



Catalysing Local Infrastructure Renewal

Australian Government leadership in establishing a ‘Local Infrastructure Australia’ can catalyse the long term reforms needed to eliminate Australia’s local infrastructure deficit

Key Points

- The \$15bn+ local infrastructure deficit and associated constraints on new investment in community infrastructure undermines the prosperity of regional Australia.
- New investment, improved management of infrastructure at the local level and better information for policy making is needed to address this problem.
- Establishing a new organisation - *Local Infrastructure Australia* – can catalyse this long-term systemic change.
- This approach will be particularly beneficial for smaller regional councils that have less capacity for funding, financing and managing local infrastructure.

Policy Implications

The Australian Government should lead an intergovernmental effort to establish *Local Infrastructure Australia* which would take carriage of local infrastructure issues at the national level.

Local Infrastructure Australia can then lead system wide change by providing services in three areas:

- project pooling and private finance brokering
- advisory services to local governments on infrastructure development and management, and
- consistent national information on local infrastructure needs and associated socio-economic benefits.

Benefits will include substantial private investment in local infrastructure, more small Councils in regional areas achieving best practice in their management and funding of infrastructure. Local infrastructure will also be better understood and positioned to compete for national and state infrastructure funding alongside large, state and national level projects.

The establishment of *Local Infrastructure Australia* can be achieved at low cost and low risk to the Commonwealth based on international experience. The relatively small initial investment required can be drawn from existing regional infrastructure funding sources and on-going costs covered by financing activities. Extension of a government guarantee to the pooled financing arrangements will ensure the private finance can be delivered at the lowest possible cost.

POLICY ISSUE

Quality local infrastructure is fundamental to the prosperity of regional Australia.

An estimated infrastructure deficit of between \$12 and \$15.3 billion exists in Australia.

This deficit continues to grow overtime despite a series of reports and stop gap funding initiatives.

ABOUT THE RESEARCH

This policy briefing is based on research by the Regional Australia Institute entitled - *The Case for a National Finance Authority for Local Infrastructure in Australia*.

Information from the Australian Government’s *Strong Foundations for Sustainable Local Infrastructure: Connecting Communities, Projects, Finance and Funds* report and other relevant reports also contribute to the conclusions in this briefing.

Context

Adequate local infrastructure is fundamental for regional prosperity. It supports the efficient functioning of local economies, connection to markets and the quality of life a region needs to attract and retain residents and businesses.

Australia has a significant local infrastructure deficit which has accumulated after years of inadequate investment. Estimates put the current deficit in the range of \$12 - \$15.3 billionⁱ.

As a result of the deficit and on-going underinvestment, each Australian incurs an average additional deficit of \$87-109 every yearⁱⁱ. As well as constraining local development, the deficit represents an ever growing liability that future generations will bear.

The existence of this problem is well known but the policy options available to deal with it are challenging. To date, initiatives such as Roads to Recovery have plugged gaps and reduced the rate of growth in the deficit without offering any long term solutions.

Solving the Problem

Solving the local infrastructure crisis requires an integrated set of reforms and all levels of government. The reform imperatives are to:

- improve the ability of local governments to fund infrastructure from their own revenue
- ensure local infrastructure secures a share of national and state infrastructure investment that reflects its benefits to society, and
- secure greater private investment in local infrastructure projects.

There are also unrealized opportunities to better utilize local revenue to support investment in infrastructure. Collaborative asset ownership or management arrangements between groups of Councils and/or the private sector can also assist in reducing the infrastructure deficit.

The Australian Government is now considering the recommendations of a new report on the issue from Ernst and Youngⁱⁱⁱ.

This report recommends the establishment of a National Finance Authority.

Findings

Amongst the policy options available to deal with the local infrastructure crisis, the establishment of *Local Infrastructure Australia* to support local infrastructure investment and management represents the best option for significant change in the current fiscal climate.

Wider reforms to build local government capacity to pay for infrastructure and increases in state and national government investment are certainly required to fully address the infrastructure deficit.

However RAI research shows that a dedicated national organisation is essential for delivering the increased levels of private investment required to overcome the deficit. With the right model, this will also support progress on systemic issues in local infrastructure beyond access to private finance.

The establishment of this entity as a national organisation focussed exclusively on local infrastructure is also essential. A national body can better leverage economies of scale, spread risk and ensure that the requirements of large investors are met compared to state based approaches.

Case for Local Infrastructure Australia

A single entity with responsibilities in both the development and financing of local infrastructure projects provides significant advantages.

RAI research suggests that the greatest benefits from establishing a new entity will flow if it is given three integrated functions – finance, advice and information. This approach is superior because it responds more fully to the key policy challenges associated with the deficit than can be achieved by an organisation devoted exclusively to one or two of these roles.

Financing Functions

Capital expenditure of the type required for local infrastructure is typically lumpy and varies greatly between different local councils, with few consistent trends.

In contrast, local government revenue streams are relatively stable over time and the social and economic benefits of infrastructure also accrue over relatively long periods. This makes borrowing the

most rational approach to financing infrastructure investments.

A dedicated national organisation with financing capabilities for local government has the potential to deliver lowest cost private sector financing to local government. This can be achieved through a financing function that supports:

- the pooling of similar local infrastructure projects into investments of a scale which makes them attractive to large private investors such as superannuation funds
- access for local government to long term finance at the lowest possible interest rates, and
- reduced transaction costs for financing activities.

All local governments will benefit from this arrangement. For the majority of local governments which are small, regional councils with limited internal capacity, this will be a significant opportunity to advance their infrastructure agenda.

Advisory Functions

A dedicated advisory capability is essential to leveraging the full benefits of a new organisation and complements the financing function.

Reducing the infrastructure deficit requires local governments to have a robust infrastructure strategy in place. This includes making the best use of available revenue streams and ensuring that cost effective management structures are used for different types of infrastructure.

By establishing an advisory function to local governments, *Local Infrastructure Australia* can provide access to high quality, low cost expert advice on a range of issues which may not otherwise be available to many local governments.

Better Information

Through its advisory and financing activities, *Local Infrastructure Australia* will obtain a level of knowledge about local infrastructure that is not currently available.

It is currently difficult for governments to assess the relative benefits of further investment in local infrastructure compared to other demands on national and state budgets. This lack of information can also constrain private sector confidence and investment interest.

Local Infrastructure Australia should be tasked with providing regular public reports on the nature of the deficit and the costs and benefits of reducing the shortfall.

Local and International Experience

The feasibility and desirability of this reform is supported by both local and international experience.

Institutions with similar roles already operate successfully in Australia and internationally. They have long history of success and have finely tuned methods for delivery of the services proposed for the Authority.

Proposed Model Local Infrastructure Australia

Establishment of *Local Infrastructure Australia* to support local infrastructure investment can build on the precedents set by local and international experience.

Projects financed via *Local Infrastructure Australia* should rely entirely on existing state regulations regarding both council creditworthiness and the validity of the proposed project.

This approach maintains the level of assurance about the quality of investment in each state and minimises barriers to implementation that may emerge during the intergovernmental process.

A dedicated secretariat possessing specialist financial skills as well as employing infrastructure finance experts will be required to run *Local Infrastructure Australia*. Operations should be overseen by a Board of Directors consisting of a majority of independent directors with appropriate expertise.

No requirement for local governments to use *Local Infrastructure Australia* as a facilitator of financing should be created. Rather, *Local Infrastructure Australia* should compete for advisory and finance services on the basis of the quality of its services.

To ensure benefits can be accessed by all local governments, the establishment process should include a requirement for fees for services to be set to reflect both the scope and complexity of advice required and the relative ability for Councils to pay for services.

Establishing Local Infrastructure Australia

RAI research recommends that *Local Infrastructure Australia* should be established as a statutory authority structure under Australian Government legislation.

The objects of *Local Infrastructure Australia* should capture its three roles in finance, advisory and information services for local infrastructure.

Establishment costs will be relatively modest and could be drawn from existing funding allocations related to regional or infrastructure issues. Following establishment, *Local Infrastructure Australia* will be able to fund its activities via revenues derived from its financing activities.

The Australian Government should provide a guarantee to *Local Infrastructure Australia's* pooled borrowings to ensure access to the lowest possible cost finance for councils. Given existing state guarantees and history of no default this can be achieved with no or negligible risk to Commonwealth finances.

As a result, establishment of *Local Infrastructure Australia* and the on-going benefits for local infrastructure can be achieved with a small upfront cost and negligible long-term financial risk.

Alternative structures

A statutory authority is the recommended approach based on RAI's research. This would provide for on-going focus, a balance of independence while maintaining close links to government policy and financial structures.

However establishment of dedicated and on-going resources to meet these needs could also occur within an existing government entity or as an independent entity if deemed appropriate by governments.

Research Approach

The Regional Australia Institute conducted independent research to complement the work and recommendations already available that demonstrate the support from local governments.

The research reviewed the recommendation for new advisory and financing bodies and more clearly defined the model that could be used to put these recommendations into action.

Contacts and Further Information

To discuss the policy briefing please contact the Regional Australia Institute via info@regionalaustralia.org.au.

A copy of the RAI research report *Renewal of Local Infrastructure* is available at the RAI website - www.regionalaustralia.org.au.

The *Strong Foundation for Sustainable Local Infrastructure* report developed by Ernst and Young can be accessed at: www.regional.gov.au/local/lqifr/files/20120622-strong-foundations.pdf

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Disclaimer

This briefing translates and analyses findings of research to enable an informed public discussion of regional issues in Australia.

It is intended to assist people to think about their perspectives, assumptions and understanding of regional issues.

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References

- ⁱ PricewaterhouseCoopers (2006), *National Financial Sustainability Study of Local Government*, PricewaterhouseCoopers, Sydney.
- ⁱⁱ *ibid*
- ⁱⁱⁱ Ernst and Young (2012), *Strong Foundations for Sustainable Local Infrastructure: Connecting Communities, Projects, Finance and Funds*, Commonwealth Department of Regional Australia, Local Government, Arts and Sport, Canberra.