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Public Values Public Infrastructure

It is rare for senior journalists to take an interest in asset management, so when they do it is worth looking at what problems they find to be noteworthy—and *what they see as the solution*.

This month, Ross Gittens, senior journalist with the Sydney Morning Herald, reviewed the report by Jeff Roorda for the Inquiry into the Financial Sustainability of Local Government in New South Wales. I have presented Ross' column in full. (31-32) And I have also presented a summary of the main issues arising from the report itself. (29-30) Compare the two!

Whilst the 'more money' solution is

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always to be regarded as a last resort, Ross' plea for the re-institution of public borrowing makes sense.

Public borrowing satisfies an important public value—namely, if the term of the loan matches the life of the asset, then we 'pay as we go' and avoid the inequity of inter-generational transfers. (But know when to borrow—see SAM 164)

What other public values are of importance to us when we consider the management of public assets? In The Netherlands, the "Next Generation Infrastructures" project has, as one of its major themes, the exploration of public values in public infrastructure. We look at the work that they are doing (28) in the light of what will be a major theme of renewal in the first half of this century (27) And in "Worth noting" (26) I look at the relationship between the words we use and the values we choose.

Comments welcome.

Enjoy!

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Words Matter

In any discussion on values, it would be hard to ignore George Lakoff's book with the curious title "Don't think of an Elephant"

Lakoff, like Noam Chomsky before him, is a linguist turned political activist. In his short but fascinating book, he shows how the words we use—subtly and often unconsciously - influence the values we choose, and the actions we then take!

When you speak about infrastructure management and renewal amongst yourselves, to your boards and to your neighbours, do you see it as a burdensome chore, or an opportunity to "invest in the future"?

Combine this thought with the work of Don Watson in "Death Sentence" where he demonstrates convincingly that our language is becoming jargonised—de-humanised! — and one has to look back at the last decade or so, when all life issues seem to have been reduced to an economic equation, and ask if that is really what we want.

For example, public infrastructure is clearly for the public good— yet how compatible is the *maintenance of this infrastructure* with a language that teaches us to put individual needs first?

In his book, Lakoff challenges the implications of the words "tax relief" (and the concomitant push to 'smaller government' (itself a pseudonym for big government in law and business support but small in public support.)

He poses the following "ad".

Our parents invested in the future, ours as well as theirs, through is that the taxes. They invested their tax money in the interstate highway system, the Internet, the scientific and medical establishments, our communications system, our airline system, the space program. They invested in the future, and we are reaping the tax benefits, the benefits from the taxes they paid. Today we have assets -- highways, schools and colleges, the Internet, airlines -- that come from the wise investments they made.

How might you apply these ideas in communicating to your communities?

And (in argument against companies seeking lower taxes)

Every businessman has used the vast American infrastructure, which the taxpayers paid for, to make his money. He did not make his money alone. He used taxpayer infrastructure. He got rich on what other taxpayers had paid for; the banking system, the Federal Reserve, and the judicial system, where nine-tenths of cases involve corporate law. These taxpayer investments support companies and wealthy investors. There are no self made men! The wealthy have gotten rich using what previous taxpayers have paid for. They owe the taxpayers of this country a great deal and should be paying it back.

Are you conscious of the words you use—and the values they imply?

George Lakoff, *Don't Think of an Elephant*. Scribe Publications, Melbourne, 2004
Don Watson, *Death Sentence: the decay of public language*, Random House, Australia 2003

The Age of Renewal

The last half of the 20th Century was an age of major construction in developed countries around the world.

It was also a time of greatly expanding governmental and personal incomes and an explosion in labour markets with women entering the workforce, followed by the arrival in the 1970s of the workforce increment of the 'baby boom'.

The first half of the 21st Century will be an age of major renewal

But we will not have the income and workforce advantages which made the initial expansion possible. It could also be a time of major disruption for services and communities with difficulties for heritage and social management. To deal with these issues we will need to be more than usually creative.

If we focus on building things and repairing things, this quantum leap in creativity will be hard to come by

It will be all too easy to slip back into old ways of doing things and to be satisfied with small, 5%, improvements, when what is needed is an order of magnitude difference.*

* How much do we need to change?

The Inquiry into the Financial Sustainability of Local Government, in New South Wales suggested that the level of the renewal gap was 12%, suggesting that we need rate increases—or cost decreases—of this magnitude just to stay where we are. But staying where we are as the world advances is, itself, a backward step. To both sustain *and* develop we need more than this.

But if we seek innovations in the way in which we use infrastructure to support public values, a whole new world opens up for us.

What Public Values?

Whilst individual values may differ, I suspect that, as a group, our public values could be pretty common. Here are some of the things that I think we hold in common and are supported (or not) by the way in which we choose and manage our public infrastructure. (What have I left out?)

- Universal access to services
- Affordability
- Reliability and minimal disruption
- Safety
- Financial Sustainability
- Environmental Sustainability
- Heritage conservation and the importance of our history
- Strengthening Communities
- Inclusiveness in decision-making
- Equitable distribution of costs and benefits
- Protection of the weak

Safeguarding Public Values

If we can change our language to focus on the values that enabled us to create public assets in the first place, would this help us now to restore and renew?

I was intrigued when I first saw the work of the NG Infra group (Next Generation Infrastructures). My first thought—and it might be yours, too—was that it was an impossibility to even define, let alone 'safeguard' public values. But the more I thought about it and read through the extensive and detailed research proposals that they have developed (www.nginfra.nl) the more convinced I became that part of our problem today in generating the public will to tackle the tasks we know need doing, is that *we have forgotten the public values that led us to establish public infrastructure in the first place.*

The NGInfra Group, which operates out of the University of Delft, has programs in place to define and to analyse the success in safeguarding these public values by different organisational arrangements in the area of water and roads management in Holland and Europe more generally. If you would like to know more about this, or to examine how a better understanding of public values might help you—please contact me.

An Overview of NGInfra's Approach to Public Values & Public Infrastructure

Problem

There are no appropriate governance models to safeguard the public values we traditionally associate with infrastructures.

Objective

To assess and redefine public and private values in the light of European liberalization policy and to develop new governance models for safeguarding these values.

Ask anyone what public values are associated with infrastructures, and you will get answers such as: universal access, affordability, reliability, safety and sustainability. (Ed: see list on previous page)

We are annoyed when a power failure occurs, when we get sky high cell-phone bills, when the Internet goes down, when gas leaks are reported in the neighbourhood or when a smog alert forces us to stay indoors. And when these things happen on a regular basis, we tend to hold the public authorities responsible. But due to European liberalization policy, many utility sectors are now run by private companies, which tend to be only interested in public values if they generate a reasonable profit. So how should we safeguard these public values? Can we trust technology to come up with the answers? Do we need more government regulation? Will the market provide its own solutions? Or will public values be best protected by negotiations between client organizations and service providers?

And what exactly are 'public' values in the first place? It is very interesting that certain values are considered to be public in one country and private in another. We argue that public values cannot be defined objectively and unambiguously. For instance, in modern industrialized countries access to the Internet gradually has become a public value, while in most underdeveloped countries even a simple telephone is a rare commodity. This issue is even harder to solve in the case of liberalized and privatized infrastructure sectors. So who is responsible to take the appropriate measures to safeguard these public values? And what measures should that be? What governance models are effective and how are all parties involved to be stimulated into cooperation? International empirical research is being done into 'best practices' in different infrastructure sectors. The findings will result in the design of new governance models for safeguarding the redefined set of public values.

4 Questions

1. *What is the condition of local government infrastructure in New South Wales?*
2. *What will it cost to bring it to a satisfactory standard and fund its renewal in future?*
3. *What is the state of Councils' current asset management practices?*
4. *What should be done?*

In answer to the first two questions

This study's survey found that while Councils are able to fund ongoing routine maintenance of their infrastructure **they do not have sufficient revenue to fund 30-50% of future asset renewal. Nor do they have the revenue capacity, or in most cases the asset management skills and systems,** to undertake future asset renewals. This means Councils are falling behind in their infrastructure upkeep by \$500 to \$600 million per year, with **no long term funding plan** to replace assets when their renewal is due. It's akin to a family that does not make sufficient provision for replacing worn out parts, let alone saving enough to buy a new car when it reaches the end of its economic life (the point at which repairing the car is more expensive than replacing it).

In answer to Question 3

Very limited use of asset management plans

"Local Councils provide the bulk of essential services to local communities, including recreation, transport, culture, and drainage and in some cases water and wastewater. Most Councils do not have a complete understanding of the assets that underpin these services. Only 20% of Councils have adopted asset management plans for services. A further 30% of Councils intend to have asset management plans completed within the next one to two years. The remaining 50% have no current intent to prepare asset management plans."

Lack of data on current asset replacement costs

"The majority of Councils [85%] are reporting on assets on an "at cost" basis rather than "fair value" primarily to avoid the need for regular revaluation of assets. For most of these Councils, the asset register used for financial reporting is "frozen" at 1995 – 1996 when assets were first capitalised under new accrual accounting requirements (i.e. AAS 27). Asset values, depreciation and estimates of asset life have not been updated for assets capitalised at that time."

Lack of understanding of service levels

"Even more fundamental is the lack of agreement on service levels and quality standards. The determination of what constitutes a "satisfactory standard" for asset related services is usually based on engineering estimates or analysis. Analysis based on community-based outcomes such as quality, life cycle, functionality, risk & safety were applied in fewer than 20% of Councils. Managing the future requires information about future events, but most of the information currently available to councils is not future oriented; it is backward looking."

In answer to Question 4:

What is to be done?

Given the current state of knowledge it will not be surprising to find that not one of the recommendations refers to increasing rates, extra funds or borrowings. (But c.f. the SMH review pp 31-32). Instead all are related to better asset management practice and capacity building.

Of particular interest is the report's discussion on that perennial question—**should asset management be mandated?** So I have dealt with this in more depth over the page.

Should Asset Management be Mandated?

Those who argue YES point to New Zealand's benefits, such as

- definition of, and consultation on service levels;
- a better understanding of demand and asset constraints;
- the building of asset registers and a better understanding of asset life cycles;
- and a structured approach to funding asset maintenance, renewal and acquisition.

Those who argue NO, look to the disadvantages

These benefits come at a cost in terms of human resources and additional funding. Larger authorities have managed but the smaller ones have struggled to meet minimum compliance requirements, and to provide enough management and engineering resource to adequately undertake asset management programmes.

This has led to a very stop-start approach to asset management as legislative compliance pressures have developed, which in turn has led to very lumpy funding requests to Councils, additional pressure on already stretched human resources, and the potential gains of a sustained asset management programme not being captured.

Reference Panel argued that Mandating was inappropriate and could be harmful

Asset management is a process. Regulation should apply to outcomes and not to process, otherwise the incentive for process innovation and improvement is removed and evolution, which has been so evident over the past ten years, will slow and perhaps even stop; and

Asset management plans when mandated, encourage a 'tick the box' mentality of mindless compliance. Asset management is then perceived as a means of being held accountable rather than as a process for achieving better outcomes. If a process is mandated it is done to a minimum.

But councils should be required to be financially sustainable for the long term – and to demonstrate that they are.

In the private sector if an organisation is insolvent it may not continue to trade. So regulators have a duty to ensure that the future viability of the organisation is clearly displayed in its annual reports. Because many local governments are running operating deficits without sufficient reserves, they are effectively 'trading whilst insolvent'.

This has arisen because they have either:

- Failed to correctly state the total costs of their operations (by understating the valuation and therefore depreciation of their infrastructure); and/or
- Failed to ensure that their total revenues will cover their total costs (including asset maintenance and depreciation) over the longer term.

You can access the whole report at

http://www.lgi.org.au/research_reports.html

Financial sustainability can be assured by requiring that all councils have a long term funding plan.

“They fiddle while assets slowly burn”

Ross Gittens
Sydney Morning Herald
February 1 2006
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Inquiry into the
Financial Sustainability
of Local Government,
New South Wales

Governments that save costs by letting public works run down are in for a shock.

WHAT happens when politicians keep promising the electorate new and better government services, but also reinforce the belief that we're already overtaxed - and, for good measure, adopt the attitude that it's a terrible thing for governments to borrow? The short answer is, something's got to give. To make that inconsistent trio of propositions add up, there's got to be something somewhere that's being squeezed. Something that's not terribly noticeable. A path of least resistance.

For some time now, the more alert among us have suspected that the meat in the sandwich may be public works. That the politicians may be making heroes of themselves and proving they can do the impossible by quietly running down the quality and adequacy of public infrastructure.

If that was happening, you might expect it to be occurring at the lowest level of the public sector - local government. Local government is the Cinderella of the system. It's the level that gets the least public scrutiny and the ultimate level to which miracle-working state and federal pollies can surreptitiously shift costs they are happy to incur, but unwilling to meet.

If you've ever harboured such suspicions, I have worrying news. A report prepared by the consultants Jeff Roorda & Associates for the Independent Inquiry into the Financial Sustainability of Local Government confirms there's a problem. The inquiry was established by the Local Government and Shires Associations of NSW.

The state's 152 local councils are the custodians of community assets worth at least \$50 billion. They include local roads, bridges, kerbing, paths, traffic facilities, stormwater drains, plant and equipment, buildings, parks, swimming pools and other recreation facilities.

That figure includes \$8 billion for the water and sewer infrastructure of councils outside Sydney, Wollongong and Newcastle. But it's not precise because most councils haven't revalued their assets since the second half of the 1990s.

The usefulness of these assets is being used up at the rate of almost \$1 billion a year, but councils are making provision of only about half of this. So they're effectively running down their capital, and risk being caught short when the time comes to replace the assets.

According to estimates by council engineers, it would require immediate spending of more than \$6 billion - 12 per cent of their total value - to bring the existing assets up to a satisfactory standard. That's almost eight times the annual level of spending.

That's the backlog to date. Looking forward, about \$15 billion more will be needed over the coming 15 years to replace existing assets when they get too old to be reliable and economically maintained.

The other way to put it is that councils are incurring a "renewal gap" of \$500 million to \$600 million a year. This is equivalent to about 12 per cent of councils' annual revenue from rates and charges. So council rates are roughly 12 per cent lower than they should be to stop the value of their capital being run down.

What does Gittins see as 'The Problem'?

Insufficient provision has been made for replacing assets as they wear out

According to the report, the situation is "akin to a family that doesn't make sufficient provision for replacing worn-out parts, let alone saving enough to buy a new car when it reaches the end of its economic life" - which is the point where repairing the car is more expensive than replacing it. And the present backlog of \$6 billion to bring assets up to a satisfactory standard is "equivalent to driving a vehicle with serious structural and mechanical problems that have not been attended to".

In which case, why haven't councils been hitting the panic button? Because, although in some cases it may be obvious to the public that council assets are run-down or even dangerous, for the most part the problem is hidden.

The issue has been easy to ignore because infrastructure typically has a life of 50 to 60 years and only a small proportion has required renewal so far. Councils have been able to fund the operation and routine maintenance of assets, with a limited amount of renewal. The crunch is still some years off.

Councillors would find the technical condition of infrastructure difficult to relate to the quality of service provided until the assets are badly deteriorated.

"By the time infrastructure condition is at such a bad state as to be noticeable to the community, it will long have passed the optimal time for renewal," the report says.

About half the money councils devote to infrastructure each year is spent on additional assets, not the renewal of existing assets. Where communities are growing, this is understandable. But it just adds to the problem of setting aside enough to cover renewals.

Councils in country areas where the population is static or declining, with commensurate weakness in their rate revenue, are tempted to allow their assets to run down. But this may hasten the district's decline.

What does he see as 'The Solution'?

- Raise rates
- Federal and State level Grants

Or

- Re-institute Public Borrowing

So what's the solution to the problem?

Well, a good start would be better management. Most councils have quite primitive arrangements for managing their assets. They don't give enough attention to keeping track of them, regularly revaluing them, ensuring their maintenance is adequate and setting aside sufficient funds for their ultimate replacement.

Part of the problem is that much of the infrastructure in the custody of local government was built or paid for by other levels of government. The Howard Government's local road-building program, Roads to Recovery, is a case in point. In new suburbs, much of the infrastructure is taken over from property developers. This explains why local government can end up with an amount of infrastructure that's out of whack with its ability to renew that infrastructure.

So while one obvious solution would be simply to allow councils to raise their rates, it's more likely that when eventually a lot of infrastructure falls past due for renewal, state and federal governments will be forced to step in and stump up.

[Ed: Note that these are only the 'easy-to-understand' 'more money' options—we still have a selling job to do on cleverer management!]

Then, perhaps, borrowing to finance long-lived public works will come back into fashion. It's just a pity that, so often, problems have to reach crisis point before politicians will face up to them.