



Buildings – some not very glamorous, but lots of them and important to the community – long life but high maintenance

3. BACKGROUND, TERMS OF REFERENCE AND APPROACH

3.1 Objectives

The objectives of this study are to:

1. determine the ability of Councils to meet long term investment needs in the renewal and acquisition of infrastructure assets;
2. develop a model for examining the challenges of the task; and
3. make recommendations to improve the management of Victorian local government infrastructure assets.

3.1.1 Ageing Assets

Councils all over Australia are now facing the problem of ageing assets in need of renewal. Many of these assets were never funded by the Councils in the first place but came by way of grant (State or Commonwealth), from developer contributions or from a shift of responsibilities for previously State owned assets to local government. It has been suggested that had Councils been responsible for funding all of their infrastructure, it is highly likely that they would have acquired less. Moreover their rate levels would have been increased to meet the needs of asset acquisition and some of this higher level of rate revenue may have continued on to be available for renewal. As it is, Councils now have to prepare for increased funding to meet the needs of asset renewal.

3.1.2 Planning and Funding

Thus asset renewal creates two separate, but related, problems for Councils:

- planning; and
- funding

Following amalgamations, rates were reduced and capped at CPI less 1%. Although efficiency gains were made through the introduction of compulsory competitive tendering, it was not known whether the degree of savings achieved and achievable would be sufficient, with the reduced rate levels, to sustain Councils infrastructure assets as the time for renewal approached.

Rates are only one means of revenue raising but they are the major means. Increased use of user-pays charging can be used to improve revenues, and the appropriateness of grant levels can be reviewed. However, it is clear that if there is a need for a large increase in funding for infrastructure asset renewal, the major part may need to come by way of rate increases.

3.1.3 Focus on Expenditure Projections

Initially it was considered that the renewal problem would be examined by focussing on revenues: whether the revenue/charges split was appropriate, whether the rate base was appropriate, whether the rate burden on ratepayers was appropriate. This is reflected in the Terms of Reference attached as Appendix 1.

However, as the problem was examined further, it was apparent that little was known on the expenditure side and that measuring the gap between required future asset renewal expenditures and current revenue would need the focus to be placed on estimating the expenditures in the first instance.

Clearly if there is an imbalance between expenditures and revenues as asset renewal increases, Councils not only have the option, they have the requirement, to reconsider all sources of revenue and all types of expenditure. However, choices of what is to be foregone must lie with an individual Council and it would be inappropriate for this study to assume that one type of expenditure took preference over another.

Quite early in discussions with the Steering Committee it was established that the adequacy of existing budgets to fund a higher level of renewal would depend on the willingness and the capability of Councils to restructure their budgets. It was recognised, however, that it was beyond the brief of this study to deal with this restructuring, other than by suggesting ways in which capital expenditures themselves could be restructured.

3.1.4 Modelling Renewal Requirements

In order to model future renewal requirements, certain assumptions needed to be made, namely that all existing assets (unless already tagged for disposal) would be replaced, that maintenance and management practices would remain as they are now, and that the real replacement costs would be constant.

With these assumptions it was possible to project the cost and timing of renewal of Council infrastructure. As with all projections based on default assumptions, the opportunity always remains to change the assumptions if the outcomes projected are undesirable.

Thus, depending on the outcomes, Councils may wish to rationalise their asset stocks, change their maintenance and management practices and look for more cost effective ways of replacing assets.

Similarly on the revenues side. The model assumes existing debt levels, debt redemption policies and funding practices. However, outcomes may be improved by operating on debt levels, debt redemption and funding practices.

3.1.5 Making Optimum Use of Limited Data

It was recognised from the start that the data held by Councils was extremely limited. The Office of Local Government estimates that only about one third of Councils have 5 year forward forecasts of their capital requirements. Infrastructure assets are now required to be reported in balance sheets but a number of Councils only report those infrastructure assets acquired in recent years and there has been no attempt to adjust the acquisition cost for subsequent inflation. Distinctions between maintenance and asset renewal for infrastructure assets varied between Councils as did capitalisation practices.

The approach taken was to devise a survey, with input from Councils, to collect basic data needed to forecast renewal. Initially it was intended to collect information on a sample basis. The Office of Local Government decided that every Council should be visited and this turned out to be extremely beneficial and produced a stronger result.

Analysis of financial measures has been limited to rate revenues with other measures, e.g. debt levels, incorporated as one of the mechanisms by which Councils may choose to manage their situation.

Renewal profiles were analysed against local government classifications to determine whether the growth rates and other features of Councils reflected in these classifications provided any guide to future problems, i.e. to determine whether there were any identifiable “cost drivers”.

3.2 Deliverables

The deliverables from the study were:

- The Survey Form which can be used to update information and ensure the continued usefulness of the database;
- A complete database containing asset profiles, economic lives, and replacement costs for major asset groupings;
- This report, with analysis and recommendations; and
- A formal presentation of the results to a meeting of CEOs.

3.3 Approach

To achieve these results, the Consultants

- Designed a survey form;
- Accepted input from two Reference Groups established by the Office of Local Government, one on roads, and the other on parks and recreation and culture;
- Pilot tested the survey on ten Councils;
- Explained the process and intended outcomes to two meetings of CEOs, one in Melbourne and one in Shepparton;
- Conducted five regional meetings in which the survey forms were explained to both technical and financial staff who were to complete the surveys;
- Visited every Council, discussing problems and survey outcomes;
- Verified and validated the information;
- Returned the cleaned up data to CEOs for checking and confirmation;
- Analysed the data: and
- Produced this report.

A full discussion of the methodology applied will be found in the next chapter, Chapter 4. The analysis is in Chapter 5

3.4 Acknowledgements

Many people have contributed to this report.

Officers at every Council have spent a great deal of time finding, categorising and providing information about their infrastructure assets and asset management practices. Without their assistance and knowledge this report would not have been possible and that help is greatly appreciated. Additionally, about thirty Councils, along with VicRoads and the RACV, made comments on the draft report, many of which are reflected in this final document.

The Steering Committee, the Reference Groups and the Pilot Councils have been particularly helpful in shaping the direction of the study and providing valuable feedback during discussions and meetings.

The Office of Local Government has provided helpful staff, office accommodation and other office services to facilitate the data-gathering and reporting.

Data quality remains with Councils. The authors accept responsibility for the conclusions and recommendations of this report.