Office of the CEO

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Committee Secretary
Infrastructure, Planning and Natural Resources Committee
Parliament House
George Street
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Dear Committee Secretary

Submission regarding the *Inquiry into the long-term financial sustainability of local government*

In accordance with the terms of reference for the ***Inquiry into the long-term financial sustainability of local government***, the following information constitutes a formal submission from the Moreton Bay Regional Council.

In making this submission, the Moreton Bay Regional Council contends that it is in a strong and sustainable financial position, as acknowledged by the Queensland Audit Office (QAO) and Queensland Treasury Corporation. However, this submission will focus on the challenges facing the local government sector more broadly, as well as some specific concerns this council has regarding the QAOs recent reports into the sector.

As a broad comment in terms of the Inquiry, council makes the following comments:

Local government is the closest level of government to the people of Australia, responsible for large, complex and expanding roles. This includes the delivery of infrastructure and services to our communities, supporting and enhancing the everyday lives of our residents. This is all achieved using a limited funding basis from which this level of government operates – being rates and some charges. This is supplemented by some grants, subsidies and one-off funding agreements from other tiers of government. However, the ratio of income to expenditure is difficult to sustain when combined with the ever-increasing expectation of local communities in terms of services and infrastructure, the need to meet the demands of a growing population, and the devolution of unfunded responsibilities over time from both Federal and State Governments (commonly referred to as cost shifting).

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In order for local governments to sustain the provision of services and infrastructure to their communities, there is a need to review the funding mechanisms for local government. For example, until very recently the untied funding from the Federal Government (Federal Assistance Grants or FAGs) was frozen. This had an impact not just on our council, but on the local government sector nationally. By Government estimates, over the four years to 30 June 2018, the sector will have taken a $925 million hit to the bottom line as a result of the freeze. This means councils will have been deprived of nearly $1 billion of vital funding to provide better infrastructure and better services for our local communities. Whilst the unfreezing has been very welcome, the financial impacts have already been felt and are lasting.

Accordingly, whilst Moreton Bay Regional Council maintains a financially sustainable position, any criticism of the sector more broadly should be countered by a parallel review of funding mechanisms such as the FAGs. Moreton Bay Regional Council has long argued that a more equitable share of the federal taxpayer funding pools needs to be made available. The Commonwealth Government has the greatest capacity of any tier of government to raise revenue (via taxes), and yet they provide the least direct service and infrastructure (commonly referred to as vertical fiscal imbalance). Currently local governments receive less than a 0.7% allocation of the Commonwealth taxation through financial assistance grants and other infrastructure grants and subsidies. This allocation should be increased to provide Commonwealth taxpayers with a fair return of their tax dollars through their local government areas.

More specifically against the terms of the Inquiry, council makes the following comments:

a. **Financial planning and long-term forecasting**

QAO contend that most councils' long-term financial planning is a mere compliance exercise. Converse to this claim, our council constantly reviews and updates its long-term financial forecasting, thus ensuring this planning is based on the most up-to-date and accurate information available. Our long-term plan is consistent with our corporate, operational and asset management planning outcomes.

We dispute the QAO's contention that councils are unable to demonstrate they are meeting their ratepayer's expectations on service level and asset condition. Our council's performance is regularly measured against corporate and operational plan performance indicators, and asset management planning plays a major part in this assessment. Council does not explicitly ask its ratepayers about their preferred asset service level and condition expectations, instead focusing on delivery by ensuring we meet/exceed turnaround times on customer requests.

The resources Council invests in its long-term financial and asset management plans ensure they are an integral part of its business practices and further regulation in this area is both inappropriate and unnecessary.

b. **Asset condition data and asset management plans**

Council supports the QAO recommendation that councils need to improve the robustness of asset condition data and associated data management plans. Even though our asset management planning is progressing steadily, there is still more work required in acquiring the information needed to better understand the condition of assets.

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However, the process of collecting and processing this information is complex and time consuming. The process requires appropriate due diligence to ensure the information appropriately contributes to the planning process.

As council's asset information and knowledge continues to improve over time, we expect to see more robust asset management and maintenance planning - which will continue to progressively improve our overall long-term financial forecasts.

Council's planning has, since amalgamation, continued to improve and is now an integral part of the Council's business as usual work practice.

c. **Decision-making frameworks for major infrastructure asset investments**
Council supports the QAO recommendation that decision-making frameworks need to be in place to support major infrastructure asset investments. Council has existing systems and processes that assist it to rank and prioritise expenditure on all infrastructure projects. As with all planning and management tools, this framework remains the subject of continual improvement.

d. **Community engagement on future service levels**
Council is of the firm belief that its councillors appropriately represent their community's views on this matter, and that the development of asset management plans that include service standards (that are formally approved by council) already adequately meet this requirement. Accordingly, further regulation in this area is unwarranted.

e. **Financial sustainability targets**
Council supports the QAO recommendation for the Department of Infrastructure and Local Government to allow councils to set their own financial sustainability targets where they can justify that a different target is more appropriate for their long-term sustainability.

The current three legislated ratios that council discloses have certain targets that the Department of Infrastructure and Local Government and Planning consider appropriate.

These ratios include the operating surplus ratio which is set between 0% and 10%. Council supports this as a suitable indicator. Councils need to be able to demonstrate the level of surplus or deficit produced from operations. However in our case, this ratio is skewed. For 15/16, the ratio was 21.7% which is in part due to the share of participation right recorded (using equity accounting method) for our council's share of participation right in the water retailer/distributor for its local government area (Unitywater). The issue is that the full share of participation right in the associate is entirely regarded as an operating revenue line item ($79.3 million in 15/16) when only a portion of that total is actually received by council as cash ($25.5 million in 15/16). The remainder ($53.8 million) represents a non-cash revenue amount related to an increase in the value of the Unitywater business. (It should be noted that this non-cash revenue can only be realised by council if it sells its participation right in Unitywater - which is not achievable under existing State legislation.

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Council believes that our "real" operating surplus is being overstated and accordingly our operating surplus ratio is also overstated. If the non-cash portion of the share of participation right is removed from the calculation, council's operating surplus ratio would actually reduce to 11.8%, which a more realistic representation of council's actual realisable operational surplus.

Council considers that the operating surplus ratio upper range of 10% is not appropriate and that Council should be able to set an appropriate upper target in accordance with their own individual circumstances.

The ratios also include the net financial liabilities ratio which is set for less than 60%. Whilst Council is achieving this target, it is unrealistic for an infrastructure and capital-based industry such as local government. We contend that the operations of a local government could sustain higher debt levels, which means a higher ratio is more realistic for local government.

The final legislated ratio is the asset sustainability ratio. Council contends this ratio is not useful as it only really provides a loose guide, given renewal expenditure varies from year to year and is even less useful when factoring in that depreciation is only an approximation (designed to apply a cost to the consumption of the asset during the accounting reporting period). This is further exacerbated in high-growth areas which generally require a greater level of capital expenditure on new assets in order to support the growth. A comparison of renewal rates against council's planned renewals (based on its asset registers) in accordance with its asset management plans is a far more useful ratio.

f. **Organisational governance**
Council supports the QAO recommendation for the Department of Infrastructure and Local Government to have greater oversight of councils' financial sustainability by analysing their reported actual positions. However, it is not appropriate for the Department to use the Long Term Financial Forecast to perform this analysis as this tool is only ever indicative of financial sustainability. The Long Term Financial Forecast provides a road map for council to plan to provide sustainable services in the longer term. Therefore, it would only really be appropriate for the Department to use this indicator to analyse the planning process. Accordingly, auditing the Long Term Financial Forecast would also be inappropriate and irrelevant.

g. **Strategic planning and organisational capacity**
Council supports the QAO recommendation for the Department of Infrastructure and Local Government to support councils in building their capability and capacity to produce reliable financial forecasts and asset management plans that are integrated with the annual budget process. Whilst council does not have any concern with this proposal, we understand how some smaller councils may struggle to ensure strong strategic planning can occur given limited organisational resources.

h. **Budget transparency**
No comments.

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i. **Financial sustainability ratios**
Council supports the QAO recommendation for councils to have more financial sustainability ratios in their financial plans Council actually uses more ratios than mandated to monitor areas such as ongoing liquidity (for example, cash expenses cover ratio; interest cover ratio). Council acknowledges that it would be advantageous to compare the planned asset renewal funding with that indicated by the council's asset registers, however (as the Auditor-General has stated) asset management plans would need more useful data available to achieve a valid use of this ratio.

j. **Procurement policy and value for money**
No comments.

k. **Other matters the committee determines are relevant to the inquiry.**
No comments.

I trust the information provided in this submission outlines the key challenges facing the sector more broadly, as well as highlighting key suggestions and issues from this council.

Yours sincerely

Daryl Hitzman
Chief Executive Officer