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Department of Local Government, Sport and Cultural Industries,
Government of Western Australia
PO Box 8349
Perth Business Centre WA 6849

Via email: actreview@dlgsc.wa.gov.au

IPWEA Response to the Western Australian Governments' Proposed Local Government Act Reform Agenda

The Institute of Public Works Engineering Australasia (IPWEA) welcomes the opportunity to present its response to the Western Australian Government's proposed Local Government Act Reform Agenda.

IPWEA is the peak association for infrastructure asset managers and professionals who deliver essential public works and services to our communities.

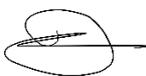
Representing more than 4,750 members and an online community in excess of 35,000, IPWEA is an industry leader in infrastructure planning, reporting, delivery, and operation. We have a keen interest in the management of a scalable and consistent framework for the local government sector.

Our experience has shown that with the right legislative framework, supportive guidance, training, audit and follow up, significant improvement in the performance and management of the most asset intensive level of government in Australia (i.e., local government) is possible.

IPWEA is proud to promote professionalism, education and knowledge sharing to enhance the quality of life for our communities and we look forward to discussing our response to the proposed reforms in due course.

Should you have any questions regarding our submission please by all means contact me directly for further discussion.

Yours sincerely



David Jenkins
IPWEA CEO

IPWEA Response to the Western Australian Governments' Proposed Local Government Act Reform Agenda

Introduction

The Institute of Public Works Engineering Australasia (IPWEA) is the peak professional association that leads public works and services, asset management planning, reporting, delivery, and operations. It provides member services and advocacy for those in the public works sector.

IPWEA provides guidance material and training courses on infrastructure asset management and financial planning and reporting. It works closely with its members, other membership bodies and government agencies in the development and provision of these services.

Much of IPWEA's work is of relevance to the local government sector, including a strong relationship with the Australian Local Government Association and its member state and territory associations.

IPWEA's manuals pertaining to asset management and financial planning & reporting include the:

- International Infrastructure Management Manual (IIMM),
- Australian Infrastructure Financial Management Manual (AIFMM),
- International Infrastructure Financial Management Manual (IIFMM),
- Practice Note N^o. 6: Long-Term Financial Planning,
- Practice Note N^o. 8: Levels of Service and Community Engagement, and
- Practice Note N^o. 12: Useful Life of Infrastructure.

Training is provided in:

1. Writing asset management policy, strategy and plans using the online guided pathway for asset management planning, known as NAMS+.
2. Infrastructure financial planning and reporting where students complete several financial planning calculations and report against industry recognised sustainability indicators using the International Infrastructure Financial Management Manual (IIFMM).

The reform agenda

The recommendations from the Western Australian 'Local Government Review Panel Final Report' provides a roadmap for a more agile and inclusive local government, with a clear purpose to deliver sustainable services to local communities.

The proposed legislative framework aims to ensure community engagement and integrated planning is a centrepiece of a local government's operations, as well as an emphasis on regional and intergovernmental collaboration.

This is an ideal IPWEA supports.

The focus of our response

A large focus of the proposed reform is on oversight and intervention particularly when significant problems arise within a local government.

Our focus is on enabling local government to prevent the problems from arising in the first place.

Of the six reform themes, our key response is focussed on:

- Improving financial management and reporting.

We have provided supplementary comments relating to:

- Reducing Red Tape, Increasing Consistency and Simplicity
- Stronger Local Democracy and Community Engagement, and
- Clear Roles and Responsibilities

In addition, IPWEA believes a commitment to ongoing awareness, guidance and training is key to delivering sustainable outcomes for the sector.

The key issues

Across-the-board, councils of all shapes and sizes are struggling with:

- human resources (absolute shortages in some cases, skills gaps in others);
- poor quality and/or insufficient data;
- limited understanding of how to set appropriate service levels (including a balanced assessment of risk); and
- failure to integrate asset management and long-term financial plans.

The above trends are not endemic to Western Australia. The Australian Local Government Association's 2021 National State of the Assets technical report identifies the above-mentioned issues as a national trend.

To explore these issues in more depth we offer the following.

Financial Sustainability

Our research indicates the Western Australian local government sector has made some headway since 2007, when all the state and territory local government ministers agreed on three Nationally Consistent Frameworks to improve local government's financial sustainability and management of fixed assets.

From work previously undertaken we understand that Western Australian councils on average are now generating sufficient operating revenue to offset operating costs. However, a significant number of councils still have underlying operating deficits. These are predominantly councils in the rural areas of the state, particularly those with small and/or declining populations. Their underlying operating deficits will need to be progressively remedied over time if they are to maintain preferred, affordable service levels.

Many councils with underlying operating deficits are likely to have limited scope to increase operating revenue on an ongoing basis. As such, improvement in financial management and reporting will need to come about to a large degree through cost savings and reductions and refinements in the range and level of services provided. Ignoring these challenges will not make the associated consequences go away. In fact, it will exacerbate them as it is likely to result in underspending on infrastructure needs and therefore more rapid and significant declines in service levels over time than would otherwise occur.

Those councils' with 'poor performance' outcomes in part distort the overall picture. Reports seem to suggest that they 'must do better', but this begs questions about the 'one size fits all' approaches/objectives, and even whether achieving high standards of asset management and financial reporting is worth the effort – especially for councils that survive on 'hand to mouth' grants and are in areas of economic and population decline. Over much of rural Australia the issue to be addressed is not how to make existing (or even, where feasible, amalgamated) councils more functional; but rather, what alternative form of local and regional governance could sustainably deliver essential services and incorporate an acceptable level of community democracy.

The key issue as already emphasised, should be whether a council can maintain a satisfactory Operating Surplus Ratio over time. If it can, then it will have the capacity to undertake asset maintenance and renewal (consistent with current service levels) on an ongoing basis. If it does not, then even if the council has good asset management plans and systems then sooner or later it simply will not have the resource capacity to carry out preferred asset management activities, and service levels must fall and/or related risks must rise.

The Department would know Councils are often the largest and most complex business in many if not all towns across the state, and it is essential that councillors as the board of directors have the necessary skills, resources, and

information to fulfil their governance role as custodians of councils' \$45 billion investment in infrastructure assets¹.

The consequences of poorly managing the \$45 billion investment in local government asset portfolio is not realising the best possible benefit of this investment.

Infrastructure assets being the largest component of this investment will continue on their path of decline, risks will be more apparent, and community service levels will likely deteriorate to a point where quality of life and economic conditions will likely not support community expectations.

Western Australian councils remain at a relatively early stage in the development of robust asset management and long-term financial plans that are based on affordable long-run service levels with consistent outlay inputs in both documents. It has been common elsewhere in the early years following the introduction of asset management planning for asset management plans to be based more on aspirational rather than affordable service levels. This may be the case too in WA. Whatever the explanation, the implication is that many councils have considerable further planning work to do. They need to ensure that their asset management and service level plans for the future are consistent with their reasonable financial capacity and hence support rather than detract from their ongoing financial sustainability.

The National Frameworks work well to provide a scalable and consistent approach to address the challenges. They form the basis of the National Assessment Framework Maturity Model developed by IPWEA in conjunction with state and local government finance professionals.

The National Assessment Framework remains a current and practical tool to inform decision making on service delivery, it focuses on allocating the scarce resources to where the greatest need is and provides direction and co-ordination of effort towards achieving the long term economic, environment and social sustainability for our communities.

Reliability of data inputs

According to the Australian Local Government Association's 2021 National State of the Assets technical report, less than 20% of councils say they base their infrastructure performance data on high quality evidence, such as reliable and up to date records, procedures, and/or the application of high quality investigative and analytic skills.

¹ Office of the Auditor General Western Australia, 2021, Regulation and Support of the Local Government Sector, p 3.

This suggests most councils continue to base their data inputs on low to medium quality evidence, procedures, investigations, and analysis which is incomplete, unsupported, or extrapolated from a limited sample.

These are worrying observations as NSoA data, in theory, is sourced from the same systems that inform the integrated planning and reporting requirements including audited financial statements and annual reports. It raises questions on the effectiveness of the investment decisions being made when around 50% of councils state data is based on judgement or low-quality evidence and 30% say supporting data is based on moderate quality evidence, procedures, investigations, and analysis which is incomplete or unsupported, or extrapolated from a limited sample.

It is acknowledged the confidence in reporting community infrastructure condition ranked higher than the knowledge of, and confidence in, reporting the function and capacity metrics. Overall, it is fair to draw the conclusion that:

- the reliability of data inputs is unacceptably low.

This indicates that there continues to be lower levels of knowledge and confidence in:

- Planning for infrastructure that meets needs now and in the future; and
- Understanding whether local government is accommodating asset renewal and replacement needs in an optimal and cost-effective way from a timing perspective relative to the risks it is prepared to accept, and the service levels it wishes to maintain.

Local councils that have high level asset management reporting capability have high confidence regarding the integrity of the underlying data used by their asset management system. They can rely upon it to make informed decisions, highlight opportunities, identify, and manage risks.

Funding environment

For every council, funding may not be an absolute constraint to improved performance, but the funding environment may increasingly be problematic and send the wrong messages, particularly when it comes to integrated strategic planning.

To explain, an increasing trend of submission-based, one-off 'special projects', in an addition to the traditional untied general-purpose and/or formula-driven grants (principally federal but also some states programs, such as R2R and FAGs).

This has the potential to increase uncertainty and lure councils into creating new assets that they cannot afford to operate and maintain (the 'can't say no' dilemma for councillors).

In addition, there is a real risk that in the post COVID environment, federal grant funding is likely to decline overall, and that increasingly local government will find itself competing for federal support with its state government masters, whose needs may be much greater.

Combined with deteriorating AM planning and low confidence data inputs, including poor understanding of performance measures such as 'function' (is it the right asset providing the right service) and 'capacity' drivers (do we need more or less assets) places a greater imperative for councils, particularly the larger metro councils who are faced with an acceleration of changing circumstance to better plan for the future.

Poor strategic planning and community engagement

Most councils have the financial capacity to at least reasonably adequately address future scenarios provided they have a sensible and informed conversation with their communities on performance, costs and risks.

For councils' dependent on discretionary grants, planning and engaging effectively with stakeholders and community will be a critical factor for success. Councils need to manage community expectations regarding the delivery of services within the bounds of the revenue sources they have available.

Without supportive guidance there is likely to be an increasing inability to meet the future needs demanded by their communities. It is essential that confidence in lifecycle costing, and customer engagement strategies improve thereby ensuring the affordable finance is allocated at the most appropriate time to mitigate risks to future service delivery.

The challenge for councils is to undertake meaningful engagement with their communities on the value for money proposition while demonstrating they are financially, environmentally, and socially responsible.

Effective community engagement allows government to tap into diverse perspectives and potential solutions to improve the quality of its decisions. It enables citizens and communities to better understand the processes of government and to build their capacity to participate in deliberative processes through the acquisition of confidence, skills, knowledge, and experience.

Questionable performance reporting

The ratio indicators and result target ranges applied to report the financial and asset management performance of Western Australian councils and the weighting given to each indicator in assessing a council's overall performance and position via the 'MyCouncil' website warrant review. Use of indicators is encouraged but the currently applied indicators, targets, and weightings are sub optimal and, in some instances, not conducive to supporting improved financial sustainability.

An approach that highlights the primary indicators and targets that drive financial sustainability imperatives at a local, regional, jurisdictional, and national level should be the focus. In other words, less indicators the better. Indicators that offer tangible benefit to decision makers. Too many indicators become a box ticking exercise and decision makers rarely know which ones to focus on and invariably pick those that make them look better than other councils, generally at the expense of the indicators that they should be focussing on.

Aversion to debt

An Access Economics' 2006 Report² identified an aversion to borrowing by councils and suggested that it was contributing to the incurring of underspending on asset renewal. It concluded that 'the long-run decline in councils' reliance on borrowing needs to be reversed'. Our research suggests that this has not occurred as most WA councils balance sheets tend to be very strong.

There is an assertion that many councils, if they are likely to be able to operate in a financially sustainable manner in future (that is, if they are able to achieve and maintain a satisfactory underlying operating surplus result), have capacity to make greater use of debt if so warranted.

² P.39 Access Economics 2006, Local Government Finances in Western Australia

Addressing the Issues

The key to meeting the identified challenges is to match the community's need for services with their ability and general acceptance to pay. It requires:

- Improved service planning to define what services the community can afford over the short, medium, and long-term,
- Ensuring a net operating surplus over a 3–5-year or longer period while accepting the service levels and risk consequences.
- Careful consideration of the financial implications of acquiring new assets.
- Community engagement to inform on current and projected service levels, risks and costs, and
- Informed and trained infrastructure asset managers that guide councils' planning, budget and investment decisions.

This requires strong leadership from the department and local government councillors and executive.

In recognition of the ALGA 2021 National State of the Assets report findings, IPWEA believes the 'Local Government Financial Sustainability – Nationally Consistent Frameworks' which were agreed to in 2007 and 2009 need to be re-activated. The Frameworks provide a scalable and consistent approach to address the issues identified by encouraging all councils to achieve and maintain at least a core level of maturity. Those councils who wish to progress to a more advanced level of maturity can do so under the same framework.

Everyone agrees the long-term financial sustainability of local councils requires good asset management integrated with the financial planning and reporting task. When councils fail to budget appropriately for the cost of maintaining, replacing, and upgrading built assets, they risk being unable to provide and maintain safe and reliable services to the community.

Reliability of data inputs need to improve

Fragmented systems combined with low data confidence does not bode well for ensuring an affordable and sustainable future is possible. If councils are to manage and provide services from infrastructure in a financially sustainable way, it is critical they take a consistent approach to data integrity and improvement.

Focus on the key performance indicators

Key performance reporting indicators are signals used to convey evidence of certain directions being taken by a council and to assess whether or not desired outcomes are being achieved.

To be effective, it is essential that these indicators:

- measure those factors which define financial sustainability;
- be relatively few in number; and
- be based on information that is readily available and reliable.

Indicators are measures of outputs or outcomes. Individually and without associated explanations, they can only ever tell part of the story.

It is important to put indicator results in context and to understand that they only give an indication of where to start looking for the reasons behind differences. The usefulness of indicators is not in the numbers themselves but the analysis of what is driving the indicator.

It may, therefore, be more useful to consider the combined results of several broad indicators in assessing performance rather than any one indicator on its own.

In keeping with the National Frameworks, IPWEA supports the use of indicators that support:

1. Income generating efforts
2. Efficiently delivered services that are appropriate to needs
3. Short and long-term financial sustainability
4. Ability to maintain, renew and upgrade assets

The primary financial sustainability indicators to support these imperatives are:

1. Operating Surplus Ratio
 - a. $\frac{\text{Operating result (exclusive of capital income)}}{\text{operating income (also exclusive of capital income)}}$
2. Net Financial Liabilities Ratio
 - a. $\frac{\text{Net Financial Liabilities}}{\text{Operating Income}}$
(Note: Net Financial Liabilities = Total Liabilities less Financial Assets)
3. Asset Renewal Funding Ratio
 - a. $\frac{\text{Actual or proposed renewal expenditure for a period}}{\text{Renewals as deemed warranted in an AMP for the same period}}$

Indicative targets for councils are:

1. Operating Surplus Ratio between 0% and 10% over any five-year period.
2. Net Financial Liabilities Ratio between 0% and 100% of operating income.
3. Asset Renewal Funding Ratio between 90% and 110%.

Details on the basis for these indicators can be sourced from the:

- Local Government Financial Sustainability Nationally Consistent Frameworks (2007 – 2009)

- Australian Infrastructure Financial Management Manual (IPWEA, 2015)
- International Infrastructure Financial Management Manual (IPWEA, 2020)

Need for audit and follow up

In the years following the national local government reform initiatives, Western Australian councils were progressing well in implementing the National Frameworks. However, it is apparent the momentum and commitment has waned in recent times, mainly due to poor audit and follow up. If the challenge is to be overcome, continual improvements in infrastructure planning and financial management must be an absolute imperative.

Councils can do this by ensuring the lifecycle forecasts in the asset management plan are considered and incorporated into the long-term financial plan. These forecasts need to be updated annually to generally ensure ongoing achievement of (or at least satisfactory progress towards) a net operating surplus over the immediate 3–5-year period. The LTFP then becomes the basis for preparing each year's annual budget.

Local governments are required to focus on a minimum 10-year planning period and strive for small ongoing operating surpluses based on accrual accounting principles. Accrual accounting recognises asset depreciation and generating revenue sufficient to offset operating expenses including depreciation (based on periodically revised asset values) facilitates the generation of funds that can help address ongoing asset renewal needs.

Achieving a sustainable position in providing services is not a once-off task. It is an ongoing essential part of local government business in providing services to their communities.

It is therefore essential that asset management and long-term financial plans are regularly updated. An annual update ensures organisational resilience to deal with emerging unplanned expenditure during times of significant disruption and changing circumstances.

Appropriate audit parameters ensure a level of assurance that asset management and financial planning information is reliable and compliant with legislated requirements.

A simple ongoing program that audits asset and financial plans to understand their currency, update frequency and maturity would help ensure alignment with legislative requirements and the IP&R and National Frameworks. This need not be costly or complex or require additional auditing analytical skills and could easily be undertaken by each council's appointed external auditor adopting a simple and pragmatic approach.

The Department itself could:

- Develop an ongoing audit program that tests the existence, currency and alignment of the asset management and financial plans.
- Test if the:
 - Asset Management and Financial Plans are adopted within 12-months of each general election;
 - Forecast expenditure needs identified in the adopted Asset Management Plan are included in the Long-term Financial Plan.

Provide support to where it is needed most

Without supportive guidance there is likely to be an increasing inability of councils to meet the future needs demanded by their communities. It is essential that confidence in lifecycle costing, and customer engagement strategies improve thereby ensuring that affordable finance is allocated at the most appropriate time to mitigate risks to future service delivery.

- Provide targeted support to those councils that have demonstrated asset management and financial sustainability challenges.

This could be delivered by a government sponsored mentoring service utilising asset management planning and financial tools, templates, and specialist training that already exist in the sector.

Deploy skilled infrastructure asset managers

Resourcing the asset management system involves having skilled people capable of reporting the capacity of the organisation to meet its strategic and asset management objectives. The skill requirements of the asset manager have changed significantly in recent times, requiring not just technical expertise but strategic and financial planning insight, and stakeholder engagement knowledge and much more.

Prior to the COVID pandemic the shortage of skilled asset managers was an issue and will likely exacerbate if left unattended. It is necessary therefore to consider:

- Developing ongoing asset management capacity building programs that assist councils in meeting and maintaining at least core level asset management maturity.
- Raising awareness of the importance of sustainable asset management amongst elected representatives and senior management within the sector.
- Enhancing collaboration within the sector to develop specialised infrastructure management training programs for local government practitioners.

- Investigating innovative solutions to address the skills shortage within the asset management discipline that promotes sector wide collaboration.

Shared resources can be appropriate where gaps exist for those councils who face financial, physical and location constraints. Success is dependent on having an effective governance structure in place.

Support and Resources

For many years, IPWEA has been pleased to support the Local Government sector in assisting councils improve their expertise in asset management and long-term financial planning.

We believe past department initiatives have been positive and councils have improved their skills base, however there is clearly much more to do.

The momentum, and extent of reform, must not be lost.

It is likely that many councils still have 'information gaps' in their overall planning process. It is crucial to demonstrate effective management of infrastructure assets and that current asset management systems provide for the true lifecycle costs to be accurately captured, evaluated, and reported on a consistent basis.

Guidance that assists local governments implement effective asset management systems and prepare asset management plans have been available since 1994 with the development of both the Institute of Public Works Engineering Australia's (IPWEA's) National Asset Management Manual and International Infrastructure Management Manual (2002) and subsequent updated editions in line with the international standards.

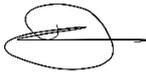
It is worth highlighting the Department of Local Government's Integrated Planning and Reporting Framework is also informed by the:

- Local Government Financial Sustainability Nationally Consistent Frameworks 2 & 3 published by the Local Government and Planning Ministers' Council;
- IPWEA's – National Asset Management Strategy (NAMS.AU) Policy documents;
- IPWEA International Infrastructure Management Manual; and
- IPWEA Australian Infrastructure Financial Management Manual.

The IPWEA NAMS+ structured asset management program aligns with the IIMM principles, the National and WA IP&R Frameworks and provides various support tools and templates to assist councils in preparing asset management plans. Currently, 25 Western Australian councils subscribe to NAMS+, down from a peak of 45 in previous years.

In addition to our detailed response to the proposed reforms we have summarised our comments in the departments consultation paper template which is attached to this document.

We look forward to hearing how the proposed Western Australian Local Government Act reform initiative unfolds. If you have any questions, we would be happy to hear from Department representatives to discuss further.



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