

**LOCAL GOVERNMENT AND PLANNING  
MINISTERS' COUNCIL**

**Local Government Financial Sustainability**

**Nationally Consistent Frameworks**

**Framework 1**

**CRITERIA FOR ASSESSING FINANCIAL  
SUSTAINABILITY**

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## **CRITERIA FOR ASSESSING FINANCIAL SUSTAINABILITY**

### **1. INTRODUCTION**

#### **1.1 Task**

To develop a nationally consistent approach to criteria for assessing financial sustainability and to set out the elements of the national framework.

#### **1.2 Scope and Purpose of this Paper**

This paper sets out the background, principles and elements of national criteria for assessing financial sustainability framework with a view to this material being endorsed by LOGJOG.

The paper:

- outlines why national criteria for assessing financial sustainability are important for the overall financial sustainability of local governments;
- presents key challenges that councils face in managing their finances;
- identifies the key principles that underpin national criteria for assessing financial sustainability framework; and
- identifies the proposed elements of national criteria for assessing financial sustainability.

#### **1.3 Definition of criteria for assessing financial sustainability**

This paper is concerned with developing national criteria for assessing financial sustainability which focus on the areas which need to be assessed and the characteristics that need to be considered rather than how this assessment will be done in terms of specific indicators and targets.

A council's long-term financial performance and position is sustainable where planned long-term service and infrastructure levels and standards as prioritised through community engagement and consultation are met without unplanned increases in rates and charges or disruptive cuts to services.

#### **1.4 Background**

The outcomes of the 26 May 2006 Local Government Ministers' Roundtable on Financial Sustainability of Councils proposed the development of nationally consistent approaches to: (i) criteria for assessing financial sustainability of local councils; (ii) asset planning and management; and (iii) financial planning and reporting.

It was considered that a case for more funding through Financial Assistance Grants may be enhanced by jurisdictions implementing a nationally consistent approach to these issues.

### **2. TOWARDS A NATIONAL FRAMEWORK**

#### **2.1 Assessment of local government financial sustainability**

A national approach should promote prudent, transparent and accountable financial management by local governments. It should encourage a strategic approach to meet current and emerging challenges.

All States and the Northern Territory conduct some level of examination into the financial sustainability of their local government bodies. The national criteria complement and endorse the current practices as they apply in each jurisdiction.

The national criteria have been developed as a high level guide for councils to develop a more comprehensive tool to monitor their financial sustainability. This information can be used to inform the community, and other levels of government, of the financial issues that may require remedial action within individual local governments.

### **3. GUIDING PRINCIPLES FOR A NATIONAL APPROACH**

The guiding principles that underpin the development of national criteria for assessing financial sustainability should allow each State and Territory to consider and determine how the elements of the national framework will be accommodated and implemented.

The guiding principles are that:

- a nationally consistent approach to criteria for assessing financial sustainability should sit within the context of each State and Territory's legislative and operating framework. States and Territories should be able to assess their councils financial sustainability in accordance with their own particular circumstances which may include legislative reform, policies, programs or best practice guidance; and
- the elements of a national framework should not limit States and Territories in their assessment of their councils financial sustainability. There may be additional elements that individual jurisdictions may wish to pursue.

### **4. ELEMENTS OF A NATIONAL FRAMEWORK**

#### **4.1 Use of indicators**

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 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.

Local government responsibilities and priorities vary intra and inter State in the circumstances, needs and expectations of their communities. Any evaluation of sustainability needs to be informed by consideration of the challenges faced by different local governments.

Indicators should be examined through the relevant socio-demographic, economic and political lens to avoid misinterpretation and ensure the right actions are taken.

## **4.2 Indicators for a national framework**

### **I. Income Generating Efforts**

#### *Rates*

- The following characteristics may indicate a need for closer examination:
  - where adopted rate increases that have fluctuated substantially; and
  - where rates are at a level that are considerably different to the group median of comparable councils, *particularly where councils indicate a long term inability to maintain and renew assets, have persistent underlying operating deficits, and significant debt.*

#### *Other own source revenue*

- The following characteristics may indicate a need for closer examination:
  - where there is a lack of transparency in the determination of the pricing of services.

#### *Operating Costs*

- The following characteristics may indicate a need for closer examination:
  - where significant and continuous annual increases in operating costs per assessment have been incurred; and/or
  - where operating costs are well above the group median.

#### *Operating Results*

For these purposes the operating result refers to a surplus or deficit, calculated on an accruals basis, excluding asset revaluations, developer contributions, capital grants and accounting corrections.

- The following characteristics may indicate a need for closer examination:
  - where operating deficits have been consistently incurred; and
  - where a resource plan has been adopted that does not make adequate provision to rectify the situation.

### **II. Efficiently delivered services that are appropriate to needs**

Councils should be delivering services appropriate to the needs of their communities in an efficient manner. They might consider a “best value” type assessment together with changes in operating costs.

- The following characteristics may indicate a need for closer examination:
  - where there is an absence of robust community engagement processes to determine appropriate service standards and levels;

### III. Short and long term financial sustainability

#### *Liquidity*

- The following characteristics may indicate a need for closer examination:
  - where difficulty in meeting short term financial obligations is being experienced; and
  - where no prospect of improvement is evident.

#### *Debt*

- Councils may be considered as being less sustainable if they: -
  - have debt which limits their capacity to fund essential needs and negatively impacts on the capacity to provide operational services;
  - leave future generations of ratepayers facing an unmanageable bill for services provided for current ratepayers; and
  - the level of net interest costs associated with debt cannot be met comfortably from a council's operating revenue.

### IV. Ability to maintain, renew and upgrade assets

#### **Asset Renewal**

- The following characteristics may indicate a need for closer examination:-
  - where spending is considerably less on capital works compared to depreciation expense; or (preferably)
  - where renewal levels as stipulated in the asset management plan are not being met – in other words there is a renewal gap that is not being addressed.