

National Local Government Finance Authority

The Draft Report *Public Infrastructure* tackles *inter alia* the funding of local public infrastructure, most commonly provided by local government. However, the discussion in *Public Infrastructure* is deficient in several respects, mostly notably the fact that the authors of the Draft Report have almost entirely ignored the literature on a National Local Government Finance Authority as the most efficient means of financing local public infrastructure through local infrastructure bonds provided through a National Local Government Finance Authority.

An Australian literature exists on this question which has not even been considered by the authors of *Public Infrastructure*. This literature has examined the range of instruments available for financing local government infrastructure.

In essence, only three generic policy options exist. Firstly, much higher property taxes, fees and charges, developer charges, and other ‘own-source’ methods of revenue-raising could be embraced by the local government sector. An alternative policy option resides in substantially increased intergovernmental transfers from Commonwealth and state governments in the form of grants and *ad hoc* payments, along the lines of the R2R Program, or through substantial tax-sharing arrangements, as epitomised in Commonwealth GST payments to the states and territories. Finally, much greater reliance could be placed on the use private financial capital through borrowing.

However, given contemporary Commonwealth and state government fiscal circumstances, no realistic prospect exists of considerable increases in grants or other types of transfer payments. Moreover, given the Productivity Commission’s (2008) findings in its *Assessing*

Local Government Revenue Raising Capacity Report, the majority of local government entities possess neither the financial capacity nor the political will to impose the kind of harsh increases in rates and other fees and charges necessary to raise the massive quantity of funds required. In practical terms, borrowing from the private sector thus represents the only feasible solution short of a complete reassignment of expenditure and revenue powers in Australian fiscal federalism.

Several promising instruments for local government borrowing have been considered in the literature. For instance, in a paper in *Australasian Journal of Regional Studies*, Byrnes, Dollery, Crase and Simmons (2008) have suggested the establishment of an Australian municipal bond market, along similar lines to the American municipal bond market.

However, given the expertise and funding required to use a bond market, small councils - which comprise a majority of Australian local government - would be unable to use this market. In another paper in the *Australasian Journal of Regional Studies*, Dollery, Grant and Kortt (2012) considered and rejected the feasibility of municipal banking in Australia which would have mirrored widespread practice in many European local government systems.

Similarly, in a contribution to *A Global Economy*, Dollery, Grant and Kortt (2011) advocated the establishment of a national local government bond bank to pool individual council risk in aggregated infrastructure bonds issues guaranteed by the Australian government.

Arguments for the establishment of a National Local Government Finance Authority in Australia have been further refined in the following contributions:

Dollery, B. E., Kortt, M. and Grant, B. (2013), *Funding the Future: Financial Sustainability and Infrastructure Finance in Australian Local Government*, Sydney, Federation Press, xi + 276.

Dollery, B. E. (2012), *Catalysing the Renewal of Local Infrastructure in Regional Communities: The Case for Local Infrastructure Australia*, Regional Australia Institute, Canberra, November, 36.

An Australian National Local Government Finance Authority would have to deal largely with long-term bond pooling to accommodate the comparatively small size of most Australian local authorities. The mechanics of long-term bond pooling for local councils are straight forward. The National Local Government Finance Authority would issue bonds and uses the revenue to make loans to numerous small municipalities, which have applied for finance through the bond bank. As lenders to local authorities, bond banks typically apply credit tests which borrowing councils must satisfy in order to qualify for loans. These commonly take the form of a general obligation by local borrowers and various forms of minimum requirements for debt service coverage.

An Australian National Local Government Finance Authority run along these lines would have several advantages. Bond purchasers would be secured by loan repayments from the pool of local government borrowers as opposed to a single municipality. Moreover, since the bond bank would enjoy a Commonwealth guarantee, lenders would receive further security. This would also serve to reduce the interest costs associated with borrowing due to the Commonwealth's AAA credit rating.

The case for an Australian local government bond bank has gained converts. For example, in their *Strong Foundations for Sustainable Local Infrastructure: Connecting Communities, Projects, Finance and Funds*, published on 18 June 2012, Ernst and Young have echoed the

findings of Dollery, Grant and Kortt (2011) and recommended that the Commonwealth establish of national financing authority for local government.

Institutions of this kind already exist in some local government jurisdictions. For example, all of the Nordic countries have independent national finance authority, with one dating back to 1898! In Anglosphere nations, many similar examples can be found. Thus the Local Government Finance Authority of South Australia fulfils many of the functions of a national finance authority in that state. The Authority was established under the Local Government Finance Authority Act 1983 and it is managed and administered by a Board of Trustees. The functions of the Authority are to develop and implement borrowing and investment programs for the benefit of local councils and prescribed local government bodies. In Canada, six provinces have analogous arrangements, 17 American states have 'bond banks' and New Zealand has recently successfully launched a national local government finance authority.

Brian Dollery is Professor of Economics and Director of the Centre for Local Government at the University of New England in Armidale NSW.