Financial sustainability in Australian local government

Australian Local Government Association

2 July 2024

SGS Economics & Planning

Certified B Corporation

SGS Economics and Planning acknowledges the First Nations Peoples of Australia and on whose Country we live and work.

SGS Economics and Planning acknowledges that the Aboriginal and Torres Strait Islander peoples of Australia are one of the oldest continuing living cultures on Earth, have one of the oldest continuing land tenure systems in the World, and have one of the oldest continuing land use planning and management systems in the World.

We pay our respects to the First Nations Peoples, past and present, and acknowledge their stewardship of Country over thousands of years.

SGS Economics and Planning Pty Ltd
ACN 007 437 729
www.sgsep.com.au

OFFICES IN CANBERRA, HOBART, MELBOURNE, AND SYDNEY ON THE COUNTRY OF THE NGAMBRI/NGUNNAWAL/NGARIGO, MUWININA/PALAWA, WURUNDJERI, AND GADIGAL PEOPLES.

Executive Summary

SGS Economics and Planning has prepared this analysis to support ALGA in its submission to the Inquiry into Local Government Sustainability.

This paper quantifies the instances and implications of local government finances at risk through the lens of conventional financial performance indicators, the degree of vertical fiscal imbalance, uneven service access across Australia, and the influence of the Commonwealth on spending decisions at the state and local government level.

Key findings include:

Financial sustainability

- In 2021-22, over a quarter of all Australian councils assessed in this report experienced low financial sustainability. These councils only met one or none of the conventional tests of financial sustainability out of three indicators. These indicators are: an operating surplus ratio of between 0-10%, a debt service ratio of <60%, and an asset sustainability ratio of >90%.
- Between 2016-17 and 2021-22, the highest proportions of councils by jurisdiction experiencing low financial sustainability was in Tasmania (66%) and Queensland (39%).
- A significant proportion of councils also cannot properly maintain assets due to revenue constraints. Cumulative asset maintenance shortfalls therefore worsen over time.
- Compound annual growth in Australian local government expenditure was 2.4 per cent, compared to a 2.6 per cent compound annual growth in the Consumer Price Index over the same period. This represents a cut in real terms, as growth lags inflation.
- This is leading to potential trade-offs and/or budget reallocations between core services, with the Northern Territory, South Australia, and other jurisdictions reducing spending on General Public Services and Social Protection over the last decade.

Vertical fiscal imbalance

- Many councils are highly dependent on grants from other tiers of government.
- Long-term growth in local governments' own-source revenue has stagnated relative to state and Commonwealth revenue growth. This is compounded by rate pegging and capping in Victoria and New South Wales.
- There are many instances of state governments shifting services to councils without commensurate resourcing.

Uneven service access across Australia

- Service and infrastructure access across Australia is not equal. Even between capital cities, there is a disparity in access to services. This has implications for equitable outcomes in community wellbeing.
- The value of Financial Assistance (FA) Grants as a proportion of Commonwealth Government outlays, Commonwealth taxation revenue, Gross Domestic Product has shrunk over time.

Financial barriers to local decision-making

- The number and value of state and Commonwealth programs involving tied funding to councils has grown over recent decades.
- The competitive nature of state and Commonwealth programs also makes tied grant funding difficult to access for many local communities. This weakens the effectiveness of grants as a revenue source for local government.

A $7 billion boost to national Gross Domestic Product from improving financial sustainability in local government

Greater local government financial sustainability would boost productivity, Gross Domestic Product (GDP), employment and tax revenues. Productivity gains would arise from a range of efficiencies. This includes:

- saved vehicle operating and accident costs on better maintained roads,
- health cost savings as communities make greater use of appropriately equipped and programmed open spaces,
- saved time and costs for development proponents as councils deal with their applications expeditiously, and
- savings in recruitment and training costs in councils as they will be better able to offer career pathways.

This research has modelled the economic benefits from these efficiencies. This modelling suggests that:

- A $1 billion dollar investment in local government road maintenance will deliver a $3.5 billion increase in real GDP.
- $250 million invested in better supply and curation of parks and gardens will result in a $900 million GDP boost
- Efficient design of regulatory processes within councils can yield an annual benefit of $1.6 million. If realized across Australia's 537 councils, this would increase GDP by $1.7 billion.
- Increased block transfers of funds from Commonwealth and states to local government can save $235.64 million in administrative costs and increase GDP by $300 million each year.
- Increase retention of local government workers can save up to $424.5 million in administration costs and boost GDP by $600 million each year.

01 Financial sustainability

Indicators of financial sustainability

There are three key indicators of financial sustainability in the Australian local government sector:

- **Operating surplus ratio**: A measure of councils' financial health. A positive ratio indicates that the council generates more revenue (excluding grants and other contributions) than operational expenditure. A negative ratio indicates that operational expenditure exceeds revenue.
- **Debt service ratio**: A measure of the proportion of councils' general income used to repay financial liabilities. If financial liabilities account for a significant portion of operating revenue, a council will have limited capacity to increase loan borrowings and may experience stress in servicing existing debt.
- **Asset sustainability ratio**: A measure of whether assets are being renewed and replaced in an optimal way, relative to depreciation. A ratio below 100 per cent could indicate underinvestment and lead to higher costs in the future.

Generally, councils are considered 'financially unsustainable' if they have experienced an operating deficit for several years, a relatively high net financial liabilities ratio, and are without a clear plan to address these matters.

Councils must report their financial performance to their jurisdiction's audit department each financial year. Where available, it has been used by SGS to generate a headline assessment of local governments' financial sustainability. Northern Territory and South Australia are excluded from the analysis due to a lack of easily accessible data.

FINANCIAL SUSTAINABILITY INDICATORS: CALCULATION AND THRESHOLDS BY JURISDICTION

Juris-diction	Operating surplus	Debt service ratio	Asset sustainability ratio	Assessment of financial sustainability
NSW	Net operating result divided by operating revenue (excl. grants and contributions). Target: 0 - 10%.	Cost of debt service divided by operating revenue (excluding grants and contributions) . Target: 0 - 20%.	Capital expenses on replacement of assets (renewals), divided by depreciation expenses. Target: > 100%.	**High:** Meets all 3 targets. **Medium:** Meets 2 of 3 targets. **Low:** Meets one or none of 3 targets.
VIC	Net operating result divided by operating revenue (excl. grants and contributions). Target: 0 - 10%.	Total liabilities less current assets, divided by operating revenue. Target: < 60%.	Capital expenses on replacement of assets (renewals), divided by depreciation expenses. Target: > 100%.	**High:** Meets all 3 targets. **Medium:** Meets 2 of 3 targets. **Low:** Meets one or none of 3 targets.
QLD	Net operating result divided by operating revenue (excl. grants and contributions). Target: 0 - 10%.	Total liabilities less current assets, divided by operating revenue. Target: < 60%.	Capital expenses on replacement of assets (renewals), divided by depreciation expenses. Target: > 90%.	**High:** Meets all 3 targets. **Medium:** Meets 2 of 3 targets. **Low:** Meets one or none of 3 targets.
WA	Net operating result divided by operating revenue (excl. grants and contributions). Target: 0 - 10%.	*Data unavailable.*		**High:** Financial Health Indicator (FHI) >= 70 **Medium:** FHI >= 50 **Low:** FHI < 50
TAS	Net operating result divided by operating revenue (excl. grants and contributions). Target: 0 - 10%.	Total liabilities less current assets, divided by operating revenue. Target: < 60%.	Capital expenses on replacement of assets (renewals), divided by depreciation expenses. Target: > 90%.	**High:** Meets all 3 targets. **Medium:** Meets 2 of 3 targets. **Low:** Meets one or none of 3 targets.

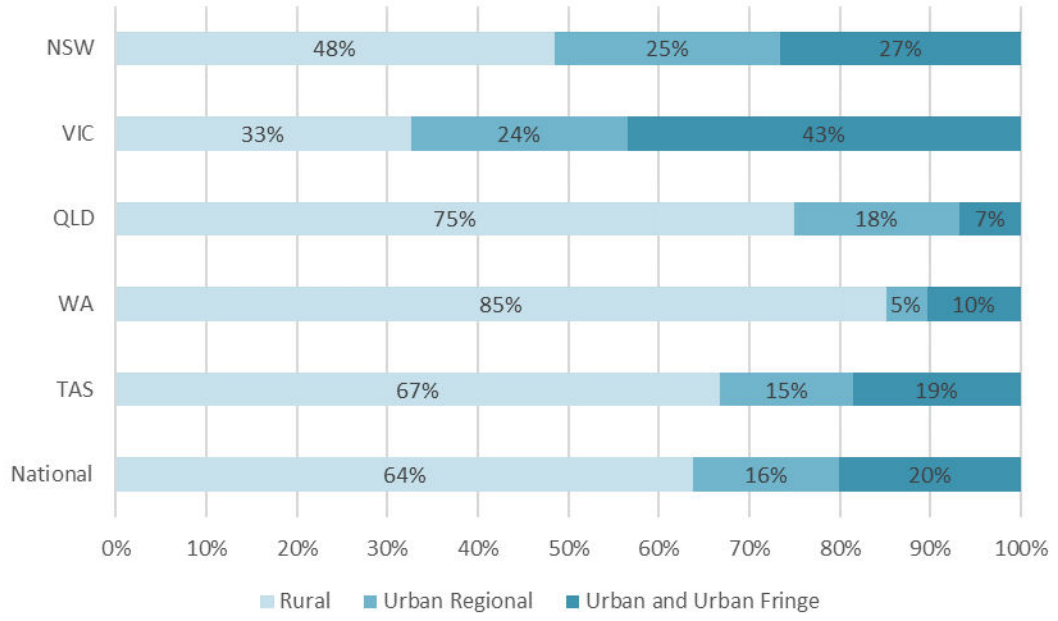
Notes: The WA Government provides a Financial Health Indicator (FHI) for each local council. Targets by indicator have been sourced for each jurisdiction where publicly available. Sources: YourCouncil NSW; Victorian Audit Office; Queensland Audit Office; Tasmania Government; WA MyCouncil.

Without financial assistance grants and other contributions, a significant proportion of councils would not meet conventional tests of financial sustainability

Operating surplus ratio

- The operating surplus ratio indicates the extent to which revenues raised cover operational expenses. It is the total continuing operating revenue (excluding capital grants and contributions) minus operating expenses, as a proportion of total continuing operating revenue. Councils should try to maintain a positive operating surplus ratio because grant funding certainty and continuity is not always guaranteed.
- There were 268 councils nationally who did not meet the target operating surplus ratio of 0 to 10 per cent in 2021-22. A jurisdictional breakdown is as follows: 87 councils in Western Australia, 64 councils in New South Wales, 46 councils in Victoria, 44 councils in Queensland, 27 councils in Tasmania.
- Rural councils are disproportionately affected by the inability to generate sufficient operating income above operating expenditure. 64 per cent of all councils nationally who did not achieve a target operating surplus ratio in 2021-22 were rural councils (171 councils).
- 87 councils in Western Australia did not meet this target in 2021-22, of which 74 (85%) were rural councils. In Queensland, the share of Rural councils not meeting this target was 75% (33 of 44 councils).
- The average operating surplus ratio for councils considered in this analysis was -1.8 per cent. This signals financial stress at the sector scale.

SHARE OF COUNCILS NOT MEETING OPERATING SURPLUS TARGET BY REMOTENESS CATEGORY, 2021-22

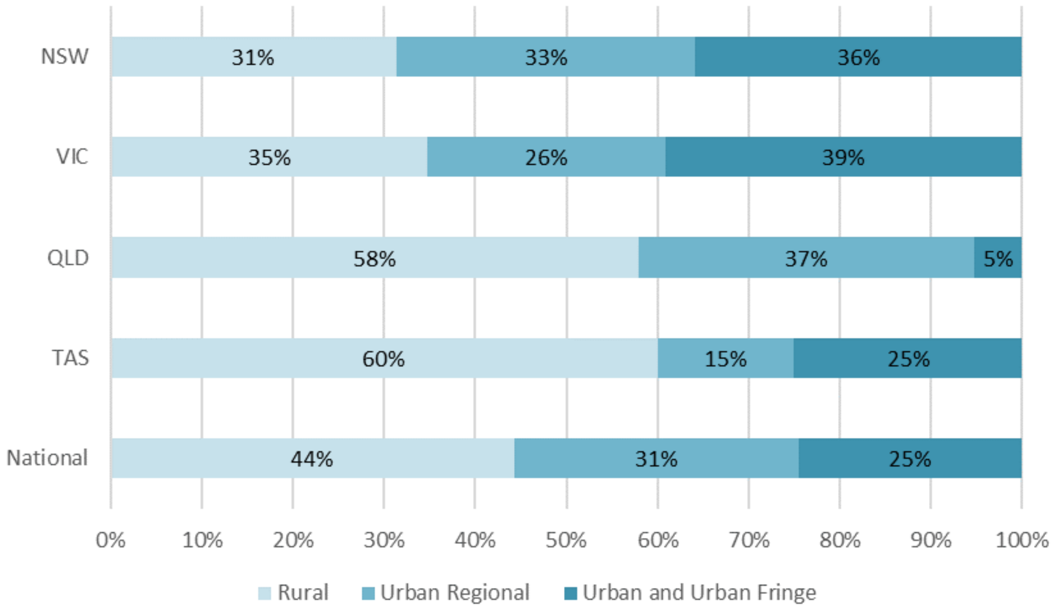


Source: SGS Economics and Planning (2024).

Asset sustainability ratio

- There were 167 councils nationally who did not meet the target asset sustainability ratio (>90 per cent) in 2021-22. This comprised 67 councils in New South Wales, 57 councils in Queensland, 23 councils in Victoria, and 20 councils in Tasmania.
- Rural councils are over-represented in this analysis. This is due to their limited financial flexibility from smaller rate bases and large infrastructure assets. 44 per cent of all councils who did not meet this target were rural councils.

SHARE OF COUNCILS NOT MEETING ASSET SUSTAINABILITY TARGET BY REMOTENESS CATEGORY, 2021-22

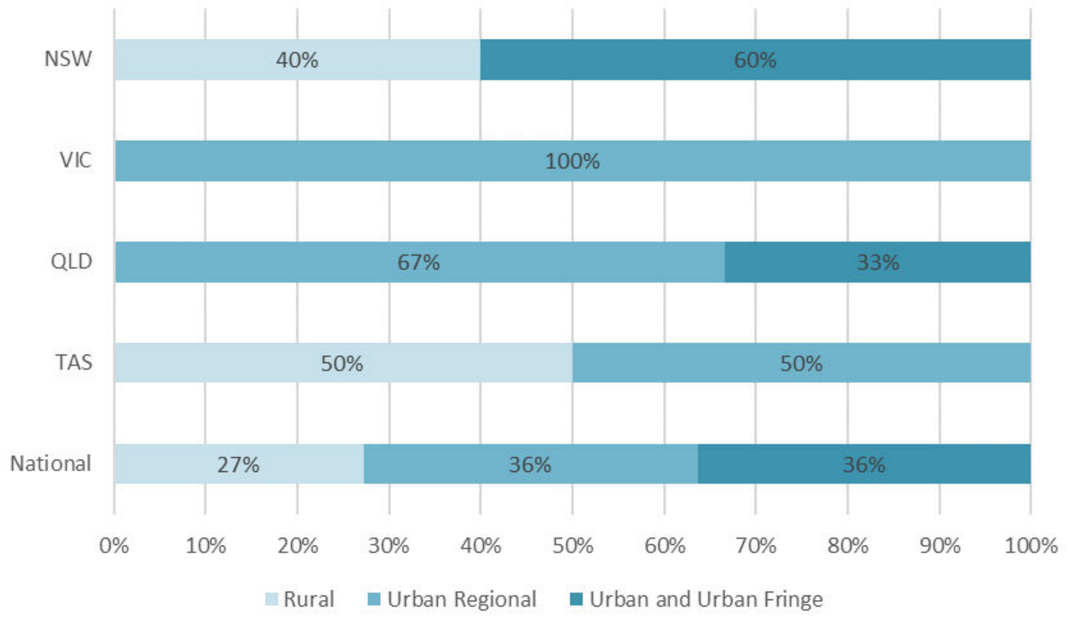


Source: SGS Economics and Planning (2024).

Debt service ratio

- Based on available data, 11 councils nationally did not meet debt servicing targets in 2021-22. This comprises 5 New South Wales councils, 3 Queensland councils, 2 Tasmanian councils, and 1 Victorian council.
- This provides evidence that the majority of councils are financially responsible and have sufficient operating income to service debt obligations.
- 1 Victorian council had a debt service ratio of over 100 percent.
- For Queensland councils who did not meet debt service ratio targets, their debt service ratios ranged from 67 to 125 per cent.
- For Tasmanian councils who did not meet debt service ratio targets, their debt service ratios ranged from 61 to 74 per cent,
- *Note*: The New South Wales councils who did not meet targets reported no debt. The benchmark is greater than 0 per cent and less than 20 per cent.

SHARE OF COUNCILS NOT MEETING DEBT SERVICING TARGET BY REMOTENESS CATEGORY, 2021-22



Source: SGS Economics and Planning (2024).

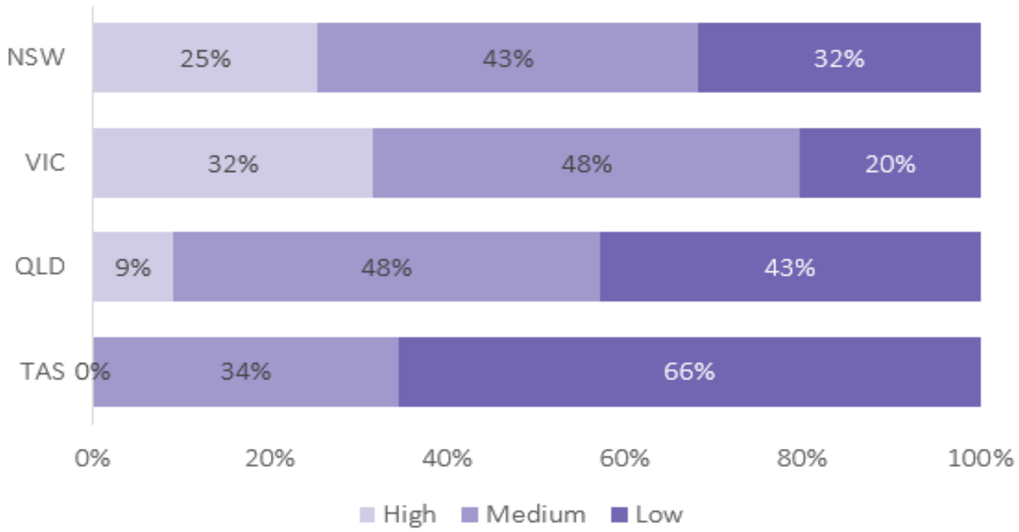
Over a quarter of all Australian councils experienced low financial sustainability in 2021-22

Consolidating national performance on the three financial stability indicators shows that:

- 27 per cent of all councils considered had low financial sustainability in 2021-22.
- Tasmania had the highest proportion of councils (66 per cent) with low financial sustainability, followed by Queensland (43 per cent) and New South Wales (32 per cent) (see chart at top right),.

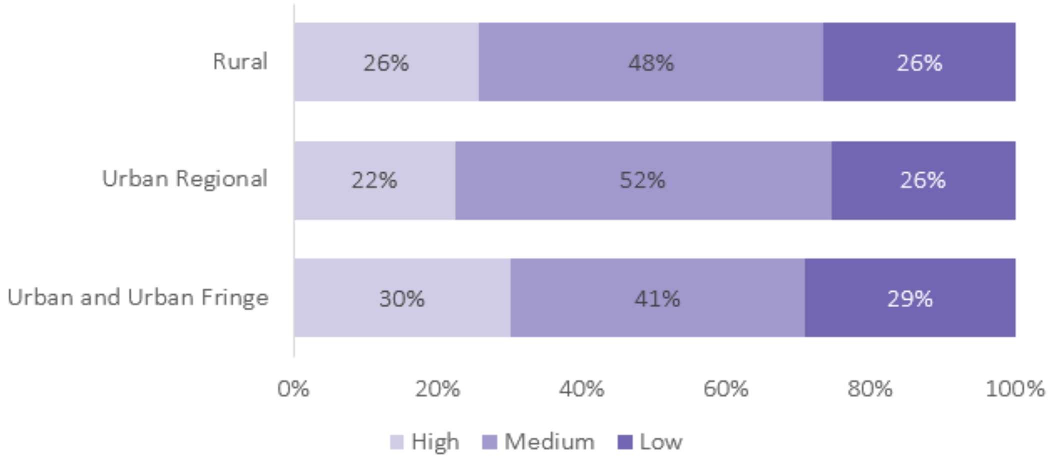
Overall, financial sustainability in Australian local government did not differ markedly by remoteness. Approximately half of all councils, regardless of remoteness, had moderate financial sustainability. The remaining councils are roughly evenly split between the high and low financial sustainability categories.

% OF COUNCILS BY CATEGORY OF FINANCIAL SUSTAINABILITY, 2021-22



Note: Western Australia is excluded from this consolidated analysis as asset sustainability ratio data is not available.

% OF COUNCILS BY CATEGORY OF FINANCIAL SUSTAINABILITY AND REMOTENESS, 2021-22



Source: SGS Economics and Planning (2024).

Many councils have consistently fallen short of financial sustainability targets over the past five years

Assessing the **operating surplus ratio** and **asset sustainability ratio***as a five-year average provides additional insight into council financial sustainability.

On average over the past five years:

- Tasmania had the highest proportion of councils (66 per cent) with low financial sustainability. These were councils that met at most one of three indicator targets.
- Thirty nine per cent of Queensland councils had low financial sustainability over the past five years. This is less than the forty three per cent of councils with low financial sustainability in 2021-22.

Comparing the five-year average to 2021-22 results shows that Victoria had the highest proportion of councils shift into the band of low financial sustainability.

**Debt service ratio is best used as a point-in-time ratio. Only the most recent year of data for councils is used for the purposes of this assessment.*

% OF COUNCILS NOT MEETING FINANCIAL SUSTAINABILITY TARGETS OVER 5-YEAR PERIOD

	5-year average				
Jurisdiction	% councils not meeting operating surplus ratio targets	% councils not meeting asset sustainability ratio targets	% councils by category of financial sustainability		
			High*	Medium	Low
NSW	45%	60%	20%	52%	28%
VIC	37%	22%	56%	29%	15%
QLD	64%	53%	18%	43%	39%
TAS	97%	72%	0%	34%	66%

Source: SGS Economics and Planning (2024). Data for Northern Territory and South Australia is not available, per earlier analysis. Western Australia is excluded from this consolidated analysis as asset sustainability ratio data is not available. *The ‘High’ category of financial sustainability includes councils whose five-year average performance on the operating surplus and asset sustainability ratios met target and whose most recent performance on the debt service ratio met target.

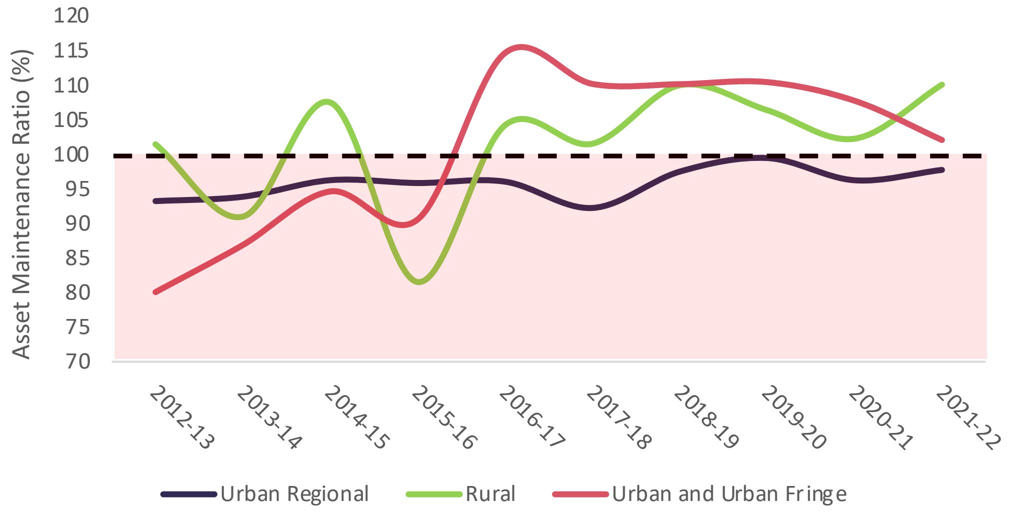
A significant proportion of councils cannot properly maintain assets due to revenue constraints

Australian councils managed over $588.6 billion worth of non-financial assets in 2022-23. Councils should aim to renew assets at a rate equal to or greater than depreciation. Spending on asset renewal is not keeping pace with the rate of asset deterioration for a significant number of councils. The cumulative impacts of these renewal gaps are significant.

Based on available data for 2020-21:

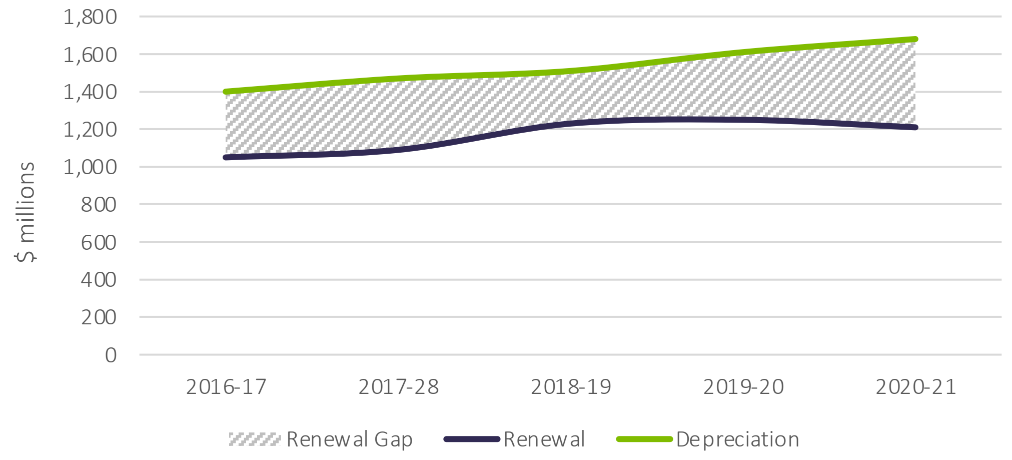
- 50.8 per cent of councils in New South Wales (65 councils) reported that their required asset maintenance expenditure in that year was greater than their actual asset maintenance expenditure. This suggests that many councils do not have the funding to meet their asset maintenance requirements each year.
- While rural and urban councils have generally met this target over the years, urban regional councils have consistently fallen short over the past decade. The figure at top right shows the average asset maintenance ratio across all New South Wales councils by regional classification. A ratio equal to or greater than 100 per cent indicates that sufficient funds are being directed towards asset maintenance and renewal.
- Victorian local governments reported a total asset renewal gap of $470 million in 2020-21, and a cumulative total asset renewal gap of $1.84 billion between 2016-17 and 2020-21 (graph at bottom right). Depreciation can be considered a proxy for the funding required to renew assets each year. Depreciation greater than renewal expenditure indicates a shortfall in capital maintenance.

AVERAGE ASSET MAINTENANCE RATIO BY REGIONAL AREA, NSW (2013-2022)



Source: NSW Office of Local Government.

TOTAL ASSET RENEWAL GAP, VICTORIA (2017-2021)



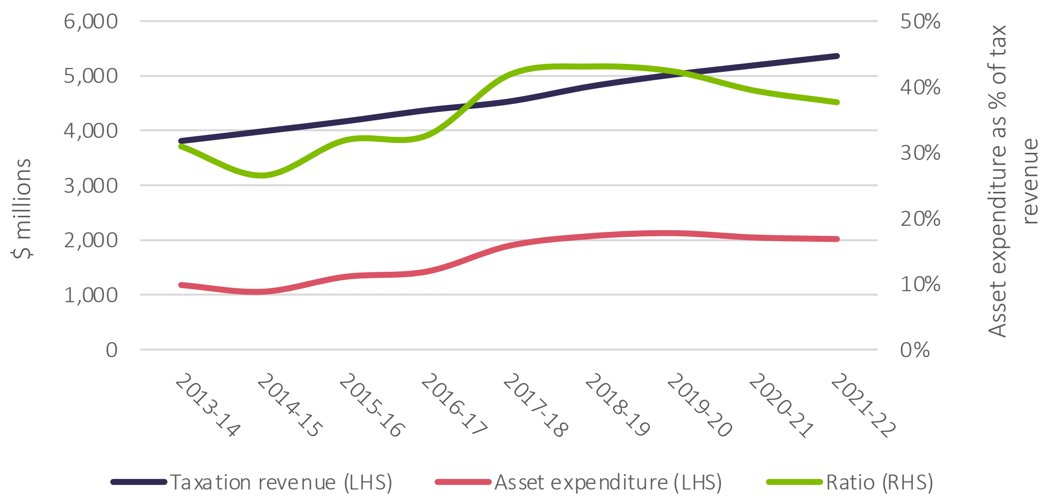
Source: Municipal Association of Victoria.

Asset maintenance shortfalls risk becoming worse as cumulative renewal gaps grow each year

Asset maintenance expenditure has fallen as a proportion of local government taxation revenue in New South Wales since 2018-19.

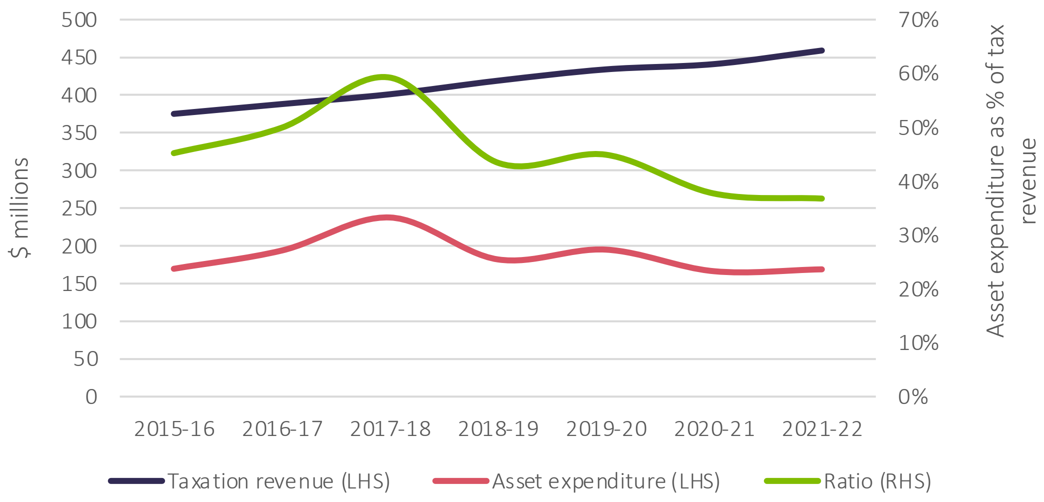
Asset maintenance expenditure in Tasmania has fallen from 59 per cent of local government taxation revenue in 2017-18 to only 37 per cent in 2021-22.

ASSET EXPENDITURE AS % OF LOCAL GOVERNMENT TAXATION REVENUE, NSW (2014-2022)



Source: SGS Economics and Planning (2024), NSW Office of Local Government; ABS Government Finance Statistics.

ASSET EXPENDITURE AS % OF LOCAL GOVERNMENT TAXATION REVENUE, TASMANIA (2016-22)



Source: SGS Economics and Planning (2024), Tasmanian Local Government Consolidated Data Collection; ABS Government Finance Statistics.

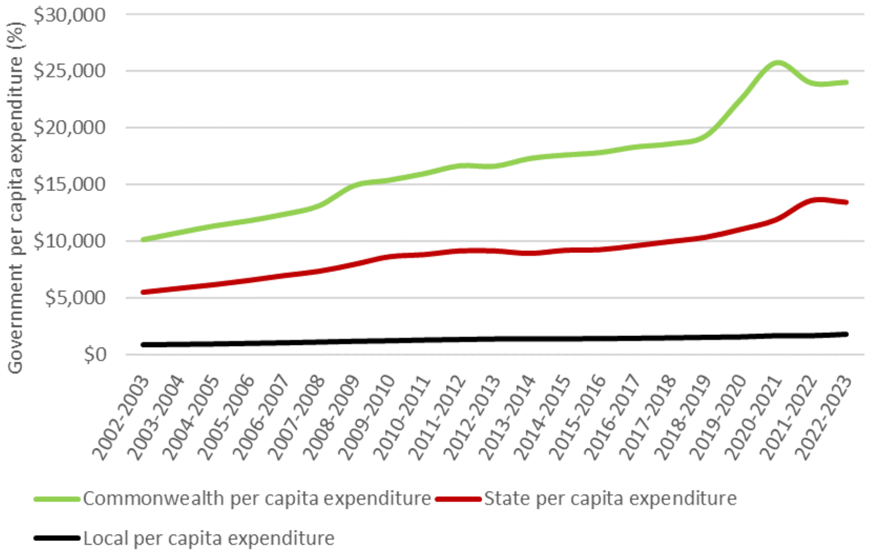
Local governments' growth in per capita expenditure lags that of other tiers of government

Councils make good use of the limited funds available to them. Local governments' **per capita expenditure** has grown at a slower pace over the last two decades than in state and Commonwealth governments. Between 2002-03 and 2022-23 local government expenditure doubled form $887 per capita to $1,801 – a multiple of 2.03, compared to a multiple of 2.4 for state and 2.36 for Commonwealth governments.

Local government also has the lowest **compound annual growth rate of per capita government expenditure** of all three tiers. This comes as councils experience ongoing pressures to expand the range and community access to services.

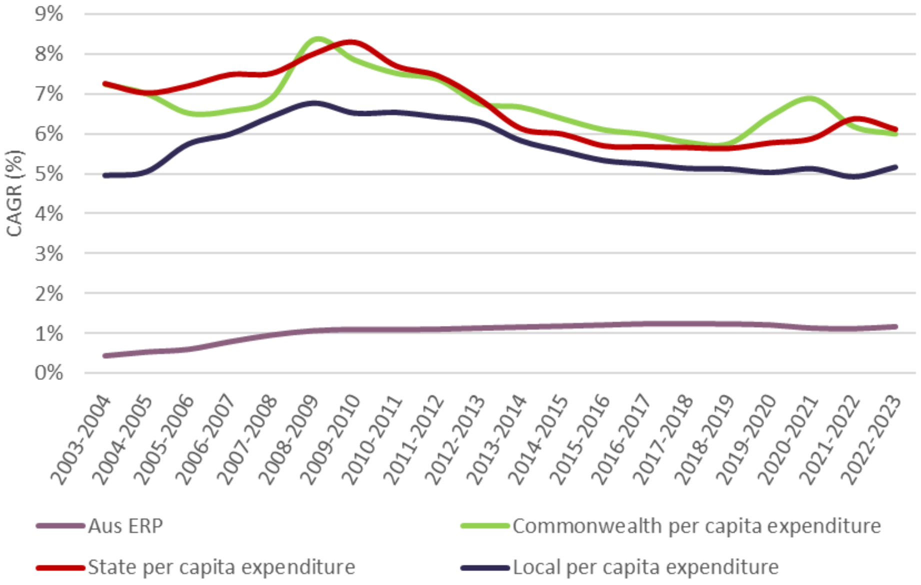
Local government consistently has higher levels of community trust than the State and Commonwealth Governments (Stoker et al, 2018). Trust is, in part, linked to the quality and reliability of government services delivered. Local government has maintained high satisfaction levels with slow growth in resources.

GOVERNMENTS' PER CAPITA EXPENDITURE, 2002-03 TO 2022-23



Source: SGS Economics and Planning (2024), ABS Government Finance Statistics.

GOVERNMENT EXPENDITURE PER CAPITA & ESTIMATED RESIDENT POPULATION, 2003-04 TO 2022-23



Source: SGS Economics and Planning (2024), ABS Government Finance Statistics.

Financial pressures place core and valued services at risk

Local government is under financial pressure. This pressure has far-reaching impacts on both councils and communities. The following examples shed light on pressures stemming from the inadequacy and inflexibility of funding, state and federal funding arrangements that are no longer fit for purpose, cost shifting, rate capping and rate pegging.

New South Wales

- **Georges River Council** has experienced reported projected operating and cash flow deficits. These were worsened by 'higher than anticipated costs and reduced income in 2019-20 and 2020-21' due to the COVID-19 pandemic. Georges River Council also faces a longer-term trend of growth in operating expenditure that exceeds growth in operating income.

  Impacts: Since 2016-17, Georges River Council has implemented a range of cost containment strategies to manage financial pressures. Publicly reported impacts highlight voluntary redundancies and the removal of staff benefits between 2016 and 2019. In 2020-21, Georges River Council reported a deferral of capital projects, including of the 'new skate park, public art program, synthetic fields program, San Souci Bathers Pavilion construction, and Hurstville Civic Precinct development'.

  To improve long-term financial sustainability, Georges River Council successfully applied for a Special Variation (SV) and Minimum Rate Application from 2021-22. Without the SV, however, the council had contemplated 'reducing the number of hours libraries are open, reduction of total employee numbers by 120 (over three years), the closure of childcare centres, reduction of the frequency and extent of maintenance of open spaces, parks, sporting fields, and reduced maintenance of council assets leading to their deterioration'. Although the SV was approved on this occasion, this illustrates that councils must resort to deferring, reducing, or deleting capital projects and services, which impacts community outcomes.

- Cessation of the Resources for Regions scheme in the 2023-24 State Budget. The program supported the ongoing prosperity of mining communities in regional NSW by providing vital infrastructure, economic opportunities, and positive social outcomes.

  Impacts: At least **26 regional councils** have benefitted as grant recipients since 2012. Discontinuing this funding will make it harder for councils to deliver new community infrastructure and services, economic opportunities, infrastructure upgrades, tourism projects, sports facility upgrades, walking and cycling tracks, main street beautification projects, improvements to amenity and public spaces, targeted skills development programs, community events and more.

Financial pressures place core and valued services at risk

New South Wales (cont'd)

- The New South Wales Government cut public library funding by 5 per cent in 2018-19. New South Wales already has a lowest proportionate state government funding contribution compared to other jurisdictions

  Impacts: Reducing library funding impacts the diversity of community programs on offer, events and meeting spaces, digital access, a community hub, and administration support hubs. *See also:* example of impacts to City of Greater Geelong's libraries.

- Rate pegging imposes significant challenges to councils' ability to fund infrastructure and services. **Warren Shire Council** noted that 'there are no more creative solutions to address the financial constraints from rate pegging, except reductions in levels of service, poor condition ratings of assets and higher risks in regard to public liability insurance actions.'

  Impacts: In 2021, Yarram, Dollery & Tran's empirical analysis found that rate capping reduced council budgets for aged care and disability services (in metropolitan, regional and rural councils) and reduced expenditure on family and community services in urban councils.

Victoria

- Cost shifting, specifically the transfer of service responsibilities to local government (e.g. the Victorian Government's year-old Kindergarten Reform Agenda) without corresponding state government funding is another source of financial pressure for many councils. Some council-run childcare centres have been running at significant losses for some time. Capital grants provided to local government to build new facilities often do not include ongoing operational funding for the maintenance of the facility over time. Councils are often left to find these resources from within their existing budgets.

  Impacts: Many councils are reconsidering their future role as a service provider, given the infrastructure gaps and the high wage costs of service delivery compared to when these services are delivered by the private and the not-for profit sectors. **Knox City Council** will cease standalone kindergarten services from January 2025, citing that local government funding has not kept up with the cost of providing many of the services provides on behalf of state and federal governments.

Financial pressures place core and valued services at risk

Victoria (cont'd)

- In 2022, the **City of Port Phillip** was among 23 Victorian councils that have either withdrawn or are in the process of ceasing in-home aged care services. The federal government's aged care reforms will transition from block funding, where councils receive money to provide services based on the number of people needing support, to a consumer-directed or 'packaged' model where funding is based on individual need and provider(s) of choice. The City of Port Phillip estimates that keeping its in-home aged care service would require a new delivery model costing $1.42 million annually, a threefold increase to current costs.

  Impacts: Withdrawal of aged care services (domestic assistance, personal care, shopping assistance, property maintenance), with services to be outsourced to a private provider. While an exit from the service may be a positive outcome for councils who no longer need to fund it, short-term implications include the redundancy of council staff and the costs of ensuring a smooth transition of service for affected residents. Moreover, the withdrawal of aged care services in remote localities has significant impacts if neither non-governmental organisations nor private operators are present to fill the service gap. Some councils therefore continue to provide the service at a loss or at the expense of maintaining other assets or cutting other services.

- Disparity in proportionate state and local government contributions towards library projects. For example, Victorian government has provided $1.5 million via a Living Libraries Grant to the Biyal-A-Armstrong Creek library, compared to $20.36 million contributed by the **City of Greater Geelong.** In 2023-24, shortfalls in the City of Greater Geelong's draft budget led to plans to close library branches in Geelong West, Highton, and Barwon Heads.

  Impacts: An agreement was reached in May 2023 that would see the libraries remain open. Nonetheless, service impacts include a reduction in operating hours across the local network and an approximate 4 month delay to the new library opening in Armstrong Creek.

Queensland

- Limited council budgets to attract qualified early childhood educators in outback areas, leading to the inability to recruit staff. This compounds longstanding staffing challenges in the childcare sector, particularly in regional areas.

  Impacts: In January 2023, Longreach Regional Council cancelled a travelling childcare service that had operated for over 15 years. Despite an extensive waiting list for the service, financial pressures and the inability to offer more competitive remuneration meant that the council was unable to attract staff.

Financial pressures place core and valued services at risk

South Australia

- Funding cuts to the Obesity Prevention and Lifestyle (OPAL) program in 2016 forced local councils to rethink scope and scale of program delivery.

  Impacts: The OPAL program was initially planned to run for five years, but was later reduced to three. This restricted the scope of the program evaluation to only half of the council areas involved in the program. This resulted in a missed opportunity to comprehensively study the effect of the OPAL program in modifying rates of childhood obesity.

Northern Territory

- Funding freeze to youth programs, meaning they are set at 2014 levels and have depreciated in value.

  Impacts: In March 2023, it was reported that several federally funded youth programs ran by the **MacDonnell Regional Council** would be forced to shut down. Rising costs have made delivery financially unviable. These programs regularly serviced approximately 1,500 young people. In Australia, youth and recreation programs have had a positive impact on crime prevention and help to promote positive health behaviours. Community consultation also demonstrates that youth and family mentoring programs promote positive social change. Cancelling these services would undermine the progress made in a community-driven approach to civic and social development.

Tasmania

- **West Coast Council** lost a variety of health services as a result of funding cuts from the Federal government. In 2016, funding was significantly reduced from $3.9 million to $1.4 million.

  Impacts: Availability of General Practitioners, diabetes educators, mental health professionals and optometrists. The shortage of health practitioners in Tasmania is well documented, with consequential impacts to population health.

Western Australia

- Internal financial constraints and the economic impacts resulting from COVID-19, funding was forced to be cut from a wide variety of community-oriented ‘non-essential services’ across the City of Kwinana in 2020.

  Impacts: Cancellation of regular community events, including outdoor family concerts and senior Christmas luncheons. This impacts sense of community, social cohesion and overall wellbeing.

Local government spending on education, environmental protection, and public order and safety has grown the fastest over the past decade

Analysis of local government spending per capita by service type shows significant variation across portfolios.

However, proportionate expenditure by service has remained stable between 2013-14 and 2022-23.

Compound annual growth in Australian local government expenditure was 2.4 per cent, compared to a 2.6 per cent compound annual growth in the Consumer Price Index over the same period. This represents a cut in real terms as growth lags inflation.

AUSTRALIAN LG SPENDING PER CAPITA ($M) BY SERVICE TYPE, 2013-14 AND 2022-23

Service type	2013-14 spending per capita ($m)	2022-23 spending per capita ($m)	Compound annual growth rate
Economic affairs	570	583	0.3%
Education	45	69	4.8%
Environmental Protection	1,175	1,662	3.9%
General public services	2,441	3,084	2.6%
Health	147	163	1.2%
Housing and community amenities	1,120	1,335	2.0%
Public order and safety	261	361	3.7%
Recreation, culture and religion	1,660	2,128	2.8%
Social Protection	536	565	0.6%
Transport	2,193	2,617	2.0%
Total	**10,148**	**12,567**	**2.4%**

Source: SGS Economics and Planning (2024), ABS (2013-22). Service types are based on the Classification of the Functions of Government (COFOG-A), an Australian application of an international classification that supports the reporting of government expenses according to the purpose for which the funds are used.

Declines in local government spending indicate service re-prioritisation

There were significant proportionate declines in local government spending between 2013-14 and 2022-23:

- In the Northern Territory, local government spending on Economic affairs declined by 39.5 per cent (or -$57 per capita). Spending on Health declined by 23.1 per cent (-$4.7 per capita) while spending on Recreation, culture, and religion declined by 5.4 per cent (-$13.4 per capita).
- In South Australia, local government spending on General public services declined by 11.6 per cent, or -$11.9 per capita.
- In dollar terms, Queensland, Tasmania, and Victoria also recorded slight declines in Social Protection spending: -$1.1, -$0.8, and -$3.1 per capita respectively. For Queensland, however, the proportionate decline in Social Protection spending between 2013-14 and 2022-23 represents a 9 per cent decline overall.

LARGEST PROPORTIONATE DECLINES IN PER CAPITA SPENDING BY SERVICE ($), 2013-14 AND 2022-23

State / Territory	Service type	2013-14 spending per capita ($)	2022-23 spending per capita ($)	10 year change in $ per capita	Proportion-ate change (%)
NT	Economic affairs	144.1	87.1	-57.0	-39.5%
NT	Health	20.6	15.8	-4.7	-23.1%
SA	General public services	102.6	90.7	-11.9	-11.6%
Qld	Social Protection	12.1	11.0	-1.1	-9.0%
NT	Recreation, culture and religion	247.0	233.6	-13.4	-5.4%
NT	Education	16.5	15.8	-0.6	-3.8%
VIC	Social Protection	163.4	160.2	-3.1	-1.9%
TAS	Social Protection	40.9	40.1	-0.8	-1.9%

Source: SGS Economics and Planning (2024), ABS (2013-22). Service types are based on the Classification of the Functions of Government (COFOG-A), an Australian application of an international classification that supports the reporting of government expenses according to the purpose for which the funds are used.

02 Impacts of more sustainable local government finances

Local government financial sustainability and Australia's macro-economic performance

This report reveals a long-term trend of adverse financial pressures in the local government sector. The implications are varied across Australia, though an overall theme emerges of impacts to the coverage, quality, and continuation of core and valued services and infrastructure.

This section considers the potential benefits that would flow from effective funding of local government. Effective funding would allow councils to deliver policies and programs that are tailored and respond directly to local needs.

The Centre of Policy Studies at Victoria University used Computable General Equilibrium modelling to test five scenarios developed by SGS and ALGA. These scenarios test the macroeconomic impact of a more financially sustainable local government. The five scenarios span improved:

- roads maintenance,
- maintenance and programming of public open space,
- efficiency in regulatory services,
- efficiency in intergovernmental financial relations, and
- workforce attraction and retention.

For each of scenario, the modelling simulated the impacts to Gross Domestic Product (GDP) from reduced local government financial pressures compared to a base case where local government finance remains unchanged. More detail on the scenarios is provided at Appendix A.

Greater local government financial sustainability would boost productivity and therefore GDP, employment and tax revenues. Productivity gains would arise from a range of efficiencies. This includes:

- saved vehicle operating and accident costs on better maintained roads,
- health cost savings as communities make greater use of appropriately equipped and programmed open spaces,
- saved time and costs for development proponents as councils deal with their applications expeditiously, and
- savings in recruitment and training costs in councils as they will be better able to offer career pathways.

The CGE modelling traces the impacts of these efficiencies through the economy. It factors in the switching of resources/spending from other sectors of the economy, or other spheres of government, to enable local government to work within a more sustainable financial framework. It calculates a net impact on GDP and related macroeconomic performance indicators.

The combined effect of the 5 scenarios is estimated at a GDP boost of more than $7 billion in a typical year. A 'typical year' is nominally 10 years after the commencement of the reforms to provide local government with greater financial sustainability. This allows for a transition period during which the productivity gains and cost savings discussed above would gradually take effect in the economy.

A $7 billion GDP boost from improving financial sustainability in local government

Placing local government on a more sustainable financial footing would increase Gross Domestic Product (GDP) by at least $7 billion each year. Targeted investments in local government service delivery provide positive economic outcomes.

- A $1 billion dollar investment in local government road maintenance will deliver a $3.5 billion increase in real GDP.
- $250 million invested in better supply and curation of parks and gardens will result in a $0.9 billion GDP boost.
- Efficient design of regulatory processes within Councils can yield an annual benefit of $1.6 million. If realised across Australia's 537 councils, this would increase GDP by $1.7 billion.
- Increased block transfers of funds from Commonwealth and States to local government can save $235.64 million in administrative costs and increase GDP by $300 million each year.
- Increase retention of local government workers can save up to $424.5 million in administration costs and boost GDP by $600 million each year.

Collectively these reforms and actions can increase Australia's national GDP by $7 billion per year from a Federal Government investment of $1.75 billion. The $1.7 billion annual investment is comparable to the additional tax revenue that the Commonwealth would generate from improving local government financial sustainability. Improving the financial sustainability of local government would largely pay for itself.

Detail about the specific scenarios is at Appendix A.

03 Vertical fiscal imbalance

A growing proportion of councils are dependent on transfers from other tiers of government

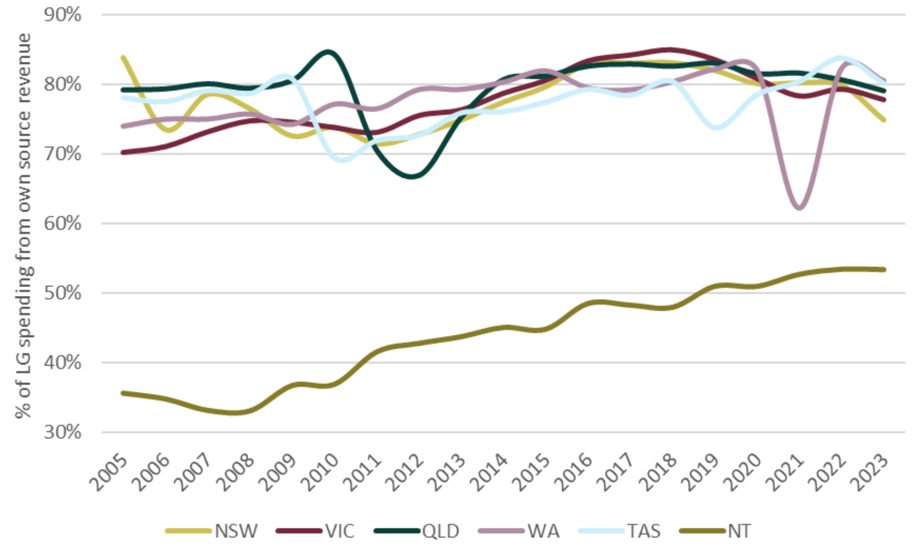
The proportion of local government expenditure covered by own source revenue has generally varied between 70 and 80 per cent since 2005 (the NSW Office of Local Government cites a benchmark own source revenue ratio of 60 percent). The primary exception is in the Northern Territory, which has increased from 33 per cent in 2007 to 53 per cent in 2022.

However, the headline figures mask the range in own source revenue ratios from council to council. Some councils, particularly in regional areas, are highly dependent on grant funding. In New South Wales for example, councils' own source revenue ratios ranged between 9.8 per cent and 87.3 per cent in 2021-22.

Over half (72 councils; 56 per cent) of New South Wales councils in 2021-22 had an own source revenue percentage under the benchmark, compared to 44 councils (29 per cent of the then 152 councils) in 2014-15. This suggests that a growing proportion of New South Wales councils are dependent on transfers from other tiers of government.

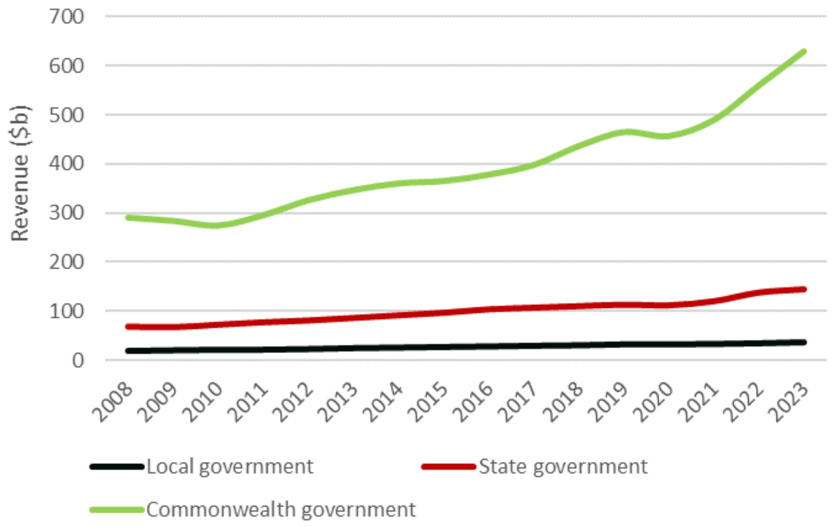
A comparison of local governments' own source revenue and revenue raising in state and Commonwealth governments sheds light on the differences in financial autonomy between the tiers of government. Long-term growth in local governments' own source revenue has stagnated over the past 15 years, compared to increases in state and Commonwealth revenue.

OWN SOURCE REVENUE COMPONENT OF LG SPENDING BY JURISDICTION, 2005-23



Source: SGS Economics and Planning (2024), ABS Government Finance Statistics

REVENUE BY GOVERNMENT SECTOR, 2008-23



Source: SGS Economics and Planning (2024), ABS Government Finance Statistics

Growth in local governments' own source revenue has lagged revenue growth in other levels of government

Over the medium medium (5 year average) and long-term (10 year average) local government revenue growth is slower than other tiers of government. State and Commonwealth government revenue recorded some of largest annual increases in revenue between 2021 and 2022. Rates are a major source of local government revenue. Other sources include the sale of goods and services and developer contributions.

In New South Wales and Victoria, local governments do not have full freedom to raise their own source revenue to meet local needs, due to the system of rate pegging and rate capping. This is despite the evidence that citizens generally have greater trust in their local councils compared to other governments that are making resource allocation decisions on their behalf.

INTERGOVERNMENTAL COMPARISON OF REVENUE GROWTH, 2014-23

Annual growth												Average annual growth	
Sector	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	5 yr	10 yr
Local	9.9%	4.8%	5.4%	4.4%	5.1%	3.9%	6.4%	-0.1%	2.7%	4.6%	6.2%	**4.0%**	**4.8%**
State	6.4%	6.2%	5.5%	7.3%	3.1%	2.9%	2.7%	-1.0%	7.3%	14.7%	4.8%	**5.2%**	**5.4%**
Cwth	10.2%	3.9%	1.3%	3.6%	5.2%	9.6%	6.5%	-1.7%	7.1%	14.3%	12.3%	**8.0%**	**6.2%**

Source: SGS Economics and Planning (2024), ABS (2023).

There is growing evidence that state governments are shifting services to councils without commensurate resourcing

Local Government NSW's latest cost shifting report highlights a **$1.36 billion cost shift to councils in 2021-22**. While metropolitan councils face the highest amount of cost shifting, ratepayers of large rural councils experience the highest cost shift per ratepayer.

In Queensland, cost shifting was estimated at **$360 million in 2020-21**, a 378 per cent increase from the $47 million estimated in 2001-02. South Australia's first Cost of Compliance Survey (2024) is underway, while instances of cost shifting in other states and territories have been well documented over the years.

COST SHIFTING TO NSW LOCAL GOVERNMENT BY COUNCIL CLASSIFICATION

Classification	Total cost shift ($m)	Cost shift per ratepayer ($)
Metropolitan	638.3	456.6
Metropolitan Fringe	213.0	420.9
Regional Town/City	416.5	434.6
Large Rural	85.8	490.1
Rural	10.3	$590.8

Source: LGNSW (2023).

Cost shifting arises in a range of ways. Examples include changes to emergency service contributions and to the waste levy, forced rates exemptions, additional regulatory functions under legislation that are administered by councils, axing or inadequately funding services (e.g. library subsidies, flood mitigation program, road safety funding program), councils having to provide pensioner rebates, and councils providing services as a provider of last resort to fill service gaps. Other areas of cost shifting include a road reclassification program which increased the amount of roads for councils to maintain, and the state government requiring a transfer of revenue generated from council-managed crown reserves.

04 Horizontal fiscal equalisation

Improving local government financial sustainability would help to address uneven access to services across Australia

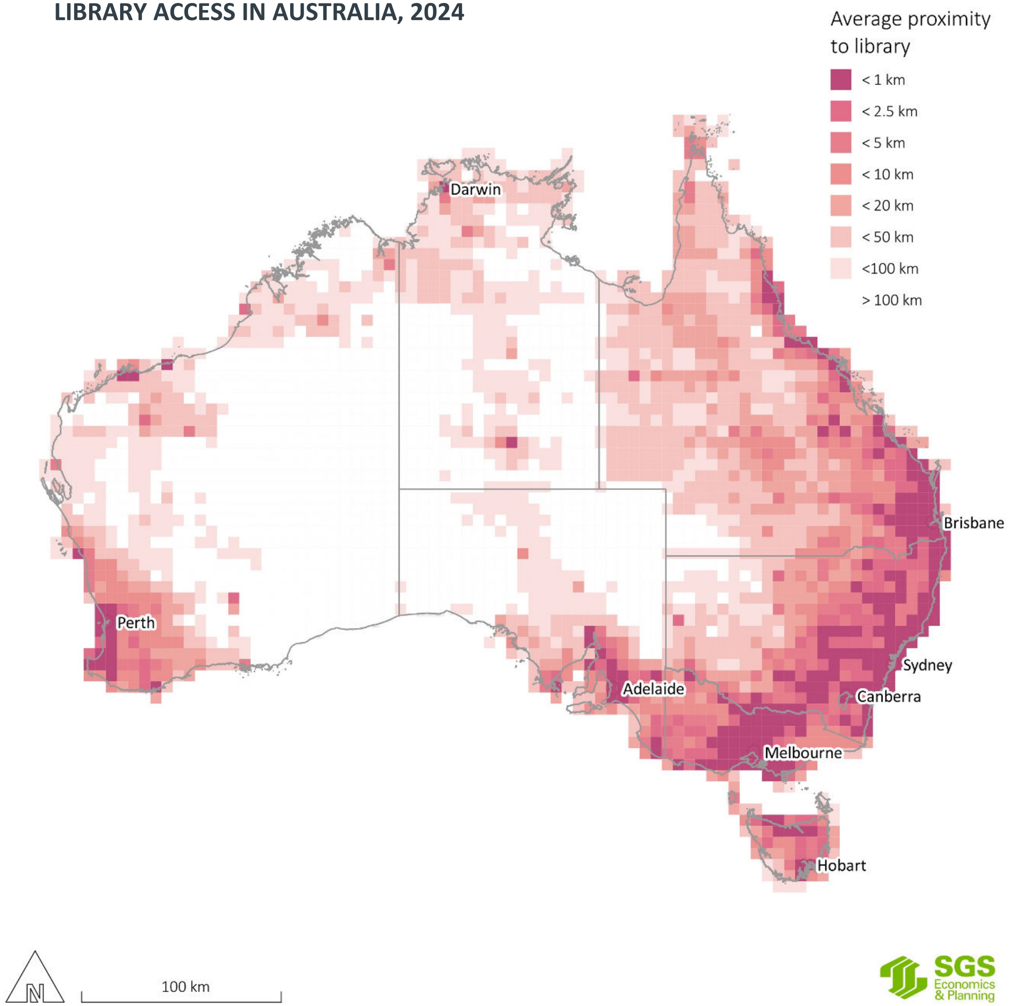
Local governments are among the most effective agents for redressing localised disadvantage. Local governments play an important role in mitigating disadvantage within communities, due to their knowledge of community needs, history, and strengths. They are well placed to engage in 'joined-up' approaches that involve multiple levels of government, the private sector, and communities.

Longer-term certainty of funding is required to optimize this role. Local governments deliver an array of services to community with limited budgets. Many also struggle to hire and retain staff in regional and rural areas. Improving council financial sustainability is an important first step to enable councils to progress initiatives that overcome disadvantage. Segments of the Australian population will continue to be impacted by poorer quality and a lack of council-provided services and infrastructure without a better financial footing for local government.

Library services provide a clear example of the spatial divide in access to council-provided services across Australia. Library services are used as an example for two reasons: they are a service that is widely provided - in 2018-19, there were 1,410 public library branches across Australia – and spatial data is publicly available through OpenStreetMap. Library services are also among the most valued of local government services (State Library Victoria 2018). Libraries also act as a good proxy for other local government services.

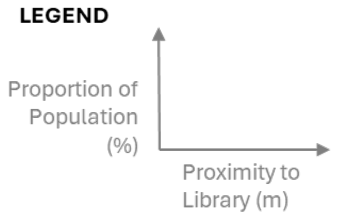
SGS mapped spatial variation in access to library services. Areas in white are located more than 100km from the nearest library service. This highlights that there are areas in remote communities in South Australia, the Northern Territory, and Western Australia that remain without access to library services.

LIBRARY ACCESS IN AUSTRALIA, 2024



SGS Economics & Planning

A financially stable local government is better equipped to provide important community services



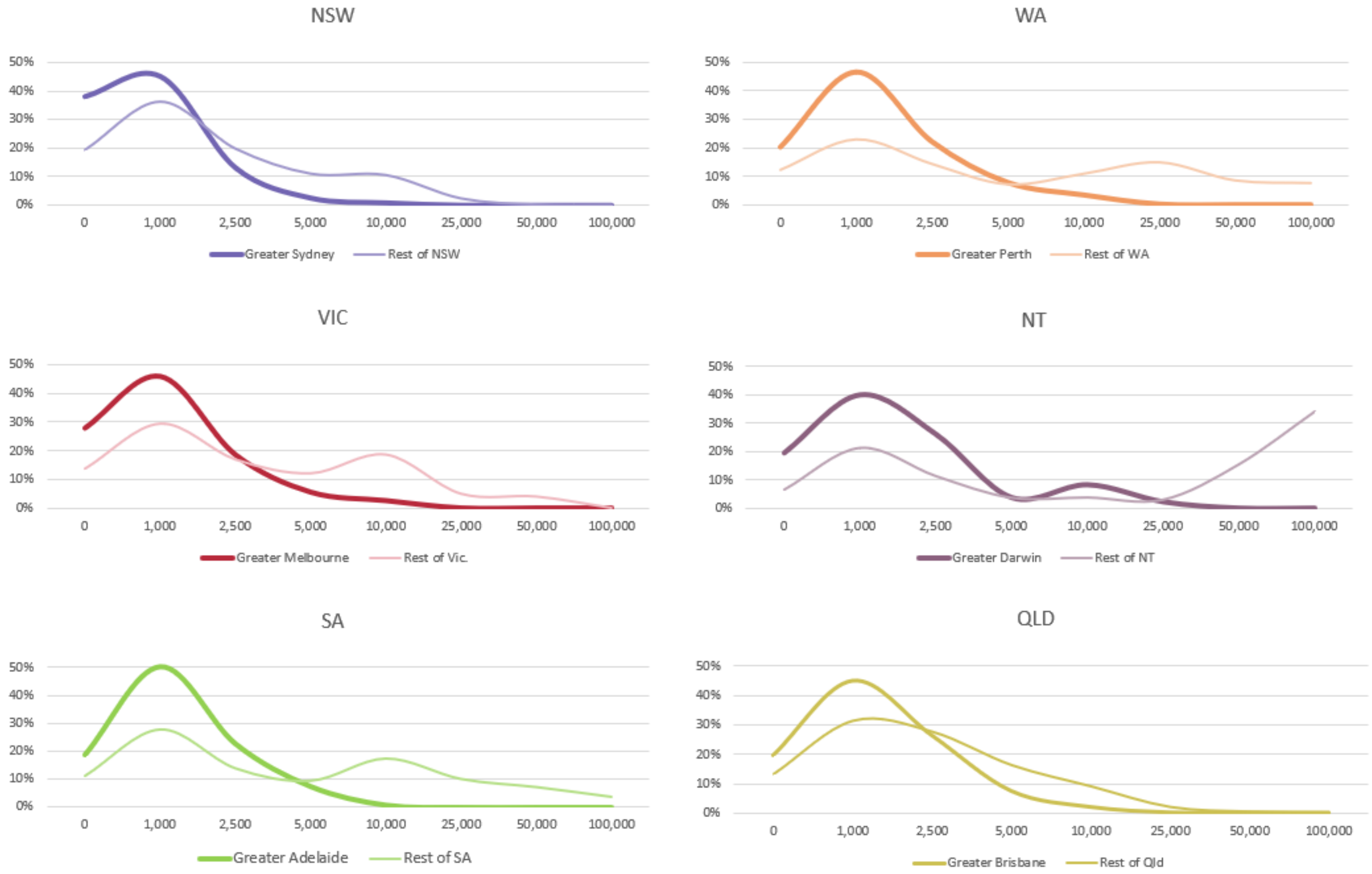
There are benefits to the wider community when local governments are supported to deliver services without financial disruption. For example, Australia's public libraries 'deliver more educational outcomes, and social and economic benefits per dollar invested than any other institution'. In Victoria, SGS research has estimated a net annual benefit (i.e. benefits less costs) of $234.7 million in health and wellbeing benefits.

Wider benefits can only be sustained and enhanced if councils are financially supported to maintain and modernise library infrastructure (physical and digital) and to hire librarians and other staff. Some libraries staff are trained social workers, and many libraries offer a range of services for new migrants or disengaged youths.

Libraries work best when they are a readily accessible neighbourhood service (SLV, 2018). Local government funding constraints mean that large numbers of Australians do not have reasonable access to important services libraries provide.

The charts at right display the percentage of each state or territory's population located near a library. They highlight that a spatial divide persists within capital city areas. For example, 83 per cent of Greater Sydney's population are located within one kilometre of a library service. Greater Melbourne follows at 73 per cent. In contrast, only 44 per cent of Greater Hobart's population are located within one kilometre of a library.

PROXIMITY TO LIBRARIES BY STATE AND TERRITORY, 2024



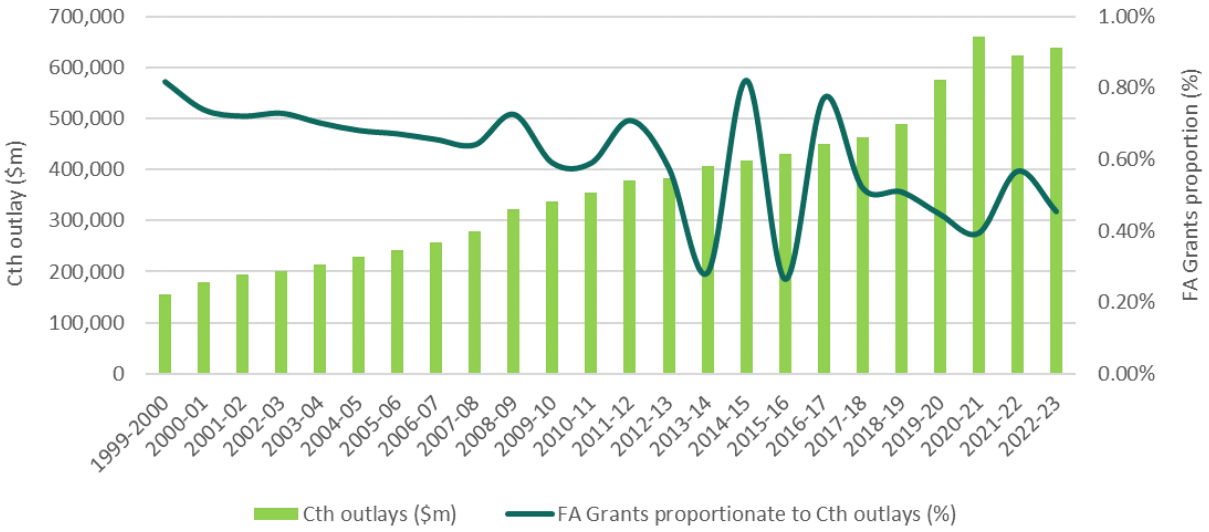
Source: SGS Economics and Planning (2024). Charts show the proportion of population in the Greater Capital City Area or Rest of State region residing within a given distance (metres) to a library.

The proportion of national taxes allocated to local government has shrunk over time

The value of FA Grants as a share of total Commonwealth government expenses has declined from approximately 0.8 per cent to 0.4 per cent between 1999-00 and 2022-23.

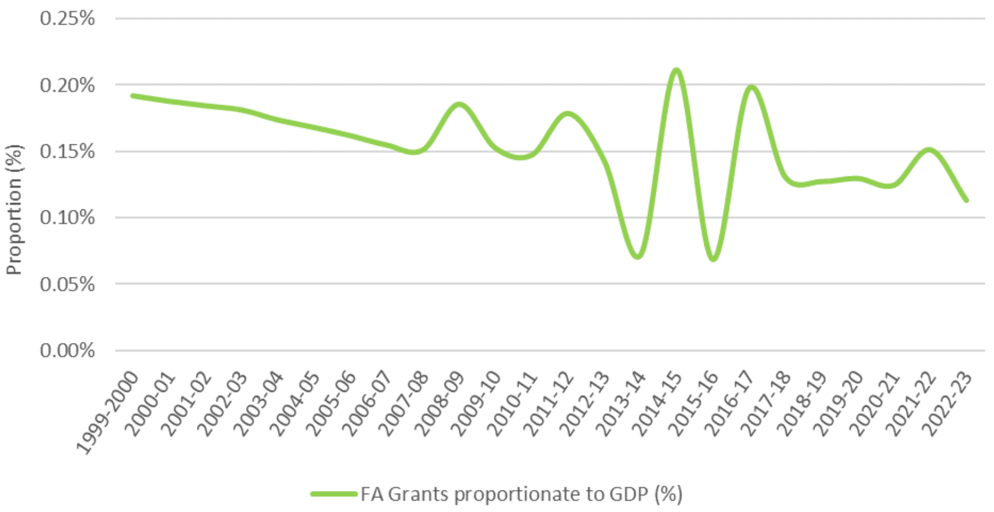
There has been a decline in the value of FA Grants from 0.19 per cent of national Gross Domestic Product (GDP) in 2000 to 0.13 per cent of national GDP in 2023.

FA GRANTS AS SHARE OF COMMONWEALTH OUTLAY, 2000-23



Source: SGS Economics and Planning (2024), ABS Government Finance Statistics

FA GRANTS AS SHARE OF NATIONAL GDP, 2000-23



Source: SGS Economics and Planning (2024), ABS Government Finance Statistics

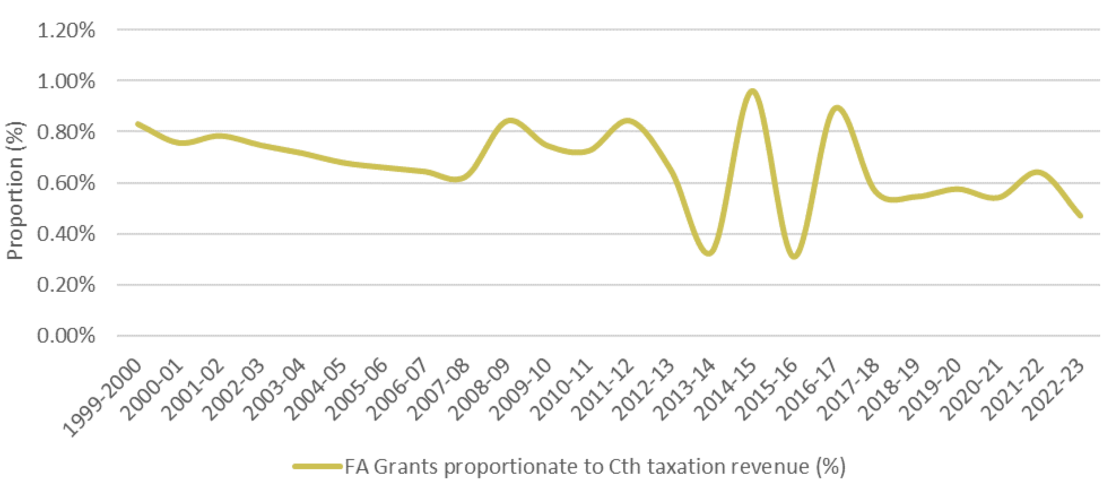
The proportion of national taxes allocated to local government has shrunk over time (cont'd)

There has been a long-term decline in the share of FA Grants as a proportion of Commonwealth government taxation revenue. FA Grants represented 0.83 per cent of Commonwealth taxation revenue in 2000. They declined to 0.62 per cent by 2008. The share has further dropped to range between 0.53 and 0.58 per cent over the past 5 years.

The growth of FA Grants has considerable variability including significant decreases in some periods. In contrast, GDP and Commonwealth taxation revenue exhibit a more stable trend over time. Over the last 20 years, CTR and GDP have experienced an average compound annual growth rate of 6 per cent, compared to 4 per cent for FA Grants.

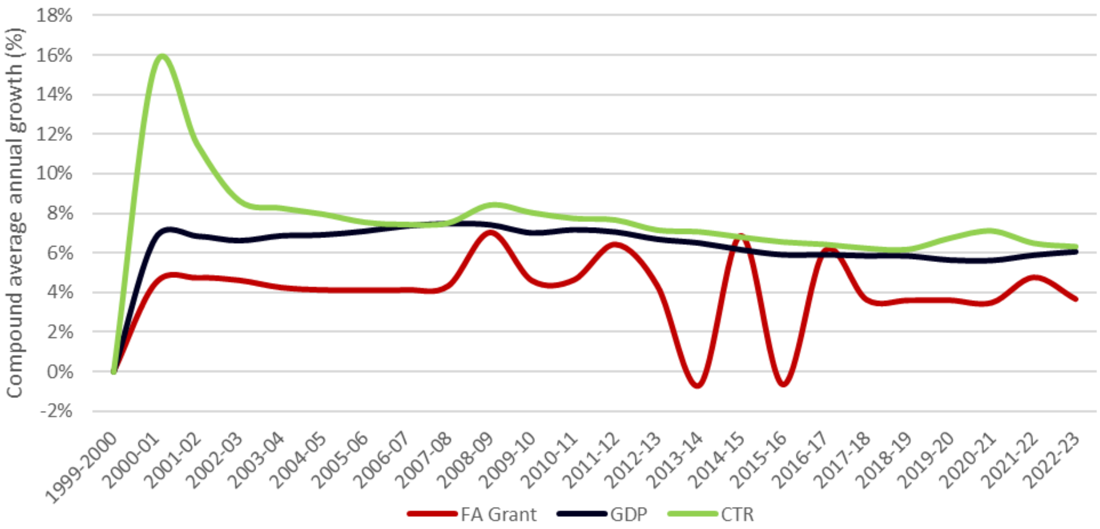
The volatility of transfers and declining amount is concerning. Volatility impedes the ability of councils to plan for infrastructure provision and maintenance. This can impact on the vital infrastructure services local government provides.

FA GRANTS AS SHARE OF COMMONWEALTH TAXATION REVENUE, 2000-23



Source: SGS Economics and Planning (2024), ABS Government Finance Statistics

AVERAGE COMPOUND ANNUAL GROWTH IN CTR, GDP, AND FA GRANTS, 2000-23



Source: SGS Economics and Planning (2024), ABS Government Finance Statistics

05 Financial barriers to local decision-making

State and Commonwealth programs involving tied funding to councils are not always tailored to council needs

There is no standardised reporting of tied grant funding to local government. A desktop review of tied funding to local governments shows that councils consistently undergo competitive tendering processes involving the development of businesses cases and/or demonstration of co-contributions to access funding for necessary services and infrastructure. This model of funding allocation is not conducive to longer-term planning by councils on objectives that have been agreed by the community as the highest priority.

This process of grant funding is inequitable. Some councils will not have the financial means to co-contribute or the ability to prepare compelling business cases which are selected from a competitive tendering process. The process of writing the grant application can take from 20 to 30 hours for smaller grants up to 50-100 hours for longer grants, adding to local government resource pressures.

Year	Name	Description	Grant value	Total Commonwealth spend
2024	Community Energy Upgrades Fund (CEUF)	Local governments can apply for grants to improve energy efficiency.	$25,000 to $2.5 million to successful applicants (co-funding of 50%)	$100 million over 3 years 2024-27 ($33.3 million per annum)
2022	Strengthening Local Government Partnerships (Vic Gov)	For projects that reduce risk of bushfires and build local capability in emergency management	$150,000 per financial year, per LGA	$182 million ($91 million per annum, based on funding available for applications of up to 24 months duration.)
Since 2016	Works for Queensland (W4Q)	Funding to support regional councils to deliver infrastructure, planning, maintenance and capability development for essential services and economic development	$1.5 million	$1.1 billion ($92 million per annum, averaged since 2016)
2015	Growing Suburbs Fund (Vic)	Build facilities to support healthy and liveable communities in fast growing suburbs	Grants of up to $2 million.	$425 million ($53 million per annum)
Since 2011	Restart NSW	Funding and delivery of high-priority infrastructure projects that improve economic growth and productivity	$4 million to $3,400 million.	$2.47 billion ($190 million per annum)

Source: Compiled by SGS Economics and Planning (2024).

The amount of Commonwealth tied grant funding to state and local governments is growing

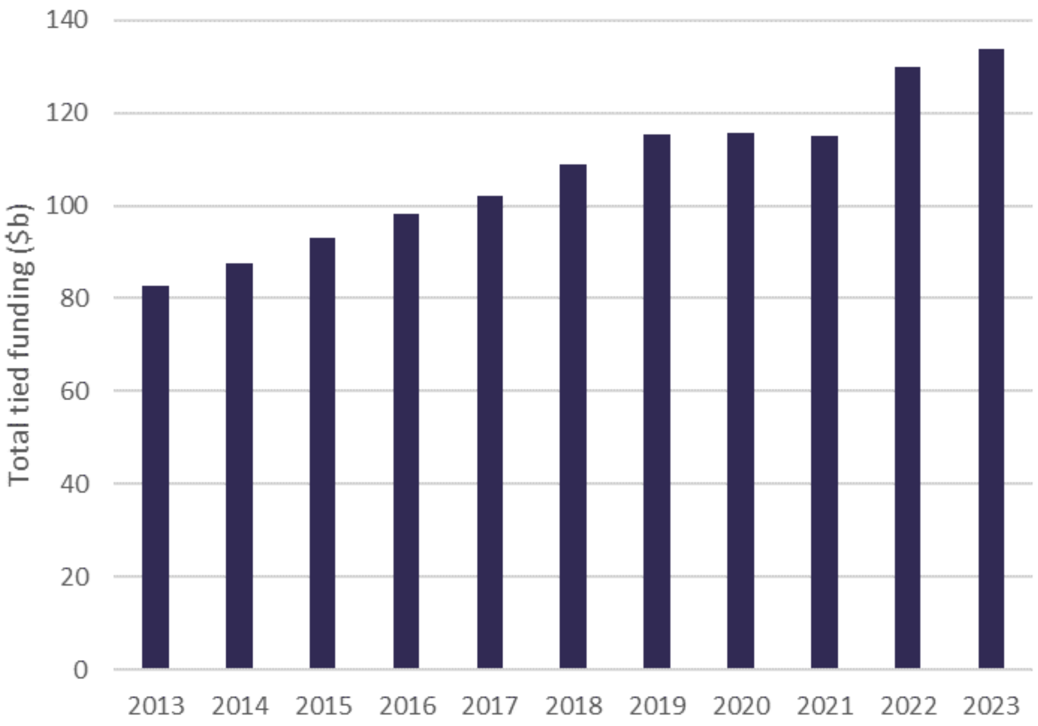
There is a growing tendency for the Commonwealth to influence the spending decisions of other tiers of government.

This is problematic for local government for two reasons. First, compared to block funding, councils are less able to align resources with community priorities. Second, councils may face an unwanted additional cost burden from compliance and reporting requirements.

The chart at right illustrates growth in total tied grant funding from the Commonwealth to state and local governments. It shows a clear trend to increased tied grant funding.

It is not possible to disaggregate the respective state and local government amounts, based on publicly available information.

TIED GRANT FUNDING ($B) FROM COMMONWEALTH TO STATE AND LOCAL GOVERNMENTS, 2013-23



Source: SGS Economics and Planning (2024), ABS Government Finance Statistics (2024). Amounts are GST exclusive. Amounts are calculated from Commonwealth grant expenses to other tiers of government, less the FA Grant amount for each year.

Tied grant funding is difficult to access due to competitive state and Commonwealth programs

Tied funding to local governments is ad hoc and not consistently reported. SGS has compiled the following list from a desktop review.

Variable funding amounts from year to year suggest that funding is allocated on an as-needed basis. This indicates reactive rather than proactive action on councils' financial pressures. The majority of grants are competitively tendered, if not a closed application. Often, these applications are resource intensive for smaller local governments and heavily oversubscribed. The timing of competitive grant rounds may also influence the selection of 'shovel-ready' projects. Where tied grants require a co-contribution of up to 50 per cent of grant value, this could create inequities as some councils may not be in a financial position to meet grant eligibility requirements.

Year	Name	Description	Value ($)	Competitive status	Total Commonwealth spend
2024	Regional Precincts and Partnership Program (rPPP)	Investment into regional, rural and remote areas to grow economies and serving communities	$500,000 to $5 million for planning and development. $5 million to $50 million for delivery.	Open grant process for eligible areas.	$400 million allocated over three years (2023-24 to 2025-26)
2022	Building Better Regions Fund	Create jobs, drive economic growth and build stronger regional communities	$20,000 to $10 million. Co-contribution of 50% except for remote and very remote areas which has a contribution ratio of 3:1	Competitive application with project plan.	$1.38 billion
2022	Priority Community Infrastructure Program	Support community and sporting infrastructure, open space improvement and other priorities.	$1 billion over 5 years funding pool.	Closed non-competitive.	$1 billion ($200 million per annum)
2021	Preparing Australian Communities Program	Funding to improve the resilience of communities against natural hazard	Up to $10 million	Competitive application with project plan.	$600 million, of which $257 million was spent
2018	Regional Growth Fund	Transformational long-term economic growth projects which create jobs.	$10 million to $25 million.	Competitive application with business case.	$272.2 million ($54.4 million per annum)
Since 2016	Stronger Communities Programme (SCP)	Grants to community organisations and local governments for small capital projects that deliver social benefits to communities.	$2,500 to $20,000	Invited to apply by local Federal MP.	$181 million under Rounds 1-8 of the SCP
2015	National Stronger Regions Fund. Subsequently the Building Better Regions Fund from 2016.	Fund investment for economic growth and sustainability of regions.	$20,000 to $10 million.	Competitive application with project plan.	$1 billion over five years

06

International comparisons of local government funding

In England, financial challenges have led some councils to declare bankruptcy

The financial challenges described earlier in this report are not unique to Australian local governments. Similar financial challenges have led six English councils to effectively announce bankruptcy since 2020. Other councils have warned of similar risks arising from unprecedented financial challenges. This illustrates the risks to the Australian local government sector if they are not supported to withstand rising cost pressures and other barriers to long-term financial sustainability.

English councils are experiencing:

- Declines in the value of grant funding from central government. Central government grants were cut by 37 per cent in the decade to 2019-20 and local governments have been unable to meet the difference via local income sources.
- Barriers to planning for the future due to successive rounds of competitive and short-term funding. As with the large volumes of competitive State and Commonwealth funding rounds in Australia, English local authorities bear the burden of 'bureaucratic overhead' with no guarantee of funding success.
- Barriers to revenue raising capacity. Similar to the Australian sector, local property taxes represent a large share of revenue. At the same time, annual increases are subject to central caps and higher charges are only permissible through a local referendum. Only one referendum was held in 2015-16, however the proposal to raise council tax was unsuccessful. Other revenue sources are 'peripheral' and include levies for transport and community infrastructure.
- Inadequate mechanisms for local needs assessment. In England, the system for determining transfers is entirely top-down, based on a central government assessment of how to share a total allocated fund for local government across different local authorities. Needs assessment in the United Kingdom has been suspended since 2013. This system was designed to include regular 'resets', where needs would be reassessed, although these have not taken place. Meanwhile, the UK Government launched a 'fair funding review' in 2016, but this has not progressed beyond a consultation in 2018. The fair funding review would have reassessed a range of indicators of local need and taken decisions about the relative weighting of those indicators.

Four reforms are recommended to make UK local government finance more stable. These are to:

- Reinstate and rework a system of annual needs assessment (thereby improving councils' flexibility in funding allocations),
- Promote an equitable funding system that has mechanisms to redistribute taxes from central government to councils, and also between councils,
- Establish a standing commission that handles financial negotiations between governments and local authorities, and
- Assign a fixed proportion of national revenue to local authorities based on a needs assessment.

Lessons from Germany on local, needs-based assessment

Key features of the German system of needs-based assessment

In Germany, the distribution of funds from state to local governments is based on two key indicators: fiscal capacity and fiscal need. Fiscal capacity is a measure of how much revenue a local government can raise themselves with local taxation. Fiscal need is a measure of the amount of funding the local government needs to fulfil their duties.

There are laws that provide safeguards around the distribution process. For example, there are laws that dictate the proportion of state taxes that must be given to local governments, while other laws ensure that similar councils receive equitable treatment by the state level.

If fiscal capacity exceeds fiscal need, then the council does not receive equalisation grants. However, if fiscal need exceeds fiscal capacity, then the council receives grants to compensate for the funding shortfall. The effect is that local governments with lower revenues 'have financial means that are not vastly different from the average'. It also improves the resilience of councils to weather unexpected revenue shocks, therefore enabling councils to provide a steadier flow of services.

The assessment of fiscal need often begins with an examination of a council's population. While population size is a central factor for determining requirements, the assessment also typically accounts for differences in spending requirements based on geography (e.g. urban, regional, and rural areas), population age profile, trends in population growth or decline, the number of schoolchildren, the number of roads, the size of a territory, and others (Bullerjahn and Thone 2020).

A needs-based assessment system helps to ensure that councils have adequate finance to deliver services to their communities and to deliver these equitably across the nation.

There is little vertical fiscal imbalance in Germany as legislation assigns revenues to state (Länder) and the federal governments in line with their respective requirements. There are several key lessons for Australia:

- Design a comprehensive and transparent method for determining the fiscal capacity (calculated from council's municipal revenue from joint taxes and standardised revenue from property and local business taxes) and fiscal need (a measure of budget requirements per resident),
- Determine fiscal need and capacity using robust evidence and indicators,
- Calculate fiscal need having regard to the true costs of councils' operations,
- Give municipal financing processes legal recognition, rather than relying on executive decisions (as in England). This means that unfounded mandates may be legally challenged (Bullerjahn and Thone 2020).

Lessons from Germany on local, needs-based assessment (cont'd)

Benefits of the needs-based assessment system

An effective needs-based assessment system has several benefits. First, it empowers local decision-making by councils. Funding certainty means that councils have more control over how they plan and what they plan for in the long-term. Second, the system of equalisation grants reduces inequities between councils and the types of services and infrastructure they provide to their communities. Third, the grants support councils facing revenue shocks.

In contrast, there is no needs-based assessment system in England. Councils are not guaranteed additional funding above and beyond the amount estimated to fulfil their statutory obligations. In fact, they are not even guaranteed the level of funding needed to meet their duties, hence the rising number of councils issuing effective bankruptcy notices. This diminishes their local decision-making capacity because they are unable to go beyond centrally set statutory requirements.

What institutional arrangements are needed to facilitate these decisions?

In Germany, municipal associations play a key role in the design and implementation of financial equalisation laws (Bullerjahn and Thone 2020). They do so informally, as lobbying agencies, or formally as part of a consultation process. In many cases, municipalities will be guaranteed representation for decisions relevant to local government. In the German state of Brandenburg, adequate financing of municipal tasks is enshrined in the state constitution:

> *'In order to promote local self-government and to protect their interests, municipalities have the right to form associations. The State Government must maintain contact with these associations and cooperate with them in the preparation of laws, legal ordinances and administrative regulations that directly affect the interests of municipalities. The committees of the State Parliament should hear the views of the associations of municipalities when discussing draft laws.'*

In addition to the various levels of German government, the courts also play a significant role. Municipalities are entitled to challenge decisions under state law. State-level audit bodies may also be involved to ensure the regulation of budgets or to evaluate performance against minimum standards.

How is the scope of local government services determined?

In Germany, the principle of subsidiarity means that all services should be provided at the lowest possible level of government, unless there is a specific reason to move them up. The duties of local governments are outlined in state law (Geissler 2020). These duties are a foundation for determining fiscal redistribution and are monitored by several agencies at the federal and state levels.

In Australia, the principle of subsidiarity is similarly regarded as 'intrinsic to the efficient and effective allocation of responsibilities in a federal system (Evans, 2017). While local government services in Australia *typically* include services and infrastructure related to public health, local roads and footpaths, parks and open space, libraries, and many others, there is no prescribed list. Indeed, cost shifting has resulted in many Australian councils being required to provide an increasing range of services. In England, the default assumption is that the central government performs most tasks. It is up to the discretion of politicians what powers and responsibilities are passed on to local government.

Appendix A

CGE model inputs

A $7 billion GDP boost from improving financial sustainability in local government

Placing local government on a more sustainable financial footing would increase GDP by at least $7 billion each year. Targeted investments in local government service delivery provides positive economic outcomes. These benefits are felt across the country.

NATIONAL AND STATE REAL GROSS STATE PRODUCT, ABSOLUTE CHANGES FROM BASELINE ($M, 2024 PRICES)

	1: Improved road maintenance	2: Improved public open space	3. Improved capacity for regulatory services	4. Increased block transfers	5. Improved workforce retention
NSW	1,057.8	260.0	300.0	96.2	177.9
VIC	665.0	191.2	193.9	77.6	139.3
QLD	716.4	158.9	402.4	58.6	115.3
SA	198.3	45.5	50.4	14.8	30.0
WA	755.3	165.8	678.6	77.2	139.6
TAS	47.4	13.1	5.5	3.9	7.8
NT	55.6	11.3	26.5	3.2	7.7
ACT	66.7	14.4	-12.0	-0.8	1.1
National	**3,546.3**	**858.7**	**1,670.9**	**330.7**	**619.8**

Source: Centre of Policy Studies, Victoria University (2024). Note: State totals do not add exactly to national totals due to the assumptions and/or parameters applied at different geographic scales to reflect regional interactions.

Scenario 1 – Improved ability to finance roads maintenance

Hypothesis	Literature	Notes	CGE inputs
Improved LG maintenance of roads would generate benefits in avoided accidents, lower vehicle operating costs, and travel time savings.	• For every additional GBP£1 spent on direct road maintenance works, a benefit of GBP£2.70 (discounted) is derived in reduced user costs. • Annual injection of $1 billion from federal government to make up shortfall in funding for maintenance of local roads. • Austroads have published a Cost Benefit Analysis on the costs of maintaining road surfaces, bridges and associated navigational infrastructure (signs etc), indicating a benefit cost ratio of 5.2:1.	For the sake of conservatism, SGS proposes to apply a benefit cost ratio of 4.0:1 for road maintenance. This is roughly the midpoint between the cited UK and Austroads studies.	• Annual national investment of **$1billion** in maintenance of local government roads. • ***Each*** $1billion investment will yield $300 million per annum for **30** years in saved user travel costs (67%) and saved safety costs (33%). • Therefore by year 10, a 'typical' year, a $3 billion saving in user costs is expected.

Scenario 2 – Improved ability to finance open space

Hypothesis	Literature	Notes	CGE inputs
Improving the financial capacity of local government will lead to the better maintenance of open spaces. This would result in a healthier population, enabling more productive workers and producing cost savings for the public healthcare system. Additionally, more open space would serve to mitigate the urban heat island effect.	• $1.13 in avoided public health costs for every additional km of walking. • SGS estimated in 2021 that recreational walking in NSW, supported by parkland and public realm assets generated an annual benefit of $25.6 billion in leisure and health benefits (unpublished).	• SGS proposes to apply an annual benefit of $1.5 billion from better supply and maintenance of parks and gardens arising from greater financial sustainability in local government. • This figure is the estimated uplift in annual leisure and health benefits in NSW based on an increase in recreational walking from 43.4% of the 15+ population to 46%, the latter being the figure for Victoria. • While other states would also benefit, we have ignored this for the sake of conservatism in the modelling.	• Annual benefit of $1.5 billion comprising unpriced leisure value (56%) and health cost savings (44%). • $0.7 billion in health cost savings is estimated from the improved provision and maintenance of open space. • This benefit is generated at an annual resource cost of $350 million.

Scenario 3 – Improved ability to perform regulatory services

Hypothesis	Literature	Notes	CGE inputs
Improved capacity for LGs to perform regulatory services in planning and building would lead to the improved operational efficiencies.	• SGS research (2023, unpublished) shows that more efficient design of regulatory processes within Councils (in respect of development assessment) would yield annual benefits of $1.6 million, comprising a mix of holding cost savings for proponents and various workforce benefits for Councils. • This benefit was gained through a facilitated process of human centred design of regulatory processes, and would not require ongoing funding.	-	• Annual benefit of $859 million (537 councils x $1.6 million), comprising holding cost savings for development proponents (87%) and miscellaneous other benefits including improved customer satisfaction (13%). This benefit is assumed to be generated at zero additional resource cost. It would be funded via efficiency gains in redistributing tax raising from Commonwealth and State to local government.

Scenario 4 – Increase block transfers of Commonwealth and State funding to local government

Hypothesis	Literature	Notes	CGE inputs
Increased block transfers of funds from Commonwealth and States to LGs would increase LG productivity through cost savings in administrative overhead.	In 2022-23 (ABS Government Finance Statistics): • $5,891 million estimated tied funding from State to local governments nationally (sum of State grant expenses to LG, less FAG funding), • $133,614 million estimated tied funding from Cth to State *and* local government nationally (sum of Cth to State and LG, less FAG funding. Includes Cth grants to state), and • Average admin cost of 4c per dollar of grant funding.	• Between 2014-15 and 2022-23, the ABS' Government Finance Statistics reported a 'nil or rounded to zero' in grant expenses from Commonwealth to local governments. • On this basis and for the sake of conservatism we have assumed $5,891 million in tied funding to local governments from State and Commonwealth.	• Annual administrative cost saving of $235.64 million.

Scenario 5 – Improved rates of workforce attraction and retention

Hypothesis	Literature	Notes	CGE inputs
Improved finances would increase LGs' success in workforce attraction and retention and lead to avoided costs in employee turnover.	• Average council worker salary of $100k per year. • Cost of replacing an employee is 1.5 times annual salary. • 5,660 unplanned departures form the workforce (pro-rated from the 1,855 'unplanned' departures from 97 of Australia's 296 rural local governments who responded to 2022 LG workforce survey). • Assume 50% resign due to the impacts of an organisation's financial pressures (lack of resources to fulfil job requirements; inability to hire to expand team capacity).	-	• Efficiency saving of $424.5 million / year ($100k * 1.5 * 0.5 * $5,660 workers).