MAJOR PROJECTS GUIDANCE
FOR LOCAL GOVERNMENT

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1. Introduction

1.1 Funding

In developing the business case, the project team will present a case for investment in the project and a recommended funding strategy. Part B3 outlines some of the key funding options available for local government when undertaking major infrastructure projects. These include:

- funding from general operations/general revenue
- funding through special schemes or arrangements (such as special rates and charges schemes, developer contributions, sale of assets, transfer of land and land exchange)
- Federal and State Government grants.

For some projects, the recommended funding strategy may include a combination of two or more of these funding options. These options are outlined below including a brief description of the option and references to the key relevant legislative provisions.[1] A discussion of the benefits and disadvantages of the option is also featured, including policy considerations arising from the Council using the particular method of funding for a project. In addition, examples of suitable projects are provided for each option.

1.2 Financing

It is important to understand the distinction between funding and financing in this context:

> *Funding is how the infrastructure is paid for. Finance describes the money that has to be raised upfront to deliver the infrastructure, and it needs to be repaid.*
>
> *… While financing can support funding, it is ultimately a secondary consideration. Local infrastructure is (and will remain) funded by the community through taxation and user charges, and meeting the infrastructure task will always be dependent upon the quantum of this funding … But while financing will always be dependent upon funding, it can be crucial to the timely delivery of key community infrastructure projects. Debt finance enable councils to deliver infrastructure earlier than they otherwise would have been able and to spread the costs amongst future generations who will enjoy the benefit of the investments.*[2]

The funding strategy developed by the project team should include details of any recommended financing options. This will have an impact on the payment profile for the project, that is, when the infrastructure funding must be provided by the Council over the life of the project. This in turn will affect the overall assessment of affordability. Therefore, this Part B3 also sets out some of the key financing options for local government infrastructure projects. These involve the following:

- borrowings (debt financing) sourced through State Government treasuries (where available)
- borrowings (debt financing) from private banking institutions
- public private partnership arrangements – long term private sector debt financing.

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[1] The authors have endeavoured to ensure that the references to legislation are correct at the time of writing. However, legislation is subject to change and should be checked by the Council where relevant.
[2] *Strong Foundations for sustainable local infrastructure, connecting communities, projects, financing and funds,* Ernst & Young (2012) p1 and 27. A report commissioned by the Federal Department of Regional Australia, Local Government, Arts and Sport.

A brief description of each of these options, the benefits and disadvantages, and examples of suitable projects are discussed in the following sections.

2. Funding from operations

Local governments' general revenue is derived primarily from the following sources:

- general property rates
- sale of goods and services (including user fees and charges)
- interest and dividend income
- fines and penalties.

The bulk of this revenue is derived from property rates and the sale of goods and services. These are discussed in turn below.

2.1 General property rates

Property rates are the only tax levied by local government. Rates can be levied as general or ordinary rates, separate rates or special rates. Legislation limits the capacity of a Council to raise revenue through rates by stipulating the structure of rates that can be levied, the property valuation method that can be applied and the application of differential rates to different types of property (for example residential or commercial).

Relevant legislative provisions

Table 1 summarises the key legislative provisions relating to rate revenue.

Table 1: Legislative provisions regarding local government rates

State	Legislation	Rate type	Land valuation method
Victoria	*Local Government Act* 1989 (Vic)	general rates (s 158) uniform rates (s 160) differential rates where Capital Improved Value (CIV) is used (s 161), or limited differential rates where CIV is not used (s 161A)	site value, net annual value or CIV (s 157) *Valuation of Land Act* 1960 (Vic) (s 13DC)
New South Wales	*Local Government Act* 1993 (NSW)	ordinary rates (s 492) or special rates (s 493) wholly *ad valorem* or base amount plus *ad valorem* (ss 497- 499) categories of rateable land include farmland (s 515), residential (s 516), mining (s 517) or business (s 518)	land value (s 498(2)) *Valuation of Land Act* 1916 (NSW) (s 6A)

Table 1: Legislative provisions regarding local government rates			
State	**Legislation**	**Rate type**	**Land valuation method**
Queensland	*Local Government Act* 2009 (Qld)	general, separate or special rates (s 94) Council may decide by resolution the categories of land for the purpose of levying differential general rates (s 93)	site value (non–rural land) and unimproved value (rural land) *Land Valuation Act* 2010 (Qld) (s 7)
South Australia	*Local Government Act* 1999 (SA)	general rates (s 152), separate rates (s 154), service rates or charges (s 155) all land within council area, subject to exemptions, is rateable (s 147) or land against which rates may be assessed (s 148)	*Valuation of Land Act* 1971 (SA) (s 11)
Western Australia	*Local Government Act* 1995 (WA)	differential general rates (s 6.33), 'minimum payments' (s 6.35), specified area rates (s 6.37) or service charges (s 6.38) rateable land (s 6.26)	either unimproved value (rural use), or gross rental value (non-rural) (s 6.28(2)) *Valuation of Land Act* 1978 (WA) Part 3 Div 1
Tasmania	*Local Government Act* 1993 (Tas)	general rates (s 90), service rates (s 93) or service charges (s 94) Council may, by absolute majority, make a separate rate or charge in respect of land or a class thereof in its municipal area (s 100) rateable land and exemptions (s 87)	values used under the *Valuation of Land Act* 2001 (Tas) to be used as basis of rates (s 89A) *Valuation of Land Act* 2001 (Tas) (s 45) – land value, capital value, or assessed annual value
Northern Territory	*Local Government Act* 2008 (NT)	fixed charge, valuation-based charge (s 148), general rates (s 155) or special rates (s 156) rateable land (s 141), conditionally rateable land (s 142) or exempt land (s 144)	unimproved capital value, improved capital value or annual value (s 149) *Valuation of Land Act* 1963 (NT) Part 4

2.2 Sale of goods and services

The sale of goods and services includes revenue derived from user fees and charges, service and utility charges and separate rates. Typical user fees and charges include fees for parking and for the use of sporting and recreational facilities. Service and utility charges are used to provide water, sewerage and waste management. (Developer charges are another form of user fees and charges. This is discussed separately in section 3.2, *Developer contributions*).

Separate rates and charges are levied equally on all rateable land to fund services and facilities that benefit the whole community. The Council is afforded considerable discretion in its ability to impose fees and charges and, within statutory limits, may increase revenue generated from user charges.

Relevant legislation

The primary legislation governing the sale of goods and services is:

- **Victoria**: *Local Government Act* 1989 (Vic) – fees and charges for goods and services (s 113(2)), charges for administrative costs (s 159(1)), service charges (s 162) and special charges (s 163)
- **New South Wales**: *Local Government Act* 1993 (NSW) – annual charges for domestic waste management, other annual charges (s 496), charges for water, sewerage, drainage, waste management and other prescribed services (s 501) and approved fees (s 608)
- **Queensland**: *Local Government Act* 2009 (Qld) – separate charges, special charges and utility charges (s 94) and fees (Chapter 4, Part 2)
- **South Australia**: *Local Government Act* 1999 (SA) – fees and charges (s 188), power to source funds (s 133) and service rates and service charges (s 155)
- **Western Australia**: *Local Government Act* 1995 (WA) – revenue and income (s 6.15) and imposition of fees or charges for goods and services subject to absolute majority (s 6.16)
- **Tasmania**: *Local Government Act* 1993 (Tas) – service rates and service charges in relation to nightsoil removal, waste management, stormwater removal, fire protection (s 93), construction rates and charges (s 97) and separate rates or charges (s 100)
- **Northern Territory**: *Local Government Act* 2008 (NT) – imposition of charges in relation to works carried out or services provided (s 157).

Suitable projects

While some smaller infrastructure projects and maintenance services may be funded from general revenue, in many instances it will not be sufficient or appropriate for large, high cost infrastructure projects. Raising rates to fund a major infrastructure project presents a number of difficulties. In New South Wales, legislation restricts the percentage at which rates can be increased (referred to as 'rate pegging'). However, in all States and the Northern Territory, other informal constraints exist including the capacity of rate payers to bear rate increases. There is also the possibility of higher ratepayer default levels or rates being in arrears due to the increased financial pressure caused by rate increases.

In the context of a high cost infrastructure project, existing operating cash flow and cash surplus may be better utilised to facilitate another funding option. For example, funds could be used to provide the Council's equity contribution or to make repayments on debt financing for the project.

Benefits and disadvantages

The key benefits and disadvantages of funding large projects from operations are summarised in Table 2.

Table 2: Funding from operations – benefits and disadvantages	
Benefits	**Disadvantages**
Flexibility and control: The Council has ownership of the asset and is likely to be able to maintain a high degree of flexibility and control over both the development of the project and the completed asset and associated services. **Equity:** This form of funding may be appropriate to provide partial funding for a project, especially where State or Federal Government funding is dependent upon the allocation of a certain level of Council equity, or debt financing arrangements require a capital contribution from the Council. **Tax/accounting:** There are unlikely to be major tax/accounting implications as a result of this form of funding.	**Adequacy:** Existing cash flows or cash surpluses may not be sufficient to fund the full cost of a major project. **Service delay:** A funding strategy, which involves building adequate cash reserves to fund a project, will likely delay the provision of the services in connection with that asset. **Cost increases:** A funding strategy which involves building adequate cash reserves to fund a project, will likely result in increased cost due to price increases over time. **Rating stress:** Increases in rate revenue may be eroded by a rise in ratepayer default and rates in arrears. **Capacity:** The rating capacity of Councils varies dramatically; some Councils do not have a substantial capacity to levy rates and some do not have the capacity to substantially increase rates.

3. Special schemes and arrangements

3.1 Special rates and charges schemes

If an infrastructure project involves the provision of assets that will benefit land holders in a specific area, the Council may be able to levy special charges on rate payers in that area to assist in recovering the costs of the project. This is also known as a 'benefited area arrangement'.

The Council is limited to levying special rates and charges in proportion to the benefit the relevant assets provide to rate payers in the specified area. For instance, when calculating a special charge for a road construction project, consideration must be given to the benefits of the road to the adjoining properties proportionate to the benefits enjoyed by other road users.[3]

Before finalising a special rate or charge, the Council must give public notice of the proposal and provide affected rate payers with relevant information about the proposed scheme. Members of the public are then entitled to make written submissions, and in some jurisdictions, request to appear in person to present their views to the Council. The Council must consider such submissions before finalising the special rate or charge. State Governments may also be required to consider the submissions before special rates and charges may be levied.[4] In each jurisdiction there are avenues for rate payers to appeal a special rate or charge.

[3] In New South Wales the Council may waive a special rate or charge for the period or entirely if the ratepayer instead enters into a written agreement to make a capital contribution to the cost of works or services for which the special rate or charge was made.

[4] In Victoria, where objections are received by rate payers from a majority of rateable properties required to pay a special rate or charge, the Council may not levy the special rate or charge.

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Relevant legislation

The special rates and charges provisions are:

- **Victoria**: *Local Government Act* 1989 (Vic) ss 163, 163A and 163B
- **New South Wales**: *Local Government Act* 1993 (NSW) ss 492, 495, 565 and 574
- **Queensland**: *Local Government Act* 2009 (Qld) s 94 (special rates and charges)
- **South Australia**: *Local Government Act* 1999 (SA) s 154 (separate rates), s 170 (notice of rates) and s 157 (notice of differentiating factors)
- **Western Australia**: *Local Government Act* 1995 (WA) s 6.37 (specified area rates)
- **Tasmania**: *Local Government Act* 1993 (Tas) ss 100 and 101 (separate rates or charges)
- **Northern Territory**: *Local Government Act* 2008 *(NT)* ss 156 and 158.

Suitable projects

Special rates and charges are a suitable means of raising revenue for the provision of some types of assets. Common examples include the construction of footpaths, roads, kerbs and drainage. Special charges may also be imposed for the provision of services such as promotion, marketing or economic development for local businesses. However, this form of funding has limited application as a means of funding major infrastructure projects on the basis that:

- it only applies to infrastructure which provides a benefit to rate payers within a specific area
- the Council is limited to levying special rates and charges in proportion to the benefit the asset provides to the people in the specified area, and therefore may not cover the entire cost of the asset to the Council
- there is a limit on what rate payers can bear by way of special rates and charges. This may affect the scale of infrastructure which can be funded in this way.

These limitations need to be factored into the funding strategy decision. For some types of projects, such as a project primarily involving drainage upgrades, this type of funding may be capable of meeting a significant proportion of the costs to the Council. However, for most major projects, a special rates and charges scheme may enable the Council to recover a portion of the costs but not fund the entire project.

Benefits and disadvantages

The key benefits and disadvantages of using special rates and charges schemes as a means of funding major projects are summarised in Table 3.

Table 3: Special rates and charges – benefits and disadvantages

Benefits	Disadvantages
Flexibility and control: The Council has ownership of the asset and is likely to be able to maintain a high degree of flexibility and control over the project and the asset.	**Adequacy:** Charges must be in proportion to the benefit provided to the rate payers in that area, and the revenue raised may not be sufficient to fund the full cost of the project.
Bring forward service/asset provision: For appropriate projects, this form of funding may enable the Council to upgrade or provide assets or services, which would not otherwise be possible if funded from general revenue. **Allocative efficiency:** Those who benefit from the asset pay for or contribute to its cost.	**Application:** Only relates to assets or services which benefit rate payers in a particular area of the municipality. **Rating stress:** Increases in rate revenue may be eroded by a rise in rate payer default and rates in arrears.
Equity: This form of funding may be appropriate to provide partial funding for a project, especially where State or Federal Government funding is dependent upon the allocation of a certain level of Council equity, or debt financing arrangements that require a capital contribution from the Council. **Tax/accounting:** There are unlikely to be major tax/accounting implications as a result of this form of funding.	**Capacity:** The rating capacity of Councils varies dramatically; some Councils have a limited capacity to levy special rates and charges schemes.
Financing costs: No direct financing costs.	

3.2 Developer contributions

Planning schemes and planning legislation make provision for developer contributions towards public infrastructure. This is an important source of funding for local government. Developer contributions may take a number of forms including:

- **work-in-kind:** a developer constructs an asset at its cost and, once completed, transfers the asset to the Council
- **transfer of land**: the developer transfers or 'gifts' land to the Council for the construction of infrastructure (discussed further in section 3.4, *Land exchange and transfer of land*)
- **monetary charges:** a developer makes a payment towards the cost of providing new infrastructure or for the cost of acquiring land.

The imposition of developer charges generally involves calculating the full costs of infrastructure provision, identifying the benefit area of infrastructure over which costs are to be allocated and, finally, allocating total costs across the benefit area. Developer charges ideally involve full net cost recovery, but nothing more.

The contributions are required to meet standards of reasonableness and accountability. There must be a link between the development and the need for the new infrastructure or facilities for which the contribution is required. Further, the share of infrastructure costs should be proportionate to the share of the total benefit that is received by the development, and all users to benefit from the infrastructure within a particular area should make a contribution to its cost.

The scope of contributions varies widely across each State and Territory. One of the key distinctions is the degree to which contributions are prescribed or open to negotiation. The model in each State and Territory is discussed below.

Victoria

In Victoria, local government can collect development contributions in one of four ways:

Development Contribution Plan (DCP): The *Planning and Environment Act* 1987 (Vic) (P&E Act) provides for DCPs to be incorporated in planning schemes for the purpose of levying contributions to provide works, services and facilities. A DCP may impose a development infrastructure levy, a community infrastructure levy (capped at $900 per dwelling) or both in relation to the area to which the DCP applies. Items of infrastructure that may be funded this way are limited by a Ministerial Direction issued in accordance with the P&E Act.

Planning permit condition: The Council can prescribe that certain works, services or facilities are provided by a developer as a condition of the planning permit. This may be paid for in its entirety by the developer or provided/paid for partly by the developer where the remaining cost is met by another authority.

Voluntary agreements: Voluntary agreements may be entered into between the Council and a developer to provide for development contributions (either work-in-kind or monetary charges). Such agreements may be initiated when the responsible authority is considering a planning scheme amendment request or a planning permit application.

Growth Areas Infrastructure Contribution (GAIC): The P&E Act also provides for the GAIC, which came into force on 1 July 2010. The GAIC applies to land brought into the Urban Growth Boundary that is zoned for urban development (after specified dates). It is intended to provide a means of funding State infrastructure, as opposed to local infrastructure funded by development contributions.

New South Wales

Division 6 of Part 4 of the *Environmental Planning and Assessment Act* 1979 (EP&A Act) provides a range of ways in which local government can levy development contributions for the provision of public amenities and services (broadly defined). It also allows for the preparation of a contributions plan, which guides the imposition of development contributions through the various available mechanisms. The relevant mechanisms are:

Contributions plan: Section 94 conditions require local infrastructure contributions in the form of monetary charges and/or transfer of land in accordance with a contributions plan. Such contributions can be collected prospectively or retrospectively in certain circumstances. Section 94A contributions are monetary contributions calculated as a fixed percentage of the cost of the development authorised under a contributions plan. Certain restrictions apply to the imposition of a section 94A levy in growth areas.

Voluntary planning agreement: Developers can enter into voluntary planning agreements with one or more public authority for the provision of land or payment of development contributions under section 93F. These contributions are limited to 'key community infrastructure', including local roads, bus facilities, parks, sporting, recreational, cultural, local and social facilities, car parking, as well as drainage and water management works.

Affordable housing contributions: These contributions can be levied under section 94F where there is a policy identifying the need for such contributions.

Queensland

The *Sustainable Planning Act* 2009 (Qld) (SP Act) establishes an infrastructure funding framework. It incorporates two categories of infrastructure:

Trunk infrastructure: provides distribution and collection services for a catchment area larger than the development, such as water, sewerage, road upgrades and regional open spaces.

Non-trunk infrastructure: connects a building to the external trunk infrastructure (that is, works internal to the development).

Under this framework, the Council plans for the supply of trunk infrastructure through the preparation of a Priority Infrastructure Plan (PIP), which must be included in planning schemes. The Council levies charges for trunk infrastructure by giving notice under an infrastructure charges schedule (prepared in accordance with Ministerial Guidelines, approved by the Minister and adopted by the Council), or a regulated infrastructure charges schedule (contained in a regulation or State planning regulatory provision which can be adopted by the Council).

The Council may impose conditions for necessary trunk infrastructure and additional trunk infrastructure costs. The parties can enter into an agreement about the infrastructure to be provided or paid for. Such an agreement may specify the timing of payment and whether works-in-kind may be provided rather than a monetary contribution. The amount of the charge imposed by the Council in a notice may be appealed.

South Australia

In South Australia, existing legislation does not contain powers allowing for developer contributions. *The Development Act* 1993 (SA) does, however, provide for:

Open space contribution scheme: empowers the Council in whose area land is situated to have vested in itself a portion of land to be held as open space.

Car parking fund: where the relevant authority deems that a development plan does not provide for sufficient parking spaces, the applicant must make a contribution to the car parking fund of an amount in accordance with a determination of the Council.

Western Australia

In Western Australia, the *Planning and Development Act* 2005 (WA) (P&D Act) empowers the Western Australian Planning Commission (Commission) to set conditions and make demands in relation to developments and plans of subdivisions. The P&D Act is not overly prescriptive as to the nature of developer contributions. However, any determinations made by the Commission will be subject to its policies, including the *State Planning Policy 3.6 – Development Contributions for Infrastructure*. Broadly speaking, developer contributions will fall into three categories:

- land contributions – for example, public open space, foreshore reserves, primary schools and roads
- infrastructure works – for example, public utilities and roads
- monetary contributions.

The Council may seek further developer contributions beyond the standard contributions outlined above. However, it will first be required to submit a 'development contribution plan' to the Commission identifying the need for the infrastructure in question.

The P&D Act also provides for the collection of funds to be placed in the 'Metropolitan Region Improvement Account'. Owners of land in the metropolitan area are obliged to pay a tax at a rate set

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pursuant to the *Metropolitan Region Improvement Tax Act* 1959 (WA). There is further scope for developer contribution where it is expressly provided for in the relevant town planning schemes recommended by the Planning Commission. The P&D Act also provides for:

Financial contribution in lieu of open space: This is applicable in circumstances where the Planning Commission has approved a plan of subdivision subject to the condition that a portion is set aside by the owner/developer as open space, and only applies to land of greater than three lots

Expenses of construction: Developers must either fund themselves, or pay a 'reasonable amount' to the relevant local government for supervision of construction of road drainage.

Tasmania

Pursuant to the *Land Use Planning and Approvals Act* 1993 (Tas), the relevant local planning authority may enter into agreements with developers to obtain payment for infrastructure contributions, which may be made in stages. As an alternative to making a financial contribution, owners of land may undertake the infrastructure development on behalf of the planning authority. Such an agreement must be in accordance with the relevant planning scheme. The nature of such contributions is not defined. Furthermore, the *Local Government (Building and Miscellaneous Provisions) Act* 1993 (Tas) empowers the Council to impose various conditions precedent to the approval of plans for subdivisions, for example, in the instance that:

- a developer is required to sell a portion of the land to the Council at a nominal rate for open space or drainage purposes
- drainage is provided, or a designated area for river frontage is allocated.

Northern Territory

Developer contributions for infrastructure are dealt with under the *Planning Act* 2009 (NT). Pursuant to the Planning Act, a 'service authority' is empowered to compose a 'contribution plan' in relation to a 'policy area', that being a discrete area for the provision of infrastructure or car parking. A contribution plan will include the following information:

- a description of the types of infrastructure works required in the policy area
- a statement of the order of infrastructure works to take place
- an estimate of costs and method for calculating the costs of capital work
- a method for calculating the contribution.

A contribution payable is taken to be a condition of the development permit granted to the developer.

Relevant legislation

The relevant legislative frameworks are set out in the following Acts:

- **Victoria:** *Planning and Environment Act* 1987 (Vic)
- **New South Wales:** *Environmental Planning and Assessment Act* 1979 (NSW) Division 6 of Part 4
- **Queensland:** *Sustainable Planning Act* 2009 (Qld) ss 627- 652
- **South Australia:** *Development Act* 1993 (SA) ss 50, 50A
- **Western Australia:** *Planning and Development Act* 2005 (WA) Part 10

- **Tasmania:** *Land Use Planning and Approvals Act* 1993 (Tas) s 73A; *Local Government (Building and Miscellaneous Provisions) Act* 1993 (Tas)
- **Northern Territory:** *Planning Act* 2009 (NT) Part 6.

Suitable projects

Developer contributions are appropriate for funding infrastructure in growth or urban redevelopment areas. At a minimum, developers are required to contribute to basic infrastructure associated with the development of land such as roads, water, sewerage, communication, gas and electricity connections, as well as other services within the development that will ultimately be used by owners/occupiers of the development.

Developer charges are increasingly being used to fund social infrastructure such as parks, libraries and affordable housing. In addition, developers are required to contribute towards infrastructure that will be used by a broader local or regional area. This may include infrastructure such as major roads, drainage works, community and recreation centres, sporting facilities and libraries. The range of capital works for which contributions may be levied varies between the States. A brief overview is provided in Table 4.

Table 4: Public infrastructure eligible for mandatory contributions (excluding basic infrastructure):[5]

Type of infrastructure	NSW(a)	Vic	Qld
Parks	✓(1)	✓	✓(1)
Education	✓	×	×
Trunk roads	✓(2)	✓(2)	✓(2)
Public transport	✓(1)	✓	×
Childcare centres	✓(3)	✓(4)	×
Libraries	✓(3)	✓(4)	×
Community centres	✓(3)	✓(4)	×
Recreation facilities	✓(3)	✓(4)	×
Sports grounds	✓(3)	✓(4)	×
Protection	×	×	×
Housing	✓	×	×

(a) Mandatory contributions are limited to the infrastructure and land directly required to support land developments
(1) Dedication of land only
(2) Within the sub-division
(3) Restricted to infrastructure that services the development site or precinct
(4) In Victoria, contributions for community infrastructure are capped at $900.

[5] *Assessing Local Government Revenue Raising Capacity,* Productivity Commission Research Report, (April 2008).

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Benefits and disadvantages

The key benefits and disadvantages of using developer contributions as a means of funding a major project are summarised in Table 5.

Table 5: Developer contributions – benefits and disadvantages

Benefits	Disadvantages
Developing areas: Developer contributions can assist growing areas to secure adequate infrastructure funding.	**Limited risk management:** There is limited scope for using developer contributions to improve the management of project risks.
Risk transfer: Where work-in-kind contributions are made, the developer bears substantial design and construction risk in respect of those works. **Equity:** Monetary contributions provide a source of equity for the Council. **Efficiency:** Up-front developer contributions allow infrastructure costs to be included in development decision making, leading to more economically efficient decisions. Additionally, the provision of work-in-kind contributions often allow infrastructure to be delivered by developers as part of the development, which may be more cost efficient than the Council providing such infrastructure. **Allocative efficiency:** Developer charges shift the costs of providing new infrastructure onto the users who will benefit directly from that infrastructure (the costs being passed on by the developers). Developer contributions are included in the price of the land, either passed back to the seller or forwarded to the buyer. **Financing costs:** No direct financing costs.	**Transaction costs:** Contribution schemes are characteristically complex, and require extensive negotiations between the developer and the Council. This can be a costly exercise, particularly where disputes arise. Once agreed, development contribution schemes also impose administrative costs on the Council, which are required to ensure that funds are administered in a transparent and accountable manner. **Gaps in funding:** Where contributions do not cover the full or real cost of the infrastructure, the Council must source additional funding. **Implementation:** Implementation of development contribution schemes raises a number of policy concerns in relation to the quality of infrastructure, lack of transparency and overcharging.

3.3 Asset sale

A Council may sell assets, including land, to raise revenue to fund an infrastructure project. This is subject to legislative limitations. For example, in New South Wales a Council cannot sell 'community land' (*Local Government Act* 1993 (NSW) s 45).

For many Councils, land holdings in particular constitute the most valuable assets on the municipal balance sheet. In urban areas, land values are created partly by public investment in roads, water supply, parks and recreation facilities and other services. It may therefore make economic sense to strategically sell some land or sub-optimal assets to invest in public infrastructure, which may increase land values in the municipality.[6]

[6] George E Peterson, *Land Leasing and Land Sale as an Infrastructure-Financing Option*, World Bank Policy Research Working Paper 4043 (November 2006) p 2.

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Relevant legislation

The key legislative provisions relating to asset sales are:

- **Victoria:** *Local Government Act* 1989 (Vic) s 3F (general powers), s 5(2) (do all things a body corporate may do), s 189 (power to sell land) and s 186 (power to enter into contracts)
- **New South Wales:** *Local Government Act* 1993 (NSW) Chapter 6, Part 2 (dealings in public land), Chapter 9 (exercise the powers of a statutory corporation) and s 55 (enter into contracts)
- **Queensland:** *Local Government Act* 2009 (Qld) s 262(3)(a) (power to enter into contracts and to exercise the powers of an individual which includes entering into contracts and selling land)
- **South Australia:** *Local Government Act* 1999 (SA) s 37 (power to enter into contracts) and s 201 (power to sell or dispose of local government land)
- **Western Australia:** *Local Government Act* 1995 (WA) s 2.5 (legal capacity of individual) and s 3.58 (power to dispose of property)
- **Tasmania:** *Local Government Act* 1993 (Tas) s 20(5) (power to dispose of or otherwise deal with property) and s 177 (sale and disposal of land)
- **Northern Territory:** *Local Government Act* 2008 (NT) ss 25 and 26 (power to enter into contracts) and s 182 (power to deal with and dispose of property)

For further discussion on the power of local government to sell land (and the restrictions on that power) see Annexure 2, *Sources of power for local government*.

Suitable projects

It is obvious that the Council has a limited capacity to sell assets to fund infrastructure projects. Asset sales should be limited to non-core assets or surplus assets. This funding option is most appropriate where revenue generated from the sale of non-core or surplus assets is used to fund core infrastructure facilities or assets essential for the delivery of core services.[7]

Benefits and disadvantages

The key benefits and disadvantages of funding projects through asset sale are summarised in Table 6.

Table 6: Asset sales – benefits and disadvantages[8]

Benefits	Disadvantages
Flexibility: The Council may have more flexibility in managing its assets than by increasing rates/introducing additional rates (via special rates and charges schemes). **Improved rating:** The sale of non-core assets, particularly assets which are being used sub-optimally, may improve the credit rating/financial sustainability of the Council.	**Limited capacity:** The Council has limited assets, many of which are used to provide core services or which provide security for debt financing. Accordingly, there is limited potential to fund infrastructure by selling municipal assets. **Tax implications:** The sale of assets may result in a profit being recorded.

[7] *Land Leasing and Land Sale as an Infrastructure – Financing Option,* n6.
[8] Elements of this table are drawn from: *A Guide to Funding Options Available to Local Government*, Queensland Treasury, (April 2010), p 15.

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Table 6: Asset sales – benefits and disadvantages[8]	
No effect on operating revenue: The Council does not need to increase operating revenue (via rates and charges) to meet debt repayments or fund the project. **Accessible:** Has the potential to provide relatively quick access to funds if there is a willing a purchaser. **Financing costs:** No direct financing costs.	**Loss of assets:** May decrease the borrowing capacity of the Council for other projects. The assets may be needed in the future. **Delay:** It may take some time to find a purchaser willing to pay an appropriate price, potentially delaying the commencement of the project.

3.4 Land exchange and transfer of land

Instead of selling land or other assets, the Council may opt to enter into a land exchange or land transfer as a method of funding or partly funding a major infrastructure project.

Land exchange: A land exchange is where the Council 'gifts' a parcel of Council owned land to a developer, in exchange for a parcel of land owned by the developer and the construction of an asset by that developer for the Council.

Land transfer: A land transfer is where the Council 'gifts' a parcel of Council owned land to a developer in exchange for the construction of an asset, such as a recreation centre or municipal office, on another parcel of Council land. This is similar to selling a non-core asset to fund an infrastructure project, except that the land is transferred on completion of the construction of the new Council asset and accordingly the developer bears much of the construction risk.

Relevant legislation

The key legislative provisions relating to land exchanges and transfers of land are:

- **Victoria**: *Local Government Act* 1989 (Vic) s 3F (general powers), s 5(2) (do all things a body corporate may do), s 189 (power to sell land) and s 186 (power to enter into contracts)
- **New South Wales**: *Local Government Act* 1993 (NSW) Chapter 6, Part 2 (dealings in public land), Chapter 9 (exercise the powers of a statutory corporation) and s 55 (enter into contracts)
- **Queensland**: *Local Government Act* 2009 (Qld) s 262(3)(a) (power to exercise the powers of an individual which includes entering into contracts and selling land)
- **South Australia**: *Local Government Act* 1999 (SA) s 36(1) (power to enter into contracts) and s 201 (power to sell or dispose of local government land)
- **Western Australia**: *Local Government Act* 1995 (WA) s 2.5 (legal capacity of individual) and s 3.58 (power to dispose of property)
- **Tasmania**: *Local Government Act* 1993 (Tas) s 20(5) (power to dispose of or otherwise deal with property)
- **Northern Territory**: *Local Government Act* 2008 (NT) ss 25 and 26 (power to enter into contracts) as well as s 182 (power to deal with and dispose of property).

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Suitable projects

Land exchange and land transfer are opportunity driven funding options. The opportunity is created where the Council holds land that is not required to provide core community services, and that land is valuable to a developer because it enables a business opportunity to be exploited. In addition, the developer must be willing to self-fund the construction of a public asset in exchange for the Council's land.

The opportunity may arise where, for example, the Council owns land adjacent to a shopping centre and the owner of the shopping centre is seeking to expand onto the Council-owned land. In such circumstances, the shopping centre owner may be highly incentivised to take on the financing and construction risk of building an asset for the Council in exchange for the land required for expansion.

Benefits and disadvantages

The key benefits and disadvantages of using land exchange or land transfer to fund a major project are summarised in Table 7.

Table 7: Land exchange and land transfer[9] – benefits and disadvantages

Benefits	Disadvantages
Improved rating: The transfer of non-core assets to a developer, particularly assets that are being used sub-optimally, may improve the credit rating/financial sustainability of the Council. **No effect on operating revenue:** The Council does not need to increase operating revenue (via rates and charges) to meet debt repayments or fund the project. **Risk transfer:** If properly managed, the private sector bears much of the financing and construction risk in relation to the asset being provided by the developer to the Council. **Bring forward service/asset provision:** For appropriate projects, this form of funding may enable the Council to upgrade infrastructure or provide new assets (and associated services), which would not otherwise be possible if funded from general revenue. **Financing costs:** No direct financing costs.	**Complexity:** The arrangements may involve complex accounting treatment. **Limited capacity:** The Council has limited land assets, many of which are used to provide core services or security for debt financing. Accordingly, there is limited potential to fund infrastructure by transferring Council land. **Limited opportunity:** The circumstances in which a land exchange/transfer may be undertaken are limited to where a business opportunity exists for the private sector party. **Loss of assets:** May decrease the borrowing capacity of Council for other projects. The land may be needed in the future. **Delay:** Negotiation of terms can be lengthy and the Council's requirements for the asset to be constructed must be well developed prior to finalising contract documentation, or potential delays in the commencement of the project could occur.

[9] *A Guide to Funding Options Available to Local Government*, n8, p 15.

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4. Government grants

Obtaining a government grant to fund an infrastructure project and related services is a particularly attractive source of funding for local government.

4.1 Federal Government grants

Local government receives funding from the Federal Government through financial assistance grants and specific purpose payments. Government grants account for approximately 17 per cent of local government revenue, although for rural and remote Councils grants account for a higher percentage, as own-source revenue raising capacity is limited. Federal Government grants include:

- **Financial Assistance Grants (FAGs):** administered under the *Local Government (Financial Assistance) Act* 1995 (Cth) and distributed by the Local Government Grants Commission (LGGC) in each State. FAGs consist of two components:
  - general purpose grants, distributed between the States on the basis of population shares and within a State on the basis of general relative need
  - local road grants, distributed to local government within a State on the basis of relative road needs as determined in 1991.
- **Specific purpose payments (SPPs):** provided to local government for policy purposes relating to particular infrastructure or services administered by local government. Significant SPP policy areas include child care, care for the disabled and local roads. One of most successful SPPs is the ‘Roads to Recovery’ program, which provides grants directly to local government to fund local roads.

4.2 State and Territory Government grants

The Council may also be able to obtain grants from the relevant State/Territory Government.

These grants may be provided for recurrent services such as home care, child care or public libraries, or may be provided for local government projects. Project grants may be 'one off' grants or fixed term grants used to fund a range of specific projects (for example, new community facilities such as libraries, swimming pools or roads) or new programs, (for example water management, recycling and inspection).

State and Territory Government grants are usually provided under a funding agreement which impose specific conditions on the use of the funds. This may include a specified contribution of funds to the project by the Council and/or the community.

Benefits and disadvantages

The key benefits and disadvantages of grant funding for major infrastructure projects are summarised in Table 8.

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Table 8: Grant funding – benefits and disadvantages	
Benefits	**Disadvantages**
Budget impact: Grants remove the need for the Council to allocate part or all of the funding required for a project from its annual budget, or to impose higher rates or additional levies on rate payers. **Cost:** Grant funds cover part or all of a project, thereby significantly reducing the burden of the project on the Council and rate payers. **Bring forward service/asset provision:** For appropriate projects, this form of funding may enable the Council to upgrade or provide assets or services, which would not otherwise be possible if funded from general revenue. **Financing costs:** No direct financing costs. **Tax/accounting:** There are unlikely to be major tax/accounting implications as a result of this form of funding.	**Availability:** The Federal Government has indicated that the levels of grant funding to local government will not be increased (and may possibly be reduced) going forward. **Continuity:** There is some risk in the Council relying on government grants to fund ongoing projects or services as the continuity of grant funding is at the discretion of the relevant government and comes under regular budgetary review. **Equity:** Some State, Territory or Federal Government funding may be dependent upon the allocation of a certain level of Council equity, which will impact upon the Council's budget and operating revenue. **Reduced flexibility**: Grant funding is generally provided via a funding agreement, which may impose additional requirements or restrictions on the project. Changes to the project may require government approval, thereby limiting the Council's flexibility and potentially causing delays to the project. **Administrative complexity:** State, Territory or Federal Government involvement adds another level of administrative complexity (for example approvals, reports etc.).

5. Borrowing money

In developing the funding strategy for the project, the project team may wish to consider the financing options available to the Council for the project. As noted above, the project must be funded by the Council regardless of whether external financing is obtained. Any external financing obtained for the project will affect the affordability of the project as it will impact the payment profile for the Council, in particular when funding must be provided by the Council. Overall, financing delays the upfront capital expenditure component of the project for the Council and spreads it over a number of years post construction, although there are additional costs associated with doing so.

One of the primary financing options for the Council is borrowing. The reliable income stream generated by rates and fees, together with the low risk nature of many local government activities, makes local government an ideal borrower. Despite this, Australian local government has taken a particularly conservative approach to borrowing as a means of financing capital spending.

There are two main borrowing options for the Council – debt sourced from private banks and debt sourced through government treasuries (although this option is not available in all jurisdictions). These are examined in turn below. In this context, the position of local government in South Australia is unique and is separately discussed.

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5.1 Debt sourced from private banking institutions

This option involves the Council sourcing debt from a bank or other financial institution. Many Councils do not finance specific assets through debt, but will debt finance their balance sheet or a business unit such as water or sewerage. However, the Council can also use debt to finance a specific infrastructure project.[10]

Where financing is sought in relation to a specific project, different financing structures may be available. Interest on the loan amount will accrue during the construction period and the life of the loan, yet the Council will generally not be required to make periodic debt service payments until the asset has been constructed. The financier will usually want to review and approve the project documentation and may require that direct agreements be entered into by the financier and the contractor or other key parties involved in the project.

It should be noted that financiers typically offer infrastructure financing for a maximum of ten years (some for much shorter periods). Where the Council is seeking a loan period of more than 10 years, which is often the case, the Council bears the risk of refinancing after the initial loan period.

Legislative restrictions

The borrowing powers of local government are set out in the respective local government Acts. The Council may be required to seek Ministerial approval prior to entering into an agreement to borrow. State and Territory Governments often impose restrictions on the amount borrowed, the purpose for which it is used and the source of the borrowings, as outlined below.

Victoria – *Local Government Act* 1989 (Vic):

- requests for borrowing are assessed by the Victorian Government based on an analysis of financial ratios
- the Council is restricted from borrowing for ‘ordinary purposes’ or for the purposes of municipal enterprises unless proposed in a budget, except where the borrowings are used to refinance existing loans (s 146)
- the power to borrow is subject to the ‘principles of sound financial management’ (s 144 (1))
- section 193(5C) sets out the level of investment by the Council that requires approval by the Treasurer and the Minister for Local Government
- the State Government does not offer a State guarantee on borrowings by local government.

New South Wales – *Local Government Act* 1993 (NSW):

- the Council cannot borrow at a rate which exceeds the indicative rate determined by the New South Wales Treasury Corporation
- the Council is restricted to borrowing in Australia and in Australian currency according to the Revised Borrowing Order (13 May 2009), issued under section 624 of the *Local Government Act* 1993 (NSW)
- the Council cannot borrow for a period of less than 30 days or for a period that exceeds the estimated life of the asset financed by the borrowings
- the State Government does not offer a State guarantee over borrowings by local government

[10] *A Guide to Funding Options Available to Local Government*, n8, p 22.

- the Council may be able to access a 4 per cent subsidy towards interest payments on borrowings for infrastructure renewal projects via the Local Infrastructure Renewal Scheme (LIRS). Examples of local government projects that have benefited from LIRS to date include buildings and road renewals, bridge replacements, swimming pool rejuvenation, and airport reconstruction works.[11] The LIRS was introduced to:

  > *make it affordable to take out major bank loans to fund their [Council] projects. This investment in debt funding has been proven to be far less expensive than paying for the long-term recurring maintenance requirements of deteriorating assets*.[12]

Queensland – *Statutory Bodies Financial Arrangements Act* 1982 (Qld):

- the Council is a statutory body under Part 5 of the *Statutory Bodies Financial Arrangements Act* 1982 (Qld), which sets out borrowing powers. Under section 34, a statutory body may borrow with the Treasurer's approval if the borrowing is in Australian currency and undertaken with Australian security
- under section 8 of the *Local Government Finance Standard* 2005 (Qld), each Council must prepare a policy about borrowings which sets out any new borrowings planned for the next financial year and the next four financial years, the purpose of the borrowings, and the time over which it is planned to repay existing and proposed borrowings
- local government is restricted to borrowing from the Queensland Treasury Corporation (QTC); see section 5.2 *Debt from State and Territory treasury corporations*
- the State Government guarantees local government borrowings.

South Australia – *Local Government Act* 1999 (SA):

- the Council may borrow money and obtain other forms of financial accommodation, in any form considered appropriate. The Council may also give security
- the Council cannot enter into financial arrangements unless or until it has obtained independent advice about the proposed financial arrangements and risk-management policies, and has adopted risk-management policies, controls and systems by resolution passed by a majority of at least two-thirds of its members
- the State Government will not be liable for any debts or liabilities of the Council, or subsidiary of the Council, unless the liability is incurred via borrowing through the Local Government Finance Authority (LGFA), see section 5.2 *Debt from State and Territory treasury corporations*.

Western Australia – *Local Government Act* 1995 (WA):

- local government in Western Australia may borrow money or obtain credit to enable it to perform the functions and exercise the powers conferred to it under the *Local Government Act* 1995 (WA)
- where a Council proposes to borrow money, and this has not been accounted for in the budget for that financial year, the Council must first obtain an absolute majority in order to exercise the power to borrow, and then give one month's public notice of the proposal
- local government may only provide security in limited forms, as set out in s 6.21 of the *Local Government Act* 1995.

[11] www.dlg.nsw.gov.au/dlg/dlghome/dlg
[12] www.dlg.nsw.gov.au/dlg/dlghome/dlg

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Tasmania – *Local Government Act* 1993 (Tas):

- the Council must seek approval by the Treasurer in order to raise funds through borrowing. The Council may not raise a loan in any financial year exceeding any amount determined by the Treasurer for that year

- in seeking to obtain any form of financial accommodation, the Council must approve – by absolute majority – any proposal on the type of security it will provide. Where the Council seeks to issue debentures or inscribed stock for the purpose of raising money, it must adhere to the statutory requirements laid out in the *Local Government Act* 1993

- the Council may not borrow for any purpose where the total amount of borrowings will exceed 30 per cent of its revenue of the preceding financial year, except with the approval of the Minister. Grants for specific purposes are excluded from calculations of the Council's revenue.

Northern Territory – *Local Government Act* 2008 (NT):

- the Council may borrow money only with the Minister's approval, which can only be given after consultation with the Treasurer. Exceptions to this rule apply in the instance of:

    - an application made for an advance on the Council's overdraft, where the advance does not exceed 2 months, and the amount of the advance does not exceed 2 per cent of the Council's total revenue income for the preceding financial year, and

    - a 'minor transaction', as defined in the Ministerial Guidelines.

- the Council may give security for a borrowing in the form of a mortgage or charge over its property, only with the approval of the Minister. This is subject to certain restrictions as set out in the *Local Government Act* 2008.

Suitable projects

Borrowing from private banking institutions may be an appropriate source of financing, where:

- the loan is used to acquire new infrastructure assets or upgrade existing infrastructure assets

- the assets have a long life-span

- the Council has the capacity to fund the debt and interest repayments

- the assets have a high initial cost that cannot be funded through recurrent revenue or reserves.

Borrowing from private banking institutions is particularly attractive for projects involving assets that generate an income stream able to fully or substantially fund debt repayments. The 'golden rule' for borrowing is that it may be suitable for capital projects, but not for recurrent spending. It should not be used for routine maintenance or to upgrade infrastructure assets, which do not generate income, to pay fixed costs, wages or superannuation.

The Councils that are particularly reliant upon grants, rather than own-source revenue, are less suitable borrowers. This often translates to larger urban Councils, which have greater resources and revenue and are therefore able to take on a higher level of debt.

Where infrastructure benefits particular property owners, it is more equitable to recover the costs of providing such infrastructure through developer charges. If the beneficiaries of the infrastructure are few and dispersed, then user fees and charges are more equitable sources of funding.

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Benefits and disadvantages

The key benefits and disadvantages of local government using debt financing from financial institutions for major infrastructure projects are summarised in Table 9.

Table 9: Bank debt financing – benefits and disadvantages[13]

Benefits	Disadvantages
Flexibility and control: The Council has ownership of the asset and is likely to be able to maintain a relatively high degree of flexibility and control over the project and the completed asset. **Accelerated development:** Borrowing provides relatively fast financing for infrastructure that can be used to generate additional revenue and attract investments. It also avoids delays in the commencement of a project, which may lead to higher costs. **Bring forward service/asset provision:** For appropriate projects, this form of financing may enable the Council to upgrade or provide assets or services, which would not otherwise be possible if funded from general revenue. **Allocative efficiency:** Spreading the funding cost of debt repayments over the future generations who will benefit from the asset/project is an efficient allocation of resources. **Tax/accounting:** Although the debt is on the Council's balance sheet and interest is an expense, there are unlikely to be major tax/accounting implications as a result of this form of financing.	**Control:** Depending on the terms of the financing, the financier may take security over the project assets, thereby reducing the Council's level of control. **Funding costs:** Borrowing results in additional costs such as bank charges and interest. **Lead time:** Arranging and documenting financing schemes can be time consuming and complex. **Budget impact:** Debt service payments impact on the Council's budget for the duration of the loan. **Rating impact:** Debt levels may impact on the Council's rating if sufficiently high. **Financing risk:** The Council bears the financing and refinancing risks. **Risk:** Project risks are predominantly retained by the Council, subject to the procurement model used and specific contractual arrangements for the project. **Microeconomic danger:** Excessive indebtedness may lead to difficulty in repaying loans, which in turn could put the provision of public services at risk. **Macroeconomic danger:** Debt at the local government level contributes to the overall level of public debt, which may have an effect on the national economy and potentially lead to inflation. **Accounting:** Debt financing must be accounted for on the Council's balance sheet.

5.2 Debt from State and Territory treasury corporations

In Queensland, Western Australia, Tasmania and the Northern Territory, local government may borrow money through the State treasury corporations:

- Western Australian Treasury Corporation (WATC)
- Queensland Treasury Corporation (QTC)
- Tasmanian Public Finance Corporation (TasCorp)

[13] *A Guide to Funding Options Available to Local Government*, n8, p22 - 25.

- Northern Territory Treasury Corporation.

In each case, local government has the option to borrow from the State treasury corporation but is not obliged to do so, except in Queensland where local government can only borrow through QTC. As with bank debt financing, debt may be secured for general balance sheet funding or for specific projects. This funding option is widely used by local government in the jurisdictions where it is available, as it is one of the cheapest forms of debt financing available to local government.[14]

In most jurisdictions the Council can access a tool kit or guidelines developed by the relevant treasury corporation to assist with the process for applying for a loan.

Some treasury corporations also offer other services to local government, on a fee for service basis, to assist in the process of developing a project (for example, to assist with the development of a business case, financial risk modelling, cost of capital analysis etc.). Refer to the relevant treasury corporation website for details.

Relevant legislation

- **Queensland**: *Queensland Treasury Corporation Act* 1985 (Qld)
- **Western Australia**: *Western Australian Treasury Corporation Act* 1986 (WA)
- **Tasmania**: *Tasmanian Public Finance Corporation Act* 1985 (Tas)
- **Northern Territory**: *Northern Territory Treasury Corporation Act* 1994 (NT).

See also 'Legislative restrictions' in section 5.1, *Debt sourced from private banking institutions*.

Suitable projects

Debt funding through State treasury corporations is best suited to projects where:

- the capital investment is for social infrastructure where project risks are likely to be retained by the Council, or the investment is for economic infrastructure but the revenue stream is unreliable or difficult to determine, or is insufficient to service the debt repayments[15]
- the loan is used to acquire new infrastructure or upgrade existing infrastructure assets
- the assets have a long life span
- the Council has the capacity to repay the debt and interest
- the assets have a high initial cost, which cannot be funded through recurrent revenues or reserves.

Benefits and disadvantages

The key benefits and disadvantages of arranging debt financing from State or Territory Government treasury corporations are summarised in Table 10.

[14] Local government in Victorian does not have the option of borrowing through the State treasury, and TCorp does not lend to local government in New South Wales. South Australia is covered separately below, see section 5.3 *Debt from the centralised financing authority (South Australia).*

[15] For a discussion of what constitutes social and economic infrastructure see section 6, *Public Private Partnerships – private sector project financing.*

Table 10: Treasury debt financing[16] – benefits and disadvantages	
Benefits	**Disadvantages**
Flexibility and control: The Council has ownership of the asset and is likely to be able to maintain a high degree of flexibility and control over the project and the completed asset. **Accelerated development:** Borrowing provides relatively fast financing for infrastructure that can be used to generate additional revenue and attract investments. Avoiding delays in the commencement of a project may lead to lower costs. **Allocative efficiency:** Spreading the funding cost of debt repayments over the future generations that will benefit from the asset/project is an efficient allocation of resources. **Accessibility:** More accessible than many other forms of external financing given the inter-governmental relationship. Once departmental approvals have been given, access to funds may be quicker than for bank debt. **Term of loan/refinancing risk:** Treasury can often offer longer loan terms than private sector banks, thereby reducing the Council's refinancing risk. **Costs:** Interest rates are lower than bank rates. **State guarantee:** The debt product is backed by a State/Territory Government guarantee. **Tax/accounting:** Although the debt is on the Council's balance sheet and interest is an expense, there are unlikely to be other major tax/accounting implications as a result of this form of financing.	**Funding costs:** Borrowing results in additional costs such as financing charges and interest. **Lead time:** Arranging and documenting financing schemes can be time consuming and complex, although this is likely to be less so than for debt bank debt financing. **Administrative complexity:** State/Territory Government involvement adds another level of administrative complexity (approvals, reports etc.). **Budget impact:** Debt service payments impact on the Council's budget for the duration of the loan. **Rating impact:** Debt levels may impact on the Council's rating if sufficiently high. **Financing risk:** The Council bears the financing and refinancing risk, although this is a significantly lower risk than for bank debt financing. This is partly because longer debt tenure is usually available from treasury corporations than private banking institutions. **Risk:** Project risks are predominantly retained by the Council, subject to the procurement model used and the specific contractual arrangements for the project. **Microeconomic danger:** Excessive indebtedness may lead to difficulty in repaying loans, which in turn could put the provision of public services at risk. **Macroeconomic danger:** Debt at the local government level contributes to the overall level of public debt, which may have an effect on the national economy and potentially lead to inflation. **Accounting:** Debt financing must be accounted for on the Council's balance sheet.

[16] Elements of this table are drawn from *A Guide to Funding Options Available to Local Government* n8, p19.

5.3 Debt from a centralised financing authority (South Australia)

Local government in South Australian has a borrowing option that is unique in the Australian context. In this state, the Council may borrow from the Local Government Finance Authority (LGFA). The LGFA is an independent authority established under the *Local Government Finance Authority Act* 1983 (SA) (LGFA Act) to develop and implement borrowing and investment programs for the benefit of local governments. The LGFA may source funds through various avenues, including the South Australian Treasury. Liabilities incurred by the LGFA are guaranteed by the Treasurer.[17]

Local government has the power to borrow money from or lend to the LGFA, in addition to entering into such other financial arrangements with the LGFA with the approval of the Treasurer.

Relevant legislation

- **South Australia**: *Local Government Finance Authority Act* 1983 (SA).

Benefits and disadvantages

The key benefits and disadvantages of arranging debt financing from the LGFA are the same as for borrowing from State/Territory Government treasury corporations, as summarised in Table 10.

6. Public private partnerships – private sector project financing

6.1 Overview

Another strategy available to the Council is to deliver the project under a public private partnership arrangement (PPP). A typical PPP project involves a long term contract (concession agreement) between the Council and a private sector entity (commonly a special purpose vehicle referred to as the project company) to deliver infrastructure and services. The concession agreement may be for a period of 10 to 50 years (concession period).

The project company arranges finance for the up-front capital required to construct the project assets and is responsible for the design, construction, maintenance and/or operation of that asset in accordance with a performance based or 'output' specification. Accordingly, the project company bears much of the financing, construction and operation risks. Under this option the procurement model and the funding option are inextricably linked.[18]

The project company is usually established by a private sector consortium (the sponsors) and is funded through a combination of debt and equity. Equity is typically provided by the sponsors by way of a shareholding in the project company.

Debt typically constitutes a relatively high proportion of the finance for the project, and is obtained by the project company on the basis of private sector limited recourse or non-recourse project financing. This means that the financiers have only limited recourse to the sponsors if the debt is not repaid as required (generally up to the limit of their shareholding in the project company). The financiers take security over the project assets. Accordingly, the credit assessment by the financiers is focused on the

[17] LGFA Act s24(1).

[18] This approach would typically involve project delivery models such as design, build, finance, maintain/operate (DBFM/DBFO), build, operate and transfer (BOT), build, own, operate, transfer (BOOT) or build, own, operate (BOO). See Part B2, *Procurement options.*

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project company and the project assets, as well as the project agreements, rather than on the sponsors' individual financial credentials.

The drivers for the Council and the private sector must be well understood for this form of partnership to succeed. For the Council, the viability of the project depends on its efficiency and value for money compared with the economics of other funding strategies such as borrowing from private banks or State/Territory treasury corporations, or in the case of South Australia the LGFA. This assessment should not merely be an assessment of the comparative cost of finance. Although the Council may be able to borrow money more cheaply than the private sector, other factors could offset this advantage, such as private sector efficiencies and innovation, and the transfer of risk.

For the private sector, the viability of the project depends on cash flows from the project (for example revenue generated by user charges or availability payments from the Council) covering the operating and/or maintenance costs and debt service, as well as providing sufficient return on investment.[19] The Council needs to consider this proposition in structuring a PPP arrangement if the project is to be attractive to the market and ultimately successful.

PPP projects can be broadly categorised as economic infrastructure projects and social infrastructure projects. These are discussed in turn below.

6.2 Economic infrastructure projects

Economic infrastructure refers to projects where the project company derives revenue from the operation of the asset from user fees or third parties (not the Council). The project company bears the demand or patronage risk.[20] The project therefore involves the development of a revenue generating asset, for example toll roads, commercial car parks or sporting stadiums. This income stream is used to provide operational cash flow, service the debt repayments and generate a return on investment to the sponsors who provided equity for the project.

In an economic infrastructure PPP, the financiers primarily look to the anticipated revenue stream of the project to service debt repayments, and the project assets (including the key project agreements) are used as collateral for the loan. This usually involves detailed financial modelling of the project.

A true economic infrastructure PPP requires no contribution of capital to the project by the Council for the construction of the asset, and no service fee or availability charge is paid by the Council during the operations phase. However, in recent years the private sector has resisted taking on demand risks in economic PPP projects. This has been the case in some State Government PPP toll road projects. Hybrid models have been developed where project revenue is supplemented by a cash injection from the government at the completion of the construction phase, and/or an availability charge is paid to the project company in addition to the income generated by the operation of the asset.

The procurement models typically used for economic infrastructure PPP projects are the Build, Operate and Transfer (BOT) and Build, Own, Operate and Transfer (BOOT) models. For further discussion on these models see section 14 of Part B2, *BOT, BOOT and BOO.*

Suitable projects

While this approach has been used successfully by State Governments in Australia to develop economic infrastructure, the model has rarely been used by local government. It may be useful for the construction and operation of large commercial car parks, the development of a commercial marina or the refurbishment of a regional airport. For a discussion on projects suited to the PPP structure using BOT, BOOT and BOO models see section 14 of Part B2, *BOT, BOOT and BOO.*

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[19] Build Own Operate Transfer (BOOT) Projects, www.mcmullan.net/eclj/BOT.html
[20] *National PPP Guidelines, Volume 7: Commercial Principals for Economic Infrastructure*, Infrastructure Australia, Commonwealth of Australia (February 2011) p 1.

Benefits and disadvantages

The key benefits and disadvantages of a PPP arrangement for Council economic infrastructure projects using a BOT, BOOT or BOO model are outlined below in section 14 of Part B2, *BOT, BOOT and BOO*.

6.3 Social infrastructure projects

Social infrastructure refers to projects where the project company derives revenue from periodic service payments or availability charges paid by the Council during the concession period. These payments may be made monthly, annually, etc., The payments are subject to the project company meeting specified performance criteria and will be reduced or 'abated' for failure to reach the required standard. Like an economic PPP, the Council typically does not provide any up-front capital for the project. Examples include the development of a new council office complex, long term road maintenance and capital works programs and new bridges.

In social infrastructure PPP projects, the Council has the option of engaging the private sector to design and build an asset and provide the post construction maintenance and community services. Alternatively, the Council may provide the 'core' community services while the project company provides the maintenance services. The latter approach allows the Council to maintain control over the community service component of the project. The procurement models typically used for social infrastructure PPP projects are Design, Build, Finance and Operate (DBFO) and Design, Build, Finance and Maintain (DBFM). For further discussion on these models see section 13 of Part B2, *Design, Build, Finance and Operate (DBFO) and Design, Build, Finance and Maintain (DBFM).*

Suitable projects

For a discussion on projects suited to the PPP structure using the DBFM and DBFO procurement models see section 13 of Part B2, *Design, Build, Finance and Operate (DBFO) and Design, Build, Finance and Maintain (DBFM).*

Benefits and disadvantages

The key benefits and disadvantages of a PPP arrangement for Council social infrastructure projects delivered using a DBFM or DBFO procurement model are outlined in section 13.3 of Part B2, *Benefits and disadvantages*.

Legislative authority

The power to form a partnership and other relevant legislation is contained in the following provisions:

- **Victoria:** *Local Government Act* 1989 (Vic) s 193(1)(a)
- **New South Wales:** *Local Government Act* 1993 (NSW) chapter 12, Part 6
- **Queensland:** *Local Government Act* 2009 (Qld) s 40
- **South Australia:** *Local Government Act* 1999 (SA) s 46(2)(b)
- **Western Australia:** *Local Government Act* 1995 (WA) s 3.59
- **Tasmania:** *Local Government Act* 1993 (Tas) s 21(1)(a)
- **Northern Territory:** *Local Government Act* 2008 (NT) s 25(3).

7. Further resources

Commonwealth

National Public Private Partnership Guidelines, *Volume 2: Practitioner's Guide,* Commonwealth of Australia, Infrastructure Australia (March 2011).

National PPP Guidelines, Volume 3: Commercial Principals for Social Infrastructure, Infrastructure Australia, Commonwealth of Australia (December 2008).

National PPP Guidelines, Volume 7: Commercial Principals for Economic Infrastructure, Infrastructure Australia, Commonwealth of Australia (February 2011).

Victoria

Local Government Best Practice Procurement Guidelines 2013, Department of Planning and Community Development, State of Victoria (2013).

Local Government Infrastructure Program, Regional Development Victoria website, www.rdv.vic.gov.au/infrastructure-programs/local-government-program.

New South Wales

Development contributions: Practice notes – July 2005, Department of Infrastructure, Planning and Natural Resources (July 2005).

Funding Local Infrastructure: Report by the Section 94 Contributions and Development Levies Taskforce to the Minister for Infrastructure and Planning and Minister for Natural Resources, Department of Infrastructure, Planning and Natural Resources (February 2004).

Queensland

A Guide to Funding Options Available to Local Government, Queensland Treasury Corporation (April 2010).

Public Private Partnerships Guidance Material: Policy, Queensland Government, Department of Infrastructure and Planning (2008).

South Australia

Better Practice Model – Financial Internal Control for South Australian Councils, Local Government Association of South Australia, South Australian Local Government Financial Management Group Inc. (SALGFMG) (April 2012).

Developer Contributions Mechanisms Study: South Australia, Local Government Association of South Australia (February 2007).

Tasmania

Tasmanian Government Project Management Guidelines Version 7.0, The Department of Premier and Cabinet (July 2011).

Western Australia

Integrated Planning and Reporting Framework and Guidelines, Government of Western Australia, Department of Local Government and Communities, Integrated Planning (4 May 2011).

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Planning and Development Act 2005*: State Planning Policy 3.6 – Development Contributions for Infrastructure*, Government Gazette (WA) (20 November 2009).

General

Assessing Local Government Revenue Raising Capacity, Productivity Commission Research Report, Australian Government, Productivity Commission (April 2008).

Infrastructure, Finance and Funding Reform, Infrastructure Finance Working Group (IFWG) (April 2012).

Peterson, G.E., 'Land Leasing and Land Sale as an Infrastructure-Financing Option' *World Bank Policy Research Working Paper 4043* (November 2006).

The Journey Continues: PPPs in Social Infrastructure, Ernst & Young (September 2008).