

BRIEFING NOTE:

Strengthening Local Government Revenues and Availability and Use of Debt by Local Governments

Background

Local government has been pressing the case for greater levels of financial support from other spheres of government. Such an outcome is unlikely to be materially realised in the near to medium-term given the other priorities and projected financial outlooks of the Commonwealth and most states and the Northern Territory.

The Australian Centre of Excellence for Local Government (ACELG) is currently addressing the issue through two separate, but related pieces of research. The first is a working paper entitled *In Our Hands: Strengthening Local Government Revenue for the 21st Century*. The second piece of work rounds out the research by exploring the availability and use of debt by local governments. ACELG's work in this area has partly been in response to the Ernst & Young report commissioned by the Department of Regional Australia, Local Government, Arts and Sport entitled *Strong Foundations for Sustainable Local Infrastructure*, June 2012.

In Our Hands: Strengthening Local Government Revenue for the 21st Century

The aim of this paper is to formulate fresh ideas and recommendations for the local government sector and other spheres of government to further strengthen revenue raising and overall financial capabilities of local governments in the medium to long-term.

The paper was written for ACELG by John Comrie, previously head of the South Australian Government's Office of Local Government, the Local Government Association of SA and a large local government in metropolitan Adelaide.

The paper seeks to answer a number of key questions:

- What do we know about the sustainability of local government revenue to date?
- Is the revenue base adequate and appropriate?
- Are rates being effectively utilised?
- Where the revenue base is inadequate, what are the best options for local government to increase and sustain own-source revenue to meet current and future needs?
- How can we sustain smaller rural and remote councils through increased external support?
- What have we learned about how increased and sustained revenue for local government is achieved with?

The report finds that most local governments have a large degree of control over the level of services they provide, costs incurred and the revenue they generate. Councils also have more capacity than they appreciate to address perceived asset renewal needs and increased service level preferences.

Improved future financial performance will for most councils depend to a large degree on governance issues, such as the quality of decision-making. This requires (a) improved financial understanding and expertise at both officer and elected levels, and (b) better long-term planning.

Financial improvement within local government often necessitates reviewing service levels relative to:

- Community affordability and preferences
- Increasing own-source revenues, and
- The motivation within a council to seek to improved efficiency.

Other spheres of government can assist councils to:

- Improve financial strategy settings
- Make greater use of borrowings
- Adopt better treasury management practices
- Ensure their own policy settings and local government legislative frameworks support better local government financial performance.

Other conclusions:

- Property taxes are an appropriate prime revenue source for local governments
- There is scope for many councils to generate additional revenue from user charges for services
- Consideration needs to be given for alternative support to councils that have less capacity to assist themselves.

ACELG proposes a number of steps to progress the findings, including:

- Bringing jurisdictional peak local government associations and agencies with local government responsibilities together to explore opportunities for strengthening local government revenue and financial management
- To take account of the significant but varying legislative, guidance and practice improvements that have occurred in different environments in recent years.

Availability and use of debt by local governments

The second paper, also prepared by John Comrie is currently in development, explores the appropriate and current use of debt by councils. The paper is expected to be available by the end of June and is being prepared in consultation with representatives of local government and local government regulatory agencies across Australia. The research is at an early stage but it is anticipated it will conclude that:

- Local government debt levels in aggregate Australia-wide are extraordinarily low – particularly given that many local government services are provided through long-lived infrastructure
- Many (probably most) councils have capacity to make far greater use of debt
- The current low use of debt by local governments is not as a result of problems with availability of competitively priced debt.

Improved guidance is needed to encourage and support councils to make better (and in many cases greater) use of debt. The paper is likely to identify the need for changes in legislation and/or regulations in at least some jurisdictions, particularly where borrowings are currently described as income. They are not. They were treated as such in the era of cash accounting but all Australian jurisdictions have required local governments to prepare financial reports using accrual accounting now for many years. Many perceive repayment of borrowings to be an expense. Again under accrual accounting they are not. Guidance on better use of debt also requires better guidance on understanding and using accrual accounting information for decision-making.

All jurisdictions require or encourage councils to prepare long-term financial plans. Understanding and using accrual accounting information and simple, strategic level long-term financial plans is key to helping decision-makers to determine their capacity to raise and service more debt.

Councils have traditionally raised debt for specific projects (even when holding substantial cash), with loans of fixed duration at fixed interest rates that require regular principal repayments. There is considerable potential for local governments to reduce net interest costs and simultaneously reduce interest-rate risk exposure by utilising a more diverse mix of borrowings (short and long-term loans with both fixed and floating interest rates). This would involve the raising of borrowings and investment of cash (lendings) more holistically and in accordance with simple documented treasury management procedures. It is not thought that separate borrowing structures will be required to achieve this.

Further information

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