



## LOCAL GOVERNMENT ACT REVIEW ►► DELIVERING FOR THE COMMUNITY

DETAILED  
DISCUSSION PAPER

AGILE

### Financial Management

Our vision is for the local government sector to be agile, smart and inclusive.

Our objective is to reform local government so that it is empowered to better deliver quality governance and services to their communities now and into the future.

A new Local Government Act will be drafted, Transforming Local Government.

Agile includes topics that focus specifically on how local governments can best use their resources. It is important that they are transparent and accountable to their communities, while striking a balance between community expectations and the practical limitations of revenue and expenditure.

The topics addressed in this theme are:

- Financial management;
- Rates, fees and charges; and
- Beneficial enterprises.

#### Have your say!

We need your input to inform how local government will work for future generations.

#### Submissions

The simplest way to have your say is to answer the questions via the online surveys.

The survey questions relate to the matters discussed in the papers and we encourage you to read the relevant paper before completing the survey.

While you may lodge multiple written submissions via email at [actreview@dlgsc.wa.gov.au](mailto:actreview@dlgsc.wa.gov.au), you will only be able to complete each online topic survey once. The public submission period closes on 31 March 2019. This is the last day that you will be able to respond to the surveys.

**Note:** Unless marked as confidential, your submission (including survey responses) will be made public and published in full on the Department of Local Government, Sport and Cultural Industries' (the Department) website. Submissions that contain defamatory or offensive material will not be published.

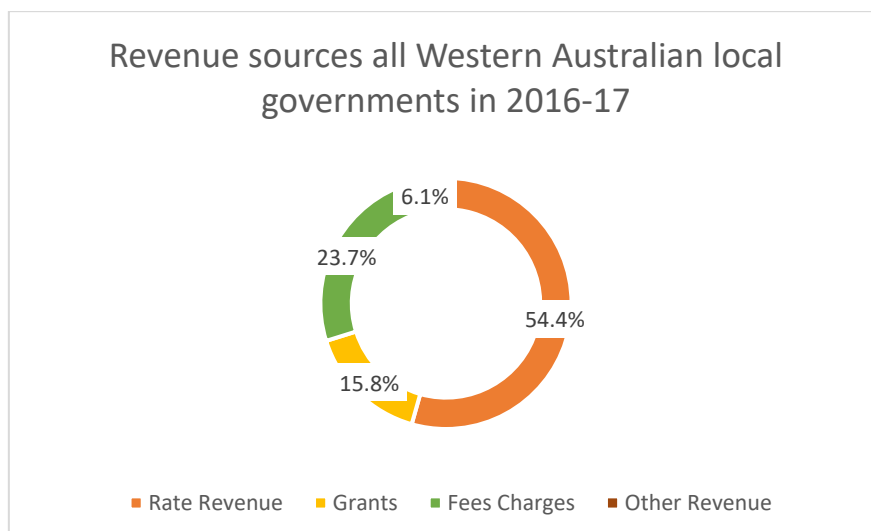
## Introduction

The local government sector's operating expenditure exceeds \$4 billion annually and local governments manage an asset base worth more than \$40 billion. To deliver services efficiently and effectively, local governments must be prudent users of public funds. Local governments must be transparent and accountable and strike a balance between community expectations and the practical limitations of revenue and expenditure.

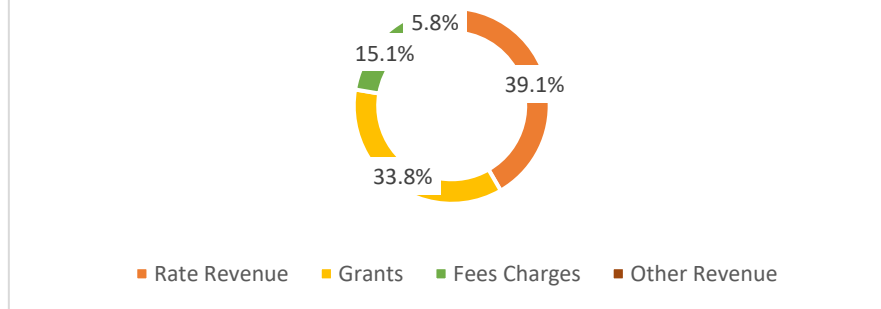
There are a number of accountability measures in place to provide financial oversight of local governments, including:

- The Office of the Auditor General, which is taking responsibility for local government audits following the introduction of the legislation in 2017;
- The requirement to give public notice for rates and other financial matters;
- Publication of annual reports (it is proposed to make these available online); and
- MyCouncil website which provides a geographic, demographic and financial snapshot of each local government.

Local government revenue is principally drawn from rates, fees and charges, and grants from the State and Commonwealth Governments. Financial Assistance Grants from the Commonwealth, administered by the Local Government Grants Commission comprise approximately 40% of the grants received by the local government sector, with the remaining 60% allocated from State Government grant programs. In the last two years, rates have made up approximately 55% of local government operating revenue, with grants from the State and Commonwealth Government making up around 15% of local government operating revenue.



### Revenue sources of the median Western Australian local government in 2016-17



The split in revenue sources varies considerably across the State which reflects the diversity of local government. In 2016-17, grants from the State and Commonwealth were the primary source of funding for 27% of the State’s local governments. In over half of the State’s local governments, revenue from State and Commonwealth grants made up more than one-third of their total operating income.

Across the sector, expenses are generally divided evenly between salaries, materials and replacement costs for assets. Again, the proportion spent on each category varies considerably between local governments.

To manage their finances, local governments are required to prepare a budget annually. The Act requires that a local government is to, having regard for its Integrated Planning and Reporting documents, prepare an estimate of its upcoming expenditure, the revenue and income it will receive independent of rates, and the amount in rates required to make up any deficiency. This approach means that local governments are required to establish their budget by first determining the amount they wish to spend and then estimate the revenue sources required to fund this outlay.

## Investments

Section 6.14 of the Act allows local governments to invest surplus funds. Many local governments hold significant amounts in cash reserves, including those obtained through development contributions. To ensure the public receives the benefits of these reserves, local governments need to invest these funds wisely.

The types of investments that local governments are permitted to make are restricted by Regulation 19C of the *Local Government (Financial Management) Regulations 1996*. This regulation states that local governments may not invest in:

- Deposits with an institution except an authorised institution;
- Deposits for a fixed term of more than three years;
- Bonds that are not guaranteed by the Commonwealth Government or a State or Territory government;
- Bonds with a term to maturity of more than three years; or

- A foreign currency.

The following table indicates the investment rules in other Australian States:

Jurisdiction	Investment rules
New South Wales	Permitted investments: <ul style="list-style-type: none"> <li>• Any public funds or securities issued by or granted by the Commonwealth, any State of the Commonwealth or a Territory;</li> <li>• Any debentures or securities issued by a council;</li> <li>• Interest bearing deposits with or any debentures or bonds issued by, an authorised deposit-taking institution, but excluding subordinated debt obligations;</li> <li>• Any bill of exchange which has a maturity date of not more than 200 days: and if purchased for value confers the holder in due course a right of recourse against bank which has been designated as an authorised deposit-taking institution by the Australian Prudential Regulation Authority; and</li> <li>• A deposit with the New South Wales Treasury Corporation or investments in an Hour-Glass investment facility of the New South Wales Treasury Corporation.</li> </ul>
Victoria	Permitted investments: <ul style="list-style-type: none"> <li>• In Government securities of the Commonwealth;</li> <li>• In securities guaranteed by the Government of Victoria;</li> <li>• With an authorised deposit-taking institution;</li> <li>• With any financial institution guaranteed by the Government of Victoria;</li> <li>• On deposit with an eligible money market dealer within the meaning of the <i>Corporations Act</i>; and</li> <li>• In any other manner approved by the Minister after consultation with the Treasurer either generally or specifically, to be an authorised manner of investment for the purposes of this section.</li> </ul>
Queensland	<p>The <i>Statutory Bodies Financial Arrangements Act 1982</i> provides for a tiered approach to local government investment rules.</p> <p>Local governments are assigned one of three bands based on size. Most local governments are category one local governments with limited investment powers, six larger</p>

Jurisdiction	Investment rules
	<p>regional councils are assigned category two, while the City of Brisbane is a category three.</p> <p>The types of investments permitted for each category of local government are specified in the Act and Regulations.</p>
South Australia	<p>Local governments in South Australia operate with a principle-based regulatory approach to investments which affords them greater autonomy than other States.</p> <p>A local government may invest money under its control but must, “exercise the care, diligence and skill that prudent person of business would exercise in managing the affairs of other persons and avoid investments that are speculative or hazardous in nature.”</p> <p>The council must also have regard to the:</p> <ul style="list-style-type: none"> <li>• Purposes of the investment;</li> <li>• Desirability of diversifying council investments;</li> <li>• Nature of and risk associated with existing council investments;</li> <li>• Desirability of maintaining the real value of the capital and income of the investment;</li> <li>• Risk of capital or income loss or depreciation;</li> <li>• Potential for capital appreciation;</li> <li>• Likely income return and the timing of income return;</li> <li>• Length of the term of a proposed investment;</li> <li>• The period for which the investment is likely to be required;</li> <li>• The liquidity and marketability of a proposed investment during, and on the determination of, the term of the investment;</li> <li>• The aggregate value of the assets of the council;</li> <li>• The likelihood of inflation affecting the value of a proposed investment;</li> <li>• The costs of making a proposed investment; and</li> <li>• The results of any review of existing council investments.</li> </ul>
Tasmania	A council may invest in any investment approved by the Treasurer.

## What are the opportunities for reform?

The current approach to regulating investments has been criticised by the sector as overly restrictive. It was informed by incidents in 2007 when multi-million dollar losses were suffered by a number of Western Australian local governments who had invested in Collateralised Debt Obligations (CDOs) with Lehman Brothers.

In 2016, the Department considered a new approach to regulate investments. The review noted that the types of investments prohibited by the Regulations did not necessarily correlate to risk. For example, while local governments are not permitted to invest in long term deposits for a period greater than 12 months (which is considered on balance a low-risk investment) there was nothing in the regulations preventing local governments from investing in shares or investments like the CDOs that were in part responsible for the Global Financial Crisis.

One approach to resolve this situation involved the introduction of a mandatory requirement for local governments to have an investment policy which would be endorsed by council and regularly reviewed.

### **Proposal - Investment policy**

A council endorsed policy, reviewed annually that describes:

- restrictions on allowable instruments;
- provisions for portfolio diversification;
- suitable benchmarks for measuring performance;
- allowance for both financial and social investments;
- valuations for reporting purposes to be on a market-to-market basis, with real property being valued every three years at a minimum, and ideally on an annual basis;
- provisions for minimum reporting requirements; and
- processes for the selection and review of investment advisors.

Further, local government investments would be defined as either Tier One or Tier Two. Tier One investments would incorporate low risk investments that local governments would be able to use with minimal regulatory oversight. Tier Two investments would require additional due diligence such as the development and approval of investment plans by the Department or another regulator.

## Development contributions

Development contributions are an important tool for local governments to fund infrastructure in growing communities.

State Planning Policy 3.6 prepared under the *Planning and Development Act 2005* describes the principles and considerations of development for infrastructure in urban areas. Under the policy, local governments may set out a system of charging development contributions through their planning scheme.

Development contributions can be sought for infrastructure required to support the development of an area. Local governments may seek:

- land contributions (for example, land for widening roads, public space, or primary schools);
- infrastructure works for public utilities and roads;
- monetary contributions for water and sewerage; and
- community infrastructure.

Contributions are for the initial capital requirements only and not for ongoing maintenance or the operating costs.

Local governments seeking contributions for community infrastructure must be supported by a community infrastructure plan, capital expenditure plan, growth forecasts and a method to determine proportional costs between new and existing areas.

The role of development contributions is being considered as part of the Department of Planning's review of the State Planning Policy.

## Debt

Section 6.20 of the Act provides local governments with the power to borrow money or obtain credit.

Local governments in Western Australia do not need to seek external approval to borrow although financial indicators, including a debt service ratio, must be reported in their annual report. Additionally, they are restricted in that their borrowings may be secured only by giving security over their income from general rates or untied Government grants (section 6.21). Under section 6.21(3), the Treasurer has the power to make directions to local government in respect to borrowing.

Debt is a contentious issue. Some people believe that debt should be avoided wherever possible. Another perspective is that the prudent use of debt serves a user pays philosophy by enabling multiple generations to contribute to infrastructure projects they will use into the future.

In 2014, an Australian Centre of Excellence for Local Government (ACLEG) report noted that local governments across Australia have low levels of debt relative to security, income levels and service responsibilities.

For the four years between 2013-14 and 2016-17, the average Debt Service Cover Score across local governments in Western Australia was 8.2 out of a possible 10.

The Municipal Association of Victoria recommends that local government debt does not exceed 60% of their annual rate revenue. Further demonstrating Western Australian local governments' conservative approach to debt, just three local governments in the state exceeded 60%, with the state-wide average being 16%. As noted by the Local Government Association of Tasmania, aiming for zero-debt usually results in under-investment in a council's infrastructure assets and is a burden on current ratepayers.

To fund infrastructure, local governments in Western Australia will often access several grants from State and Commonwealth Government sources. Even if local governments then borrow in order to make a contribution themselves, this may constitute only a small part of the whole cost. Thus many local governments operate with a very small debt load. In 2016-17, the long-term liabilities of the sector were approximately \$767 million compared to an annual operating revenue of more than \$4.1 billion.

What are the opportunities for reform?

### **Public notice of borrowing**

Local governments are required to give one month's public notice in relation to borrowing in three circumstances:

- Borrowing that has not been included in the annual budget;
- Where a local government has exercised its power to borrow for a purpose but no longer wishes to use the funds for that purpose; or
- Where a local government has exercised its power to borrow for a purpose and has funding left over.

Ceasing the requirement to give public notice would relieve an administrative burden (which local governments argue rarely generates community interest) but decrease financial transparency for this element of local government finances.

### **Security over borrowing**

Local governments are currently restricted from borrowing in that their borrowings may be secured only by giving security over their income from general rates or untied Government grants. Freeing local governments from this requirement may increase the legitimacy of borrowing as a financial management tool and serve to reduce the stigma associated with local government debt.

Some local governments have contended that they should be permitted to secure funds using their assets. Local governments have suggested that 'commercial' assets



such as property and infrastructure like airfields could be used to secure loans at competitive rates. Many of the land assets that are held by the local government are under their care and control, not outright ownership. Some local governments do own land freehold.

## Procurement

Local governments are significant procurers of goods, services and capital supplies. In 2016-17, local governments spent more than \$1.1 billion on materials and services.

The *Local Government (Functions and General) Regulations 1996* establish procurement rules for local government.

Currently, Western Australian local governments are exempt from the requirement to invite tenders in relation to contracts involving an estimated expenditure or receipt of an amount of less than \$150,000. When inviting public tenders, the local government is required to issue a State-wide public notice providing at least 14 days for interested parties to respond.

Regulation 11(2) of the *Local Government (Functions and General) Regulations 1995* provides for multiple scenarios where goods and services over \$150,000 do not need to be publicly invited:

- from expenditure authorised in an emergency;
- through the Western Australian Local Government Association Preferred Supplier Program;
- within the last six months the local government has publicly invited tenders, but no tender was deemed satisfactory or if the local government has previously sought expressions of interest but no person as a result had been deemed satisfactory;
- the contract is determined via an auction (only by resolution of Council);
- the goods or services are to be supplied through the State or Commonwealth Government;
- for goods or services related to land involved in a boundary change;
- the local government has good reason to believe that it is unlikely that there is more than one potential supplier;
- purchases of petrol, oil or fuel for internal combustion engines;
- the goods or services worth up to \$250,000 supplied by a person registered on the Aboriginal Business Directory WA;
- the goods or services are to be supplied by an Australian Disability Enterprise; or
- the contract is a renewal or extension where an open tender was used and the contract had the option for extension.

Under Regulation 24AD, local governments are also permitted to establish a panel of pre-qualified suppliers. In this case the local government is required to issue an invitation to apply to join the panel.

When assessing publicly advertised tenders, regulation 18(4) requires that local governments employ a written evaluation to determine the tender that satisfies the criteria and is the most advantageous to the local government to accept.

Local governments have consistently advocated for raising the threshold where public tenders must be advertised. Some local governments have argued that council should have discretion in setting their own rules for procurement, including tender thresholds.

Throughout this review, local governments both large and small have called for less prescription in procurement rules because of the investment required to comply with open tender rules. These concerns must be balanced with the need for a procurement framework that provides confidence for suppliers and the community. High profile breaches of tendering rules have reduced this confidence. Concerns regarding procurement practices is one of the major sources of community complaints to the Department.

The following table describes the threshold for public invitation (tendering) in other Australian jurisdictions.

Jurisdiction	Threshold for public invitation
New South Wales	\$100,000
Victoria	\$150,000 (Goods and services); \$200,000 (Capital works)
Queensland	\$200,000
South Australia	At discretion of council (none prescribed)
Tasmania	\$250,000
Northern Territory	\$100,000

It is widely acknowledged, including by the Commissioner of the Corruption and Crime Commission, that procurement is an area most vulnerable to corruption. It is important that any reforms consider the risks in terms of corruption.

Under Regulation 11(2)(b), a local government is exempt from being required to invite tenders if it obtains goods and services through the Western Australia Local Government Association's (WALGA) Preferred Suppliers Program (PSP). WALGA's PSP is designed to enable member local governments to obtain advantages from a bulk purchasing arrangement for the benefit of local government in Western Australia.

What are the opportunities for reform?

### **Align local government procurement rules with the State Government**

State Government procurement rules are set by the State Supply Commission (SSC) under its own legislation. Under the legislation, the SSC has the power to publish procurement policies that agencies must adhere to. Currently, there are six procurement policies covering matters such as value for money, open and effective competition, procurement planning and contract management. These policies also establish tender thresholds for State Government agencies.

Tender thresholds for most State Government agencies

<b>Purchases</b>	<b>Methods permitted</b>
Up to \$50,000	Direct sourcing Verbal quotations Written quotations
Between \$50,000 up to \$250,000	Written quotations (goods or services not on the Common Use Arrangement)
Over \$250,000	Open tender

Another key difference between State and local government purchasing rules is the Common Use Arrangement (CUA). The CUA requires State Government agencies to use specific suppliers for specified items. Most CUAs are mandatory for State Government agencies in the metropolitan area. There are currently no rules requiring local governments to use the CUA and the CUA operates separately to the WALGA preferred supplier scheme. Local governments can use the CUA if they wish, thereby benefiting from the buying power of the State Government.

The differences between the CUA and WALGA's PSP includes:

- PSP tends to be more inclusive of suppliers rather than exclusive as in the CUA;
- Some PSP's have been established as a national agreement to access the buying power of the local government sector nationally;
- Many CUAs are mandatory for State agencies, while it is not mandatory for local governments to use the PSP; and
- PSP's have a commission or levy as part of the agreed arrangement between WALGA and the supplier.

Overall, while the monetary threshold before public advertising used by the State Government is greater than local government, the SSC's regime of procurement policies means that in general, local governments enjoy greater autonomy and fewer procurement oversights than their State Government counterparts.

## **Scale the tender threshold to local government size and capacity**

Local governments vary considerably in respect to their expenditure. The combined operating budget of the State's 40 smallest local governments is less than the annual operating expenditure of the State's largest local government.

The variation between the size of local governments complicates setting a single tender threshold for the sector. For 88 of the State's 137 local governments, the threshold of \$150,000 represents more than 1% of their annual expenditure. This means that \$150,000 can represent a significant proportion of the total annual budget of many local governments.

At the other end of the spectrum, 27 local governments have an annual budget that exceeds \$50m annually. For these local governments, \$150,000 is a comparatively small amount of their total annual budget.

## **Tender threshold based on local government expenditure**

One option is to set tender threshold rules based on a local government's annual average expenditure. Under this approach, local governments would be required to advertise for tenders for goods, services and capital works with an anticipated value that is greater than a prescribed percentage of that local government's average annual operating expenditure over a set number of years up to a maximum amount.

### **Example – tender thresholds scaled to expenditure**

Over the last three financial years a given local government has had an annual operating expenditure of \$63 million, \$60 million and \$59 million. The three-year average annual operating expenditure of the local government is \$60.6 million.

Under an approach that scaled tender thresholds according to expenditure, the local government would need to advertise for tenders for goods, services or capital works with an anticipated value that was greater than a prescribed percentage of this average annual expenditure.

In this scenario, if the prescribed percentage was 0.25%, for example, the tender threshold for the local government would be \$151,500.

This approach would still require a nominal ceiling amount where a public call for tenders is required to take into account the comparably large annual expenditure of approximately a dozen large metropolitan local governments and floor to take into account the majority of small regional local governments with an operating budget closer to \$10m.

Another option using banding based on operating budgets could be employed is shown below:

Operating Expenditure	Threshold percentage	Range of public tender amount	Number of local governments currently in category
More than \$40 million	0.5%	\$200,000 - \$200,000 +	34
More than \$10 million but not greater than \$40 million	1.75%	\$175,000 - \$200,000	38
More than \$5 million but not greater than \$10 million	3%	\$150,000 - \$175,000	44
Less than \$5 million	3%	Less than \$150,000 - \$150,000	21

In this case, tiers of operating budget are used to set the public tender amount. As local government expenditure and capacity grows, local governments would graduate to a higher tier.

### **Tender threshold based on an assigned band**

Another approach could be to set the tender threshold based on an assigned band. Banding is currently used by the Salaries and Allowances Tribunal (Tribunal) to set the remuneration of council members and local government Chief Executive Officers.

Local governments are categorised into one of four bands by the Tribunal based on a model that incorporates factors such as population, diversity of services, significant social, economic and environmental issues and expenditure.

Incorporating Tribunal bands could better reflect the diversity and varying capacity of local government. On the other hand, it could be argued that purchasing risk is not aligned with the factors used by the Tribunal.

One example of how the Tribunal’s bands could be related to the tender threshold is shown in the table below:

Tribunal band	Tender threshold	Example local governments
1	\$250,000	Bayswater, Bunbury, Gosnells, Kalgoorlie-Boulder, Port Hedland, Swan
2	\$200,000	Esperance, Harvey, Northam, Nedlands, Vincent, South Perth, Subiaco
3	\$150,000	Capel, Claremont, East Fremantle, Gingin, Ravensthorpe, Yilgarn
4	\$100,000	Bruce Rock, Cue, Dundas, Peppermint Grove, Yalgoo, Westonia

### Assigned band based on risk assessment

Assigning a local government’s tender threshold according to risk may present a means to reward good governance. Currently, local governments are assigned a risk category by the Department annually based on their financial performance and general governance. By expanding and diversifying the factors taken into account, it may be possible to scale the tender thresholds to meet the diverse capacity of local government. This method, known as graduated compliance, would be the most sophisticated of the tiered approaches but would also be the most complex to administer and could result in substantial changes year over year.

### Reform to tender exemptions

Exemptions for public advertising of tenders reflect that in some circumstances the need to efficiently supply the goods outweighs the benefits of an open tender process. Exemptions also exist based on the notion that certain contracts can be filled using alternative tender processes that afford appropriate levels of due diligence.

For example, in much of the State securing suppliers to provide goods and services can be a challenge. Regulation 11(f) provides a broad exemption from advertising tenders in circumstances where, for any reason, the local government has good reason to believe that it is unlikely that there is more than one potential supplier. Other exemptions provide exclusions for goods and services purchased through WALGA’s preferred supplier program and for specific products like petrol or oil.

Some local governments have suggested that the rules concerning exemptions need to be clarified in the Act. They argue that the current rules concerning the definition of

a “contract” can create confusion and lead to varying interpretations. For example, on occasion local governments have sought clarification about whether the reoccurring supply of services such as repairs to a sporting facility’s lights or services with indefinite cost such as legal fees should be regarded as a single contract or multiple contracts over a period for the purposes of the threshold

### **Criteria for assessing advertised tenders**

Local governments are provided with considerable autonomy in selecting the criteria to be used for assessing advertised tenders. Regulation 18(4) requires that local governments employ a written evaluation to determine the tender that satisfies the criteria and is the most advantageous to the local government to accept.

State Government agencies are required to adhere to the SSC’s policies which include that a public authority must ensure that its procurement of goods and services achieves the best value for money outcome and are aligned with government policies, objectives and strategies and that it actively supports government initiatives.

Reforms to the regulations could provide for greater clarity of the criteria that local governments must use globally for assessing tenders. In line with SSC policies, this criterion could include value for money and acting in the public interest.

### **Consequences of non-compliance**

While the Act establishes tendering rules, the legislation does not establish consequences for non-compliance. Historically, if there is insufficient evidence of corruption, issues of non-compliance with tendering rules has been viewed as a behaviour and conduct issue for local governments to resolve. However, resolving matters at a local government level may not be practicable or appropriate if the Chief Executive Officer as the employing authority is responsible for the non-compliance.

For State Government agencies, the *State Supply Commission Regulations 1991* sets out graduated consequences for non-compliance. Under the regulations the SSC may do the following:

- Give notice of the non-compliance to the agency asking that the matter be addressed within a prescribed period;
- Require that an agency attends a meeting with the SSC;
- Appoint a person to supervise procurement at the cost of the agency;
- Publish the name of the agency in its annual report; and
- Recommend to the Minister that the agency’s ability to procure under the *State Supply Commission Act 1991* is revoked and that purchasing powers revert to the SSC.

## **Timely payment of suppliers**

The legislation does not prescribe standards for timely payments. The Regional Chamber of Commerce and Industry and the Small Business Development Corporation have called for reforms that ensure the timely payment of suppliers.

In 2018, the Auditor General published a report which found that while the majority of the 10 local governments audited made payments to suppliers on a timely basis, few had policies in place to ensure timely payments. Among the Auditor General's three recommendations was the notion that that local governments should have policies or procedures that clearly require payment of invoices within specific periods after receiving the invoice or after the receipt of goods and services. Reforms to legislation could mandate that local governments adopt a policy for invoice payment and/or specify a maximum allowed payment period.

Another option is to align the rules for timely payment of suppliers with State Government requirements. Treasurer's Instruction 323 requires State Government agencies to make payments within 30 days of the receipt of the invoice, or within 30 days of the provision of the goods or services (whichever is later).

## **Regional price preference**

The *Local Government (Functions and General) Regulations 1996* enables a local government outside the metropolitan area to offer a regional price preference. The regional price preference encourages governments to use locally sourced suppliers allowing local governments to assess a tender from a regional supplier as if the price bids were reduced.

The maximum permitted regional price preference to a regional tenderer is up to 10% for goods and services or 5% for building services up to a maximum price reduction of \$50,000. Under State Government tendering rules, the maximum permitted regional price reduction is \$250,000.

Both local government and the Regional Chamber of Commerce and Industry (RCCI) have called for the cap to be increased in line with the State Government limits.

Raising the cap may further promote opportunities for local governments to buy local but may also increase costs for regional local governments.

Local government operating budgets vary considerably. For many regional local governments, the \$50,000 cap represents a comparatively large proportion of their annual budget. The current cap restricts the value of the regional price preference of tenders with a value greater than \$500,000. More than half of the State's local governments have an annual operating budget of less than \$10,000,000.

In their submission to earlier consultation on the Act Review, Local Government Professionals Australia WA requested that the legislation be amended to specify that all purchases and not just goods and services and construction services be eligible for the regional price preference.



## **Who should authorise payments?**

Regulation 12 of the *Local Government (Financial Management) Regulations 1996* provides council with autonomy to determine what payments a Chief Executive Officer is authorised to make. If council delegates authority to make payments, Regulation 13 requires the Chief Executive Officer to prepare a list of accounts each month that shows details of the payment including the amount paid and details of the payee, the date and amount of the payment.

During the review, some staff within local government administration asserted that the autonomy provided for in the regulations contributes to confusion in roles and responsibilities between council and administration. The staff asserted that Regulation 12 allows councils to establish a delegation approach that results in routine payments being queried by council. To clarify who can authorise payments, some staff within local government administration have called for the regulations to prescribe thresholds for when council approval is required.

Currently, local governments are required to prepare a monthly report to council detailing the list of accounts paid by the Chief Executive Officer under delegated authority. As an alternative, reforms could be introduced that would require the Chief Executive Officer only to provide council with the report, when requested by council.

## **Disposal of property**

During earlier consultation on the Act Review, submissions were received concerning the disposal of property. Amendments to these provisions will be considered as part of broader reforms to the financial management framework.

## **Annual reporting**

Financial reporting is not a unique requirement to local government. All State Government and Commonwealth department financial reports are audited by their respective Offices of the Auditor General and must be tabled in Parliament. In the private sector, audited financial reports for many types of companies must be submitted to the Australian Securities and Investment Commission and prescribed types of charities must submit a general purpose financial statement that complies with the Australian Accounting Standards to the Australian Charities and Not-for-profits Commission.

## Reporting requirements of not for profit organisations in Western Australia

The financial reporting rules for not for profit organisations vary based on their operating revenue.

Small not for profit organisations with an annual revenue of less than \$250,000 may (but are not required to) submit an annual financial report to the Australian Charities and Not-For-Profit Commission (ACNC) as the sector's statutory regulator.

Medium sized not-for-profit organisations with an annual revenue of \$250,000 or more but less than \$1 million must submit an annual financial report to the ACNC that is independently audited or reviewed according to ACNC standards.

Large charitable funding organisations with an annual revenue of \$1 million or more must submit an annual financial report that complies with the Australian Accounting Standards and has been independently audited to the ACNC and submit an independently audited report to the members of their organisation.

Local governments are required to prepare an audited financial statement annually. The statement is required to meet the Australian Accounting Standards (AAS) as modified by the Act and Regulations.

Legislation requires that local governments calculate and publish seven financial ratios in their annual financial statements. Financial ratios are increasingly used across Australia as an important performance indicator for public sector entities, including local government.

Across Australia, local governments are required to calculate and publish different ratios. The lack of consistency makes the comparison of financial performance across local governments around the country more complex. Likewise, methods of valuation used to calculate ratios under the International Valuation Standard can vary, which means that ratios are a guide or indicator rather than a definitive account of financial health.

Ratio name	Calculation	Used in
Current / liquidity ratio / working capital ratio	Current assets - restricted assets / current liabilities – associated with restricted assets	Western Australia Victoria
Current ratio (method two)	Current assets – external restrictions / current liabilities – specific purpose liabilities	New South Wales

Ratio name	Calculation	Used in
Asset consumption ratio	Depreciated replacement costs of depreciable assets / current replacement cost of depreciable assets	Western Australia Tasmania
Asset renewal ratio	Net present value of planned capital renewals over 10 years / net present value of required capital expenditure of 10 years	Western Australia Tasmania <sup>1</sup>
Asset sustainability ratio	Capital renewal and replacement expenditure / depreciation	Western Australia Queensland South Australia Tasmania
Debt service cover ratio / debt ratio	Annual operating surplus before interest and depreciation / principal and interest	Western Australia
Debt service ratio (method two)	Interest expense and principal repayments / operating revenue excluding capital grants and contributions	New South Wales Victoria
Operating surplus ratio / financial performance ratio	Operating revenue – operating expense / own source operating revenue	Western Australia New South Wales Queensland South Australia Tasmania
Own source revenue / coverage ratio	Own source operating revenue / operating expense	Western Australia
Own source revenue ratio (method two)	Total continuing operating revenue – all grants and contributions / total continuing operating revenue including capital grants and contributions	New South Wales

<sup>1</sup> 20-year period in Tasmania

Ratio name	Calculation	Used in
Rates, annual charges, interest and extra charges outstanding percentage ratio	Rates, annual and extra charges outstanding / rates, annual and extra charges collectible	New South Wales
Cash expense cover ratio	Current year's cash and cash equivalents + all term deposits / payment from cash flow of operating and financing activities	New South Wales
Debt commitment ratio	Debt servicing and redemption costs / rate revenue	Victoria
Revenue ratio	Rate revenue / total revenue	Victoria
Debt exposure ratio	Total indebtedness / total realisable assets	Victoria
Net financial liabilities ratio	Total liabilities – current assets / total operating revenue – capital items	Queensland South Australia
Net financial liabilities ratio variation	Total liabilities – current assets / total operating revenue – operating expenses	Tasmania

In Western Australia, benchmarks for the seven ratios that local governments must report on were set in Departmental guidelines published in 2013. While these benchmarks are not legislated, the use of the benchmarks to inform the Department's risk management approach means that they are of considerable interest to local governments.

Ratio	Benchmark
Current ratio	100%
Asset consumption ratio	≥ 50%
Asset renewal ratio	Basic ≥ 75%

Ratio	Benchmark
Asset sustainability ratio	Basic $\geq$ 90%
Debt service cover ratio	Basic $\geq$ 200% Advanced $\geq$ 500%
Operating surplus ratio	Basic 1% - 15% Advanced $>$ 15%
Own source revenue coverage ratio	Basic 40% - 60% Intermediate 60% - 90% Advanced $>$ 90%

What are the opportunities for reform?

### **Amend the financial ratios**

Altering the financial ratios that local governments are required to calculate and report may improve awareness and understanding of local government financial performance.

The choice of ratios used in Western Australia has been the subject of criticism. Some in the sector view the ratios as an ineffective metric that can be misrepresented and that do not give a true reflection of financial performance and asset management.

The publication of the Financial Health Indicator on the MyCouncil website, which uses financial ratios in its calculations, has brought greater attention to financial health and highlighted the role that ratios can perform aggregating otherwise complex financial data. Financial ratios are a key tool in local government performance measurement in other Australian states and it is important that the metrics used in Western Australia are meaningful and useful.

### **Building Upgrade Finance**

Building Upgrade Finance (BUF) is a scheme whereby a local government administers loans issued by financiers to non-residential building owners to upgrade their buildings. The local government uses a levy on the building owner to recover the funds on behalf of the financier. The approach has been used in Victoria, South Australia and New South Wales as a mechanism to encourage non-residential property owners to invest in environmentally conscious building upgrades.

BUF involves three parts:

- The building owner agrees to undertake works;
- A financier agrees to finance the works; and

- The local government agrees to recoup the loan (known as a building upgrade charge).

The arrangement means that the loan is tied to the property rather than property owner. Responsibility to pay for the loan shifts if the ownership of the property changes. In other Australian States that have employed this approach, the local government is by law not financially liable for any non-payment by the building owner. Local governments are required to use their best endeavours to recover the loan. As the loan is recovered via the same powers as rates or a service charge, in the event of non-payment, local governments have the same powers available to recover unpaid rates or service charges. This can include taking possession of the land and selling the property.

### What are the opportunities for reform?

The City of Perth and the Property Council of Australia have advocated for reforms to Western Australian legislation that would enable local governments to guarantee finance for building upgrades for non-residential property owners. In addition to building upgrades to achieve environmental outcomes, advocates have identified an opportunity to use this approach to finance general upgrades to increase the commercial appeal of buildings for potential tenants. In this way, BUF is viewed as means to encourage economic investment to meet the challenges of a soft commercial lease market in Perth and achieve economic growth.

BUF enables building owners to obtain finance that they may not normally have access to. For local government, the approach may allow for the achievement of strategic community objectives and provide an additional revenue stream. For lenders, the scheme is said to be a way for financiers to participate in environmentally conscious investments and support technology like solar and have additional security because in the event of bankruptcy, recovery of the BUF takes precedence over other outstanding payments.

### What do you think?

The easiest way to have a say on the future of your community is to complete the survey available [here](#).

Your responses to this survey will inform the review and will take approximately 15 minutes to complete.

We ask that you take care in completing a survey. While you may lodge multiple written submissions via email at [actreview@dlqsc.wa.gov.au](mailto:actreview@dlqsc.wa.gov.au), you will only be able to complete each online topic survey once.

The public submission period closes on 31 March 2019. This is the last day that you will be able to respond to the surveys.

Unless marked as confidential, your submission (including survey responses) will be made public and published in full on the Department's website. Submissions that contain defamatory or offensive material will not be published.

The questions in the survey are provided below but we encourage you to complete the survey online which is available [here](#).

## Survey - Financial Management

1. Have you read the discussion paper associated with this survey?
  - a. Yes
  - b. No
2. Who are you completing this submission on behalf of?
  - a. Yourself
  - b. An organisation, including a local government, peak body or business
3. What is the name of that organisation? Shire of Carnarvon
4. What is your name? David Burton
5. What best describes your relationship to local government?
  - a. Resident / ratepayer
  - b. Staff member or CEO
  - c. Council member, including Mayor or President
  - d. Peak body
  - e. State Government agency
  - f. Supplier or commercial partner
  - g. Community organisation
6. What best describes your gender?
  - a. Male
  - b. Female
  - c. Other
  - d. Not applicable / the submission is from an organisation
7. What is your age?
  - a. 0 – 18
  - b. 19 – 35
  - c. 36 – 45
  - d. 46 – 55
  - e. 56 – 65
  - f. 66 – 75
  - g. 76+
  - h. Not applicable
8. Which local government do you interact with most? Shire of carnarvon
9. Would you like to be updated on the progress of the *Local Government Act 1995* review and further opportunities to have your say?
  - a. Yes
  - b. No
10. Do you wish for your response to this survey to be confidential?
  - a. Yes
  - b. No
11. What is your email address? [REDACTED]



12. To what extent do you support the following statements?

	Very unsupportive	Unsupportive	Neutral	Supportive	Very supportive
“Local government purchasing rules should be consistent with the State Government.”			x		
“Different procurement rules should apply to different local governments.”		x			
“Local governments with few staff or small operating budgets should have fewer procurement rules to comply with.”		x			

13. What criteria should be used to set the threshold for when a local government must publicly advertise a tender? (select all options that should apply)

- a. None. Procurement rules should be consistent across local government
- b. A percentage of a local government’s average operating expenditure
- c. Salaries and Allowances Tribunal bands
- d. An independent risk assessment
- e. Other (please specify)

14. Should the regulations set a threshold that a CEO is permitted to spend without needing approval from council?

- a. Yes
- b. No
- c. Unsure

15. Should the amount that a CEO is permitted to spend without needing additional approval from Council be scaled according to the local government’s size or capacity?

- a. Yes
- b. No
- c. Unsure

16. To what extent do you support the following statements?

	Very unsupportive	Unsupportive	Neutral	Supportive	Very supportive
“Local governments should be permitted to invest surplus revenue.”				x	
“Local government should have fewer restrictions on their ability to invest surplus revenue.”			x		
“Different local governments should have different investment powers and rules.”		x			
“Certain types of investments should require independent approval.”			x		

17. Should local governments be required to give public notice in any of the following situations? (please select all options that should apply)

- a. Where a local government wishes to borrow money outside amounts listed in the annual budget
- b. Where a local government has exercised its power to borrow for a purpose but no longer wishes to use the funds for that purpose
- c. Where a local government has exercised its power to borrow for a purpose and has funding left over
- d. Public notice is not required in any of these situations
- e. Unsure

18. Should local governments be permitted to secure loans using assets that they own freehold?

- a. Yes
- b. No
- c. Unsure

19. Should local government be permitted to participate in Building Upgrade Finance programs?

- a. Yes
- b. No
- c. Unsure

20. What types of upgrades should be eligible for the program?

- a. Environmental upgrades
- b. Commercial upgrades
- c. Both environmental and commercial
- d. Neither

e. Other (please specify)

21. Do you have any additional comments on the topic of financial management? Additional information can also be provided to the review team via email at [actreview@dlgsc.wa.gov.au](mailto:actreview@dlgsc.wa.gov.au).

Section 6.8 of the LG act needs to be clarified and should also include a material variance amount

6.8. Expenditure from municipal fund not included in annual budget

- (1) A local government is not to incur expenditure from its municipal fund for an additional purpose except where the expenditure —
  - (a) is incurred in a financial year before the adoption of the annual budget by the local government; or
  - (b) is authorised in advance by resolution\*; or
  - (c) is authorised in advance by the mayor or president in an emergency.

\* Absolute majority required.

This clause is a little ambiguous and has been interpreted differently by different LG's

Most of the time, when a significant variation will be considered, it is reported to Council under section 6.8, but this is based in interpretation and may not be correct.

Example A:

A road works construction or building construction has a budget allocation of \$2,500,000, but the tendered works come in at \$2,750,000. The funds required for the job are \$250,000 which is a significant variation, but as the purchase is not an “*additional purpose*” does not come under section 6.8 of the Act.

Example B:

Council considered that a new shelter is required at a playground and will cost \$5,700 and is a capital purchase, but the item has not been included previously under the capital expenditure program. As funding is required for an “*additional purpose*” an item is required to be presented to Council under section 6.8 before the expenditure can be made, yet this would not be considered a material variance by most Councils.

It is suggested that “*an additional purpose*” should be replaced with “*a material variance*” or similar.