



**University of New England**

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**An Evaluation of Performance Measurement and the  
Identification of 'At Risk' Municipal Councils in NSW Local  
Government**

by

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No. 2004-14

**Working Paper Series in Economics**

ISSN 1442 2980

<http://www.une.edu.au/febl/EconStud/wps.htm>

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# **An Evaluation of Performance Measurement and the Identification of ‘At Risk’ Municipal Councils in NSW Local Government**

David Murray and Brian Dollery \*\*

## **Abstract**

Performance monitoring is an important means of establishing accountability in Australian local government. This paper attempts to evaluate the process of performance monitoring in NSW and the method of identifying “at risk” councils. It provides a synoptic description of some salient characteristics of NSW local government by way of institutional background, focusing on council diversity, the classification of local authorities and the financial standing of NSW local government. The paper then examines the process of council performance measurement, the nature of the reporting requirements presently imposed upon councils and concept of “at risk” councils and their identification in NSW.

Key Words: “at risk” councils; performance indicators; performance monitoring.

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## **1. INTRODUCTION**

Over the past two decades public sector reform has affected all levels of government within Australia. However, reforms in the local government sector have lagged behind those in the higher tiers of governance. In general, the objectives of these reforms have been to improve productivity and efficiency in service delivery whilst simultaneously reducing costs of service provision (Industry Commission (IC), 1998). Reform in local governance is conspicuous by the fact that it has been the result of enforced “top-down” reform programs from federal and state levels. In NSW, these reforms have included the implementation of new management practices and the establishment of a clearer separation in the roles between council management and elected representatives with “more stringent annual statements and annual reports” (IC, 1998, p.152).

These new mandatory reporting requirements were designed to improve the transparency of municipal governance by facilitating higher levels of accountability to the various stakeholders. In NSW local government, councils are now required to submit annual reports with the resultant data deployed in the creation of publicly available comparative performance reports which Mr Tony Kelly (2004b, p.9884), NSW Minister for Local Government, has claimed are a “definitive resource tool for anyone with an interest in the performance of local government and councils”. The provision of these reports concurs with one

strategy of the 1994 *Australian Urban and Regional Development Review* (AURDR) that sought to “measure the performance of local governing bodies by using performance indicators” (National Office of Local Government (NOLG), 2001, p.62). The *Review* also advocated the encouragement of “processes of continuous improvement, innovation and reform that enable councils to identify best practice” (p.62). However, there appears to have been little attempt to ensure that the processes used by the overseeing bodies in measuring performance of councils represented “best practice”.

Minister Kelly (2004a, p.8678) has trenchantly asserted that he will not “hesitate to pull into line under-performing councils”. In terms of the number of councils affected directly, Burton (2004, p.6197) has observed that “the Department of Local Government (DLG) has 30 councils on financial watch, and some of them are nearly broke”. These watch lists contain councils in financial difficulties and represent those municipalities which have been identified by the DLG using its performance indicators.

Councils in NSW have been subject to the same pressures as Australian local government as a whole. Cost-shifting from federal and state governments as well as increased expectations from the community have placed a considerable financial burden on municipalities (Johnson, 2003). However, the ability of NSW councils to raise revenue is further constrained through mandatory rate capping,

increasing financial stress compared to their counterparts in other states (Vermeer, 2004).

Given the severe consequences that can flow from being identified as an “at risk” council in NSW, including investigation by the DLG and even dissolution, it is important to determine whether the performance measurement system employed in NSW operates in a efficacious manner. Accordingly, this paper seeks to examine the performance measurement requirements and techniques that have been imposed on NSW local government. Three main questions are considered. How are financially struggling councils identified? Is the methodology that is employed to this end sufficiently robust to withstand scrutiny? Finally, do the monitoring lists provide a true indication of financial performance to the extent that the financial accountability of councils is discharged?

The paper itself is divided into five main parts. The first section of the paper highlights some of the more important characteristics of NSW local government by way of institutional background, focusing on council diversity and the classification of local authorities, as well as the financial standing of NSW local government. The second section examines the process of council performance appraisal in NSW. Part three explores the reporting requirements presently imposed upon councils. Section four examines the concept of “at risk”

councils and their identification in NSW. The paper ends with some brief concluding comments in section five.

## **2. INSTITUTIONAL BACKGROUND**

### *2.1 Council Diversity and Council Classification in NSW*

There is considerable diversity within NSW local government. The significant differences across local government include “the physical, economic, social and cultural environments of local government areas”, the “range and scale of functions”, the fiscal position of councils, the “aptitudes and attitudes of communities”, and the “structures of power and influence within local communities and the extent to which elected representatives reflect a broad range of opinion” (NOLG, 2003, p.6). Moreover, this is amplified by the differing roles councils play in different areas. For instance, large metropolitan councils must provide for commercial and cultural activities beyond those which predominantly target their own residents and/or ratepayers, whereas rural municipalities may need to be involved in the recruitment of professional persons, such as doctors, where shortages of these skills exist (AHRSC, 2003).

Within the sector, essential service provision also differs between councils based on geographical location. In regional areas, councils are responsible for the provision and maintenance of water and sewerage services, while in the Sydney

and Hunter areas, these services are provided by Sydney Water and Hunter Water respectively (DLG, 2004a).

In 1994, the Commonwealth Department of Housing and Regional Transport constructed the Australian Classification of Local Governments (ACLG), a 22-category classification system for councils that illustrates the diversity of council types. This system is displayed in Table 1.

**Table 1.** Australian Classification of Local Governments

<b>Step 1</b>	<b>Step 2</b>	<b>Step 3</b>	<b>Identifiers</b>	<b>Category</b>
<i>URBAN (U)</i>	<i>Capital City (CC)</i>			UCC
Population more than 20,000	<i>Metropolitan Developed (D)</i>	Small (S)	Up to 30,000	UDS
	Part of an urban centre of more than 1,000,000 or population density more than 600/sq km	Medium (M)	30,001 – 70,000	UDM
		Large (L)	70,001 – 120,000	UDL
		Very Large (V)	More than 120,000	UDV
OR				
Population density more than 30 persons/sq km	<i>Regional Town/City (R)</i>	Small (S)	Up to 30,000	URS
	Part of an urban centre with population less than 1,000,000 and predominantly urban in nature.	Medium (M)	30,001 – 70,000	URM
		Large (L)	70,001 – 120,000	URL
		Very Large (V)	More than 120,000	URV
OR				
90% or more of LGA population is urban	<i>Fringe (F)</i>	Small (S)	Up to 30,000	UFS
	A developing LGA on the margin of a developed or regional urban centre	Medium (M)	30,001 – 70,000	UFM
		Large (L)	70,001 – 120,000	UFL
		Very Large (V)	More than 120,000	UFV
<i>RURAL (R)</i>				
An LGA with population less than 20,000	<i>Significant Growth (SG)</i> Average annual population growth more than 3%, population more than 5,000, and not remote	Not Applicable		RSG
AND				
Population density less than 30 persons/sq km	<i>Agricultural (A)</i>	Small (S)	Up to 2,000	URS
		Medium (M)	2,001 – 5,000	URM
		Large (L)	5,001 – 10,000	URL
		Very Large (V)	10,001 – 20,000	URV
AND				
Less than 90% of LGA population is urban	<i>Remote (T)</i>	Extra Small (X)	Up to 400	UFS
		Small (S)	401 – 1,000	UFM
		Medium (M)	1,001 – 3,000	UFL
		Large (L)	3,001 – 20,000	UFV

Source: NOLG (2003, p.190)



NOLG (2003, p.191) have classified each council within NSW according to this classification system. This is shown in Table 2.

**Table 2. ACLG Classification of NSW Councils (Number)**

<b>Category Name</b>	<b>Category</b>	<b>Number</b>
Urban Capital City	UCC	1
Urban Developed Small	UDS	3
Urban Developed Medium	UDM	14
Urban Developed Large	UDL	7
Urban Developed Very Large	UDV	8
Urban Regional Small	URS	15
Urban Regional Medium	URM	18
Urban Regional Large	URL	2
Urban Regional Very Large	URV	3
Urban Fringe Small	UFS	0
Urban Fringe Medium	UFM	3
Urban Fringe Large	UFL	1
Urban Fringe Very Large	UFV	7
Rural Significant Growth	RSG	0
Rural Agricultural Small	RAS	5
Rural Agricultural Medium	RAM	38
Rural Agricultural Large	RAL	27
Rural Agricultural Very Large	RAV	18
Rural Remote Very Small	RTX	3
Rural Remote Small	RTS	0
Rural Remote Medium	RTM	1
Rural Remote Large	RTL	1

Source: NOLG (2003, p.191)

Table 2 indicates that 19 categories (out of the 22 NOLG categories) are present in NSW. However, the NSW DLG has constructed their own classification system, derived from the ACLG, which comprises 11 categories. The DLG (2004a) contend that the predominant reason for this is to facilitate comparability. The DLG's derivation of the ACLG classification is presented in Table 3.

**Table 3.** Australian Classification of Local Governments and DLG Group Numbers

Step 1	Step 2	Step 3	Identifiers	Alpha	DLG Group
<i>URBAN (U)</i>	<i>Capital City (CC)</i>			UCC	1
Population more than 20,000	<i>Metropolitan Developed (D)</i> Part of an urban centre of more than 1,000,000 or population density more than 600/sq km	Small (S)	Up to 30,000	UDS	2
		Medium (M)	30,001 – 70,000	UDM	
		Large (L)	70,001 – 120,000	UDL	3
		Very Large (V)	More than 120,000	UDV	
Population density more than 30 persons/sq km	<i>Regional Town/City (R)</i> Part of an urban centre with population less than 1,000,000 and predominantly urban in nature.	Small (S)	Up to 30,000	URS	4
		Medium (M)	30,001 – 70,000	URM	
		Large (L)	70,001 – 120,000	URL	5
		Very Large (V)	More than 120,000	URV	
90% or more of LGA population is urban	<i>Fringe (F)</i> A developing LGA on the margin of a developed or regional urban centre	Small (S)	Up to 30,000	UFS	6
		Medium (M)	30,001 – 70,000	UFM	
		Large (L)	70,001 – 120,000	UFL	7
		Very Large (V)	More than 120,000	UFV	
<i>RURAL (R)</i>					
An LGA with population less than 20,000	<i>Significant Growth (SG)</i> Average annual population growth more than 3%, population more than 5,000, and not remote	Not Applicable		RSG	N/A
Population density less than 30 persons/sq km	<i>Agricultural (A)</i>	Small (S)	Up to 2,000	RAS	8
		Medium (M)	2,001 – 5,000	RAM	9
		Large (L)	5,001 – 10,000	RAL	10
		Very Large (V)	10,001 – 20,000	RAV	11
Less than 90% of LGA population is urban	<i>Remote (T)</i>	Extra Small (X)	Up to 400	RTX	N/A
		Small (S)	401 – 1,000	RTS	N/A
		Medium (M)	1,001 – 3,000	RTM	9
		Large (L)	3,001 – 20,000	RTL	10

Source: DLG (2004a, p.13)

A comparison of Table 1 and Table 3 demonstrates that the NSW DLG has merged four categories into two, regardless of the population requirements specified within the Australian Classification of Local Governments. These merged categories are rural agricultural medium (RAM) with rural remote medium (RTM), and rural agricultural large (RAL) with rural remote large (RTL).

Moreover, the DLG has abolished the categories of rural significant growth (RSG), rural remote extra small (RTX) and rural remote small (RTS), despite NOLG (2003) maintaining that three councils in NSW could be classified as RSG. It can thus be argued that this grouping of councils by the DLG does not so much diminish the variation between municipalities; rather it appears to “mask” variation for ease of comparison.

The DLG classification system takes into account the geographical location and population of councils. It need hardly be added that within NSW, municipal populations, road lengths maintained and geographical size of councils can vary considerably as is apparent in Table 4.

**Table 4.** Variation in Population, Road Length and Area of Councils

	<b>Lowest</b>	<b>Highest</b>	<b>Median</b>	<b>Mean</b>
Population	58	261,260	13,668	37,325
Road Length (km)	0	3,245	725	817
Area (sq km)	0	53,511	2,481	4,046

Source: NOLG (2003, pp.4-6)

Note:

1. An area of “0” represents those councils with non-defined boundaries (e.g. indigenous community councils).
2. The smallest defined area is 6 sq km (DLG, 2004c)

However, diversity in NSW local government is not limited to these factors. There exists considerable variation in municipal finances THAT will be explored next.

## 2.2 NSW Local Government Finances

Local government in NSW is a \$6 billion annual industry (DLG 2004c). It is financed through the collection of rates, various user charges and fees, federal and state grants, interest received, contributions and donations, and other combined minor revenue sources (DLG, 2004a). Due to the differences that exist between urban and regional councils, there is considerable disparity in the ability of councils to raise revenue through increased rates and user charges, with general acknowledgement that regional and rural councils will be more reliant on grants (AHRSC, 2003). Moreover, the same differences that constrain revenue raising also affect the costs of providing services (AHRSC, 2003). The variation in revenue across NSW local government is shown in Table 5.

**Table 5.** Dissection and Variation in Revenue from Ordinary Activities

	<b>Lowest</b>	<b>Highest</b>	<b>Median</b>	<b>Mean</b>
Rates and Annual Charges (%)	10	74	39	47
User Charges and Fees (%)	4	47	17	17
Interest (%)	0	8	3	3
Grants (%)	2	57	23	16
Contributions and Donations (%)	0	55	10	13
Other Revenues (%)	0	19	2	4
Total Revenue per Capita (\$)	464	6,261	1,048	774

Source: NOLG (2003, p.21)

Taxation through rate collections is the greatest individual source of income for NSW local government, representing 37.8% or \$2.26 billion of total revenue for NSW councils in 2001/02. In NSW, rates payments are calculated on an individual basis according to the unimproved value of the property (NOLG, 2003). Moreover, the extent to which rates can be increased annually is “capped” by the NSW state government; a constraint which is not imposed by any other state. Whilst councils may apply for Ministerial approval for an increase above this amount, municipalities are nevertheless generally unable to control their own income levels. This capped increase has been set consistently around 3-4% over the past few years; for the 2004/05 financial year rate increases have been capped at 3.5% (DLG, 2004b) down from 3.6% for 2003/04 (DLG, 2003).

Access Economics (2003, p.18) has argued that rate capping is grossly inefficient and “inconsistent with the call for local governments to become more financially secure”. Moreover, it is claimed (AHRSC, 2003, p.42) that rate capping “lacks transparency” and is vulnerable to political persuasion of the incumbent state government. Consequently, the AHRSC (2003, p.42) identified it as an “oppressive policy”, which adversely affects the capacity of councils to provide services. For example, in 2002/03 rate increases were capped at 3.3%, whilst councils faced average public liability premium increases of 30-50%, and increases in the NSW Fire Brigades Levy of 13.3% (AHRSC, 2003, p.42).

In common with revenue, there is considerable variation in expenditure between NSW councils. This variation is shown in Table 6.

**Table 6.** Dissection and Variation in Expenditure from Ordinary Activities

	<b>Lowest</b>	<b>Highest</b>	<b>Median</b>	<b>Mean</b>
Employee Costs (%)	19	54	37	39
Materials and Contracts (%)	9	44	27	25
Borrowing Costs (%)	0	13	1	2
Depreciation (%)	11	40	21	20
Other Expenses (%)	3	33	11	15
Total Expenses per Capita (\$)	479	4,745	1,055	774

Source: NOLG (2003, p.21)

Table 6 illustrates that the variation in council expenditure is extremely high. Employee costs, whilst averaging 39% across the state, vary between 19% and 54% of all ordinary activity expenditure in NSW councils. Similarly, expenditure on materials and contracts varies between 9% and 44%. These two expenditure aspects combined account for an average of 64% of all local government expenditure in NSW.

### **3. PERFORMANCE APPRAISAL IN NSW LOCAL GOVERNMENT**

The NSW DLG (2003) monitors council performance in order to “ensure greater compliance and financial viability of the local government sector”. Table 7 details the specific functions of the DLG in achieving this broad objective.

**Table 7. Department of Local Government Objectives**

1.	To monitor and review council operations.
2.	To provide assistance to individual councils experiencing either managerial or financial difficulties.
3.	Examine, investigate and attempt to resolve complaints about councils.
4.	To assist councils to improve operations as a consequence of reviews, information and investigations conducted by the Department.
5.	Monitor compliance with all aspects of local government legislation.
6.	The development and implementation of sector specific training programs.
7.	The liaison with ICAC and the NSW Ombudsman, sharing information with the view to develop best practice resources.
8.	To promote best practice achievements across the sector.
9.	To participate in sector conferences, taskforces, working parties, boards and committees.
10.	To try to improve community access to local government sector information.

Source: DLG 2003 p.43

Many of these objectives are specific to the operation of the DLG itself, although relevance to councils is found in five of these functions. Complaints handling involves the Department recording each complaint received about a council. The majority of complaints about municipalities deal with planning matters, pecuniary conflict of interest of councillors, misconduct and corruption by either council staff or councillors, mismanagement, and tendering complaints. Often the DLG merely provides an oversight role, allowing the council concerned to attempt to resolve the problem, and ensuring that local authorities have reached a satisfactory outcome. However, the Department does launch preliminary investigations into some complaints (around 20% of all complaints in 2002/03),

based on the “investigative priorities” of the Department at that time. Whilst the NSW Local Government Act (LGA) (1993) provides for investigations into council conduct under Section 430, this avenue is pursued only as a “final step” or where “the consequences of a council’s conduct are having a serious impact on the local community” (DLG, 2003, p.51). Despite this, Section 429 of the Act allows the Director-General of the DLG to request information from the council regarding complaints; this provision is often invoked in preliminary investigations.

The DLG also monitors and regulates the financial performance of councils. In essence, this is performed through examining rate variation requests, loan borrowings, and reviewing the financial accounts of councils. Councils may request from the Minister a special rates variation that exceeds the regulated rates increase, and must state the reason(s) for such a request. Approval for such a rate variation, when granted, is normally conditional for a set period of time, and councils “must reduce their income in the rating year following the completion of the approval period by the amount of additional revenue raised over the period that the special variation was applied” (DLG, 2003, p.56). Moreover, if the variation was for specific projects, councils must report on the outcomes and expenditures associated with that project for the duration of the approval. The NSW State Treasury “caps” the amount to which the local government sector can raise new borrowings each year, which for 2002/03 was \$350 million, of which \$272 million



was borrowed by councils (DLG, 2003, p.57). Councils seeking to raise such loans must seek Ministerial approval and must report the amount taken up in their annual reports. The financial position of councils is determined by the Department through an analysis of individual council annual reports, either where reports are not submitted “within a reasonable period after the due date” or, councils that “generate some level of concern in the financial area” (p.61). Once a council is identified of “having issues with their financial position”, the DLG follows a set path. Firstly, by writing to the council to inform them of their identification as having financial concerns; secondly, monitoring the council through instigating requirements, such as quarterly rather than annual reports; thirdly, investigating the council’s finances; fourthly, launching a public inquiry into the council’s operations; and finally, upon receipt of the inquiry’s findings, the Minister may dismiss the council and place the council’s operations in the hands of an administrator.

#### **4. REPORTING REQUIREMENTS OF NSW LOCAL GOVERNMENT**

NSW councils are legally mandated to submit reports within five months of the end of each financial year to the Minister for Local Government. These reports encompass eighteen areas, which include financial results, infrastructure status, employment information, and council’s performance against meeting other,

external legislative requirements. The reporting criteria of NSW local government are summarised in Table 8.

**Table 8. Reporting Requirements of NSW Councils**

A	A copy of audited financial results
B	Comparison of performance between current and previous years against management plans, including reasons for any differences in actual performance and that which was forecast. It must also incorporate projected performance for the following year.
C	A report on the “state of the environment” with council’s boundaries, including water, air, land, waste, noise, biodiversity, and aboriginal/non-aboriginal heritage. Environmental impact of activities, any special council projects and management plans should also be included.
D	Condition of council controlled infrastructure, including estimates for returning such infrastructure to an “acceptable” standard, the costs for maintaining that standard, and the maintenance program for the succeeding year.
E	Summary information of amounts paid in legal action.
F	The amounts paid to mayors and councillors, along with a copy of council’s policy on and expenditure on facility provision for these representatives.
G	A statement on the number of, remuneration paid too, and all other expenses incurred in the employment of senior staff.
H	Details of each awarded contract, whether such contracts were awarded by tender or not. This does not include employment contracts or contracts with values of less than \$100,000 or an amount specified by regulation.
I	A report on bush fire hazard reduction activities, including such activities approved under the Rural Fires Act 1997.
J	Details of programs undertaken to promote services and access to people with diverse cultural and linguistic backgrounds.
K	Details of resolutions made under Sect 67 of the Act regarding work on private premises where costs were met fully or partially by council.
L	The total amount contributed or otherwise granted by Sect 336 of the Act (financial assistance to other councils).
M	A statement of human resource activities (e.g. training) undertaken by council.
N	A statement of undertaken activities by council to implement its equal opportunity management plan.
O	A statement of all external bodies (e.g. county councils) that exercised functions delegated by council.
P	A statement of all companies in which council held a controlling interest.
Q	A statement of all partnerships, co-operatives or other joint ventures to which council was a party during that year
R	An other information required by regulations

Source: LGA (Sect428)

The NSW Department of Local Government uses the information contained in council annual reports to compile comparative performance tables which are published annually. The information contained in these comparative tables detail each council's performance in eleven categories with a total of thirty different performance indicators employed. These categories and indicators are displayed in Table 9.

**Table 9.** NSW Local Government Annual Reports: Key Performance Indicators

<b>Category</b>	<b>Key Performance Indicator</b>
1	<b>Rating</b> 1.1 Average rate per assessment 1.2 Outstanding rates, charges and fees 1.3 Percentage movement in rates and annual charges revenue from previous year 1.4 Percentage movement in user charges and fees from previous year
2	<b>Financial</b> 2.1 Sources of revenue from ordinary activities 2.2 Total ordinary activities revenue per capita 2.3 Dissection of expenses from ordinary activities 2.4 Total expenses from ordinary activities per capita 2.5 Current ratio (unrestricted) 2.6 Debt service ratio 2.7 Capital expenditure ratio
3	<b>Corporate</b> 3.1 Number of equivalent full time staff 3.2 Compliance with statutory reporting deadlines
4	<b>Library Services</b> 4.1 Library expenses per capita 4.2 Circulation per capita
5	<b>Domestic Waste Management and Recycling Services</b> 5.1 Average charge for domestic waste management services per residential property 5.2 Costs per service for domestic waste collection 5.3 Recyclables – kilograms per capita per annum 5.4 Domestic waste – kilograms per capita per annum
6	<b>Water Supply Services</b> 6.1 Average bill for residential customers (\$ per connected residential property) 6.2 Operating costs including depreciation (\$ per connected property)

7	<b>Sewerage Services</b> 7.1 Average bill for residential customers (\$ per connected residential property) 7.2 Operating costs including depreciation (\$ per connected property)
8	<b>Planning and Development Services</b> 8.1 Number of development applications determined 8.2 Mean time in calendar days for determining development applications 8.3 Median time in calendar days for determining development applications 8.4 Legal expenses to total planning and development costs
9	<b>Environmental Management and Health Services</b> 9.1 Environmental management and health expenses per capita
10	<b>Recreation and Leisure Services</b> 10.1 Net recreation and leisure expenses per capita
11	<b>Community Services</b> 11.1 Community services expenses per capita

Source: Compiled from DLG (2004a)

In the compilation of the comparative reports, the DLG indicates the state highs, lows, means and medians of each indicator, and then, utilising their grouping system, breaks the results down into the eleven groups shown in Table 9. This allows for the comparison of any given council against both other councils within that DLG cluster, and with the average result for that group. Despite this, the DLG issues a general caveat that “when assessing the performances of councils, it is important to remember that local circumstances can influence how well a council provides its services. There are often good reasons why it is harder or more costly to provide certain services in some local government areas than in others or why a different mix of services may be delivered. In some cases, councils may have made conscious decisions to provide lower or higher levels of services depending on local needs” (DLG, 2004a, p.11). In order to overcome this, the DLG provides a profile of each council which incorporates the grouping, the

ACLG classification, population, area, population density, population growth, proportion of the population that is either Aboriginal/Torres Straight Islander, or from a non-English speaking background, on grounds that use of such profiles will be of assistance in comparing performance information (DLG, 2004a).

## **5. IDENTIFYING “AT RISK” COUNCILS IN NSW**

### *5.1 Monitoring Lists*

The DLG has in place “monitoring” lists of councils that display those municipalities that have been identified as having the greatest financial difficulties. These lists have been compiled over the past few years through a process that may be described as undergoing “evolving development”. The lists themselves have been reported publicly since 2000/01 in the DLG annual reports. The monitoring lists as reported by the DLG are displayed in Table 10.

**Table 10. Monitoring Lists**

<b>2002/03</b>	<b>2001/02</b>	<b>2000/01</b>
Bourke	Bourke	Bourke
Brewarrina	Brewarrina	Brewarrina
Castlereagh-Macquarie (see note)	Canada Bay	Copmanhurst
Copmanhurst	Copmanhurst	Cowra
Cowra	Cowra	Deniliquin
Cudgegong	Deniliquin	Dungog
Deniliquin	Dungog	Eurobodalla
Dungog	Eurobodalla	Evans
Evans	Evans	Goulburn
Gilgandra	Glen Innes	Griffith
Glen Innes	Gunnedah	Gunning
Gunning	Gunning	Harden
Harden	Harden	Holbrook
Hunters Hill	Holbrook	Ku-ring-gai
Merriwa	Ku-ring-gai	Merriwa
Mid-Western (see note)	Merriwa	Moree
Moree Plains	Moree Plains	Mosman
Murrurundi	Murrurundi	Nundle
Nundle	Nundle	Warringah
Port Stephens	Port Stephens	Yallaroi
Pristine Waters	Pristine Waters	
Rylstone	Severn	
Severn	Uralla	
Uralla	Wagga Wagga	
Wagga Wagga	Wakool	
Wakool	Walgett	
Walgett	Warringah	
Warringah	Yallaroi	
Yallaroi	Young	
Young		

Note: Castlereagh-Macquarie and Mid-Western are both County Councils

Source: DLG (2001; 2002; 2003; 2004d)

The lists displayed in Table 10 demonstrate that a total of 37 different councils have appeared on the monitoring lists since 2000/01. Moreover, 14 councils have appeared three times; 13 councils have appeared twice; and 10

councils have appeared once. Table 11 separates the monitoring lists into broad categories of councils based upon location and structure and shows that since 2000/01 the monitoring lists contain a predominance of councils that are classified as “rural”. Moreover, there has been a large increase in the size of the monitoring list in 2001/02. Of special concern within these results is that in 2002/03 two County Councils (Castlereagh-Macquarie and Mid-Western) were placed on the list, despite the fact that such institutions are formed by a few councils contributing to form the County Council. County Council functions are set out by proclamation and may “comprise any one or more functions of a council” (LGA, Sect394). Consequently, County Councils as such are not subject to ACLG or DLG classification. However, the formation of a County Council immediately precludes local council members from undertaking such functions as are proclaimed to be those of the County Council.

**Table 11. Dissection of Monitoring Lists**

<b>Year</b>	<b>Urban (Metro)</b>	<b>% List</b>	<b>Urban (Reg)</b>	<b>% List</b>	<b>Rural</b>	<b>% List</b>	<b>County Council</b>	<b>% List</b>	<b>Total</b>	<b>% Change</b>
2000/01	3	15.00	4	20.00	13	65.00	0	0.00	20	
2001/02	3	10.35	5	17.24	21	72.41	0	0.00	29	45.00
2002/03	2	6.67	4	13.33	22	73.33	2	6.67	30	3.45
<b>Total</b>	<b>8</b>	<b>10.12</b>	<b>13</b>	<b>16.46</b>	<b>56</b>	<b>70.89</b>	<b>2</b>	<b>2.53</b>	<b>79</b>	

Source: DLG (2001; 2002; 2003)

## 5.2 *Creation of Monitoring Lists*

The NSW DLG (2004c, p.3) reported that in relation to its monitoring lists that “some were under notice because of poor audit reports, others because of a departmental examination of the accounts”. In discussions with the DLG, it has been advised that the monitoring lists are compiled following financial analysis of the annual reports submitted by councils. Moreover, the main aspects of the reports used are the financial ratios and liquidity information presented.

Based upon information provided by the Department, Table 12 shows the relevant Key Performance Indicators (KPI's) used in the monitoring lists.

**Table 12. Financial Performance Indicators**

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Sources of revenue from ordinary activities
Total ordinary activities revenue per capita
Dissection of expenses from ordinary activities
Total expenses from ordinary activities per capita
Current ratio (unrestricted)
Debt service ratio
Capital expenditure ratio

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Source: Compiled from DLG (2004a)

As we have seen, revenue from ordinary activities includes rates and charges, user charges and fees, receipt of interest, grants payments, contributions and donations, as well as other minor forms of revenue. Expenditure from ordinary activities encompasses costs for employees, materials and contracts, borrowings,



depreciation, as well as other minor costs. For ease of analysis, abbreviations have been adopted for each financial KPI and their elements are presented in Table 13.

**Table 13. Revenue and Expenditure Abbreviations**

KPI <sub>1Y</sub>	Total ordinary activities revenue per capita
KPI <sub>11</sub>	Rates and annual charges
KPI <sub>12</sub>	User charges and fees
KPI <sub>13</sub>	Interest
KPI <sub>14</sub>	Grants
KPI <sub>15</sub>	Contributions and donations
KPI <sub>16</sub>	Other revenues
KPI <sub>2</sub>	Total revenue from ordinary activities per capita
KPI <sub>3E</sub>	Dissection of expenses from ordinary activities
KPI <sub>31</sub>	Employee costs
KPI <sub>32</sub>	Materials and contracts
KPI <sub>33</sub>	Borrowing costs
KPI <sub>34</sub>	Depreciation
KPI <sub>35</sub>	Other expenses
KPI <sub>4</sub>	Total expenses from ordinary activities per capita

The comparative tables published by DLG report both the current and the previous year's results for each of these KPI categories.

The first indicator shown is KPI<sub>1Y</sub>, designed to “assess the degree of dependence on alternative sources of revenue” (DLG, 2004a, p.61) and displays each indicator as a percentage of total revenue. This indicator is calculated as:

$$KPI_{1Y} = \frac{Y \times 100}{\text{Total ordinary revenue}}$$

Where: Y = Source of revenue

The DLG advises (2004a, p.61) that “some factors affecting this indicator” include “the level of council's entrepreneurial and investment activity; the

socioeconomic characteristics of the area; the relative level of Federal/State funding; and the rate of new development”.

Total revenue received per capita of council population (KPI<sub>2Y</sub>) is also shown in the comparative tables. It is included to try and assess the revenue available to service the needs of the community. This indicator is calculated as follows:

$$KPI_2 = \frac{\text{Total ordinary activities revenue before capital receipts}}{\text{Estimated resident population within council boundaries}}$$

Whilst noting that this indicator can be influenced by rate capping, the acknowledged primary factors affecting this indicator are the same as for KPI<sub>1Y</sub>, with the addition of “the demographic characteristics of the population” (DLG, 2004a, p.72)

Results published demonstrate a similar pattern for costs as they do for revenues, with each cost being recorded as a percentage of total costs across two years, as well as the variation in result within that period. KPI<sub>3E</sub> assesses a council’s expenditure patterns and is calculated as:

$$KPI_{3E} = \frac{E \times 100}{\text{Total ordinary expenditure}}$$

Where: E = Source of revenue

Determining factors for this indicator include “the socioeconomic characteristics of the area; the rate of new development; the demographic

characteristics of the population; and the level of population increase or decrease” (DLG, 2004a, p.77).

Total costs are shown in monetary terms (KPI<sub>4</sub>) and as a proportion of total costs per capita within the reporting year, and is calculated by:

$$KPI_4 = \frac{\text{Total expenses activities revenue before capital expenditure}}{\text{Estimated resident population within council boundaries}}$$

The DLG concedes that there are no additional affecting factors for this indicator other than those shown for KPI<sub>3E</sub>.

The other indicators employed by the DLG are the financial ratios, which have been abbreviated as shown in Table 14.

**Table 14.** Financial Ratio Abbreviations

KPI <sub>5</sub>	Current ratio (unrestricted)
KPI <sub>6</sub>	Debt service ratio
KPI <sub>7</sub>	Capital expenditure ratio

The current ratio provides an indication of “a council’s ability to meet its financial obligations” (p.93), assessing the level of liquidity and capacity to satisfy obligations as fall due in the short term. It is calculated as:

$$KPI_5 = \frac{\text{Current assets less all external restrictions}}{\text{Current liabilities less specific purpose liabilities}}$$

This may be affected by planning and budgetary controls; cash management and the timing of cash flows; the level of restricted assets; and credit management policies and economic circumstances.

The debt service ratio is designed to assess “the degree to which revenues from ordinary activities are committed to the repayment of debt” (p.99), and include debt redemption from revenue, transfers to sinking funds and overdraft interest. This indicator is calculated as:

$$KPI_6 = \frac{\text{Net debt service cost} \times 100}{\text{Revenue from ordinary activities}}$$

Affecting factors may include: “The rate of new development; Debt policy; Interest rate movements and loan terms; Capital investment strategies and capital contributions policies; The level of cash reserves; The state of infrastructure/life stage of assets” (p.99).

The final indicator employed by the DLG is that of the capital expenditure ratio. This assesses “a council’s ability to replace or add to capital assets compared with the consumption (depreciation) of assets” (p.105). This indicator is calculated as:

$$KPI_7 = \frac{P_t \text{ property, plant, equipment} - P_{t-1} \text{ property, plant, equipment} \times 100}{P_t \text{ depreciation rate}}$$

Where:  $P_t$  = The current year/reporting period  
 $P_{t-1}$  = The previous year/reporting period

This ratio may be affected by “the capital expenditure policy; the valuation methodology; one off changes to asset base; and the depreciation rate used” (p.105)

In addition to these KPI, the DLG (2003, p.61) also monitors the financial position of councils that fail to submit their annual reports “within a reasonable period after the due date”. These reports provide an indication of the corporate governance of the council, specifically with respect to the degree to which municipalities comply with statutory deadlines. While extensions may be granted by the Director General of the DLG for the submission of the financial report, no extension is permitted for the annual report itself. Three separate indicators are used by the DLG; the timeliness of the annual report, the environment report, and the financial report. These indicators can be affected by the following factors: “How efficiently the reporting process is managed; The efficiency of data management, including record keeping; Delays in receiving component information e.g. the audited financial reports; The availability of staff; Technical delays in publication” (p.117)

## **6. CONCLUDING COMMENTS**

This paper has sought to evaluate the methods by which councils are presently defined as being “at risk” in NSW. We have demonstrated that local government

in NSW is characterized by a high degree of diversity against several criteria. However, due to the DLG's "minimalist" grouping of councils, certain categorisation criteria are ignored, and the failure to provide group specific KPI cluster commentary limits prevent the use of comparative measures as a means of discharging accountability.

Monitoring lists within NSW are created through an analysis of financial and corporate results, which at best can be described as a measure of financial soundness. However, the present construction methods provide little to indicate that an adequate analysis has occurred. It seems that the monitoring lists are being constructed on a primarily subjective basis. Moreover, as a means of attributing financial soundness or otherwise to councils, the present monitoring lists must be treated with a considerable degree of caution. This is due in part to councils lacking control over their own revenue levels owing to rate capping and the application of restrictive regulations and statutes over user charges and fees. Consequently, the ability of NSW local governments manage their accountability requirements to the Parliament and the citizenry can perhaps best be described as a compromise, which present monitoring lists fail to address.

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