, New South Wales Department of Local Government, Sydney, 2001.

^a K. Sproats, “Comparisons of agendas and processes in Australian Local Government”, Paper presented to the Local Government in Queensland Centenary Conference, August 1996, p. 5.

^b Department of Transport and Regional Services, *Local Government National Report 2004–05*, Commonwealth of Australia, Canberra 2006.

⁹ J. Pollard, ‘A hundred years of agriculture’, Australian Bureau of Statistics, January 2000, <http://www.abs.gov.au/Ausstats/abs@.nsf/90a12181d877a6a6ca2568b5007b861c/3852d05cd2263db5ca2569de0026c588!OpenDocument>

“The definition applicable in the 1950s is not applicable to 2006. We are more mobile and prepared to travel to get what we want. If services are not provided in one centre we will happily travel to another centre to access them.”

Shire of Merredin submission p 1.

Role of Council

In our interim report we explored the legislatively defined role of Local Government. Much of the focus in the current Act describes the 'process' of Local Government, rather than the outcomes or results towards which good local governance is applied. As a consequence there is little precision (indeed agreement) as to what the natural and appropriate role of a Local Government.

“Notwithstanding that the role and responsibility of Local Governments have been defined through the Local Government Act and other legislation, substantial effort is still required in reducing the overlap and duplication of service delivery with the other layers of government.”

City of Stirling submission p 2.

Amendments to the Local Government Act introduced in the 1990s enable Western Australian Councils to operate under a general competency framework in which the role of a Councillor is defined in Section 2.10 as to:

- represent the interests of electors, ratepayers and residents of the district;
- provide leadership and guidance to the community in the district;
- facilitate communication between the community and the Council;
- participate in the Local Government’s decision-making processes at Council and committee meetings; and
- perform such other functions as are given to a Councillor by this Act or any other written law.

As a consequence Local Government now routinely conducts an extraordinarily wide range of activities and functional roles. A activity dictionary description of these activities was provided by WALGA and is available on the website www.systemicsustainabilitystudy.com.au.

The lack of 'role clarity' was raised in a number of Dialogues as a source of industry vulnerability in the context of the cost shifting debate as authorities are not always able to, or willing to, evaluate the impact of a grant of funded activity on other Council operating priorities.

There is a sense that the diversity of the political charter of the Council can reduce focus and may blur the political advocacy of Local Governments. Our view is that representing the political aspirations of the community is the most important role of a Councillor and closely reflects the legislative definition of the task.

In the Socio-Cultural Viability Study¹⁰ the authors described a sustainable Local Government as one that has good governance and most adequately addresses the following issues:

1. Community of interest;
2. Accessibility to and quality of services;
3. Environmental and geographic fit;
4. Population;
5. Financial viability;
6. Capacity to represent and engage community;
7. Economic efficiency; and
8. Community attitudes and expectations.

Community of Interest and the future shape of Local Government

We were interested in the relevance and rigour of the concept of 'community of interest' and considered pertinent national or international models as may be useful in informing the future sustainability of Local Government in Western Australia.

Our advice is that the concept lacks consistent or rigorous definition linked to lack of agreement on appropriate assessment criteria and may in fact be irrelevant in determining which boundaries or catchments could be used to shape and inform Council boundaries in the future.

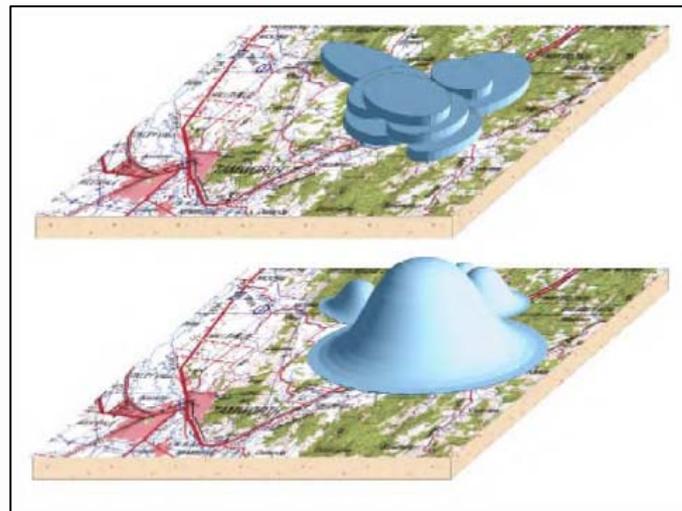
A model for determining community of interest¹¹ is found in *An Eco-Civic Regionalisation for Rural New South Wales* (Authors David Brunkhurst, Phillip Coop and Ian Reeve).

This model assessed various dimensions or measures of community of interest and attempted to simulate them through modelling.

¹⁰ Burow, Jorgensen and Associates, Best Practice Management and Administration, Consultancy Commissioned by the Systemic Sustainability Study, WALGA, June 2006

¹¹ D. Brunkhurst, P Coop and I Reeve, 'An Eco-Civic Regionalisation for Rural New South Wales', Institute for Rural Futures and Centre for Bioregional Resource Management, February 2004, p 14.

FIGURE 4.1 MODELLING COMMUNITY OF INTEREST



Clearly, Local Government boundaries that dissect these communities of interest the least are the ideal models.

In our interim report we recommend that the following definition of community of interest be adopted :

A real or perceived sense of community or belonging to a locality that comes from a critical mass of people having common interests in similar social, economic, environmental, recreational, historical attachment or other matters of common interest.

This definition of community of interest has several important dimensions:

- **A sense of belonging;**
- **The intersection of various catchments** – reflected in a range of social, economic and recreational activity, and
- **A critical mass** – this dimension may prove important in better qualifying the viability of service preference, quality and availability.

“The Panel’s definition of Community may ‘fit’ into the rural context but not in the metropolitan setting. Metropolitan communities do not have defined boundaries and may pursue common interests (i.e. economic, recreational, cultural attachment) in areas other than their own municipality. The Panel asks Local Governments to consider how they would define and measure the ‘sense of community’. It is suggested that a substantive effort would have to be placed into gathering qualitative data from ratepayers and residents to extract common perceptions of the wider community.”

City of Stirling submission p.3.

With superior transport and electronic information networks and changed retail and commercial preferences many now recognise that our sense of belonging to a particular community of interest can simultaneously be local, national or even global.

Fluid capital and labour markets, the knowledge economy and population movements have had considerable influence over, or impacts on, traditional Local Government boundaries and communities of interest. In Western Australia fly in/fly out (FIFO) working arrangements are an illustration of a widespread work practice for which Local Government is yet to develop a statewide response addressing impacts on 'home' and 'host' communities. Similarly, the significant continuing increase in the Perth population and the decreasing population in regional and remote areas are yet to be reflected in changing Local Government boundaries or jurisdictional roles.

"The sense of place and belonging that most residents feel in relation to their community is strongly influenced by the history of place. And also, historical communities of interest encourage the engagement of people in civic affairs"

Town of Cottesloe submission p 3.

Our research indicated that people's sense of belonging is strongest on a specific suburb/locality level rather than within a Local Government's broader boundaries. Given the possibility for attachment to exist with varying degrees of intensity and to varying spheres of interest, it suggests that there is no 'optimal' size or shape for a community of interest.

FIGURE 4.2 LEVELS OF ATTACHMENT



The other dimension to our consideration relates to activity clusters and service levels. The Brunkhurst model attempts to capture this dimension by incorporating all the activities of citizens.

"As society diminishes the significance of "natural community supports" and general levels of isolation grow, the ability for government to enhance the sense of community will become increasingly significant"

City of Subiaco submission p 5.

Towards Service or Activity of Interest Clusters – A new strategic direction for Local Government

A more practical approach may be to focus the Council of the future on "ensuring or deploying" services rather than direct provision of a particular service over its natural "community of interest".

Most Councils already source a range of services for their communities from across the state – similarly their advocacy for their communities does not end at the Council border. Three broad categories for activity of interest can be defined as:

- Services sourced a local level (either from Council staff or purchased from local suppliers);
- Services sourced from neighbouring authorities or the market or on a regional basis; and
- Services sourced on a state (industry-wide) basis but consumed or deployed at the local level.

As a consequence it may be increasingly more practical to apply “activity of interest” rather than “community of interest” as a key criteria for determining boundaries.

“It is of great benefit to Natural Resource Management when there is a co-occurrence of boundaries – i.e. natural catchments with local political ones. Serpentine-Jarrahdale is, virtually, one catchment which has assisted it to deal with water resource matters as well as giving it, at a more cultural level, a sense of unity.”

Peel-Harvey Catchment submission p. 2.

In the interim report we proposed a model for defining a Local Government’s boundaries according to a wide range of dimensions. Having discussed this with the industry we believe that this definition is unhelpful given the modern fluidity of Australian society and continuing changes to consumer preferences, communication methods and enabling technologies. Greater attention needs to be paid to the connections between political representation and effective service delivery. Of these, service delivery is already subject to substantial change and has a material impact on our sustainability and efficiency considerations.

What may be more practical is to ensure there is more emphasis on planning for service delivery according to service delivery ‘communities of interest while political decisions should be made according to demographic ‘communities of interest’. These two basic principles or dimensions (if supported in the industry and the community) may then provide the basis for further change in the industry.

As a consequence, the Panel considers it may be more helpful to focus on mechanisms and incentives to assist Councils who wish to pool or share service capability while retaining local political representation. Over time, communities and their elected leadership can then make further choices which may see greater use of regional and zone structures with elected representation progressively aligning with new structures.

PANEL RECOMMENDATIONS

6. The Panel recommends that Local Government adopt a strategic direction over the next decade towards two foundation roles:

- Representing the political aspirations of its communities and their citizens; and
- Ensuring delivery of efficient and effective services and infrastructure.

These two roles do not necessarily have to have contiguous boundaries or catchments. Accountability for funding and securing resources should continue to be based on the community of interest boundary.

7. It is recommended that the Local Government Industry Plan give detailed attention to mechanisms and incentives to assist Councils who wish to pool or share resources on an agreed basis. Where Councils determine to proceed with amalgamation processes, the plan should also address transition guidelines and the role of government partners in one-off capital incentives to the participating Councils to ensure successful change and better community service and infrastructure outcomes.

Chapter 5 Financial Sustainability

Overview

Our research found considerable challenges to Local Governments' financial sustainability in Western Australia. These challenges attach to the adequacy of the funding mechanisms available to the industry and the policy and regulatory requirements determined by other governments.

It is also fair to say that in some cases Local Government has made poor investment or program choices – often without a full understanding of the whole-of-life impacts on communities of service costs.

We also observed that some financial decisions are taken (or consciously deferred) with significant inter-generational impacts. There is also a lack of coherent, whole-of-industry financial information to assist individual Councils in their decision-making. At an industry level this reduces the capacity of industry leadership to demonstrate that Local Government is an effective and competent custodian of taxpayer funds.

Review of Financial Sustainability Performance

Access Economics' report, *Local Government Finances in Western Australia* adopts an assessment approach which is not dissimilar to that likely to be used by a credit rating agency. For governments, the credit rating approach considers both the cash position and the obligations of the sector.

This perspective is congruent with the principle that the Local Government sector is an autonomous and responsible sphere of government in control of its own financial destiny.

When the methodology is applied (See Diagrams 5.1 and 5.2) across 142 authorities, an operating deficit ratio of more than 4.0% is observed for the industry as a whole. Individual authorities whose operating deficit ratio was greater than 10% were assessed as financially unsustainable.

The model has a performance assumption embedded in it – that being 10% off the pace was a gap that could progressively be closed over a ten-year period using own-source revenue.

Authorities with a larger challenge will struggle to achieve this measure of sustainability without recourse to other forms of revenue or assistance, or without service reductions or radical reductions in embedded costs.

DIAGRAM 5.1 METHODOLOGY FOR INDUSTRY-WIDE PERSPECTIVE ON FINANCIAL SUSTAINABILITY

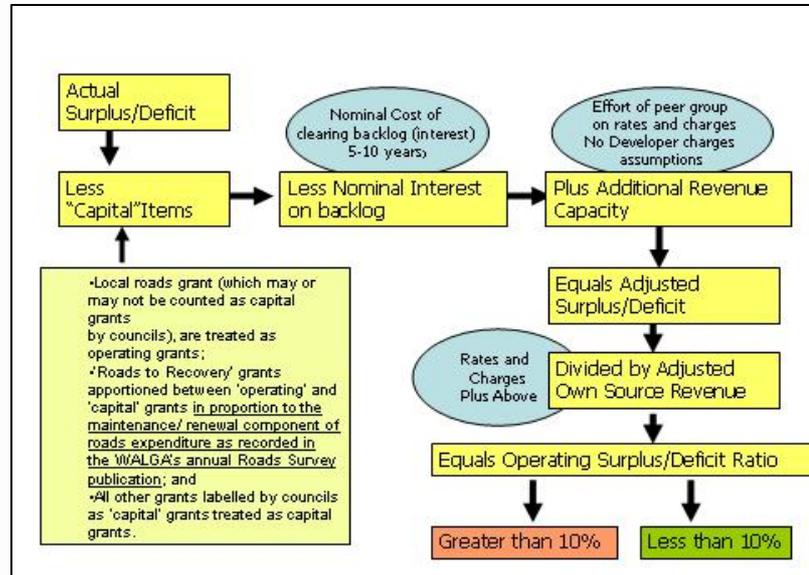
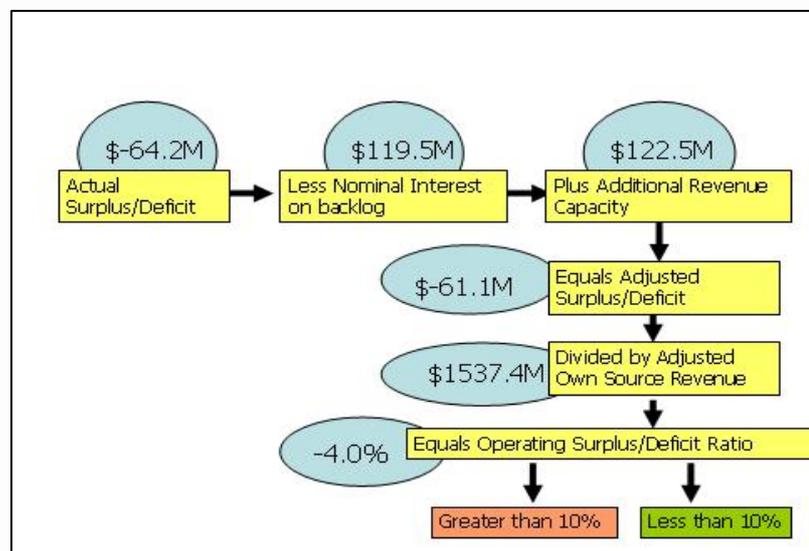


DIAGRAM 5.2 METHODOLOGY FOR INDUSTRY WIDE PERSPECTIVE ON FINANCIAL SUSTAINABILITY



Local Government Financial Health Check

- The sector is responsible for \$12.347 billion in capital, invested primarily in non-financial assets that are very significant for the Western Australian community;
- Local Government's balance sheet is very strong with the sector being a net lender;
- The use of debt by Councils is nominal – on 2004–2005 information, only 16 Councils had net borrowings in excess of 5% of the capital they employed. 60 Councils (or 42% of WA Councils) were net creditors with holdings of unrestricted cash and securities exceeding their total liabilities;
- On average, WA Councils registered operating deficits in 2004–05 that amounted to 4.5% of their own source revenue;
- There is approximately \$122.5 million in additional revenue available for the sector were it to adopt the rating behaviour of peer group Councils and if peer practices in fees and charges were achieved;
- Rather than incurring debt in order to finance their annual operating deficits Councils have been diverting capital revenue (such as capital contributions, capital grants and the proceeds of asset sales) to this purpose;
- This has resulted in an infrastructure backlog of \$1.75 billion, or 14% of the total value of Council non-financial assets in WA; and
- When the infrastructure backlog is considered, 83 Councils are deemed to be financially unsustainable.

Council Scale

The WA Councils who are financially unsustainable have a range of structural characteristics. Financial sustainability does not appear to be too much of a problem for metropolitan councils in WA, with only three such councils (or 10% of metropolitan councils) assessed as unsustainable.

Instead, the councils whose finances are most likely to be unsustainable in the longer term are mainly regional councils, and those with declining populations and small population bases at that. We have assessed 70% or so of each of these council groupings as financially unsustainable. Three-quarters of the councils we have assessed as being unsustainable are councils in the regions without large towns.

In WA, to an extent not evident in either NSW or SA, financial unsustainability is a problem particularly prevalent among smaller and/or declining population regional councils. It is hard to deny that this is evidence of a structural problem within Local Government in WA.

**TABLE 5.1: FINANCIAL SUSTAINABILITY ASSESSMENT:
BY TYPES OF COUNCILS**

Type of council	Councils whose long-term finances are assessed as unsustainable:			
	number	% of total	% of type	% of State pop'n
Metropolitan	3	4%	10%	5%
Regional, with large towns	19	23%	70%	11%
Regional, without large towns	61	73%	71%	5%
Above-average growth	13	16%	45%	8%
Declining population	53	64%	75%	9%
Largest 25%	11	13%	31%	12%
Smallest 25%	24	29%	69%	1%
All WA Councils	83	100%	58%	21%

31% of the largest councils and 45% of the above-average growth councils are also assessed as financially unsustainable. This suggests to us that more factors are at work in explaining the sustainability of a Councils long-term finances than just whether it is small in size or has stagnant growth characteristics.

The councils whose current policies seem unsustainable over the long term are mainly regional-based councils, which include most of the State's smallest and declining population councils. This is evidence of a structural problem in WA's Local Government sector not apparent in NSW and SA. Larger as well as above-average growth rate councils are sufficiently well represented among those whose finances we would classify as unsustainable to indicate that more factors are at work in explaining the sustainability of a Councils long-term finances than just its small size or stagnant growth.

The existence of chronic operating deficits and a substantial infrastructure backlog are clear evidence that an intergenerational equity transfer is occurring. We believe that the fundamental issue behind Local Government financial viability is the effectiveness of the sector as a custodian of community assets and of the aspirations of future generations.

"Long-term financial viability underpins the overall sustainability of Local Government. Without this, Local Government's capacity to provide strategic leadership, engage effectively with the community and provide good governance will be significantly reduced. In addition, it is impossible to maintain existing facilities and services and develop new ones."

Outer Metropolitan Growth Councils' Submission (2) p 3.

The thrust of the findings in our interim report is that Local Government faces a series of systemic exposures. While there are clear failures in resourcing and the revenue framework available to Councils it is also clear that there are issues which go to the prudent stewardship of community assets and services. Some

Councils, are working proactively to address the future financial sustainability of their operations – others have few options available to redress the challenge they face, or simply await contributions from other governments to ensure they can maintain baseline activities.

- Operating deficits, and their frequent co-existence with substantial infrastructure backlogs, are symptomatic as much of deficiencies in Council spending and revenue policy frameworks – compounded by poor information and understanding of asset management – as they are of shortfalls in the level and escalation of grants from other governments and any past cost shifting;
- The current deficient policies and practices evident across Local Government in Australia relate to the treatment of depreciation and the measurement of asset values, poor asset management systems and policies, and the inadequate monitoring and reporting of a Councils financial position and performance;
- Where financial governance is not well developed in some Councils it is not surprising to find a lack of community understanding of the true costs of current infrastructure and service commitments; and
- Improving such policies and practices would not only prompt Councils to do more to ensure their own financial sustainability, but might also assure governments and the broader community that investment in the future of Local Government is a prudent and valued use of taxpayer funds.

Local Government Funding Mechanisms

In exploring the financial sustainability of Local Government we considered the ability of Local Government to raise funds. Our view is that a prerequisite for an autonomous Local Government sector is that it is able and willing to fund its services. Without this capacity the sector remains captive to the political will of other spheres of government.

Rating Mechanism

Under the *Local Government Act 1995*, Councils only have the power to set a rate which is expressed as a rate in the dollar of relevant value of rateable land within its district. The Act provides that a general rate on rateable land within a Councils district:

- may be imposed either uniformly or differentially;
- may involve a specified area rate on rateable land within a portion of its district for the purpose of meeting the cost of the provision by it of a specific work, service or facility; and
- may involve a minimum payment which is greater than the general rate which would otherwise be payable on that land.

In their assessment of the general rating mechanism in Western Australia Access Economics concluded:

“Overall, rates revenue is predictable and stable and allows for a fairly high level of local financial autonomy. The ability of Councils to raise revenue depends on local political will, local household income, and any constraints that the State government may impose. Generally, the

rates base is not itself a constraint on Council revenue and most Councils do not need new forms of taxes to survive. Also, the Local Government rating system generally meets the criteria of administrative simplicity and efficiency, and – if administered carefully – is vertically and horizontally equitable.¹² This is because the rates revenue is predictable and stable and allows for a fairly high level of local financial autonomy.

An efficient tax system is also one for which the costs arising from ‘distortions’ to consumption and production are low. Taxation of property values is generally considered non-distortionary and therefore efficient because the taxation of land does not affect the total supply of land. Moreover, a tax on land value has little effect on the amount of housing consumed or produced. It follows that taxes on land value have only minor efficiency (distortionary) effects.

Overall, the rates base can be viewed as an equitable base for taxation. It provides Councils with a reasonable capacity to produce fair outcomes, where rates are related partly to services (the minimum rate) and partly to capacity to pay (the ad valorem rate on property values). In addition, because the tax base (land) is immobile and easily identified, tax cannot be evaded.” (Chapter 4)

Rate Setting

A very significant proportion of Local Government revenue comes from rates. The balanced budget calculations of the WALGGC confirm that the residential, commercial and industrial rates equate to over 70% of Local Government revenue. Access Economics found that Local Government has vigorously applied the rating mechanism over the last four years. On average, across Western Australian Councils over the years to 2004–2005, per-property residential rates revenue grew at an annual average of nearly 2.5 times more than the consumer price index.

We believe that this shows willingness and capacity to use the rating mechanism to fund activities. However, rating effort has not been evenly applied with some Councils willing to rate more heavily than others. The methodology applied by Access Economics to estimate extra rating revenue¹³ found that WA Councils could more than halve their operating deficit ratios if those among them with below-par rating and cost-recovery efforts lifted their effort to match that of peer group Councils. This would result in around an 11% increase in these Councils’ own-source operating revenue. During dialogues a number of representatives commented on the political nature of the rating decision and that “hard” decisions are occasionally deferred to avoid the Council electoral cycle. The paradox is that some Councils cite a “zero rate increase” as a highly positive achievement, notwithstanding the presence within their authority of an unfunded infrastructure backlog.

¹² Vertical equity means that those with a greater capacity to pay should bear a bigger share of the tax burden. Horizontal equity means that households with a similar capacity to pay should pay approximately the same rates.

¹³ Access Economics, *Local Government Finances in Western Australia*, consultancy for the Systemic Sustainability Study, WALGA, June 2006, pp 43–46.

We acknowledge that all rating decisions can be politically challenging. This is the nature of politics and the challenge of leading and governing in a community context.

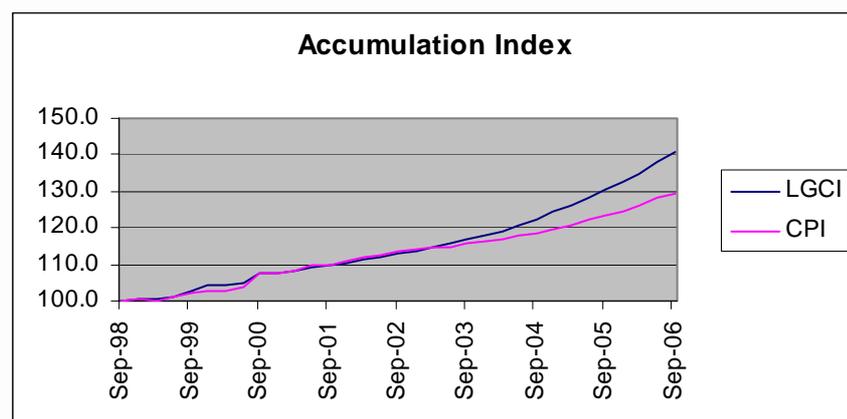
We were encouraged by practical illustrations of how Councils are working to set long run direction and plans and are applying revenue and rating frameworks to ensure these goals are achieved. As an illustration, we were informed of a Council with a policy of consistently charging 3% more than CPI.

This policy, to an extent, depoliticised the annual rating decision for this particular authority by linking the rating settings to the financial plan for the Council. The effect has been to create better fiscal discipline and planning certainty. Community engagement is focussed on the long run vision for the Local Government and the services, assets and amenities it aspires to provide, develop and maintain on a life cycle basis. The Panel encourages Councils to establish policy frameworks that link rating and revenue settings to a long run (10 year plus) financial plan.

Frequently, rate increases are compared against the Consumer Price Index (CPI) and this has considerable validity as it is a very good proxy for the capacity of residents to pay rates. Unfortunately there is a considerable difference between the costs borne by households and those carried by their Local Government.

The Panel notes that WALGA has established a Local Government Cost Index (LGCI)¹⁴ to monitor the costs borne by Local Government. Over an 8 year period, Local Government costs have increased by almost 10% more than their revenues.

CHART 5.1 ACCUMULATION INDEX¹⁵ OF LOCAL GOVERNMENT COST INDEX AND CONSUMER PRICE INDEX, SEPT 1998 TO SEPT 2006



¹⁴ The Local Government Cost Index incorporates the construction costs borne by Local Government.

¹⁵ An accumulation index measures the cumulative impact of successive increases in an underlying variable.

PANEL RECOMMENDATIONS

8. A best-practice approach be developed to ensure uniformity in considering the measures that should be undertaken to reflect the costs faced by Local Government in making rating decisions and setting fees and charges.

Special Area Rating

The Act allows Local Government to apply differential and special area rating. These forms of rating create flexible policy choices for Local Government.

Special area rating is growing in significance because of trends in property developments which involve relatively intense investments in open-space infrastructure. These newer developments frequently require a much higher level of maintenance and infrastructure to match new community expectations for treatments and amenities such as lakes, boardwalks and so forth, than may have been routinely provided in residential areas developed in earlier times.

One Outer Metropolitan Council privately submitted that almost 80 % of the rates from a new development would be invested in maintaining the condition of the area. This required rates to be almost 200% higher than those for other residents in order to ensure that the newly developed area made a matching contribution.

Capturing the full costs of such developments is a very difficult task that requires a consistent approach from all Local Governments. There is also a real challenge in maintaining such disparate rating levels on an ongoing basis.

Gross Rental Value and Capital Improved Value

The use of Gross Rental Value as the framework for residential rating tends to lead to an even distribution of rates between affluent and non-affluent areas. The GRV model faces a growing challenge on equity grounds.

The recent boom in property prices has increased the difference in value between various rateable residential properties in WA, but this is not necessarily reflected in Local Government revenue outcomes determined by changes to the Gross Rental Value.

An alternative for exploration by the industry and government is a Capital Improved Value (CIV) rating framework which takes into account the total value of the property including all land, buildings and improvements.

This system may ensure a fairer and simpler approach as the distribution of rates is based on the property's true residential use - whether modest dwellings, blocks of flats or units, or substantially up-graded or developed properties. The Outer Metropolitan Growth Councils' Submission supports a rating system that provides Local Governments with greater flexibility, (including the use of CIV) when levying rates.

PANEL RECOMMENDATIONS

9. WALGA campaign for greater flexibility and differentiation in the rating and own-source revenue options available to Local Government. This may be particularly useful in circumstances where Council boundaries change and larger geographical areas with greater diversity in size and nature of individual communities are incorporated within single authority areas.

Mobilising Debt for Local Government Infrastructure

In Western Australia, ratepayer equity is the principal source of capital employed by WA Councils. Debt capital is little used by Councils.

**TABLE 5-2 LEVEL AND COMPOSITION OF SOURCES OF CAPITAL
ALL WA COUNCILS, 30 JUNE 2005**

	\$M	%
Net financial liabilities (or 'debt capital')	-22.6	-0.2%
Ratepayer equity (or 'equity capital')	12,803.2	100.2%
Total sources of capital	12,780.7	100.0%

For Councils (as for corporations and other governments), there is no right or wrong level of financial gearing. It is more a question of the level of gearing that can be supported by a Councils revenues and net cash flows.

External borrowing can be an appropriate financing source in the right circumstances, especially to fund the acquisition of new non-financial assets or the upgrading of existing assets (as distinct from funding routine maintenance and the renewal of existing infrastructure assets which both should be funded out of internal cash flows). Use of borrowing to finance upgrading or expansion of infrastructure would then free up internally-generated funds which should be devoted to financing maintenance.

The long-term decline in Councils reliance on borrowing needs to be reversed to allow more flexibility in Local Government funding. Any limits on borrowing for the purpose of acquiring new infrastructure assets within the Local Government sector should be set - based upon expert advice and accepted standards of prudence - by reference to a Councils long-term financial capacity to service debt, rather than an anti-debt mindset.

"Defining a best practice debt policy is supported. However, in developing such a policy it would be important to recognise the differing capital requirements of individual Local Governments and changes to the economic environment that make the use of debt either more or less attractive. Nevertheless, this must not be binding on future Councils."

City of Stirling submission p 2.

A number of Councils are reviewing their asset management plans. The Outer Metropolitan Growth Councils' (OMGCs) submission¹⁶ advised that member Councils were adopting borrowing strategies to meet the infrastructure needs of future generations. They note that these strategies have resulted in significant increases in the total interest-bearing liabilities but that debt servicing ratios remain low.

PANEL RECOMMENDATIONS

10. Individual Councils reassess their debt funding levels so that a modern and efficient capital management approach can be adopted.

11. A best-practice guide for debt funding of infrastructure be developed and that training in modern capital for Councillors and staff be introduced along with other capacity building measures designed to improve financial expertise, technique, systems and outcomes for Local Government and the communities it serves.

Fees and Charges

Fees and charges provide Councils with an important form of own-source revenue. \$517 million worth of fee revenues were generated in 2004–2005. Generally, the basis for determining a fee or charge is not limited to the cost of providing the service or goods. However, in prescribed circumstances, regulations may prohibit the imposition of a fee or charge or limit the amount of a fee or charge. In addition, Councils raise other non-investment revenue through fees and fines, operating contributions and from other sources.

Table 5–3 indicates the level and composition of WA Councils' revenue from fees and charges in total.

**TABLE 5-3: FEES AND CHARGES
BY TYPE, ALL WA COUNCILS, 2004-05**

Category of Fees and Charges	\$M	%
Fees and fines	15.2	2.9%
<i>Plus</i>		
Service charges	97.0	18.7%
<i>Plus</i>		
User charges	322.1	62.2%
<i>Plus</i>		
Operating contributions	32.3	6.2%
<i>Plus</i>		
Other income (not including investment income)	51.3	9.9%
<i>Equals</i>		
Fees and charges	517.9	100.0%

¹⁶ Outer Metropolitan Growth Councils, Submission to Systemic Sustainability Study, October 2006.

In New Zealand, legislation requires that Councils identify the beneficiaries of services that they provide and attribute costs to them. Councils are then expected to raise funds according to these cost attributions, albeit with some modifications in the light of factors such as affordability, market neutrality, acceptability and consistency with strategic policies.

A submission from the Perth Economic Development Agency recommended a mechanism for pricing to reflect the true costs and relevant externalities associated with providing infrastructure currently being met by Local Government. Their view is that this could include levies on key user groups related to freight movement, vehicle sales, taxi fares, petrol taxes and other road-related users to raise the required funds to adequately manage transport infrastructure.

We observed that 'rising community expectations' are frequently cited as reasons for increasing the range and scope of Local Government services. Research commissioned by the study found that there was frequently little connection between community expectations and fees and charges.

Access Economics estimated that in 2004-05, WA Councils on average recovered 34.1% of own-purpose operating (and depreciation) expenses through the fees and charges they impose.

"There needs to be a mechanism for pricing to reflect the true costs and relevant externalities associated with providing infrastructure currently being met by Local Government. This could include levies on key user groups related to freight movement, vehicle sales, taxi fares, petrol taxes and other road related users to raise the required funds to adequately manage transport infrastructure."

Perth Economic Development Agency submission p 4.

PANEL RECOMMENDATIONS

12. Councils develop an output-based reporting framework for activities to more clearly enumerate the costs and beneficiaries of services. This should incorporate a mechanism for pricing to reflect the true costs and relevant externalities associated with Local Government services.

State Mining Agreements Review

51 of the current 63 State Agreements contain clauses that limit the valuation and rating of agreement land to unimproved value (UV). This issue has a particular resonance in the north west and for other Councils where State agreements are in prospect.

State Cabinet approved a review of this matter on 11 May 2004. The State Government has subsequently committed to phase out clauses in State Mining Agreements that limit Local Government rating to UV. Advice from DOIR indicates that this review will conclude in 2007.

A recent commitment from Rio Tinto brought to six the number of mining companies that have agreed to participate in the process aimed at phasing out the proscribed rating arrangement from current agreements.

PANEL RECOMMENDATIONS

13. WALGA continue to work with the State Government and the mining and resource industry to ensure that all local communities share directly in the benefits of the State’s natural resource strengths and that State Agreements where applied should be to ensure that service, capacity and infrastructure impacts on Local Government services and communities are funded and resourced in an appropriate manner.

Developer Charges

Developer charges are lump-sum charges designed to recover costs incurred in the provision of infrastructure from the beneficiaries of that infrastructure. They are typically levied on the owners/developers rather than the occupiers of land or the users of specific services.

Access Economics estimated that in 2004–05 developer charges funded an average of around 20% of all additions to non-financial assets, as described in Table 5–4.

**TABLE 5–4 DEVELOPER CHARGES
WA COUNCILS, 2004–05**

	\$M	%
Capital contributions (i.e., cash)	55.5	35.4%
<i>Plus</i>		
Assets donated (i.e., non-cash)	101.3	64.6%
<i>equals</i>		
Developer charges	156.8	100.0%

The main reasons for imposing developer charges are:

- to augment Council funding by taxing those who benefit directly from infrastructure improvement; and
- on economic efficiency grounds, to levy those responsible for the development so that infrastructure costs are included in development decision-making.

Ideally, developer charges should involve full net cost recovery from the beneficiary, reflect variations in the cost of servicing different development areas, result in new developments meeting no more than the cost of the services provided through developer charges, cover infrastructure expenditures which can be clearly linked to the development and be reliably forecast, and be calculated in a transparent manner so that developers can understand and assess the calculated charges.

“Given that virtually all urban developments are at the expense of environmental assets, there should be developer contributions to assist Local Governments to restore some of the environmental value or create offsets where this has not been done.”
Peel-Harvey Catchment Submission p 3.

New policy settings for developer charges need to address mechanisms to:

- avoid ‘double-dipping’ or overcharging: residents who have purchased property on which a developer charge has been levied to construct capital facilities should not then be asked to contribute monies towards the capital cost from rates or other levies;
- ensure equity on account of incidental benefits delivered to existing ratepayers through facilities to serve new ratepayers; and
- Coordinate State versus local arrangements. Any imbalance between the two is liable to distort the proper pricing of residential land.

The Panel notes that Councils on the outer metropolitan fringe will service approximately three quarters of Western Australia’s new residents between 2006 and 2021, (over 300,000 new residents). These Councils face significant challenges to provide and renew infrastructure to new neighbourhoods and communities. While the use of developer contributions may be more relevant to this metropolitan segment of the Local Government Sector, the Panel sees considerable merit in reviewing the fundamental policy frameworks to ensure appropriate use of developer contributions in developing infrastructure.

“All Local Governments must be required to have a Strategic Plan for their new Local Governments Area and a specific Organisational Development model for every Local government should become a prerequisite before receiving Federal funding.”

Personal submission by CEO of Shire of Broome p 4.

The UDIA, WALGA and the Department for Planning and Infrastructure have also been examining this issue. Their report “Contributions to Community Infrastructure”¹⁷ was reviewed by the Panel. The document outlines a new framework for developer charges. The proposed methodology requires definition of “catchment” areas for the facilities or services, quantification of need and a demonstrated nexus to connect the proportion of use attributed to growth and the proportion associated with servicing the needs of the existing community. A key recommendation of the report is that Local Governments need to develop long-term (5–10 year) community needs plans so that developer charges can be apportioned in a more transparent manner according to their contribution to community infrastructure.

“Initiatives aimed at ensuring all Councils have adequate planning and management systems in place to facilitate sustainability should be encouraged.” City of Wanneroo Submission p 2.

PANEL RECOMMENDATIONS

14. Greater use of developer charges (where appropriate) be applied throughout the State by Councils to assist the creation of new community infrastructure; and

15. Support for directions and principles established by the UDIA, WALGA and DPI in their 2006 review, especially where community planning processes are linked with long run financial and asset management plans to ensure an

¹⁷ Syme Marmion and Co., ‘Contributions to community infrastructure report 2006’, Prepared by the Urban Development Institute of Australia, the Western Australian Local Government Association and the Department for Planning and Infrastructure, September 2006.

appropriate contribution is made for funding and maintaining community infrastructure.

State Government Fee Structure

The Panel encourages Local Government to continue to examine the fee structure that is applied for undertaking various activities on behalf of the State Government. These fees should be routinely assessed to ensure that full cost-recovery occurs where agency or State-determined roles are conducted – notably in respect of licensing and certain planning processes where State-regulated fees apply.

The recently signed Inter Governmental Agreement commits the State and Federal government to ensuring they adequately fund any responsibilities that are transferred between spheres of government. All regulatory fees and charges need to be indexed to ensure they reflect the changing economic conditions of the State.

The Panel encourages an approach which routinely applies whole-of-life funding assessment – applicable to contractual roles, service or agency tasks and capital projects. Councils and the industry as a whole should determine the value of continuing involvement in providing state government services unless these are funded or resourced on a more sustainable basis in the future.

Road Funding

Funding for roads and other infrastructure remains a priority for Councils, particularly in light of the infrastructure backlog documented in the course of this study. Better quality data from Councils on asset renewal gaps across all infrastructure classes, as well as data on growth needs for infrastructure, is required to support campaigning and lobbying as well as more practical applications in asset planning and local management. Improving data quality of data on local roads has also been raised as an issue by the Commonwealth Grants Commission, DoTaRS and others at the Federal level.

While the need for more funding was recognised by the Productivity Commission their conclusion was that heavy vehicles already contribute for their use of the road network through fuel excise and vehicle licensing fees. The challenge is to improve Local Government's performance outcomes from these existing models for funding and to develop more complete and sustainable solutions for the future.

The Panel has also been encouraged to consider how Local Government is impacted by the knock-on effects of Infrastructure investment decisions (or lack thereof) by other spheres of Government. A recent example is the lack of investment in the privatised narrow gauge rail network which has the potential to see millions of tonnes of grain flow to the road network (both State and local). The original contract of sale (2000) allows the owners to close uneconomic rail lines from 2008, unless operations are subsidised. About 1,000km, or a third of the network, has been put in this category. Local Government involvement in the planning of large-scale infrastructure developments by other spheres of Government and the private sector is needed. A number of themes in this regard were set out in WALGA's submission to the

WA Government's Infrastructure Task Force. Continued, influential focus is clearly required by WALGA and the industry as a whole with the single clear objective of a more transparent and sustainable funding model for roads and associated infrastructure.

In building a case for change, the Panel would encourage WALGA to endeavour to work with other transport industry stakeholders to use intelligent transport systems to develop better baseline information for modelling the use of local roads by heavy vehicles. Other alliance-based work with motoring organisations, the tourism industry and others to find common ground for advocacy purposes may be worthwhile.

We note that WA Councils have begun to focus on improved infrastructure asset management with limited resources provided by WALGA (in partnership with LGMA, Institute of Public Works Engineers and DLGRD). So far the journey has involved the focus by WALGA of an elected member on Sustainable Asset Management (which is attracting significant interest) and pilot Councils undertaking the WA Asset Management Improvement Program (based on the Step Program rolled out in Victoria and other States). We note that WALGA is working with the Australian Local Government Association to secure Commonwealth funding to assist Councils in participating in the WAAMI Program and pursuing State contributions to this task.

Metropolitan Councils and larger regional cities also face road and associated infrastructure funding issues – particularly in the provision of infrastructure to support alternative forms of transport, i.e. cycle ways, support infrastructure for public transport, bus shelters, bike stands, etc as well as issues with the attenuation of heavy vehicles impacts on residential amenity.

The ROMAN road management system has been used by all Councils in WA (at the very least for their road inventory data) for a number of years. Work is commencing on a "replacement" ROMAN to address software platform issues as well as the need to update classification codes for deterioration modelling. It is imperative for the advancement of the road network in WA that an affordable, modular road asset management system is available to all Councils. The Metropolitan Regional Road Group is reviewing its policies and procedures and proposes a best practice standard that requires all funding applications be supported by data from an appropriate pavement management system data set.

We have also been made aware of the importance of effective partnerships with Main Roads and DPI to ensure that a quality transport and road network is provided to the whole community of Western Australia. Better awareness of works scheduling by Term Network Contractors in rural communities may present opportunities to leverage the contractors for other Council-based works around core TNC tasks and plant.

Finally, there is an important strategic opportunity available for Regional Road Groups to plan and manage the regional network as a whole (a role well beyond the distribution of funding on a regional and sub-regional basis). This may prove to be a model that adapts to the more efficient delivery of local road services across the network and may in time align with other shared service and structural roles agreed by authorities on a regional basis.

PANEL RECOMMENDATIONS

16. A more transparent and sustainable funding model for roads and associated infrastructure needs to be developed if an estimated \$120 million dollar annual infrastructure deficit faced by the Councils in Western Australia is to be addressed in a sustainable manner.

17. Any campaign position adopted by WALGA and Local Government will require better and more consistent information and quality data to support and inform its policy position.

18. A statewide 'blitz' funded by the industry to ensure accurate, consistent baseline information on road condition and backlog requirements to assist tighter definition of the infrastructure challenge and strengthen the position of the industry in Western Australia in successfully prosecuting its case for better and more equitable road and associated infrastructure funding.

Concessional Rating Treatment

The Panel supports the principle that any concessional treatment-determined legislation or policy by State Government should be funded by way of CSO or similar payment to the authority where the benefit is claimed. This approach is similar in principle to the policy setting applied by the State Government to its "arms length" Schedule 1 Government Trading Enterprises (GTEs) such as the Water Corporation in respect of water rates and rebates.

"Regarding rates exemptions for 'charitable' owned and operated retirement villages, the City of Mandurah's position is that only 'dependent' elements of retirement villages i.e. 'high care' and 'low care' places should be exempted from paying rates, and that 'independent living' should not be exempted. Where a retirement village that has been deemed 'charitable' under the Act provides both care and independent living, only the care component should be rates exempt. To do otherwise represents a significant cost-shift onto Local Government." City of Mandurah Submission p 5.

PANEL RECOMMENDATIONS

19. WALGA continue to press the State Government for consistent CSO-style treatment for revenue forgone by Local Government where State concessional policies or practices are applied to individuals and organisations.

Increasing Funding Opportunities

In calculating the sector's sustainability, Access Economics adopted a conservative approach that "factored in" the potential for Local Governments to

collect “additional” revenue if peer rating effort was applied. Their calculations suggest that the industry could raise up to an additional \$122.5 million dollars.

Table 5.5 breaks this additional revenue capacity down into peer group categories of Local Governments. The largest capacity to harness additional revenue occurs in the groups that have strong actual surplus / (deficit) levels. This suggests to us that the structural problem confronting the sector is deeper than the macro data initially suggests.

TABLE 5.5 ADJUSTED OPERATING SURPLUS / (DEFICIT) RATIOS, WA COUNCILS, 2004–05

	actual surplus/(deficit) (\$M)	<i>less</i> nominal interest on backlog (\$M)	<i>plus</i> add'l revenue capacity (\$M)	<i>equals</i> adjusted surplus/(deficit) (\$M)	<i>divided by</i> adjusted own-source revenue (\$M)	<i>equals</i> adjusted operating surplus/(deficit) ratio (%)
Metropolitan	12.3	24.3	65.2	53.2	993.1	5.4%
Regional, with large towns	-38.5	46.1	25.9	-58.7	348.0	-16.9%
Regional, without large towns	-38.0	49.0	31.4	-55.6	196.3	-28.4%
Above-average growth	-17.3	31.7	48.1	-0.9	581.0	-0.2%
Declining population	-46.7	55.2	27.1	-74.8	276.2	-27.1%
Largest 25%	-13.2	52.1	76.0	10.7	1,193.5	0.9%
Smallest 25%	-6.9	11.9	6.7	-12.2	52.8	-23.0%
All WA Councils	-64.2	119.5	122.5	-61.1	1,537.4	-4.0%

Whether the identified own-source revenue increases materialise – on average – will depend upon the policies adopted by Councils themselves. Much depends upon the willingness of Councils to responsibly address opportunities to improve their revenue-raising effort and the extent to which they are prepared to contain rates disciplines in future.

Our view of financial sustainability begins with the principle that Councils themselves must be able to raise at least a fair slice of the revenue they need to cover the costs of providing services to their communities. If they cannot, service standards must fall, or financial sustainability may be compromised – or both.

Overall, rates revenue is predictable and stable and allows for a fairly high level of local financial autonomy. We consider that the Local Government rating system generally meets the criteria of administrative simplicity and efficiency, and – if administered carefully – is capable of being vertically and horizontally equitable.

Nevertheless, Local Government’s use of taxation on property requires regular year-to-year resetting of the per-property rate of tax because property values

(the 'tax base' of Council rates) increase year-on-year in ways that are unrelated to the cost of providing Council services.

No-policy-change increases in (per-property) rates revenue should keep pace with annual expenses (over the business cycle), where expenses are prudently managed. Policy-change increases in (per-property) rates should be explicitly linked to increases in service standards or quantities.

Access Economics estimates that WA Councils with operating deficits could more than halve their operating deficit ratios if those among them with below-par rates and cost-recovery efforts lifted their effort. This would result in an increase in around 11% in these Councils' own-source operating revenue. We need to be realistic about the political and community impact of a step up in rating practice. Councils should also be aware of the exposure the industry has to the view that it is at times content to accept subsidy rather than exercise the revenue and rating tools it has available to it - against peer standards and performance.

"Decisions on rate rises should be left to the discretion of individual Councils. However it is critical that Councils have a sound strategic financial plan which will address the issue of long term financial viability."

City of Stirling Submission p 2.

A second consideration here is to ensure that supplementary WALGGC funds are deployed into an industry where all authorities are confident that their peers are managing and governing efficiently. Failure to achieve this level of mutual confidence will expose the industry to internal competition for scarce pooled resources with predictable impacts on industry cohesion and leadership.

PANEL RECOMMENDATIONS

20. Local Government adopt a best practice approach to rating that involves a more consistent rate setting process managed by the industry but with appropriate regard to peer effort to ensure that own-source contributions to a sustainable Local Government sector are maximised. Better and more consistent State-of-the-State reporting will ensure greater transparency on own-source revenue performance.

Financial Reporting

The Panel's commissioned research and discussion with the sector emphasises the urgent need to improve and simplify Local Government financial reporting. There are two dimensions to this challenge:

- Consistent, industry-wide reporting for community accountability, regulatory and industry funding purposes; and
- Quality insights on performance and Council status for better, strategic decision-making by Councillors and management.

There is limited training available to help Councillors without accounting skills to understand accounting concepts, let alone frame fiscal strategies, set budget

priorities and monitor results. The complexity of financial reporting and uneven or limited expertise and understanding among some Councillors and senior officers regarding financial governance is acknowledged and may have contributed (in part) to the high levels of financial unsustainability that have been observed.

The widespread operating deficits and their frequent co-existence with substantial infrastructure backlogs are evidence of deficiencies in Council spending and revenue policy frameworks as much as they are of shortfalls in the level and escalation of grants from other governments and any past cost shifting.

Asset Recording and Measurement

The introduction of accrual accounting required the establishment of asset registers to record asset values. In WA the quality of these registers varies – some provide detailed information whereas others are known to be neither uniform nor complete.

The view put to us is that this is, in part, because only limited guidance has been provided on how to classify assets. There are only minimal accounting requirements for Councils to group assets into uniform classes and sub-categories.

One Metropolitan Councils “fair value” of its buildings was recorded at around \$30 million with a written down value of \$17.3 million. These assets were valued for insurance purposes at around \$80 million with around \$50 million in depreciation! With accurate information on these assets, the Council has adjusted its financial plan to address their maintenance requirements.

Access Economics also noted considerable inconsistencies in asset valuation approaches across the sector. Different approaches can change the interpretation of a Councils financial position and performance. ‘Fair value’ valuations of asset items tend to be higher than ‘at cost’ valuations. As long as Councils continue with ‘at cost’ valuations, they risk underestimating their true asset values and can understate the extent of depreciation expenses in their financial reports. Approximately 70 percent of Local Governments use ‘at cost’ valuations. As a consequence the Panel is deeply concerned that the infrastructure backlog described in our interim report may be substantially understated.

Despite the fact that a range of useful life estimates for (apparently) similar assets still exists, Councils are not obliged to use consistent depreciation rates for identical assets. This results in depreciation charges that also show wide variation and impact upon each Councils operating surplus/(deficit).

The consequence is that much of the asset data available to the industry cannot be reliably used by Councils for strategic decision-making or for comparing performance throughout the sector.

External Financial Reporting

Most external financial reporting is historical in nature in Western Australia. The few long-term financial plans that do exist vary considerably in quality. As a result a major means of communicating with the community is being neglected in WA.

- Key financial aggregates are not published as a matter of course, notably annual capital expenditure let alone its renewals, upgrading and expansion components;
- There are no comprehensive Council-by-Council figures on the extent of any infrastructure renewal backlog, a key performance issue. Elsewhere the Panel has highlighted the need for this information to be “industrial strength” if successful funding and resource campaigns are to be pursued by the industry;
- Maintenance expenses are not usually distinguished from other operating expenses in WA Councils’ financial reports – this has been a significant issue for the Panel in promoting a consistent assessment of the underlying financial sustainability of the industry;
- Differences are also likely to exist between Councils regarding the extent that capital-related expenditure is expensed (as maintenance) or capitalised. This gives rise to the possibility that some recorded maintenance expense involves spending that extends the life of existing assets;
- There are apparent differences between Councils in the accounting treatment of grants received from other spheres of government. AAS27’s introduction did not lead to comparability in financial reporting as the information published does not always allow for valid comparisons to be made between Councils, or between years for the same Council;
- While the WA financial management regulations make reporting financial indicators mandatory¹⁸, those prescribed under WA regulations principally focus on balance sheet indicators (among them the current ratio and the untied cash to trade creditors ratio) which by themselves generally are uncertain predictors of the sustainability of a Councils long-term finances; and
- Considerable confusion exists within Local Government about the interpretation of operating statement deficits and surpluses, in particular whether operating surpluses should be measured before or after capital revenue. AAS27 includes both operating surplus measures in a Councils operating statement, with no guidance provided at all as to the relevance of each concept.

Internal Financial Reporting

Given the many inadequacies of external financial reports, it is not surprising that in-house financial briefing papers for Councillors vary in quality with no agreed best-practice format.

Access Economics also observed that much internal reporting within Local Government still has a cash accounting focus, thereby downplaying the operating surplus in the annual Statement of Financial Performance. Traditional cash accounting can easily lead to a misleading picture of commitments undertaken when payments can be accelerated or deferred. For instance, in cash accounting, no provision is made for funding depreciation of non-financial

¹⁸ Regulation 50(1) of the *Local Government (Financial Management) Regulations 1996* requires each WA Councils annual financial report to include a series of financial ratios.

assets, with the result that when such assets need to be renewed there may be no funds set aside for doing so – the very situation that most Councils now find themselves in.

Smarter Use of Financial Information

Improving the quality and usefulness of financial reporting is critical to addressing the financial sustainability challenges confronting Local Government by providing both Councillors and the community with a better understanding of the situation. This investment can also strengthen the basis on which to engage the community in terms of the type, quality and cost of services provided.

In the industry debate around cost shifting there is also an opportunity to better inform the community about which sphere of government is responsible for providing critical community infrastructure.

More generally, Improving such policies and practices would not only prompt councils to do more to ensure their own financial sustainability, but might also assure governments and the broader community that investment in the future of Local Government is a prudent and valued use of taxpayer funds.

Coherence and Uniformity

Information about a Councils finances, whether reported externally or internally, should be relevant and inform decision making. This requires that information be reported in a timely manner and confirm or correct prior expectations about past events or assist in forming, revising or confirming expectations about the future.

The development of uniform accounting policies could take the form either of the WA Department of Local Government and Regional Development developing an accounting policy manual such as the NSW Department of Local Government's *Code of Accounting Practice and Financial Reporting*, or the Local Government Association of South Australia's *A Framework for Local Government Financial Management*.

Such a code could be mandated (as is the case with the NSW code), that where there is a change in Council policy which affects the calculation of performance ratios, the change in policy must be stated, and ratios under the new policy provided for the current period and the three previous years.

To improve the usefulness of information it should be provided in forecast form as well as in historical form. Prospective information should be available in both narrative and quantitative form. The narrative form should provide an assessment of prospects focusing on anticipated changes in the economic environment. The quantitative form should take the form of information about the Councils future financial position and performance based on assumptions about future economic conditions and courses of action.

To ensure uniform forecasts, a standard approach to developing mandatory long-term (10 year)¹⁹ financial plans should be developed. Some Councils already recognise the value of long-term planning for determining revenue setting and strategic infrastructure decisions.

Training should be provided to assist Councillors and Officers apply new uniform standards in strategic decision making. Local government should adopt a clear statement of the role and accountabilities of Councillors for financial governance in general and the financial sustainability of their Councils in particular. The separation of these roles and accountabilities from those of general manager and senior managers could be acknowledged (financial governance is primarily the responsibility of Councillors, and cannot be delegated to a Councils administration).

Obligations required of Councillors should be made more explicit (and strengthened), including the importance of Councillors adopting a whole-of-Council approach and the need of Councillors to be more strategic in their decision making.

Spending and revenue decisions should be taken in a multi-year framework, and against the background of long-term financial rules. Otherwise, the natural short-term focus of political decision-makers may cause Councils to lose sight of future costs of decisions, the best allocation mix and the appropriate timing of spending. A Councils budgetary forward estimates framework should be the first three to five years of its long-term (10 year) financial plan.

Funding of Services

The current funding arrangements for services and infrastructure do not appear to be based on a rigorous policy framework. The current funding approach relies heavily on the use of rates revenue to fund the difference between estimated operating expenses and non-rates revenue each year. Limited consideration is given to the linkage of service beneficiaries to the funding source for each service provided by Council through greater application of user charges.

Each Council should be encouraged to develop and publish a ‘revenue and financing policy’ statement (similar to the statement required of Councils by law in New Zealand), which ensures the adoption of a comprehensive and ‘economic’ approach to funding decisions. Such a statement would state (for example) the role to be played by ‘user pays’ and how any grants shortfalls are to be covered for services provided through grants funding. It would also provide the basis to examine the role to be played by developer charges.

Each WA Council should be encouraged to develop and publish a ‘services policy’ statement as best practice that clearly stating the roles and functions that it is prepared to adopt and specifying its policies regarding the number and nature of services to be delivered and the methods for delivery similar to what is required mandatory in New Zealand. Such a statement can then be the basis for:

¹⁹ Some Councils have already determined to adopt a 20 year view of capital intensity – aligning more closely with built form infrastructure life assumptions.

- all new policy proposals being subject to rigorous analysis; and
- a regular cycle of program reviews.

State of the State Reporting

WALGA should promote and facilitate State of the State reporting using routinely generated, consistent financial Key Performance Indicators to improve whole of industry performance and transparency.

The information should be assembled in a simple, web based format where individual Councils populate the data sets and where the information is available to all in the industry to encourage a strong performance culture and to ensure the focus is kept on best practice themes.

The design of this reporting format will be strengthened by input from across the industry and is identified as a specific task for further development in the development of the proposed Industry Plan.

Given some of the exposures identified in the Access Economics report the State of the State report should (in addition to measures agreed by the industry) also include:

- Revenue side effort against peer group Councils;
- Revenue segmentation;
- Debt Ratios;
- Infrastructure Backlog Quantification and Progress;
- Key Workforce Indicators;
- Service Outputs against peer group Councils.

The data sets should have a strong predictive relationship with the degree to which a Council's finances are likely to be sustainable in the long term and be based upon generally-accepted key analytical balances. A Council should set target values, and where appropriate also minimum (floor) and maximum (ceiling) values, for each of these financial KPIs²⁰.

We also believe that a best-practice model advocating a balanced budget should be promoted by WALGA as the practice standard for individual Councils.

This could be similar to the New Zealand model where a Council's annual income (excluding capital grants) in any financial year must be set at a level that covers all expenses²¹. Such a balanced-budget 'golden rule' would put at the top of Councils' agenda the fostering of intergenerational equity, and so:

²⁰ Independent Inquiry into the Financial Sustainability of NSW Local Government, *Are Councils Sustainable?* Sydney, May 2006, pp.272–274. The NSW Inquiry proposed a series of such indicators, and suggested some indicative target values.

²¹ Refer to the *New Zealand Local Government Act 2002*, Section 100.

1. ensure that each year's ratepayers meet the full cost (including depreciation) of that year's use of services and infrastructure; and
2. provide for the maintenance and replacement of infrastructure assets.

Finally, to encourage the acceptance and understanding of the key financial KPIs applying to Councils, WALGA (or the WA Department of Local Government and Regional Development) should sponsor the annual publication of a compilation and analysis of the comparative financial position and performance of WA Councils, perhaps along the lines of the NSW Department of Local Government's annual *Comparative Information on NSW Local Government Councils* publication.

PANEL RECOMMENDATIONS

21. A working group be established within the framework of the proposed Industry Plan to develop an on line State of the State reporting framework to be hosted by WALGA. Further work is required to define the key data sets to ensure a best practice framework is developed and embraced by authorities across the state.

22. Specific actions to address or strengthen financial capacity and reporting technique are set out across Section 5 – these should be the subject of detailed development and focus in the Industry Plan.

Chapter 6 Asset Management & Infrastructure Renewal

The difficulty with which Local Government is confronted is that the sector manages a substantial amount of infrastructure that *is not being appropriately maintained*. Nor can it be with current revenue streams

With almost \$13 billion in non-financial assets that make a critical difference to the community, an important role of Local Government is to be an effective custodian or steward of this infrastructure. 97% of all capital employed by the sector is invested in non-financial assets and as a consequence asset management is central to good governance, financial sustainability and ensuring an appropriate community legacy for the future.

Overview

The panel observes that many Councils have continued to operate on a cash based approach to asset management. This results in understating the maintenance of infrastructure so sufficient reserves are not kept and can also expose the Council to higher replacement cost at the end of the asset's life.

- A common characteristic of infrastructure assets is that it takes approximately 50% of the useful life before the first 10% of wear indicators become visible²²; and
- Typically asset management costs occur at the end of the asset's life cycle which leads to significant cash-flow management issues.

During the Council Dialogues representatives commented that a disconnection exists between depreciation rates and the actual condition of assets. This disconnect was particularly pronounced in rural communities where it was felt that depreciation represented a "Perth centric" perspective of asset condition or service quality that was just not possible in rural and regional Western Australia.

The Panel considers this perception is due in part to a misunderstanding of depreciation and that depreciation levels may not reflect the actual conditions throughout Western Australia.

Accrual accounting was introduced, in part, so that Councils could focus on the cost of depreciation and maintain reserves to renew/replace ageing non-financial assets. Depreciation is the financial representation of the consumption of the asset over its useful life. It is not a measure of the required maintenance and renewals expenditure on an asset in any given year. Nor does it reflect the actual deterioration pattern of an asset as monitored by an engineer. In fact, for a single asset, straight-line accounting depreciation is likely to overstate the desired amount of annual renewals capital expenditure in the early life of the asset (and understate the status quo renewals capital expenditure likely in the later life of the asset).

²² Independent Inquiry into the Financial Sustainability of NSW Local Government, Are Councils Sustainable?, Sydney, May 2006, pp.129.

The reason accountants depict assets as depreciating by an equal percentage each year is to prompt asset owners to set enough money aside for their eventual renewal. If Councils were to use an engineers' asset degradation path for funding assets, they would delay depreciating them and consequently delay amassing funds for their replacement until they showed wear and tear. By then it would be necessary to fund most of the renewals cost in a short time span, increasing the financial burden on future ratepayers.

The advantage of accrual accounting for depreciation is that it should ensure adequate reserves are set aside for replacing the asset. One identified difficulty is in information gathering. To be useful, accrual accounting must be based on 'fair value' valuations of asset items which tend to be higher than 'at cost' valuations and also involve relatively extensive information gathering compared with historical cost.

Asset Management Accounting

"Local Government need to come to grips with Asset Management principles. Training and education is required to ensure that these principles are adopted" Shire of Merredin submission p 2.

Improving asset management and unifying infrastructure accounting is critical to addressing infrastructure problems, including by giving both Councillors and the community a better understanding of the infrastructure challenge.

Each Council should be working towards adoption of a total asset management system for the whole-of-life planning, funding, acquisition, registration, accounting, operation, maintenance, disposal, and renewal or enhancement of each component of its infrastructure. Minimum asset management requirements should be mandatory although phased in over time and with additional requirements added progressively.

An asset management framework that meets accepted industry standards should include:

- a clear definition of the services to be provided by each of its classes of infrastructure;
- a detailed knowledge of the assets held (thereby allowing predictions to be made about performance);
- the risks associated with managing the infrastructure being well understood;
- asset-related spending distinguishing between spending on the maintenance, renewal, upgrading and expansion of assets; and
- the cost of long-lived assets over their useful lives being accurately recognised.

We recommend that the sector embrace the Western Australian Asset Management Improvement Program (WAMI) that has been developed in partnership with the Local Government Managers Association (LGMA), Institute of Public Works Engineers and the Department of Local Government and Regional Development.

The WAMI program is similar to the Municipal Association of Victoria’s staged asset management improvement program that has been increasing the asset management capability in the Local Government sector.²³ The MAV program has been building infrastructure asset management capacity over recent years by promoting awareness raising of asset management obligations to all Councils, and by providing tools and templates to assist in developing asset management policies, asset management strategies, asset management plans and operational plans. This voluntary program funded by the Councils is delivered through six monthly visits to them by MAV-appointed consultants who identify priority deficiencies in asset management and rate each Council in respect to asset management adequacy through a series of questions and provide targeted training and improvement recommendations to be completed by the next visit.

In the process, accounting inconsistencies should be resolved by requiring:

- a standard format for asset registers;
- regular valuation of infrastructure at ‘fair value’;
- common definitions to enable the maintenance, renewal, upgrading and expansion of assets to be distinguished; and
- a standard depreciation schedule for assets whose total life has not been independently verified by a recognised assessment process or service.

Additional reporting requirements in Council annual reports should be introduced to deal with the infrastructure renewals gap.

On the liabilities management side, Councils should avoid undertaking separate or specific borrowing to finance particular projects or assets, and rely instead on taking a coordinated approach to managing a Councils borrowings and financial investments. Associated with this, Councils should be managing their interest rate exposures in an up-to-date and deliberate fashion.

PANEL RECOMMENDATIONS

23. WALGA champion an accrual based best-practice approach towards asset management for all Councils. This will involve an extensive change of practice for the 70% of Councils that still operate on a ‘historical cost’ basis and cannot occur without a significant investment by the industry and state government in strengthening capacity and technique across Local Government. All asset management reporting should be in accordance with the model described in Asset Management and Infrastructure Accounting.

24. Councils should be encouraged to move towards a renewal-based approach that is consistent with asset management and strategic financial plans.

25. The sector embrace the WAMI program and seek to roll it out to all Local Governments as a key initiative within the proposed Industry Plan.

Asset Management Plans

Along with improving Local Government asset management there is a strong need for strategic decisions to be made around what services to offer and also the level of service that will be provided with an asset. Effective asset management involves allocating resources to maintain community infrastructure, but given the continuous shortfall of funds that inevitably exist, Councils need to make strategic decisions on their asset management.

The decision on which service to provide has, historically, been based on the initial construction costs for creating infrastructure and has seldom incorporated the ongoing costs for operating, maintaining and replacing the asset. Strategic decision making by Councils requires the incorporation of the whole-of-life cost of an asset to ensure that the ongoing and replacement costs can be met by future generations.

A formal and more rigorous approach to managing infrastructure is necessary, and this must involve the establishment of long-term asset management plans. Without accounting for the formal long-term asset management needs a financial plan can only be of limited value. The Outer Metropolitan Growth Councils stated:

“Over the projected period to 2011, most OMGCs are likely to be spending between 40 and 60% of their capital expenditure on the creation of new capital. Given that the OMGCs are characterized by both high growth rates and the legacy of aging infrastructure from previous growth periods, there is a concern that there is not enough focus on managing existing assets.”

PANEL RECOMMENDATIONS

26. Local Governments should establish a comprehensive 10-year asset management plan that is integrated within their business and financial plans. These long-term plans must address the issues of infrastructure renewal, upgrade and replacement. Asset management planning should translate broad strategic goals to specific objectives. The purpose of the asset management plan is to set the broad framework for decision-making by Councils which enables them to undertake asset management in a structured and co-ordinated way.

27. The broad asset management plans should be implemented through shorter-term plans for specific asset categories that provide a detailed program of costs and service delivery.

28. Completion of these plans to an agreed and verifiable industry standard to be a precondition for future SPP road funding, other infrastructure and specialist funding allocation to Councils.

29. WALGA to use the International Infrastructure Management Manual (IIMM 2006) to create templates to assist Local Governments in preparing their asset management plans.

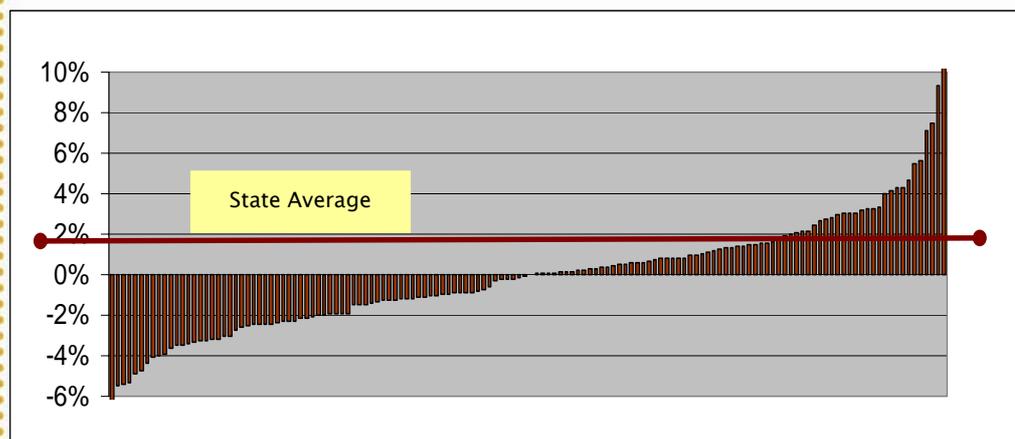
Managing infrastructure in changing communities

While infrastructure management is an issue for all Councils, it presents unique and particularly difficult challenges for those facing a changing demographic, either rapidly growing or in decline.

The research conducted in the Social and Cultural Viability Report explored the sustainability of Local Government service delivery in the face of a rapidly changing population. The broad findings were:

- o 79 Local Governments will find the mix of services they offer their community will need to change as their population demographic changes between 2006 and 2021.
- o 35 Local Governments are predicted to experience an absolute decline in their population.

FIGURE 6.1 AVERAGE ANNUAL RATES OF RESIDENT POPULATION GROWTH – ALL COUNCILS, 2000–2001 TO 2004–05



The rating mechanism presumes a stable population base that is available over a long period to fund a service over its entire lifecycle (from implementation, maintenance and finally renewal).

As figure 6.1 above illustrates, this is already not the case for the majority of Western Australian Councils – these communities are in the position of having to fund the maintenance and renewal of infrastructure with a rate base that is declining, pushing more and more of the burden on to fewer people.

Councils with declining populations may also experience the results of past intergenerational transfers as past asset management has been on a cash basis, meaning there are inadequate reserves to renew the infrastructure. This problem will become even more acute as the infrastructure reaches the end of its life cycle and requires replacement.

The community debate ahead will continue to explore whether it is feasible for all Australian citizens to enjoy access to equivalent services and, in a Local Government setting, what services are best sourced on a regional or statewide basis.

In growing communities the challenge is to manage the coordination of infrastructure to ensure that land is developed and released in a planned and

timely manner and that infrastructure (economic and social) is provided to support this development.

There key issues associated with rapid growth are:

- Pressures and constraints on the orderly development of urban land;
- Planning and infrastructure priorities to address these issues;
- Funding strategies (including forward budget allocations, developer contributions and public/private partnerships).
- Ensuring the rating effort within a district is balanced with the need to ensure that people with less disposable income do not bear the bulk of this need; and
- Recognition that in some newer estates, rate revenue is likely to be exceeded by the whole-of-life cost of maintaining and replacing foundation infrastructure.

"Whilst the OMGCs are indicating that they will be spending significant sums on capital, it is unlikely that this will meet the needs of the community. The forecasts reflect what the OMGCs estimate that they can afford rather than what the community needs.

It is apparent that OMGCs are spending between 30 and 80% of their capital expenditure on new capital. In general the trend is to increase the proportion of capital expenditure that is spent on new capital. This raises the issue of the impact on revitalising, upgrading and replacing existing infrastructure particularly as any new capital created, along with contributed assets, will add to the long-term asset management burden of Local Government." Outer Metropolitan Growth Councils submission page 34.

PANEL RECOMMENDATIONS

30. For high growth Councils the options include:

- Consistent use of new developer charge regimes;
- Prudent use of debt; and
- Negotiation with the State Government to apply provide bilateral funding and, where appropriate, to consider the appropriateness of implementing a development agency model to share risk and cost in development.

In communities where populations are in decline, and in the absence of economic development initiatives which may see the creation of new communities or business opportunities in areas, the course open is to:

- Engage the community to establish priorities within the resources available; and
- In some cases this may require adjustments or reductions in service frequency or presence to match local demand.

Other longer-term remedies will attach to the success of the individual authority and the industry in general by achieving better revenue outcomes from other levels of government to supplement local capacity to sustain minimum service standards.

Reducing the Infrastructure Backlog

Access Economics estimated that an infrastructure backlog of approximately \$1.75 billion exists in Western Australia and this represents about 14% of the total value of Council non-financial assets, which compares with approximately 10% for the finding of a \$6.3 billion backlog made for the NSW Inquiry²³.

Adopting proactive asset management will require a considerable change in policies and practice within the sector, supported by excellent community engagement of the choices available to the industry and better technique and tools applied to asset management, planning and funding. The infrastructure backlog is a consequence of almost 100 years of vertical fiscal imbalance and is, in our perspective, beyond the capacity of Local Government to resolve on an organic basis, although elsewhere we note that the industry has some additional financial capacity available to it. The backlog is a particularly challenging issue for Local Governments with rapidly growing populations and those with declining populations. Some Council representatives expressed the view that the current infrastructure backlog primarily results from infrastructure being endowed to Local Government which it would not actually build or maintain itself if contemporary standards were applied.

The Panel notes with interest the approach taken by the Department of Sport and Recreation to a comprehensive whole-of-life costing as part of the funding arrangements for any capital sport grant applications made by Local Government. Once Local Government develops whole-of-life costing for different asset classes, it can reduce the incidence of the type of cost-shifting that occurs when funding is provided for the initial construction of an asset but not for the assets entire life.

“What is required is the management tools to enable ongoing assessment of future costs and a basis for setting priorities for future asset replacement.” Shire of Dardanup submission p 3.

PANEL RECOMMENDATIONS

31. WALGA develop sector-wide standards for service levels and consistent processes for calculating the whole-of-life costs associated with core asset classes.

32. WALGA develop a standardised methodology for Local Government to engage the community in asset management issues and in the process of establishing service levels and their funding arrangements.

33. WALGA develop a campaign strategy to leverage funding to eliminate the infrastructure backlog in conjunction with improved asset management practices, recognising that sustainable progress will not be made on reducing the backlog unless additional annual revenues of approximately \$120M per year are secured, based on current calculations of the infrastructure deficit.

²³ Independent Inquiry into the Financial Sustainability of NSW Local Government, *Are Councils Sustainable?*, Sydney, May 2006, pp.24. These figures are not strictly comparable, as regional Councils in NSW are responsible for water and sewerage assets.

Chapter 7 Capability Development

Overview

Employing over 13,500 people in over 600 roles, the Local Government sector has a very large and continuing demand for a competent and diverse workforce. Council workers live and work in most Western Australia neighbourhoods and communities. The sector represents (in aggregate) the third largest employer in Western Australia (behind the State Government and the mining and resource sector).

The industry is routinely exposed to the same changing economic, social and demographic conditions as face other employers, especially in the context of the very strong labour market impacting WA at present. It is not unique in facing a range of acute skill shortages. The systemic challenge is to demonstrate that it can offer exciting and vibrant careers to future workers and employees.

The competition for labour from the resources industry is set to continue. A study by the National Institute of Labour²⁴ stated that, within Western Australia, the resource sector will need an additional 42,000 employees by 2015.

Many of the current workforce-planning challenges are a result of the strong Western Australian economy and require short-term attraction and retention strategies. Other matters require a more strategic or long-term approach to address the prospective (and inevitable) loss of senior, experienced and long run employees (as will happen with the ageing of the current workforce). The industry must also acknowledge and address a set of risks which result from some of its own practices and a perceived lack of investment in the human capital of Local Government.

“The issue facing many Local Governments is not an unwillingness to adopt a more strategic approach to the way they do business, but having the capacity to introduce and maintain systems that improve decision making. This is a particular problem for the OMGCs who are competing for specialist skills such as planning, engineering and building in a highly-competitive marketplace. The problems associated with managing rapid growth are more pronounced in Local Government areas that are in transition from essentially rural to urban Local Governments such as the Shires of Serpentine-Jarrahdale and Murray.”

Outer Metropolitan Growth Councils’ Submission 1, p 4.

There is also a recognition that the increasingly diverse role of the Local Government may require new skill profiles. In other smaller authorities, the small scale and immediacy of the local workforce, while having some superb cultural and performance characteristics, will struggle to sustain quality services and supervision without recourse to a larger and more complete talent bank of expertise and services.

²⁴ D. Lowry, S. Molloy, and Y. Tan, *Staffing the Supercycle: The labour force outlook in the minerals resource sector: 2005 to 2015*, National Centre for Vocational Education Research, Perth August 2006.

Investing in Talent and Development of the Local Government Workforce

We found that Local Government needs to develop a suite of retention and capability development strategies to:

- Address workforce planning on a systemic, industry-wide basis – to ensure an adequate workforce for the future;
- Strengthen Councillor capabilities to match their governance, leadership and strategic roles in the future of the industry;
- Invest in talent and upgrade officer skills to match the diverse range of technical and service requirements now characteristic of Local Government delivery;
- Develop and apply flexible employment arrangements and practices to ensure that the workplace experience of Local Government employees is innovative and supports excellent community and citizen experience in their dealing with Local Government; and
- Competitively position the Local Government workforce in a new workforce market in which employees increasingly choose the employer or context in which they work rather than the reverse.

Our research found that many individual Local Governments have initiated strategies to attract, develop and retain staff but also observed that few sustained, industry-wide initiatives are currently in operation.

Industry competition for staff is endemic. In other times, this network-based activity was seen as a strength and characteristic of the way the industry worked together. In the current context, staff predation will favour Councils that are better equipped to reward and support staff. Inevitably a talent war has emerged which has reduced confidence and enthusiasm for some forms of resource sharing.

In the dialogue process a number of excellent ideas and innovative strategies were identified and can now be further explored as part of the proposed Industry Plan for Local Government:

- A statewide Local Government graduate intake scheme –including incentive arrangements in respect of HECS, overseas placement with partner local authorities as part of the development program and assistance with post graduate study or other relevant industry qualifications;
- Creation of regional and pool-based employment structures to ensure that the industry's specialist expertise (perhaps including the proposed graduate pool) has a secure base for employment and is able to be deployed to projects and roles across the region or zone served;
- Active targeting of senior students in rural and regional high schools with vacation employment and work experience placements to cultivate interest in continuing to live and work in their community as a Local Government employee;

- Reconsideration of apprentice and traineeship levels for the industry in vocational skills settings;
- Flexible, on and off-site training arrangements for existing staff to continue to develop expertise and capability to perform – significant use of on line, or self paced content;
- An active partnering program with local authorities in overseas jurisdictions to identify opportunities for staff exchange and participation in developmental activities of mutual interest;
- A residential induction program offered 3–4 times per year for foundation training for all new staff – conducted on a zone, regional or statewide basis;
- Development of long-range alliance arrangements with preferred suppliers in the tertiary sector to ensure degree specialisation and content appropriate to the requirements of the industry – notably in respect of planning, environmental health, community engagement, works and engineering;
- Industry awards to celebrate good practice and innovation in respect of the people of Local Government and their achievements;
- Work and process redesign to encourage greater flexibility in workplace arrangements, including greater acknowledgement of the possibilities of mobile workforces and ‘virtual’ workplaces, seasonal scheduling of some Council works, shared service and cooperative arrangements with other local employers and best-in-class use of programs to ensure opportunities in Local Government for indigenous Australians, people with disabilities and others with special workplace requirements; and
- Partnering relationships such as have been developed between the City of Subiaco and the Shire of Victoria Plains to leverage training, development and staffing expertise to best effect.

An Industry Workforce Plan

The interim report sets out our perspective that the current skill shortage telegraphs structural issues that will become more significant in time. The inference is that Local Government employers have an opportunity to consider more profound changes to their employment policies and practices to ensure that other short and long-term issues are addressed.

The following disciplines and professions have been identified as core Local Government roles where recruiting and retaining qualified staff has proved especially problematic:

- planning;
- engineering;

- finance; and
- environmental health.

Some Councils have recruited internationally and interstate. There is also greater use of agency personnel, consulting firms and other third party mechanisms to ensure services are maintained in the short term.

A more complete workforce profile and skills development plan is required to better enumerate and specify future skills requirements to ensure appropriate targeting of future investment.

Strengthening the Capacity of Councils and Councillors

Commentary at the dialogues suggested that Councillor training and skill development is critical for Local Government. The panel has identified the growing complexity of the governance role of the Councillor and the uneven nature of their qualifications, expertise and organisational experience as contributing to some of the poor financial and program decisions impacting Councils.

As the strategic decision-making body, it is very important for every Council to have a thorough understanding of its roles and responsibilities. Research commissioned by us has highlighted that substantial gaps currently exist in the skills and abilities of Councils. Access Economics stated:

“Where financial governance is not well developed in Councils, it is not surprising that there is a lack of understanding on the community’s part of the true costs of current infrastructure and service commitments.”²⁵

While some representatives at the dialogues suggested mandatory training *prior* to election, we believe this would be impractical and could in fact reduce the number of people willing to be involved with the democratic process of Council elections.

The Panel considers that a comprehensive induction or “foundations” training program should be mandatory for *elected* Councillors, with explicit payment for attendance and participation in addition to course expenses.

“Non-compulsory but recommended training of Councillors in company director’s roles would be beneficial.”

Shire of Wongan-Ballidu submission p 64.

This training should incorporate governance, best practice and strategic decision making and be periodically updated to incorporate legislative change, governance practice and related professional issues. We would encourage WALGA to work with the Institute of Company Directors and other industry stakeholders such as the LGMA and the Department of Local Government and Regional Development to explore whether an appropriate curriculum and accreditation approach might be jointly agreed and offered.

²⁵ Access Economics, Local Government Finance in Western Australia, June 2006, p 80.

More generally, a culture of continuing professional development for Councillors should be encouraged to ensure ongoing exposure and insights to the role of Local Government in a period of significant change. A mix of online and residential content should be offered, recognising that most Councillors have other family, business and employment commitments to manage in addition to the role they play in Council life.

The CEO and Local Government

Ensuring that the CEO leadership has time and space to support Council to grow the business of Local Government is a key success factor in our vision for a more sustainable system of Local Government in Western Australia.

While every authority needs “safe hands” in the delivery of its programs and services, it is also clear that the industry needs strong executive leadership focused on the growth of communities and the development of a resilient and talented Local Government workforce.

For many Council CEOs the working day is largely consumed in compliance administration and the recording of “corporate history” – with the inevitable outcome that Local Government is “administered” rather than “managed”.

“Local Government is bound by a whole raft of reporting and compliance requirements. These need to be rationalised into more transparent and consistent management practices.” Outer Metropolitan Growth Councils’ Submission 1, p.3.

A confident and respected relationship between the Council and its most senior officer is a key success factor for best governance and community outcomes. Councils may need to give consideration to better internal structural arrangements to ensure that appropriate focus on both operational and strategic tasks for the CEO are supported and well resourced.

PANEL RECOMMENDATIONS

34. WALGA lead the development of an industry skills strategy as part of the industry plan to:

- Address workforce planning on a systemic, industry-wide basis – to ensure an adequate workforce for the future;
- Strengthen Councillor capabilities to match their governance, leadership and strategic roles in the future of the industry;
- Invest in talent and upgrade officer skills to match the diverse range of technical and service requirements now characteristic of Local Government delivery;
- Develop and apply flexible employment arrangements and practices to ensure that the workplace experience of Local Government employees is innovative and supports excellent community and citizen experience in their dealing with Local Government; and
- Competitively position the Local Government workforce in a new workforce market in which employees increasingly choose the employer or context in which they work rather than the reverse.

Chapter 8 Improving Service Delivery Outcomes

Overview

The social and business environment in which Local Government operates has changed considerably over the course of its history. Our research has found that individual Local Governments have responded to this change with great innovation, passion and a commitment to doing their best by the community. The absence of system-wide approaches to process improvement, resource sharing and other best practice experience is evident.

The BJA consultancy report “Best Practice Management and Administration” commissioned by the Study, cited many examples of innovative service delivery developed by Local Government and observed that innovation typically was a direct result of the constrained resource pressures in the sector. This has driven Councils to continually evaluate the best way of providing services against a constrained resource basis. One observed consequence is a focus on cost reduction rather than benefit or quality.

The research also reveals that innovation and process improvement are characterised by a localised and sometimes parochial approach. Elsewhere, change imperatives are not well understood or championed across the sector.

From survey activity conducted by the Systemic Sustainability Study it was observed that:

- 92% of the Councils / Shires that responded to the survey indicated that they have had experience in resource sharing;
- 58% of the Councils / Shires that responded indicated that they have been involved in State or Federal Government partnerships;
- 56% of respondent Councils had participated in Regional Councils;
- 40% of respondent Councils / Shires had undertaken some sort of process improvement;
- 78% of responding Councils indicated that they had explored or implemented models or initiatives that would assist their Local Government’s sustainability;
- Surprisingly, 22% of the responding councils indicated that they hadn’t explored or implemented models or initiatives that would assist their Local Government be more sustainable in the future.

The most recent ALGA report by PricewaterhouseCoopers on Sustainability and the work completed earlier this year by this review should leave Local Government leaders in no doubt about the challenges facing the industry and the need to change initiatives on both the revenue and the service provision fronts.

Options for Service Delivery

Dollery and Johnson describe eight models for service delivery that are generally acknowledged throughout the Local Government sector. These are:

- Existing Local Government arrangements. This particular model does nothing to improve the sustainability of individual Local Governments;
- Resource sharing on an ad hoc basis. This avoids the potential problems associated with more formal arrangements and allows for maximum flexibility. This model is already recognized in the Local Government Act 1995;
- Regional organisations of Councils to promote cooperation;
- Area Integration / Joint Board Models which retains existing Local Government but with a single employing body with shared administration and joint operations, overseen by a joint board of elected members;
- Virtual Local Government. An extension of the joint board model that consists of smaller Councils linked through a 'shared service centre' with service delivery contracted out;
- Agency Models where services are provided by State Government agencies at levels established by locally-elected officials;
- Amalgamated large Councils. This is the historical approach to structural reform adopted in Australia;
- Major boundary change, including unincorporating some of the sparsely settled areas. Other states have developed specific entities for delivering Local Government services in their unincorporated areas; and
- Community consultation mechanisms.

The Panel has also made the two suggestions which either build on the models mentioned above or are applications of approaches in other domains.

The first was a "State/Territory" model involving a two-tier local and regional government with certain services provided at local level (and largely funded from own-source revenues) and others on a regional basis with elected arrangements in place for both systems. Funding for the Regional Council would be principally sourced from SPP sources and, where individual Councils consent to provide funds for shared services, provided on a regional basis.

The State/Territory model also has considerable potential to enable the State Government to consider abolishing its network of Regional Development Commissions and incorporating their charter and budget within the Regional Council role. A key feature of the Regional Model would be alignment with other boundary jurisdictions for State agencies to facilitate better planning for regional infrastructure and services.

A second proposal was to place greater emphasis on regional service efficiencies. Here the option is focussed on an industry-owned service provider that provides regional services at Council discretion. This is a variant of the Agency Model in that the service provider could be:

- A specially established industry entity
- A Single Council operating under contract to other Councils ;
- A private sector provider;
- A partnering arrangement with the WA Government's Shared Service initiative;

- The Western Australia Local Government Association or a
- Regional Council.

"This Regional Local Government (RLG) concept is unique, innovative and potentially revolutionary in its deliverables. The model is specifically set up so that the RLG can service the individual Shires in as many projects and tasks as possible. Traditional areas such as ranger, planning, waste and health services can all be serviced by the RLG due to its size and buying capacity." North Midlands Voluntary Regional Organisation of Council's submission p 4.

Other measures included introducing compulsory tendering for all services used by Local Government; eliminating monopolistic arrangements within the current system and allowing cross-boarder competition; and clarifying the capacity of Local Government to engage in commercial enterprises to diversify income sources.

Improving Resource Sharing in Western Australia

The most commonly used service delivery model was resource sharing, indicated by the vast majority of survey respondents saying they engaged it to some degree.

Our conclusion is however that there is potentially a much greater scope for resource sharing in the Western Australian Local Government sector than is currently being utilised. This conclusion aligns well with the strategic direction described in Chapter 4 and the staffing imperatives and challenges in Chapter 7. While the literature is cautious about economic advantages attaching to economies of scale in Local Government reform, we see particular advantages to the industry of agreed regional pool arrangements for key staff, back office services and for some whole-of-region infrastructure services.

This approach would preserve the policy setting of no forced amalgamations and enable Councils to build confidence and experience with regional or zone-based mechanisms to support their role.

"While this organisation does not see mergers as the only way forward, nor even an appropriate approach for many Local Governments, it is probably the most effective and ultimately the most efficient approach for many Local Governments in Western Australia."

City of Geraldton submission page 1.

Our case for change is based on a recognition that the sector is characterised by:

- extensive and disparate systems across the sector resulting in wasted investment and inefficiencies;
- a proliferation of craft processes specific to individual Councils;
- a lack scale or depth in some Councils to support efficient processing;
- duplication of overheads, including supervisory positions, ICT infrastructure and systems maintenance - areas where other jurisdictions and

organisations are looking to achieve better leverage from investment and resourcing; and

- critical skills shortages in technical and professional disciplines in some segments of the industry.

The recent National Financial Sustainability Study of Local Government for ALGA completed by PricewaterhouseCoopers provides the following portrait of councils “feeling the pinch” which aligns well with the context assessment described above. PWC characterise the challenge as:

- Minimal (or negative) revenue growth;
- Cost growth which has exceeded revenue growth. Expenditures have been rising by an average of CPI plus 2-3% per annum. This cost growth is mainly due to a combination of factors including the rising skill level required for most senior roles and hence the higher level of remuneration (award wage rises of typically 4% pa for most mid to lower level roles); stronger cost escalations in the maintenance and construction sectors; and service diversification;
- Increasing involvement in non-core service provision due to rising community demands, coupled with a related tendency by some councils to step in to provide a non-traditional service;
- A tendency by some Councils to run operating deficits creating a need to defer or underspend on renewal of infrastructure, particularly community infrastructure;
- Limited access for some Councils to the strong financial and asset management skills which are critical to identifying sustainability problems, optimising renewals expenditure and improving revenue streams; and
- Limited access, for a small proportion of Councils, to rate revenue due to relatively small populations reducing the size of the rates income stream coupled with constraints on the size of annual rates increases.

Improving Incentives for Collaboration

From the Panel’s point of view, a key success factor is to ensure that any new arrangement shows appropriate benefit through business case and service outcomes. Stronger financial incentives for collaboration are required.

The recent formation of the Wildflower Regional Council and the commencement of amalgamation processes in Northam are encouraging signs that Councils are considering alternative management and service arrangements however, we sense that further regional or zone-scale arrangements will struggle for traction and support in the industry unless a strong leadership role is taken by participating Councils and their management – and stronger encouragement and incentives for pooled services are developed or demonstrated by the State Government, progressive Councils and WALGA.

While improvements to service delivery have the potential to provide substantive economic benefits, we believe that the key motivation for moving to a more integrated sector will be for capability reasons. The tight labour market for professional staff will make shared service delivery an operational necessity. By taking proactive leadership on this issue, Local Government can ensure its communities receive the best service delivery possible.

Ultimately, improving Local Government service delivery is not about cost reduction but about strengthening the quality and reach of services provided.

The Panel notes with interest the findings of the recent ALGA report on Local Government Sustainability, especially recommendations which propose a Local Community Infrastructure Renewals Fund to support councils in the more timely funding of renewals work for infrastructure. That study recommends that this proposed fund could be distributed based on relative need and use the R2R or Financial Assistance Grants (FAGs) General Purpose distribution methods, or perhaps through a new or hybrid approach.

The panel sees an opportunity to implement this fund in Western Australia on a regional basis to ensure a regional or network view of infrastructure is taken in planning and allocation processes. The change imperative could be further enhanced if participation in the fund was determined by a pre-qualification process to ensure that recipient Authorities have established and verifiable infrastructure plans, asset condition status and associated best practices to make sure that new funds are applied appropriately. The more general intent is to ensure that the Industry supports and encourages changes to practice and operation to ensure a more sustainable future for all Councils in the State.

Amalgamation

In the interim report, the Panel promoted the view that, until a range of system issues and challenges facing Local Government were resolved, there was little prospect that forced amalgamations would achieve lasting community benefit.

There is a growing literature and operating experience to this effect elsewhere in Australia. Our sense is that structural reform through forced amalgamation is a flawed approach that fails to account for Local Government as an important and valued advocate for communities and neighbourhoods.

“Instead of the State Government trying to recommend particular Local Governments amalgamate to ensure sustainability, based on limited information, the whole Local Government industry needs to be educated and encouraged to initiate proposals for improvements themselves. The State Government also needs to allocate significant funding to assist Local Governments to progress these initiatives.”
Town of Kwinana submission p 3.

The 1997–98 *Local Government National Report*²⁶ commented that the Commonwealth Government financially assisted structural reform in local governance, involving amalgamation, for three principal reasons:

- ‘Larger Councils have a more secure and adequate financial base; are better able to plan and to contribute to economic development; are more effective community advocates; and interact more effectively with government and business.’ (This is basically an argument that small Local Governments lack administrative and technical capacity compared with larger municipalities)

²⁶ Department of Transport and Regional Services, *Local Government National Report 2000–01*, Commonwealth of Australia, Canberra 2006, Chapter 4
http://www.dotars.gov.au/local/publications/reports/2000_2001/C4.aspx.

- Since Commonwealth funding equates to around ten percent of Council income, Councils must ‘deliver value-for-money services to local communities,’ and because ‘structural reform delivers economies of scale and permits Councils to employ a wider range of professionals’, Council amalgamations will generate a greater range of services and improved quality of service.
- Structural reform is pivotal since ‘without change, Councils face the possibility of an ever-diminishing role as individual services are contracted to the private or voluntary sectors while other concerns, such as the environment, are addressed by special interest groups or agencies,’ which can ‘undermine local democracy and reduce service integration.’

The Panel considers these arguments need to be acknowledged but that the main benefits can be obtained by methods other than enforced structural reform. Local Government in Western Australia has the opportunity to determine its own future and become an effective service deliverer to its community provided it can address systemic revenue challenges and continue to adjust its form and mode of operation to meet new community expectations, changing demographic pressures plus secure and retain a workforce to engage with and support communities across the state.

“The level of services that Local Government is expected to provide to its community is continually expanding in terms of statutory requirements, core business activities and discretionary activities. The expanding service demands are not matched with increases in funding and access to available skills to successfully deliver services.”

Perth Economic Development Agency Submission p.2.

Securing economies of scale and scope – this is a useful argument for shared services, but not for structural reform as gains are usually only achieved in highly capital-intensive production processes and related corporate services. In the Local Government context a great deal of the “back-office” activity has the potential for significant cost savings provided service arrangements focus on standardised processes, appropriate service expectations and the best use of enabling technology. Other than where call centre-style services are offered to the public we see little only limited gains in prospect for “front office” services on a regional basis.

Better depth and capacity for skills – larger Local Governments can employ a greater depth and range of technical and specialist staff on a full-time basis – others can only achieve this outcome through resource sharing and pool-style arrangements. The growing depth and complexity of the Local Government task is readily acknowledged with an inevitable consequence that economies based on capacity and skills seem likely to provide the key imperative for further structural change.

Consolidation to address administrative and compliance costs – this argument contends that larger administrations allow Local Government to directly reduce the direct costs of administration and compliance costs. The Panel’s view is that the compliance burden on Local Government is onerous. A preferred approach is to simply reengineer and reduce the compliance burden and determine whether the function is best performed on a regional, zonal or local basis.

Improving Industry Confidence and Support for Inter-Council resource sharing

There are several reasons why ad hoc resource sharing does not naturally create the best outcome for local communities. The reasons fall into two broad categories:

- local political imperatives; and
- overcoming or addressing fixed investment costs.

Various local political and practical barriers were raised directly with the Panel and also through various consultancies conducted or reviewed by us. The common theme is that that local political imperatives constrain better and more rational arrangements for resource sharing and associated service provision. The considerations were:

- lack of tangible benefits including overcoming fixed investment costs;
- lack of co-ordination;
- compliance issues;
- lack of trust (rivalry with neighbouring Councils);
- concern about economic leakage where families associated with pooled services leave a locality in favour of a regional centre or neighbouring authority;
- loss of Councils individual identity and autonomy; and
- fear that voluntary resource sharing is a precursor for amalgamation.

“The Wildflower Country Regional Council is an exciting initiative for the Local Government industry across Australia. Structural reform undertaken elsewhere in Australia has in the main been driven by influences outside of the sector. This concept is significantly different in its shape, intent and aims – importantly, Local Government itself is the driving factor.” North Midlands Voluntary Regional Organisation of Councils Submission p 4.

We believe Local Government should adopt resourcing policies that focus on the good of the *entire* community. The financial sustainability discussion shows that Councils simply may no longer have the option to retain a full range of stand-alone services or staff

Incentives for Change

We note that while the “Connecting Local Government” fund is a very positive step to encouraging increased integration of service delivery in Local Government, it has some failings. These are:

- The fund (at present levels) is simply too small to bring about significant change as the magnitude of need is much greater than the quantum of funds available.
 - Assistance of up to \$50,000 is available for initial business case assessment and feasibility studies;

- Up to \$200,000 is available for Local Governments to implement projects that have been the subject of previous agreements or feasibility studies. This will have demonstrated that the project can improve the capacity and efficiency of Local Government in Western Australian through collaborative service delivery. The guidelines provide for discretionary payments beyond the \$200,000 ceiling.
- There is no overall strategic perspective provided with the fund and its direction or intent. The strong sentiment of “choice” in the current guidelines means that Councils are left to explore the benefits of sharing services themselves. What is needed is for clearer direction and encouragement that includes:
 - Change management expertise;
 - Funding for business case development for second-phase acquisition of technology and related procurement costs;
 - Staff transition (including appropriate reskilling, transfer and redeployment considerations);
 - One-off capital support for new infrastructure;
 - Secondment or funding of interim “transition” staff to the management any new entity pending merit based appointments or the ability to release existing Council staff to focus on the development and transition processes;
 - Support for transition costs which may include other “bonus points” incentives for participating Councils;
 - Stronger focus on a standardised process for change to drive out uncertainties that may impede effective change management;
 - Investment in evaluation and process improvement associated with any funded project to ensure the rest of the industry can benefit from lessons learned and experience gained.

PANEL RECOMMENDATIONS

35. WALGA to use the Industry Planning Process to identify 3–4 case study or demonstration projects to pilot new resource sharing approaches to:

- Regional road funding, planning and management;
- Technical services; and
- Corporate Services.

36. WALGA to work with the State Government to strengthen the scope and intent of the Connecting Local Government Fund.

Chapter 9 Industry Plan

Introduction

This study represents a significant investment by Local Government in its own future.

An Industry Plan is proposed as a coherent and agreed process by which the Industry can now leverage the investment made through this study into a program for change and rejuvenation across the sector.

To facilitate this process, the Panel has presented its major recommendations into a format that the industry can now assess and amend to meet its requirements going forward.

“Local Government in Western Australia cannot and will not be able to survive in its current form.”

Personal submission by CEO of Shire of Broome p 2.

While our research discusses a large number of issues, we believe that the key challenges to Local Government are to provide a joined up approach to a five point plan and framework for the future:

- Leadership in the process of change by Councils, Councillors, senior management and WALGA;
- Securing better revenue outcomes for the industry from government and from the sector itself;
- Strengthening practice and technique in all authorities to improve financial and planning disciplines using a best practice approach;
- Strengthening the focus by government and the industry on new models for efficient service delivery at regional and zone levels; and
- Securing talent and investing in expertise to ensure Councillors, Management and Staff are well equipped for the challenges of 21st century Local Government.

In the detail of this report and our earlier consultancies is a wealth of information and experience the industry can apply to its future. The detailed recommendations in this document provide focus for investment and resourcing by government and the industry.

To enhance the best elements that exist within the Local Government sector, we recommend best-practice frameworks rather than the less certain approaches associated with regulatory change or industry codes of conduct.

In response to the question: Is there a need for more transparent and authoritative sector-wide financial practices to be developed? “As best practice and models yes – as legislative requirement – no.”

Shire of Wongan-Ballidu Submission p 63.

While we recommend some changes to the regulatory framework we do not believe regulatory reform is the best way to introduce change. A set of suggestions raised during the course of the review process are set out in Appendix 3 and may warrant further attention by WALGA and the Department of Local Government and Regional Services.

PANEL RECOMMENDATIONS

37. WALGA promote a range of procedural changes to the Local Government Act as set out in Appendix 3 to this report.

A Task Force Approach for WALGA

To this end we believe that WALGA should establish a task force to develop an implementation approach and to build the detail of the proposed industry plan with input from across the sector. It will be vital to achieve consensus on what, if any, changes Local Government wishes to embrace. The plan should have a strong action focus – with clear “By Whom?/By When?” tasks and milestones set out.

We believe that this task force will have two roles:

- Action plans for those recommendations that the Association wishes to endorse; and
- Subsequent development of best-practice models for each area of change endorsed by the sector and to champion them within the sector.

As a first step we understand that WALGA will take this report to its State Council for consideration and that WALGA will take those recommendations that receive endorsement back to the industry for a comprehensive engagement process towards an industry wide action plan.

Industry Summit

We recommend that WALGA host an industry summit early in 2007 to formalise the sector’s position on each of the recommendations and to consider implementation proposals as may be developed by the Task Force described above.

We believe that this summit should seek to confirm the sectors willingness to lead and shape its own future.

Funding

Initially we believe the task force should be funded and solely made up of representatives of Local Government. The task force will need to engage State and Commonwealth government stakeholders and may consider their participation as members in due course.

Given the scale of the recommendations that we have made there is a significant scope for the State Government to provide funding support for implementation, especially in initiatives for capacity building.

While the exact magnitude and duration of funding for the changes should be determined by the sector, we believe it is substantially larger than the funds available through the existing *Connecting Local Government Initiatives*. We have made some specific, short term recommendations in relation to the focus of this fund but believe a separate and more substantial investment by State Government is required in a new and more complete program focused on industry rejuvenation. We envisage that the magnitude of the task parallels the Size, Shape and Sustainability project being undertaken in Queensland where \$25 million has been provided.

PANEL RECOMMENDATIONS

38. WALGA establish a task force to develop an implementation approach and to build the detail of the proposed industry plan with input from across the sector.

39. WALGA host an industry summit early in 2007 to formalise the sector's position on each of the recommendations and to consider implementation proposals as may be developed by the Task Force.

40. WALGA use the task force process to more fully scope the financial investment required by the industry and government to secure a sustainable future for Local Government.

41. The Panel recommends short term expansion of the Connecting Local Government program and proposes the establishment of a new Program (Big Ideas for a Big State) with an indicative budget of \$25M to address and fund the anticipated range of capacity building and rejuvenation projects

Schedule of Recommendations

Leadership in the change process	1. That WALGA develop a comprehensive engagement process to enable industry consideration of this report and its recommendations leading towards an industry wide action plan.
Leadership in the change process	2. A Local Government Summit is recommended for the early part of 2007 to debate and consider the basis for further industry investment and Council implementation of priority recommendations and actions.
Leadership in the change process	3. WALGA develop and commit to a 10 year industry plan (Big Ideas for a Big State) shaped around a range of best-practice reforms in the Local Government sector as a foundation for future campaigns to improve the systemic fiscal imbalance faced by Local Government.
Securing better revenue outcomes	4. WALGA should continue to press for changes to the escalation methodology for FAGs to a new formula tailored to Local Government cost movements (perhaps involving a combination of the Australian Bureau of Statistics (ABS) Wage Cost Index and Construction Cost Index coupled with population growth).
Strengthening financial and planning disciplines	5. That the Industry Plan strengthen the information base used to inform and influence policy, legislation and revenue frameworks at State and Federal level and that the document provide guidance and secure resources to assist individual Councils to improve their performance in a more systemic manner. Investment by

	the State and Federal Government and Councils in the processes described in the plan is recommended.
Strengthening service delivery	6. The Panel recommends that Local Government adopt a strategic direction over the next decade towards two foundation roles: <ul style="list-style-type: none"> • Representing the political aspirations of its communities and their citizens; and • Ensuring delivery of efficient and effective services and infrastructure. These two roles do not necessarily have to have contiguous boundaries or catchments. Accountability for funding and securing resources should continue to be based on the community of interest boundary.
Strengthening service delivery	7. It is recommended that the Local Government Industry Plan give detailed attention to mechanisms and incentives to assist Councils who wish to pool or share resources on an agreed basis. Where Councils determine to proceed with amalgamation processes the plan should also address transition guidelines and the role of government partners in one off capital incentives to the participating Councils to ensure successful change and better community service and infrastructure outcomes.
Securing better revenue outcomes	8. A best-practice approach be developed to ensure uniformity in considering the measures that should be undertaken to reflect the costs faced by Local Government in making rating decisions and setting fees and charges.
Securing better revenue outcomes	9. WALGA campaign for greater flexibility and differentiation in the rating and own source revenue options available to Local Government. This may be particularly useful in circumstances where Council boundaries change and larger geographical areas with greater diversity in size, nature of individual communities are incorporated within single authority areas.
Strengthening financial and planning disciplines	10. Individual Councils reassess their debt funding levels so that a modern and efficient capital management approach can be adopted.
Strengthening financial and planning disciplines	11. A best-practice guide for debt funding of infrastructure be developed and that training for Councillors and staff on modern capital management be introduced along with other capacity building measures designed to improve financial expertise, technique, systems and outcomes for Local Government and the communities it serves.
Strengthening service delivery	12. Councils develop an output based reporting framework for activities to more clearly enumerate the costs and beneficiaries of services. This should incorporate a mechanism for pricing to reflect the true costs and relevant externalities associated with Local Government services.
Securing better revenue outcomes	13. WALGA continue to work with the State Government and the Mining and Resource Industry to ensure that all local communities share directly in the benefits of the State's natural resource strengths and that State Agreements where applied should be to ensure that service, capacity and infrastructure impacts on Local Government services and communities are funded and resourced in an appropriate manner.
Securing better revenue outcomes	14. WALGA advocate to increase the use of developer charges (where appropriate) by Councils to assist the creation of new community infrastructure.
Strengthening financial and planning disciplines	15. WALGA support the directions and principles established by the UDIA, WALGA and DPI in their 2006 Contributions to Community Industry report, especially where community planning processes inform and linked with long run financial and asset management plans to ensure an appropriate contribution is made for funding and maintaining community infrastructure.
Securing better revenue outcomes	16. A more transparent and sustainable funding model for roads and associated infrastructure needs to be developed if an estimated \$120 Million dollar annual infrastructure deficit faced by the Councils in Western Australia is to be addressed in a sustainable manner.
Securing better revenue outcomes	17. Any campaign position adopted by WALGA and Local Government will require better and more consistent information and quality data, to support and inform

	its policy position.
Securing better revenue outcomes	18. A statewide “blitz” funded by the industry to ensure accurate, consistent baseline information on road condition and backlog requirements to assist tighter definition of the infrastructure challenge and strengthen the position of the industry in Western Australia in successfully prosecuting its case for better and more equitable road and associated infrastructure funding.
Securing better revenue outcomes	19. WALGA continues to press the State Government for consistent CSO style treatment for revenue forgone by Local Government where State concessional policies or practices are applied to individuals and organisations.
Strengthening financial and planning disciplines	20. Local Government adopt a best practice approach to rating that involves a more consistent rate setting process, managed by the industry but with appropriate regard to peer effort to ensure that own source contributions to a sustainable Local Government sector are maximised. Better and more consistent <u>State of the State reporting</u> will ensure greater transparency on own source revenue performance.
Strengthening financial and planning disciplines	21. A working group be established within the framework of the proposed Industry Plan to develop an on line State of the State reporting framework to be hosted by WALGA. Further work is required to define the key data sets to ensure a best practice framework is developed and embraced by authorities across the state.
Strengthening financial and planning disciplines	22. Specific actions to address or strengthen financial capacity and reporting technique are set out across Section 5 – these should be the subject of detailed development and focus in the Industry Plan.
Strengthening financial and planning disciplines	23. WALGA champion an accrual based best–practice approach towards asset management for all Councils. This will involve an extensive change of practice for the 70% of Councils that still operate on a ‘historical cost’ basis and cannot occur with a significant investment by the industry and state government in strengthening capacity and technique across Local Government. All asset management reporting should be in accordance with the model described in asset management and infrastructure accounting.
Strengthening financial and planning disciplines	24. Councils should be encouraged to move towards a renewal based approach that is consistent with asset management and strategic financial plans.
Strengthening financial and planning disciplines	25. The sector embrace the WAMI program and seek to roll it out to all Local Governments as a key initiative within the proposed industry plan.
Strengthening financial and planning disciplines	26. Local Governments should establish a comprehensive 10 year asset management plan that is integrated within their business and financial plans. These long terms plans must address the issues of infrastructure renewal, upgrade and replacement. Asset management planning should translate broad strategic goals to specific goals and objectives. The purpose of the asset management plan is to set the broad framework for decision making by Councils to undertake asset management in a structured and co–ordinated way.
Strengthening financial and planning disciplines	27. The broad asset management plans should be implemented through shorter–term plans for specific asset categories that provide a detailed program of costs and service delivery.
Strengthening financial and planning disciplines	28. Completion of asset management plans to an agreed and verifiable industry standard to be a precondition for future SPP road funding, other infrastructure and specialist funding allocation to Councils.
Strengthening financial and planning disciplines	29. WALGA uses the International Infrastructure Management Manual (IIMM 2006) to create templates to assist Local Governments in preparing their asset management plans.
Securing better revenue outcomes	30. For high growth Councils the options include: <ul style="list-style-type: none"> • Consistent use of new developer charge regimes; • Prudent use of debt; and • Negotiation with the State Government to apply provide bilateral funding and

	where appropriate to consider the appropriateness of implementing a development agency model to share risk and cost in development.
Strengthening financial and planning disciplines	31. WALGA develop sector wide standards for service levels and consistent processes for calculating the whole-of-life costs associated with core asset classes.
Strengthening financial and planning disciplines	32. WALGA develop a standardised methodology for Local Government to engage the community over asset management issues and in the process of establishing service levels and their funding arrangements.
Securing better revenue outcomes	33. WALGA develop a campaign strategy to leverage funding to eliminate the infrastructure backlog in conjunction with improved asset management practices, recognising that sustainable progress will not be made on reducing the backlog unless additional annual revenues of approximately \$120M per year are secured, based on current calculations of the infrastructure deficit.
Investing in talent	34. WALGA lead the development of an industry skills strategy as part of the industry plan to: <ul style="list-style-type: none"> • Address workforce planning on a systemic, industry wide basis – to ensure an adequate workforce for the future; • Strengthen Councillor capabilities to match their governance, leadership and strategic roles in the future of the industry; • Invest in talent and upgrade officer skills to match the diverse range of technical and service requirements now characteristic of Local Government delivery; • Develop and apply flexible employment arrangements and practices to ensure that the workplace experience of the Local Government employees is innovative and supports excellent community and citizen experience in their dealing with Local Government; and • Competitively position the Local Government workforce in a new workforce market in which employees increasingly choose the the employer or context in which they work rather than the reverse.
Strengthening service delivery	35. WALGA to use the Industry Planning Process to identify 3–4 case study or demonstration projects to pilot new resource sharing approaches to: <ul style="list-style-type: none"> • Regional road funding, planning and management; • Technical services; and • Corporate Services.
Securing better revenue outcomes	36. WALGA to work with the State Government to strengthen the scope and intent of the Connecting Local Government Fund.
Strengthening service delivery	37. WALGA promote a range of procedural changes to the Local Government as set out in Appendix 3 to this report.
Leadership in the change process	38. WALGA establish a task force to develop an implementation approach and to build the detail of the proposed industry plan with input from across the sector.
Leadership in the change process	39. WALGA host an industry summit early in 2007 to formalise the sector’s position on each of the recommendations and to consider implementation proposals as may be developed by the Task Force.
Leadership in the change process	40. WALGA use the task force process to more fully scope the financial investment required by the industry and government to secure a sustainable future for Local Government.
Securing better revenue outcomes	41. The Panel recommends short term expansion of the Connecting Local Government program and proposes the establishment of a new Program (Big Ideas for a Big State) with an indicative budget of \$25M to address and fund the anticipated range of capacity building and rejuvenation projects.

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Appendix 1: Panel membership and terms of reference for the Systemic Sustainability Study

Study Panel

An independent Panel was established to provide direction for this review and to provide WALGA with advice, strategies and a plan for the future of the industry for its further consideration and development with Local Government in Western Australia.

The Governance Panel appointed to conduct the Systemic Sustainability Study comprised:

- **Professor Greg Craven** (Acting Deputy Vice Chancellor of Curtin University).

Greg Craven is a lawyer and academic with a wide experience in public policy. He holds the Chair in Government and Constitutional Law at Curtin University of Technology. Prior to this, he was Executive Director of the John Curtin Institute of Public Policy, Foundation Dean and Professor of Law at the University of Notre Dame Australia, and a Reader in Law at the University of Melbourne. He served as Crown Counsel to the Victorian Government from 1992–95, where he oversaw the implementation of a wide range of policy initiatives.

- **Professor Fiona McKenzie** (Acting Executive Director of the John Curtin Institute of Public Policy).

Prior to her current appointments, Professor McKenzie was a Curtin Research Fellow at the Curtin University Graduate School of Business. She is a regional development specialist with extensive experience in population and socio-economic change, regional economic development and analysis of regional and urban social indicators. Professor McKenzie is also the Director of the Housing and Urban Research Institute of Western Australia.

- **Mr George McCullagh** (Principal Cressida Consulting).

George McCullagh is the principal of Cressida Consulting Pty Ltd, a consulting business focussed on the provision of management advice to a range of public and private sector clients in Western Australia. He is a former Partner with Deloitte Consulting and Deloitte Touche Tohmatsu and was previously a Director with the WA Public Service Commission.

While the Study was initiated and funded by WALGA, the Governance Panel was given an independent charter and was responsible for managing its agreed budget, arranging and directing its research, consulting stakeholders and producing findings and recommendations.

A WALGA employee, Nathan Taylor, was seconded to work on the project on a full time basis as Executive Officer.

Terms of Reference

The Systemic Sustainability Study Governance Panel was to inquire into, report and provide recommendations to WALGA (and State Government) on:

- Generally, the adequacy of Western Australia's Local Government system and its operations, its strengths and weaknesses, and means by which it might be improved.
- The structural, financial, administrative and other principles upon which Western Australia's system of Local Government should be based.
- Contemporary social communities of interest, environmental catchments and economic clusters to help define the Local Government arrangements (both structural and functional) that would best facilitate sustainable service delivery;
- Local Government infrastructure assets, including compilation of a statewide inventory of all such assets, their gross value, method of depreciation, replacement timing, cost of maintenance and other relevant matters identified by the Study;
- The adequacy of existing Local Government funding mechanisms, such as rates, debt, fees and charges, fines and the desirability of mechanisms identified from other jurisdictions, such as developer levies, product sales, business activities or other mechanisms or trends identified by the Study;
- The economic capacity of the existing Local Government structure to fund the service and infrastructure obligations it currently has and to recommend how any deficit might be addressed;
- Current and expected future labour market issues impacting on the sector and what strategies might be adopted to address these issues;
- Recent and expected future demographic trends and their likely impact on the Local Government sector and associated strategies to deal with them; and
- Any proposals, initiatives or directions which might significantly improve the operations of Western Australia's system of Local Government.

Acknowledgments

The terms of reference presented us with the challenge of building a well informed agenda for change and rejuvenation. The measure of success we set for ourselves was the extent to which valued change was then taken up and lead by the industry itself.

The Panel's role has brought with it a strong sense of responsibility and obligation – especially as we came to better understand the pressures and drivers of activity in Local Government today and to appreciate the passion and commitment the industry has for its task and the communities its serves.

We were greatly helped in our work and deliberations by a range of well thought out submissions and contributions from across Local Government in Western Australia.

Appendix 2: Submissions to the Systemic Sustainability Study

We received a number of well considered and valuable submissions in the course of the study. The following Local Governments and stakeholders made submissions on the initial discussion paper:

- Town of Bassendean;
- Town of Cottesloe;
- City of Gosnells;
- Town of Kwinana;
- City of Mandurah;
- Shire of Merredin;
- North Midlands Voluntary Regional Organisation of Councils;
- Outer Metropolitan Growth Councils;
- Peel–Harvey Catchment Council Inc.
- Personal submission, Shire of Broome CEO Ian Bodill;
- Perth Economic Development Agency;
- City of Subiaco; and
- City of Wanneroo.

We also received a small number of submissions based on the Interim Report:

- Shire of Dardanup;
- City of Geraldton;
- Outer Metropolitan Growth Councils;
- Personal submission Kalgoorlie–Boulder CEO Don Burnett;
- City of Stirling;
- Western Suburbs Organisation of Regional Councils; and
- Shire of Wongan–Ballidu.

In addition to written submissions, we also conducted a series of in–person dialogues in the following locations:

- Northern Dialogue in Geraldton;
- Inner Metropolitan Dialogue at Melville;
- Outer Metropolitan Dialogue at Wanneroo;
- Wheatbelt Dialogue in Bruce Rock;
- Goldfields Esperance Dialogue at Kalgoorlie–Boulder;
- Great Southern Dialogue in Mt Barker;
- Kimberly Dialogue in Broome; and
- South West Country at Bunbury.

The comments from these dialogues can be view at www.systemicsustainabilitystudy.com.au

Appendix 3: Changes to the Local Government Act

Councils were asked whether there were any amendments to the Local Government Act and State Government regulatory or policy settings for the industry that would enable their Local Government to improve service delivery and be more sustainable in the future. The following is a summary of the key amendments proposed – many with streamlining or simplification themes.

- Increase tender limits in Local Government to generally match procurement thresholds applied by the State Supply Commission to State Government activities
- Increase the threshold levels for Major Land Transactions to \$2m.
- Regulate for Asset management plans and Long Term Community Financial Plans.
- Enable regional councils to undertake duplicated reporting / compliance requirements on behalf of member councils.
- Revisit provisions in Act allowing for rates exemptions (charities, aged care, educational establishments, state and federal governments etc). A mechanism akin to the pensioner rebate scheme (i.e. whereby Council obtains rates which the state government has subsidised) would be more appropriate.
- Reduce reporting and compliance requirements.
- To be able to rate land occupied by State agencies.
- Councillor remuneration.
- Reduction in numbers of Councillors.
- Removal of ward based frameworks within Council boundaries and reinforcement of whole of Council whole of community basis for representation and decision making.
- Mandatory Councillor education and induction following election and on a continuing basis.
- Provision for clear process and easier transition in situations of amalgamation.
- Allow Councils to administer the conduct of postal voting elections.
- Less prescriptive requirements in section 3.58 and 3.59 would assist Councils to be more entrepreneurial and remove some requirements that put Local Government at a disadvantage when dealing with Commercial In Confidence business dealings.
- Consider implementation of two-tiered system of legislation. to suit operating context of smaller Councils.
- Allow electronic meetings for smaller Councils that are still relatively diverse.

PANEL RECOMMENDATIONS

We recommend that these legislative changes be pursued in conjunction with the Department of Local Government and Regional Development.