COMPULSION VERSUS A COLLABORATIVE REGIONAL APPROACH

An Empirical Analysis of Forced Amalgamation versus a Regional and Shared Services Approach

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Contacts:

Professor Brian Dollery
Telephone: 02 6773 2500
Email: bdollery@une.edu.au

Mr Roy Newsome
Group Manager Corporate Services
Telephone: 02 9952 8243
Email: lsafi@ryde.nsw.gov.au

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EXECUTIVE SUMMARY

Key Findings of the Report

This Report has eight major policy implications for NSW local government reform:

1. Empirical evidence on amalgamation in the literature falls overwhelmingly against forced amalgamation. Indeed, the bulk of the empirical literature shows that shared services and other kinds of inter-council collaboration best secure the advantages of scale.

2. Empirical analysis of the 2000/2004 NSW council amalgamations shows no difference in the performance of merged and unmerged councils using *Fit for the Future* criteria. In an analogous vein, empirical analysis of the 2008 Queensland amalgamations shows that most amalgamated councils now operate under diseconomies of scale. Taken together, this provides convincing empirical case against proceeding with a further round of municipal mergers in NSW in 2015.

3. Critical assessment of the *Fit for the Future* process found it severely flawed in numerous respects: its arbitrary use of financial sustainability ratios (FSRs) and associated benchmark values; its problematic 'scale and capacity' approach; unreliable data employed in sustainability assessments; and an incorrect measure employed to assess the operational efficiency of councils. The NSW Office of Local Government

should thus to halt the *Fit for the Future* process and solve these problems before proceeding with the reform program.

4. IPART's (2015) *Methodology for Assessment of Council Fit for the Future Proposals* – only released on 27 April 2015 – add a further twist to a convoluted reform process. IPART will replace the Panel of Experts promised in *Fit for the Future* as the assessor of council submissions and its new assessment methodology introduces significant changes to the process. In particular, 'non-rural', 'rural' and 'merged' councils in IPART (2015) replace the 'one size fits all' approach in *Fit for the Future.* Performance benchmarks also now diverge widely between IPART (2015) and *Fit for the Future.* However, the Report demonstrates that the IPART approach is badly flawed and does not correct the problems identified in *Fit for the Future*.

5. By 'changing the rules of the game' IPART has rendered much hard work already done by local councils obsolete. Thus Hunters Hill, Lane Cove and Ryde, which have cooperated fully with the *Fit for the Future* process, undergone self-assessment using the requisite OLG (2014) templates, and engaged in extensive and *bona fide* community consultation, now find that much of this effort has in vain.

6. An empirically investigation of the proposed Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby council mergers in the Report found numerous problems: challenges posed by significant current disparities in rates, fees and charges, and capacities to pay across the six councils; problems determining democratic representation post-merger; apportioning the burden of liabilities inherited by a newly merged council; complications derived from the dismemberment of the City of Ryde;

Commonwealth financial assistance grants post-merger, information disclosure to local residents, and the critical fact that almost all of the North Shore group of councils would be less financially sustainable under the *Fit for the Future* criteria than they had been pre-merger.

7. The Report conducted two modelling exercises to investigate the outcomes of the proposed Sydney mergers: (a) multiple regression analysis showed that the Independent Panel's claims about scale economies proved false and (b) DEA analysis also demonstrated most proposed Sydney amalgamations would yield over-scaled councils too large to efficiently provide local services. Taken together, this shows that there is no empirical justification for the proposed merger of the Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby councils.

8. The Report presented a detailed analysis of the socio-economic characteristics of the Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby councils. This demonstrated that no common 'community of interest' existed.

7. Following a detailed review of the empirical literature, the Report which found strong evidence that shared services could yield significant benefits. However, not all local services are amenable to regional provision through shared service arrangements.

9. The Report found that shared services represent a superior alternative to forced amalgamation to improve the performance of the Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby councils. Moreover, the best method of delivering shared services lay in a variant of the successful Hunter Councils model.

10. The Report thoroughly examined the community engagement programs conducted by Hunters Hill, Lane Cove and Ryde and found that they easily met the community engagement assessment criteria stipulated by IPART (2015) in its *Methodology for Assessment of Council Fit for the Future Proposals.*

CHAPTER 1: INTRODUCTION

1.1 Introduction

The current NSW Government *Fit for the Future* reform process had its genesis in the *Destination 2036* Workshop held in Dubbo on 19th August 2011. Introduced by (then) Minister for Local Government Don Page, *Destination 2036* witnessed the inauguration of the Independent Local Government Review Panel (ILGRP) as well as the Local Government Acts Taskforce. In its April 2013 interim report – entitled *Future Directions for NSW Local Government* – the Independent Panel (2013, p.48) recommended radical compulsory council consolidation across NSW, concentrated largely in the Greater Sydney metropolitan region. With respect to Greater Sydney, *Future Directions* (2013, p.5) observed that it 'seek[s] to reduce the number of councils in the Sydney basin to around 15, and create major new cities of Sydney, Parramatta and Liverpool, each with populations of 600-800,000'.

The Panel's specific recommendations included the merger of Auburn, Holroyd, Parramatta and Ryde councils to form the 'Parramatta group' of councils, on grounds that the 'incorporation of Ryde would strengthen western end of "Global Sydney Corridor" and improve socio-economic mix' of the Parramatta group, although the Panel also suggested part of Ryde could be incorporated in the 'North Shore group', consisting of Hunters Hill, Lane Cove, Mosman, North Sydney and Willoughby The Panel's (2013, p.45) rationale for merging Ryde with the Parramatta group was as follows:

> A major expansion of the City of Parramatta to include Auburn, Holroyd, most or all of Ryde, and areas of Hornsby and The Hills south of the M2. This will create a city with a broad socio-economic mix and with the resources needed to develop a 'second CBD'.

In addition, the Panel (2013, p.48) called for the forced merger of the Hunters Hill, Lane Cove and Mosman councils, together with the eastern part of Ryde, to form the 'North Shore group', even though Mosman did not share a common boundary! This was justified on the argument that there existed a 'close functional interaction and economic/social links between these councils'. The Panel (2013, p.49) also recommended the compulsory consolidation of the North Sydney and Willoughby councils contending that there existed a 'need for integrated strategic planning for Lower North Shore, development of major centres, Sydney Harbour foreshores, etc.'

Despite repeated assurances that it would adhere strictly to 'evidence-based' policy prescription, in *Future Directions* the Panel offered no empirical evidence at all in support of the proposed mergers, including those involving Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby.

The forced merger program advocated in *Future Directions* by the Independent Panel was greeted with dismay by NSW local government. It was attacked on numerous counts, not only because of the absence of any empirical basis for its merger recommendations, but also the poor quality of its commissioned research, particularly

Assessing Processes and Outcomes of the 2004 Local Government Boundary Changes in NSW by Jeff Tate Consulting (2013) (see, for example, NELG, 2013). Instead of assessing the success of the 2004 forced amalgamation in NSW by comparing the subsequent performance of merged and unmerged councils in the same council classification categories against the *NSW Government Comparative Information on NSW Local Government Councils* data, Jeff Tate Consulting (2013) simply consulted (in qualitative terms) some members of five of the amalgamated councils!

After public consultation with local government and other interested parties across NSW, in October 2013 the Panel submitted its final report *Revitalising Local Government*. The main difference between *Future Directions* and *Revitalising Local Government* lay in a shift away from outright compulsory council consolidation to the establishment of a 'strengthened' Boundaries Commission. This reinforced Boundaries Commission would be empowered to deliberate on proposals for council amalgamation and make binding recommendations concerning mergers, with or without the consent of affected councils.

However, in common with *Future Directions*, *Revitalising Local Government* continued to insist that municipal mergers were indispensable for improving NSW local government. Furthermore, in its overall assessment of local government financial sustainability in NSW, *Future Directions* (2013, p.6) had argued that 'it is also clear that the financial base of the sector is in urgent need of repair', and added that 'put simply, there are too many councils chasing too few resources'. This theme was

reiterated in *Revitalizing Local Government* where the Panel (2014, p. 720) noted that 'NSW simply cannot sustain 152 councils'!

Revitalising Local Government (2014, p.104) recommended the merger of Auburn, Holroyd, Parramatta, part of The Hills and 'about one-third population of Ryde'. The justification advanced in support of this municipal merger was fourfold: (a) 'close functional interaction and economic/social links between these councils', (b) 'need for stronger unified local government to develop Parramatta as second CBD', (c) 'Parramatta's northern boundary is very close to its CBD; relocation to M2 would facilitate planning and improve socio-economic mix and community linkages' and (d) 'incorporation of part of Ryde would strengthen link between Parramatta and "Global Sydney Corridor" and improve scope for integrated planning around Epping station'.

Furthermore, *Revitalising Local Government* (2014, p.104) called for the amalgamation of Hunters Hill, Lane Cove, North Sydney, Willoughby and the remaining 'about two-thirds population of Ryde'. A quadrilateral rationalisation was offered for this proposed merger: (a) 'projected 2031 population 365,400, including about two-thirds population of Ryde', (b) 'close functional interaction and economic/social links between these councils', (c) 'need for integrated planning for major centres, Sydney Harbour foreshores, etc.', and (d) '3 of these councils projected to have fewer than 50,000 people in 2031'.

Following the approach adopted in *Future Directions, Revitalising Local Government* offered no empirical evidence in support of its proposed council mergers. This understandably further alienated the NSW local government community, especially those councils targeted for amalgamation.

The NSW Cabinet delayed until early January 2014 before making public *Revitalising Local Government.* In April 2014, after the shock resignation of Premier O'Farrell, incoming Premier Baird reshuffled the NSW Cabinet, replacing *inter alia* Minister for Local Government Don Page with Paul Toole. These events may account for the fact that the NSW Government only formally responded to the recommendations in *Revitalising Local Government* in September 2014 in the form of a *Fit for the Future* policy package.

Under *Fit for the Future,* each local authority must assess itself to determine if it is 'sustainable', 'efficient', 'effectively manages infrastructure and delivers services for communities' and 'has the scale and capacity to engage effectively across community, industry and government' (OLG), 2014a). Assessment reports must be lodged with the NSW Government by 30 June 2015. To assist in this process, the NSW Government has appointed 'expert facilitators' to help local authorities to explore regional collaboration with other councils under newly established Joint Organisations (JOs), to be established following five 'pilot' JOs trialled in early 2015.

Under the *Fit for the Future* program, the 'eastern two-thirds' of Ryde is supposed to merge with Hunters Hill, Lane Cove, Mosman, North Sydney and Willoughby, with the remaining 'western third' to amalgamate with Auburn, Parramatta and the 'North Parramatta area of the Hills', roughly in line with the recommendations of *Revitalising Local Government* (2014).

An Expert Panel will be established to evaluate proposals to determine if councils meet *Fit for the Future* criteria. $258 million will be provided to councils which voluntarily merge. Councils which are deemed to have satisfied *Fit for the Future* guidelines will enjoy several benefits, including 'a streamlined IPART process for rate increases above the rate pegging limit' and interest subsidies on loans for capital expenditure (OLG, 2014, p.15). Councils which are judged not to meet *Fit for the Future* criteria face forced mergers.

In its council amalgamation recommendations, both the deliberations of the Panel and the subsequent NSW Government *Fit for the Future* policy program follow a depressingly well-trodden path. Australian state and territory governments have historically often employed structural reform programs of different degrees of intensity which have almost invariably involved compulsory council consolidation, especially in rural and remote areas of Australia. Thus, over the past twenty years, NSW, Victoria, Queensland, SA, Tasmania and the NT have all witnessed extensive municipal restructuring. To date, WA is the only local government jurisdiction to have escaped forced amalgamation, recently recommended by the now defunct Metropolitan Local

Government Review *Final Report* in July 2012, which proposed a reduction in the number of local authorities in the Greater Perth metropolitan region to a mere 12 local entities. However, the ongoing obsession on municipal amalgamation as the primary policy instrument for local government reform – as evidenced most recently in t *Fit for the Future* program – underlines the traditional view of Australian local government policy makers that 'bigger is better' in local governance (Dollery and Crase, 2006).

Against this background, the present Report critically considers in detail the case for merging the Hunters Hill, Lane Cove and Ryde councils under the *Fit for the Future* program, especially the proposed Hunters Hill, Lane Cove, Mosman, North Sydney, Willoughby and 'two-thirds population of Ryde' amalgamation. The Report not only provides a rigorous empirical examination of the proposed merger, including its impact on financial sustainability and scale economies, but also alternative methods of securing any advantages attendant upon scale, notably joint regional collaboration with other councils through a regional 'joint organisation'.

1.2 Outline of the Report

The Report itself is divided into nine chapters, each of which considers a separate dimension of the problem.

Chapter 2 provides an assessment of structural reform through council mergers in Australia by way of empirical evidence. Chapter 2 is divided into four main parts. Section 2.2 provides a summary of the international and Australian scholarly research on local government mergers. Section 2.3 describes the magnitude of municipal mergers

in Australia since 1910. Section 2.4 considers the effects of these structural changes on the financial viability of local government through the prism of a series of state-based and national public inquiries into financial sustainability in local government. Chapter 2 ends with some brief concluding remarks in section 2.5.

Chapter 3 provides empirical evaluations of the 2000/2004 NSW council mergers and the 2008 Queensland council amalgamation episode. Chapter 3 is divided into three main parts. Section 3.2 deals with the NSW mergers over the period 2000/2004. Section 3.2.1 provides a critical account of the analysis of the 2004 NSW local government merger program conducted by Jeff Tate Consulting Pty Ltd (2013) for the Independent Panel, which focused on an unrepresentative sample of only five amalgamated entities and involved no quantitative assessment of post-merger performance with unmerged councils. Section 3.2.2 provides an empirical analysis of the 2000/2004 NSW council mergers. Section 3.3contains an empirical evaluation of the 2008 Queensland forced amalgamation program. Chapter 3 ends in section 3.4 by drawing some policy lessons for the current *Fit for the Future* NSW from the two earlier amalgamation episodes.

Chapter 4 is divided into five main parts. Section 4.2 considers the multitude of problems which have arisen in the *Fit for the Future* criteria for evaluating councils which have derived from arbitrary and often illogical selection of financial sustainability ratios (FSRs) and the associated benchmark values and changes which have been made. Section 4.3 considers 'scale and capacity' in *Fit for the Future* and demonstrates severe problems in its approach. Section 4.4 examines the deleterious effects that the use of unreliable data for sustainability assessments has had. Section 4.5

demonstrates that the OLG has employed an erroneous approach to the assessment of efficiency in local government which has serious adverse consequences. Chapter 4 ends with some brief reflections in section 4.6.

Chapter 5 is divided into seven main parts. Section 5.2 considers the difficulties posed the existence of significant current disparities in rates, fees and charges, and capacities to pay across the six councils which were simply ignored by both the Panel and the OLG in the merger recommendations. Section 5.3 discusses the many difficult decisions which must be made regarding changes in democratic representation which will occur should amalgamations proceed. Section 5.4 tackles current and non-current liabilities of each of the six local councils targeted for a North Shore group merger, the total liabilities likely to be inherited by any proposed new amalgamated municipality, and its probable impact on local residents. Section 5.5 assesses the complication derived from the question of how to dismember the City of Ryde financially. Section 5.6 probes the question of the allocation of Commonwealth financial assistance grants post-merger and the difficulties this poses. Section 5.7 considers other problems attendant upon forced mergers, notably the need for full information disclosure in a transparent and democratic manner given the inevitability winners and losers amongst local residents post-amalgamation. Section 5.8 analyses whether merged combinations of the North Shore group of councils would be more financially sustainable under the *Fit for the Future* criteria than they had been pre-merger. Chapter 5 ends with some brief concluding remarks in section 5.9.

Chapter 6 is divided into four main parts. Section 6.2 discusses the inter-relationship between population size and population density in local government and conducts estimations which finds that when councils are stratified as either urban or non-urban, all evidence of scale effects (predicated on population size) disappears. Section 6.3 focuses on a data envelopment analysis of the proposed mergers recommended by the Panel and finds that over two-thirds of the amalgamated entities would be operating with decreasing returns to scale, and just two of the amalgamated entities would be operating at optimal scale if the ILGRP (2013) recommendations were enacted. Section 6.4 examines the proposed North Shore merger and finds that five of the six existing councils currently operate with increasing returns of scale at varying levels of TE and an amalgamated entity would operate with decreasing returns to scale. Chapter 6 ends with some brief concluding remarks in section 6.5.

Chapter 7 is comprised of two main parts. Section 7.2 provides a socio-economic overview of Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby. Chapter 7 concludes in Section 7.3 with a discussion of 'community of interest' based on community characteristics and argues that Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby should not be merged.

Chapter 8 is divided into four main parts. Section 8.2 provides a synoptic account of the empirical evidence on shared services in Australia. Section 8.3 provides a summary of the empirical evidence on shared services internationally. Chapter 8 concludes in section 8.4, which considers the policy implications associated with body of evidence.

Chapter 9 is divided into four main parts. Section 9.1 considers the broad implications of the conceptual literature on shared services in local government for the selection of functions to be provided by a joint regional organisation for Hunters Hill, Lane Cove and Ryde and the other North Shore group of councils. Section 9.3 outlines the Hunter Councils model as a desirable design for a joint regional organisation for the councils in question. Section 9.4 sets out a proposed design for a joint regional organisation for these councils drawing on the draft model previously considered by the NSROC and SHOROC groups of councils. Section 9.5 tackles the thorny question of which local functions and local services could be collaboratively delivered by a regional body and provides a survey instrument which can be employed to determine which services to provide. Chapter 9 ends with some brief concluding comments in section 9.6.

Chapter 10 is divided into three main parts. Section 10.2 provides a synoptic review of the approach to evaluating community consultation in IPART's (2015) *Methodology for Assessment of Council Fit for the Future Proposals.* Section 10.3 summarises the community consultation undertaken by Lane Cove, Hunters Hill and Ryde. Chapter 10 ends with some brief concluding remarks in section 10.4.

Chapter 11 is divided into three main parts. Section 11.2 briefly summarises the IPART (2015) *Methodology for Assessment of Council Fit for the Future Proposals*, sets out its evaluative criteria, and compares these with the criteria originally developed by TCorp (2013) and modified in *Fit for the Future.* Section 11.3 considers the numerous

problems inherent in the *Fit for the Future* criteria and the IPART (2015) *Methodology for Assessment of Council Fit for the Future Proposals* assessment technique:

- IPART (2015) assessment methodology for scale;
- IPART (2015) assessment methodology for sustainability;
- IPART (2015) assessment methodology for infrastructure and delivering services; and
- IPART (2015) assessment methodology for efficiency.

Chapter 11 ends with some brief concluding remarks in section 11.4.

The Report concludes in Chapter 12 which is divided into two main parts. Section 12.2 provides a short synoptic review of the chief findings of the Report whereas section 12.3 briefly reiterates the policy implications flowing from the Report.

CHAPTER 2: EMPIRICAL EVIDENCE ON MUNICIPAL MERGERS

Chapter Summary

- Empirical evidence on amalgamations in the academic literature falls overwhelmingly against forced amalgamation.
- Recent Australian empirical studies suggests that there is little, if any, evidence that forced municipal mergers will result in cost-savings.
- The weight of opinion in public inquires suggests that the traditional Australian stress on council mergers has been misplaced.

2.1 Introduction

Notwithstanding the omnipresent use of forced mergers in all Australian local government systems, excepting WA, compulsory council consolidation remains contentious (see, for example, Dollery, Grant and Kortt, 2012). Advocates of forced amalgamation, such as the NSW Independent Panel, typically argue that it represents an effective method of enhancing the operational efficiency of local councils, improving their administrative and technical capacity, generating cost savings, strengthening strategic decision-making and fostering greater political power.

By contrast, opponents of municipal mergers underline the divisive nature of forced amalgamation, the absence of supportive empirical evidence, the equivocal outcomes observed in case studies, and the diminution of local democracy. Furthermore, the case for structural change through municipal mergers is often met with the claim that shared

services represent a superior means of securing any benefits attendant upon council size and its scale of operations (Dollery, Crase and Johnson, 2006). Chapter 2 considers conceptual and empirical evidence on the controversial question of amalgamation in Australian local government, and especially the impact of municipal mergers on the financial sustainability of local authorities, as a means of assessing the likely success of the council amalgamation program proposed in the Independent Panel's *Future Directions* and *Revitalizing Local Government*, as well as the NSW Government's *Fit for the Future* program.

Chapter 2 is divided into four main parts. Section 2.2 describes the magnitude of municipal mergers in Australia since 1910. Section 2.3 provides a summary of the international and Australian scholarly research on local government mergers. Section 2.4 considers the effects of these structural changes on the financial viability of local government through the prism of a series of state-based and national public inquiries into financial sustainability in local government. Chapter 2 ends with some brief concluding remarks in section 2.5.

2.2 Municipal Mergers in Australian Local Government

Structural reform through compulsory council consolidation has been a ubiquitous policy instrument in local government reform since Federation in 1902 (see, for instance, Dollery and Grant 2011; Grant, Dollery and Crase 2009; Marshall 2008; Dollery, Byrnes and Crase 2008; Dollery and Fleming 2006; Aulich 2005; Byrnes and Dollery 2002; Aulich 1999; Vince 1997). Table 2.1 provides a synoptic 'snapshot' of the magnitude of compulsory consolidation through local council numbers over time:

Table 2.1: Number of local councils in Australia, 1910-2012

	1910	1967	1982	1990	1995	2008	2012
NSW	324	224	175	176	177	152	152
VIC	206	210	211	210	184	79	79
QLD	164	131	134	134	125	73	73
SA	175	142	127	n/a	119	68	68
WA	147	144	138	138	144	142	139
TAS	51	49	49	46	29	29	29
NT	0	1	6	22	63	16	16
TOTAL	**1,067**	**901**	**840**	**726**	**841**	**559**	**556**

Source: DLG [NSW] (2013); DPCD [VIC] (2013); DLGCR&R [QLD] (2013); LGA [SA] 2013; DLG [WA] (2013); DPC [TAS] (2013); DLG [NTG] (2013).

Table 2.1 has several notable features:

- The total number of local authorities in Australia has decreased from 1,067 to 556 (a fall of 48 per cent) between 1910 and 2012.
- The only exception to this trend occurred in the NT, where the number of councils substantially increased from 22 in 1990 to 63 in 1995.
- The timing of municipal merger programs has been uneven across state and territory jurisdictions. For instance, major mergers occurred in NSW in the period between 1967 and 1982 (a reduction from 224 to 175 councils), whereas an analogous amalgamation program occurred in Tasmania over the period 1990 to 1995 (a reduction from 46 to 29 councils). In Victoria, a period of major structural reform took place during the period 1995 to 2007 (a reduction from 184 to 79 councils). In Queensland, major consolidation was implemented in 2007 (a reduction from 125 to 73 councils) and in the NT in 2008 (a reduction from 63 to 16 councils). This distinct lack of uniformity in timing suggests that amalgamation processes are independent of both national economic conditions

and public policy trends at the national level, despite a general bias towards centralisation in the Australian federation (see, for example, Moore 1997).

It should be stressed that these episodes of compulsory consolidation have occurred despite long term population growth in Australia, where average council size – defined as the number of residents per council – has increased markedly. For example, Table 2.2 shows that the average council size for each state and territory jurisdiction (excluding the ACT which has no local government system) has increased between 1910 and 2012. Perhaps one of the most striking features of Table 2.2 is that the average size of councils nationally has grown from 4,147 persons per council to 40,118 persons per council between 1910 and 2012.

Moreover, as shown in Figure 2.1, it is clear that the most populous jurisdictions have, on average, larger councils. For instance, in 2012 the average size of municipalities in Victoria (71,183 persons per council), Queensland (62,467 persons per council) and NSW (47,963 persons per council) lay above the national average of 40,118 persons per council, while the average size of councils in SA (24,335 person per council), WA (17,484 person per council), Tasmania (17,666 person per council) and the NT (14,677 person per council) fall well below the national average.

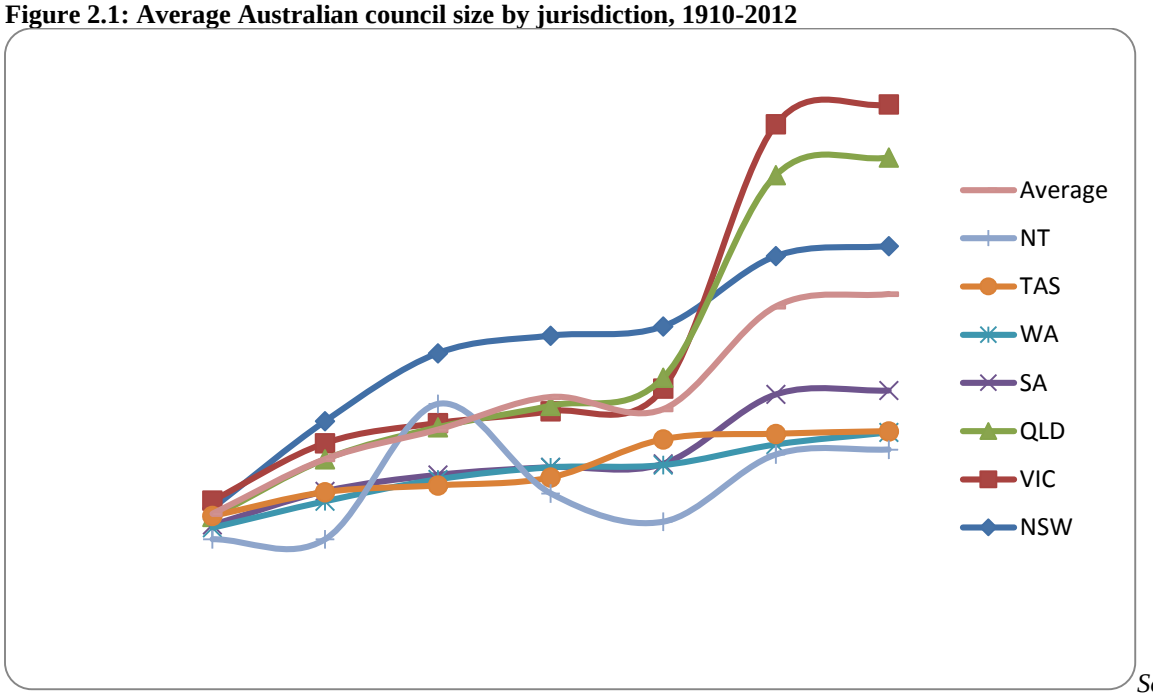
Table 2.2: Average Australian council size by jurisdiction, 1910-2012

	1910			**1967**			**1982**			**1990**			**1995**			**2008**			**2012**		
	Pop	Councils	Pop/Councils	Pop.	Councils	Pop/Councils	Pop	Councils	Pop/Councils	Pop.	Councils	Pop/Councils	Pop	Councils	Pop/Councils	Pop	Councils	Pop/Councils	Pop	Councils	Pop/Councils
NSW	1,643,855	324	5,074	4,329,913	224	19,330	5,328,221	175	30,445	5,862,497	176	33,310	6,168,820	177	34,852	7,041,393	152	46,325	7,290,345	152	47,963
VIC	1,301,408	206	6,318	3,303,606	210	15,731	4,012,687	211	19,017	4,400,707	210	20,956	4,539,796	184	24,673	5,364,796	79	67,909	5,623,492	79	71,183
QLD	599,016	164	3,653	1,715,803	131	13,098	2,456,475	134	18,332	2,928,713	134	21,856	3,303,352	125	26,429	4,349,529	73	59,583	4,560,059	73	62,467
SA	410,169	175	2,344	1,115,926	142	7,859	1,337,783	127	10,534	1,438,882	122	11,794	1,471,245	119	12,363	1,612,002	68	23,706	1,654,778	68	24,335
WA	276,832	147	1,883	896,988	144	6,229	1,354,971	138	9,819	1,624,390	138	11,775	1,749,319	144	12,148	2,204,040	142	15,521	2,430,252	139	17,484
TAS	193,803	51	3,800	377,841	49	7,711	430,974	49	8,795	464,520	46	10,098	474,136	29	16,350	500,278	29	17,251	512,019	29	17,666
NT				64,399		64,399	132,784	6	22,131	165,047	22	7,502	180,479	63	2,865	221,682	16	13,855	234,836	16	14,677
Total /**mean**	4,425,083	1067	**4,147**	11,804,476	901	**13,102**	15,053,895	840	**17,921**	16,884,756	726	**23,257**	17,887,147	841	**21,269**	21,293,720	559	**38,093**	22,305,781	556	**40,118**

Source: Table 2.1 (above) and ABS (2007; 2012).

Note: Population figures do not include population for Australian Capital Territory (ACT) since the ACT has no system of local government.

Figure 2.1: Average Australian council size by jurisdiction, 1910-2012



Source: Source: Table 2.2 (above) and ABS (2007; 2012).
Note: Population figures do not include population for Australian Capital Territory (ACT) since the ACT has no system of local government.

In the amalgamation debate, it is also important to consider Australian local government in international perspective. How does the average size of Australian councils compare with other advanced countries? Table 2.3 sheds light on this question by providing an international comparison of average council size in 2007. Of the 18 countries listed in Table 2.3, the Britain has the largest councils with an average of 143,000 persons per council, whereas France has the smallest councils with an average of 1,500 persons per council. Relative to other OECD nations, Australia has the fourth largest councils with an average of 40,118 persons per council. Put differently, Australian councils are already large by the standards of other advanced countries.

Table 2.3: An international comparison of average council size, 2007

Rank	Country	Number of councils	Average council size*
1	Britain	415	143,000
2	Denmark	98	55,500
3	New Zealand	85	49,000
4	**Australia**	**556**	**40,118**
5	Japan	3,200	39,943
6	Netherlands	441	37,000
7	Portugal	308	34,500
8	Ireland	140	32,050
9	Sweden	290	31,500
10	Belgium	589	18,000
11	Poland	2,793	13,500
12	Finland	416	12,500
13	Canada	3,752	9,000
14	Germany	12,340	6,500
15	United States	71,343	4,000
16	Austria	2,357	3,500
17	Switzerland	2,758	2,500
18	France	36,783	1,500

Source: Adapted from Callanan, Murphy and Quinlivan (2012)
*Number of persons per council

However, the national local government systems listed in Table 2.3 cover a broad range of types of local government arrangements, embracing European systems (Britain, Ireland, France, Germany, Belgium, Switzerland, Austria, Netherlands and Poland), including two from the Nordic zone (Finland and Denmark), as well as federal countries outside of Europe, such as Australia, Canada and the United States, together with unitary states (Japan and New Zealand). There is thus a high degree of functional and other differentiation in the local government systems contained in Table 2.3. Various academic commentators, including Stoker (2010) and Mouritzen and Svara (2002), have pointed out that local government size is not an absolute

measure, but rather a relative measure, if we take into account the functions performed by local authorities

2.3 Empirical Evidence on Impact of Amalgamation

Most empirical work on the impact of amalgamation has been conducted on American local government. Extensive summaries of this work have been provided by Leland and Thurmaier (2006; 2010), Faulk and Hicks (2011) and Faulk and Grassmueck (2012). In general, American researchers have found that mergers have not met expectations in terms of efficiency gains and cost savings. For example, in an assessment of empirical work on whether consolidation produced greater efficiency, Feiock (2004) concluded that mergers had not met their intended economic objectives, but had rather led to increased expenditures. Similarly, in their review of the impact of city-county consolidation programs, Martin and Schiff (2011) found little evidence that municipal consolidation enhanced performance, through either improved service provision or reduced costs for delivering the same services. Leland and Thurmaier (2010) examined nine case studies of amalgamated and comparable unmerged local authorities and concluded that efficiency gains are not a predictable consequence of amalgamation.

These general conclusions have been echoed in the Canadian empirical literature. For instance, in her analysis of Ottawa amalgamations, Reese (2004) noted that remuneration levels increased in the post- merger period, resulting in a net rise in overall council expenditure. In a similar vein, Vojnovic (2000) examined the short-term effects of consolidation among five Canadian councils and found that aggregate costs increased in three of the five local councils.

Scholars have also examined the consequences of local government amalgamation in a number of European countries. For example, contributors to Dollery and Robotti (2008) considered council mergers in France, Germany, Italy and Spain and concluded that amalgamation had not achieved its intended effects. Moreover, in a Special Edition of *Local Government Studies* on European amalgamation programs, Swianiewicz and Mielczarek (2010) drew a similar conclusion with respect to Eastern Europe, Vrangbæk (2010) found much the same with the 2007/09 Danish merger program, Wollmann (2010) concurred in his analysis of the German amalgamation, Hlepas (2010) was scathing in his evaluation of the 1998 and 2008/09 Greek program, and Kreci and Ymeri (2010) drew bleak conclusions from the Macedonian experience. In their analysis of local government reform in Belgium and the Netherlands, De Ceuninck et al. (2010) concluded that council mergers had not met expectations.

The bulk of Australian evidence on the outcomes of amalgamation programs in state and territory local government systems derives largely from public inquiries into local government. As we shall see in section 2.4, a host of recent inquiries into municipal financial sustainability has established that numerous councils in all local government jurisdictions still face daunting financial problems, despite amalgamation. In the light of these findings, Dollery, Byrnes and Crase (2007; 2008) have argued that compulsory merger programs have not only failed as a 'silver bullet' for solving systemic financial and other problems in Australian local government, but have also not provided a coordinated regional dimension to local service provision.

In addition to these public inquiries, some empirical work on Australian amalgamation programs has been considered in the academic literature, as well as in consultant reports, although largely of a descriptive nature. In *Councils in Cooperation*, Dollery, Grant and Kortt (2012) provided a detailed evaluation of this work. With some exceptions, such as Soul's (2000) empirical analysis of council size and per capita service costs in NSW, and *Consolidation in Local Government* (2011), the scholarly literature is pessimistic on the efficacy of amalgamation as a means of improving local government efficiency.

In contrast to the marked emphasis the Australian academic literature has placed on a descriptive approach to the assessment of amalgamation through the case studies and the like, a new strand of the Australian literature has focused on empirical investigations using state-wide data. For example, Drew, Kortt and Dollery (2013) critically examined the empirical evidence adduced in favour of radical amalgamation of Tasmanian local authorities in *Local Government Structural Reform in Tasmania*, produced by Deloitte Access Economics (DAE) (2011), and commissioned by the Property Council of Tasmania. They found that if the DAE model is re-estimated – employing alternative functional forms – then the empirical evidence in support of Tasmania council merges evaporates.

Similarly, Drew, Kortt and Dollery (2012) examined whether scale economies exist in local government outlays by analysing the expenditure of 152 NSW councils. When the correlation between population and population density was taken into account, areas are decomposed into subgroups on the basis of density, there is no evidence of scale economies. In Chapter 3 of this

Report, we will examine in detail the outcomes of the 2004 NSW council amalgamation program and the 2008 forced mergers in Queensland.

2.4 Evaluation of Australian Municipal Merger Programs

Over the past two decades Australian local government has been exhaustively evaluated by a series of national and state-based public inquiries, largely focused on municipal financial sustainability. At the national level, the Commonwealth Grants Commission's (CGC) (2001) *Review of the Operation of Local Government (Financial Assistance) Act 1995*, the House of Representatives Standing Committee on Economics, Finance and Public Administration ('Hawker Report') (2004) *Rates and Taxes: A Fair Share for Responsible Local Government*, the PWC (2006) *National Financial Sustainability Study of Local Government* and the Productivity Commission's (PC) (2008) *Assessing Local Government Revenue Raising Capacity* all examined aspects of the financial problems plaguing Australian local government.

At the state level, the South Australian Financial Sustainability Review Board's (FSRB) (2005) *Rising to the Challenge Report*, the Financial Sustainability of NSW Local Government ('Allan Report') (2006) *Are Councils Sustainable?*, the Local Government Association of Queensland (LGAQ) (2006) *Size, Shape and Sustainability* Inquiry, the Western Australian Local Government Association (WALGA) (2006) *Systemic Sustainability Study*, the Local Government Association of Tasmania (LGAT) (2007) *Review of the Financial Sustainability of Local Government in Tasmania*, the Queensland Local Government Reform Commission (QLGRC) (2007) *Report of the Local Government Reform Commission*, and the Queensland Treasury

Corporation (QTC) (2008) *Financial Sustainability in Queensland Local Government* all investigated dimensions of financial viability in their respective state local government systems.

While the overwhelming emphasis in most of these public inquiries fell squarely on financial sustainability in local government, many inquiry reports considered the impact of policies designed to improve the operation of local government and its financial viability, including structural reform through forced amalgamation. We now examine the findings of the public inquiries on the efficacy of compulsory consolidation in chronological order.

2.4.1 Hawker Inquiry (2003)

A striking feature of the Hawker Report (2003) *Rates and Taxes* lay in its sweeping nature. Although originally designed to investigate cost-shifting, its terms of reference were extended to include almost all other aspects of local government (Dollery, 2005). Chapter 5 of *Rates and Taxes* assessed structural reform in terms of 'amalgamations' and 'regional cooperation and resource sharing'. The Hawker Report (2003, p.84) set out two kinds of 'efficiencies gained by amalgamations':

- As a general rule, large councils had a 'more secure and adequate financial base, are better able to plan and contribute to economic development, are more effective community advocates, and interact more effectively with government and business'. In addition, 'structural reform can deliver economies of scale and can enable councils to employ a wider range of professionals so they can offer a wider range and usually higher quality of services'.

- Amalgamations yielded ‘savings’ as evidenced in the South Australian and Victorian amalgamation episodes, Western Australian projections that structural reform of small councils could produce ‘notional annual savings’ of a total of $74.4 million or 5.2 per cent of total municipal expenditure and sizeable ‘savings projections’ from five New South Wales mergers.

However, this was followed by an appraisal of ‘why amalgamations may not work’. Three arguments were advanced (Hawker Report, 2003, p.89):

- The ‘multitude of challenges’ confronting ‘small rural councils’ often mean that ‘amalgamations are not viable’.
- Merger was not a panacea; other structural solutions involving ‘mentoring with a larger more prosperous council’ or ‘membership of a regional organization of councils’ are superior.
- ‘Continued cost shifting’ by state governments diminished the efficiency enhancing effects of compulsory consolidation.

The Hawker Report (2003, p.90) put forward two main recommendations:

- Recommendation 13 held that ‘the Commonwealth Grants Commission, in consultation with the LGGCs [Local Government Grants Commissions] in each State, assess the efficiencies of amalgamations or regional cooperation of local government, and use available mechanisms to adjust FAGs [Financial Assistance Grants] for the benefit of the

sector at large'. To promote mergers, 'councils should not be financially penalized through a net loss of FAGs for the benefit of the sector at large'.

- Recommendation 14 held that the Commonwealth 'continue to develop partnership arrangements with local government on the delivery of Federal programs and service delivery; and as appropriate, engage established regional organizations of councils, or similar regional bodies, which have demonstrated capacity, in regional planning and service delivery'.

2.4.2 South Australian Financial Sustainability Review Board (FSRB) (2005)

While the focus of the FSRB (2005) fell squarely on the definition, measurement and assessment of 'financial sustainability', it also considered council size, drawing various conclusions on compulsory amalgamation. The FSRB established that 'there is no strong relationship between a council's organisational size and either a strong financial position or a good annual financial performance' (FSRB, 2005, p.49). Furthermore, 'the size and density of councils played little role in explaining the observed differences in the sustainability of the long-term financial performance and position of councils'. The *Final Report* concluded that 'because relative growth rates, size and density of councils altogether explain only a fraction of the differences observed in the sustainability of the long-term financial performance and position of councils, other financial characteristics must be more important contributors'.

The FSRB (2005, p.85) also assessed the claims made by the SA Local Government Boundary Review Board in the lead up to its structural reform program which decreased the number of local authorities from 118 to 68 after 1995, forecasting 'recurrent savings' of $19.4 million per

annum and ‘one-off savings’ of $3.9 million. The FSRB (2005, p.85) found that ‘whether the ongoing savings have in fact continued is a moot point’ since ‘fewer, larger councils are not the instant or easy fix that many would like to believe’, particularly in ‘non-metropolitan areas dominated by the “tyranny of distance” and other impediments’.

In sum, the FSRB (2005, p.85) concluded that ‘amalgamation brings with it considerable costs and often exaggerated benefits’. Alternative models of council cooperation should thus be pursued instead, since there are ‘many intermediate forms of cooperation/integration among councils, with amalgamation being the most extreme (and confronting) form of integration’. The FSRB (2005, p.85) then considered the most promising alternative options and found that numerous ‘voluntary arrangements’ in shared services and joint enterprise had proved successful in the South Australia.

2.4.3 Financial Sustainability of NSW Local Government (‘Allan Report’) (2006)

In common with the bulk of the public inquiries into local government, the Allan Report (2006) in NSW concentrated mainly on fiscal viability. However, Chapter 10 of *Are Councils Sustainable?* examined the putative relationship between council size and council efficiency which frequently underpinned arguments for amalgamation. The *Final Report* observed that ‘past local government amalgamations were based on the primary rationale that larger councils with larger populations could exhibit greater economic efficiencies’ because bigger local authorities would exhibit ‘lower administrative costs, smaller unit costs of representation, increased purchasing power, improved utilization of depots, plant and equipment and draw from a more diverse funding base’ (Allan Report, 2006, pp.259-60). Moreover, the Report (2006,

p.261) observed that uncertainty existed ‘as to whether such a concept has a sound empirical basis’. It concluded that ‘achieving increased economies of scale and greater efficiencies through forcible amalgamation seems questionable and generally not desirable from a local government or community perspective’.

2.4.4 Queensland Size, Shape and Sustainability (SSS) Program (2006)

Chapter 4 of the *Size, Shape and Sustainability: Guidelines Kit* (LGAQ, 2006, pp.4-5) considered alternative forms of structural reform in Queensland local government. It proposed four different ‘option for change’: ‘Merger/amalgamation’; ‘significant boundary change’; ‘resource sharing through service agreements’; and ‘resource sharing thorough joint enterprise’. Chapter 4 examined the ‘advantages’ and ‘disadvantages’ of each of these options. With respect to amalgamation, it argued that the benefits which can flow from council amalgamation could include a ‘sufficient resource base’, a reduction in the ‘total costs of government’, scale economies, lower staff levels, an ‘opportunity to review’ operations, rationalization of assets, ‘cross-border’ facility and service utilization, better promotion of economic development, improved growth management, the ‘formalization’ of communities of interest, increased political lobbying power, and potential for ‘full-time’ elected representatives. However, potential costs embraced ‘exposure’ to liabilities of other local authorities, addressing ‘major difference in rates’, fewer grants, high costs of ‘integrating’ constituent councils, dealing with ‘widely differing organisational cultures’, creating ‘differing levels of service in some areas’, diluting existing representation, and the loss of direct representation by ‘small areas’. In addition, Chapter 4 stressed the importance of the ‘voluntary’ nature of any amalgamation proposal to its ultimate success.

2.4.5 Western Australian Systematic Sustainability Study (2006)

While the bulk of the Western Australian (WA) *Systematic Sustainability Study* (2006) (the 'Report') was devoted to financial sustainability, council mergers were also considered. Chapter 8 of the Report considered council consolidation as part of the broader range of alternative models of service delivery. The WA Local Government Association (WALGA) (2006) argued that a 'state/territory' model and an 'industry-owned service provider' which delivered selected services on a regional basis for member councils represented the most promising options. With respect to council amalgamations, the Report noted that 'there was little prospect that forced amalgamations would achieve any lasting community benefit' on grounds that 'there is a growing literature and operating experience to this effect elsewhere in Australia' (WALGA, 2006, p.70). In short, WALGA (2006) argued that the main benefits which purportedly derived from amalgamation 'can be obtained by methods other than enforced structural reform'.

2.4.6 PriceWaterhouseCoopers (PWC) Report (2006)

Although the major emphasis in the PWC (2006) *National Financial Sustainability Study of Local Government* fell on local government financial sustainability, it nonetheless considered structural reform. PWC (2006) drew four main conclusions on compulsory council consolidation:

- With respect to state-based inquiry findings on council mergers, PWC (2006, p.15-16) observed that while 'the sustainability report undertaken in SA indicated that sustainability may be more linked to policy skills rather than size, evidence from other

states indicates that scale, and implicitly size, does assist in improving sustainability'. Moreover, this 'divergence in results is largely due to the majority of SA being an unincorporated zone, which would minimise the incidence of rural councils that cover large areas with a small population base and limited opportunities for economies of scale'. However, scale economies could best be achieved through 'regional or shared service provision, outsourcing, and use of state-wide purchasing agreements'.

- PWC (2006, p.72) noted that whereas 'structural reform through amalgamations is necessary in some instances, each potential amalgamation needs to be assessed carefully to avoid the risk of simply creating large inefficient councils'. Moreover, it also emphasized that 'remote councils' faced 'higher cost structures' largely due to the 'tyranny of distance', which amalgamation could not alter.
- In section 2.6.2 of its report, PWC (2006, p.75) considered the net impact of Australian municipal merger programs. It concluded that 'mergers can bring greater financial strength and stability to councils, however, simply merging a number of adjoining unviable councils is unlikely to increase financial sustainability to the stage where there is a single viable council and it may decrease effectiveness and result in greater disputes between councillors based on parochial interests'.
- In its formal recommendations, PWC (2006, p.149) held that 'efficiency, effectiveness and scale' could be enhanced by means of regional service provision, shared service arrangements, outsourcing, state-wide purchasing initiatives, and similar initiatives, rather than through compulsory council amalgamation.

2.4.7 Local Government Association of Tasmania (LGAT) (2007)

In common with most other inquiries, LGAT (2007) was focused on financial sustainability. However, in section 6.3 of its report, LGAT (2007, p.65) considered structural reform through mergers and argued that 'forced amalgamations have limited prospects for achieving lasting community benefit'. Furthermore, whereas small local authorities typically 'lack administrative and technical capacity compared with larger councils' and 'council amalgamations will generate a greater range of services and improved quality of service', LGAT insisted that the 'main benefits of amalgamation can usually be obtained by methods other than enforced structural reform', most often 'resource sharing and pool-style arrangements'. Following WALGA (2006), LGAT (2007, p.68) recommended that local government in Tasmania should explore the introduction of a 'state/territory' model comprising a 'two-tier local and regional government' providing some services at local level and others at the regional, level with elected arrangements in place for both systems. In addition, 'sector-owned service providers' should be investigated, where these entities could be 'specially established sector entities', single councils operating under contract to other local authorities, private sector providers, LGAT or a regional council.

2.4.8 Queensland Local Government Reform Commission (2007)

The specific council amalgamation recommendations of the Queensland Reform Commission (2007) were set out in detail in its *Report of the Local Government Reform Commission*. However, this report provided little justification for the structural reform process. The rationale for the radical program of forced amalgamation was set out by the Queensland Department of Local Government, Planning, Sport and Recreation (DLGPS&R) (2007) in its *Local Government*

Reform: A New Chapter for Local Government in Queensland (Dollery, Wallis and Crase, 2007). This document argued that the motivation for local government reform in Queensland was 'not unique to Queensland'. Moreover, it had four main strands: (a) the need to address the 'medium to long-term sustainability' in local government; (b) the 'need for greater collaboration in infrastructure and regional planning'; (c) the need for local councils in Queensland to avoid their current 'internally focused parochial mindset' and consider instead the 'bigger picture'; and (d) the need to reduce the 'inconsistency of performance and service delivery across the local government sector' (DLGPS&R, 2007, p.11).

Invoking PWC (2006), it was argued that 'large numbers of Australian local councils were 'non-sustainable', with severe local infrastructure backlogs. These problems were 'typically more acute in smaller councils', particularly in 'rural or remote areas'. Drawing on the financial analysis by the QTC as at March 2007, it noted that 43% of councils fell in the 'weak' or below categories. Section 2.4 of *Local Government Reform* emphasised that financial assistance provided to local councils in Queensland by higher tiers of government in terms of per capita grants was the highest in Australia at $88.50. In Chapter 4, the DLGPS&R (2007, p.39) underlined the problem of securing administrative and technical staff and the impact of this on small non-metropolitan councils. It postulated that 'large councils with greater financial resources would be significantly better placed to establish robust regionally-based employment frameworks'. Finally, Chapter 5 considered structural reform programs in New Zealand, the Northern Territory, South Australia, Tasmania and Victoria. It concluded that these had been generally successful.

2.5 Concluding Remarks

Chapter 2 of this Report has sought to consider the efficacy of compulsory council consolidation as a means of improving financial viability in Australian local government through the prism provided by eight national and state-based public inquiries into financial sustainability in local government. Given the ubiquity of forced amalgamation in the Australian milieu, the most interesting feature of the deliberations of these inquiries on the question of structural change resides in the fact that they echo scepticism in the academic literature on compulsory council consolidation. Indeed, the weight of opinion in the public inquiries suggests that the traditional Australian stress on council mergers has been seriously misplaced.

While it is true that the Hawker Report (2003) conceded that structural reform could deliver scale economies and amalgamations had evinced savings, mergers were not a 'panacea'. It recommended that Commonwealth Grant's Commission methodology should be adjusted to accommodate amalgamation, but called for partnership arrangements with local government through regional organisations of councils and other regional bodies. The FSRB (2005) disputed empirically purported relationships between council size and council performance, as well as questioning claims advanced on the savings generated by amalgamation. It concluded that alternative models of council cooperation should be pursued. The Allan Report (2006) also found that population density – and not population size – represented the dominant component in council cost structures. It recommended that policy instruments other than amalgamation should be employed. Whereas the LGAQ (2006) noted that some benefits could flow from council mergers, it pointed to high costs, and concluded that only voluntary amalgamation held promise.

WALGA (2006) rejected the efficacy of consolidation and argued that state/territory and industry-owned service provider models were more suitable to WA conditions. In its formal recommendations, PWC (2006, p.149) argued that efficiency, effectiveness and scale could best be improved through regional service provision, shared service arrangements, outsourcing, and state-wide purchasing initiatives, rather than by means of council mergers. LGAT (2007) held that forced amalgamations were unlikely to achieve lasting benefits and it recommended resource sharing and 'pool-style arrangements', such as state/territory models and sector-owned service providers. In contrast to these other inquiries, the DLGPS&R (2007) presented strong arguments in favour of amalgamation, stressing the greater financial resources available to bigger post-amalgamation councils.

However, a serious shortcoming of these inquiry reports, which is also reflected in the empirical academic literature, is a lack of sophisticated econometric modelling of previous forced merger episodes. Fortunately, an embryonic Australian empirical literature has done some analysis of this question. In Chapter 3 of this Report we consider in detail analyses of two forced amalgamation programs: (a) the 2004 NSW compulsory council consolidation program and (b) the 2008 Queensland forced amalgamation program.

CHAPTER 3: EMPIRICAL ASSESSMENT OF THE 2000/2004 NSW MERGER PROGRAM AND THE 2008 QUEENSLAND MERGER PROGRAM

Chapter Summary

- An empirical analysis of the 2000/2004 NSW council amalgamations shows no difference in the performance of merged and unmerged councils using the *Fit for the Future* criteria.
- An empirical analysis of the 2008 Queensland amalgamations shows that most amalgamated councils now operate under diseconomies of scale.
- Taken together, this provides a convincing empirical case against proceeding with a further round of municipal mergers in NSW in 2015.

3.1 Introduction

Despite the fact that municipal mergers are mired in ongoing controversy, with little support in the empirical literature (see, for instance, *Public Finance and Management*, Special Editions, 13(2) and 13(3), 2013), Australian local government policymakers continue to use forced amalgamation as a major policy instrument. Indeed, over the past two decades, compulsory council consolidation programs have been conducted in every Australian state and territory, with the sole exception of Western Australia, where the Barnett Government recently unsuccessfully attempted to impose mergers on Perth metropolitan councils.

Australian forced amalgamation programs follow a common pattern (Dollery, Grant and Kortt, 2012). In the first instance, a newly-elected state government typically complains publically of

general council inefficiency and its ostensible lack of fiscal viability and then launches 'independent' inquiry to examine methods of improving local government. After a period of deliberation, the inquiry usually publishes a discussion paper(s), an interim report and a final report, which almost invariably recommends forced mergers. After perfunctory period of 'public consultation', the proposed mergers proceed, despite widespread public opposition.

Once forced amalgamation has taken place, a common pattern is also evident (Dollery, Grant and Kortt, 2012). Ongoing public discontent with council consolidation characteristically continues, often for years, which occasionally results in de-amalgamation (see, for example, De Souza, Dollery and Kortt, 2014). Furthermore, no public reporting of the costs of mergers to affected councils or their local communities occurs, state governments do not undertake assessments of merger outcomes, and no improvement in the operational efficiency or financial viability of merged local authorities is observed. After period of years, the cycle begins again.

As we have seen in Chapter 1, the current NSW local government process closely approximates this pattern. The NSW Government initiated an inquiry into NSW local government led by the Independent Panel immediately after its *Destination 2036* Workshop in Dubbo in August 2011. The Panel published its preliminary thinking in *Better Stronger Local Government: The Case for Sustainable Change* in November 2012, followed by an interim report *Future Directions for NSW Local Government* in April 2013, which recommended drastic council mergers. Its final report *Revitalising Local Government* which was submitted in October 2013, but only made public early in 2014. In common with *Future Directions, Revitalising Local Government* claimed that council consolidation was vital for improving NSW local government, although it softened

Future Directions hard-line stance on forced mergers by recommending a strengthened Boundaries Commission consider its proposed council amalgamations on a 'case-by-case; basis and make binding recommendations. The NSW Government's *Fit for the Future* program has subsequently adopted the Panel's merger recommendations with alacrity and the process is now underway.

A significant problem with both the recommendations of the Panel and the subsequent embrace of its merger proposals in *Fit for the Future* resides in the absence of supporting empirical evidence for council amalgamation in NSW. Indeed, as we have seen in Chapter 2 of this Report, the weight of both the scholarly literature and public inquiries into local government runs strongly against the efficacy of municipal mergers as an instrument of local government reform.

Despite repeated assurances by the Panel that it would adhere to 'evidence-based' policymaking, such as its claim in *Revitalizing Local Government* (2013, p.7) that its approach to municipal mergers 'has been evidence-based and pragmatic, not ideological', the Panel barely bothered to assess the outcomes of the 2004 NSW forced amalgamation program conducted by the Carr Government. However, with respect to the outcomes of the 2004 amalgamation program, all the Panel actually did was engage the South Australian commercial consultants Jeff Tate Consulting Pty Ltd to conduct a cursory assessment of five merged councils, without even calling for a comparative study of merged and unmerged councils using published official data. As we shall see in Chapter 3, it is thus not at all surprising that the Panel blithely proceeded to recommend council mergers with little knowledge of the effects of amalgamation on councils merged in 2004.

Much the same is true for the 2008 Queensland forced amalgamation program. In 2007 the Queensland Government imposed forced amalgamation with the number of local authorities falling drastically from 157 to just 73 councils. Amalgamation was justified *inter alia* on the assumption that increased economies of scale would generate savings. The failure of the Queensland compulsory council consolidation program to achieve its intended aims should surely have alerted the Independent Panel and the authors of the *Fit for the Future* program to the plethora of problems plaguing forced amalgamation, not to mention the subsequent cases of de-amalgamation.

The purpose of Chapter 3 is twofold:

- In the first place, we empirically assess the performance of municipalities merged in NSW over the period 200/2004 NSW in an effort to determine quantitatively the relative impact of amalgamation on council performance using official data.
- Secondly, we present the findings of the most comprehensive empirical evaluation of the 2008 Queensland amalgamation program yet undertaken.

The NSW amalgamations executed over the period 2000 to 2004 and the 2008 Queensland amalgamations are particularly relevant to the *Fit for the Future* regime. The former merger program is relevant because it occurred in the same jurisdiction as the mergers proposed under *Fit for the Future*, although the different combination of councils was rather complex resulting in limited opportunities to make direct comparisons. By way of contrast, the Queensland

amalgamation episode involved (a) lower levels of boundary complexity, (b) resulted from a single radical program of forced amalgamations consistent with the *Fit for the Future* regime and (c) allow for robust comparisons owing to the wealth of financial and contextual data available to investigators.

The analysis of these two municipal merger programs generates information which would have proved most helpful to NSW policymakers weighing up the likely effects of municipal mergers on council performance. Had thorough empirical analyses been conducted by the Independent Panel, it is highly unlikely that the Panel would have prescribed further municipal mergers in NSW.

Chapter 3 is divided into three main parts. Section 3.2 deals with the NSW mergers over the period 2000 to 2004. Section 3.2.1 provides a critical account of the analysis of the 2004 NSW local government merger program conducted by Jeff Tate Consulting Pty Ltd (2013) for the Independent Panel, which focused on an unrepresentative sample of only five amalgamated entities and involved no quantitative assessment of post-merger performance with unmerged councils. Section 3.2.2 provides an empirical analysis of the 2000/2004 NSW council mergers. Section 3.3 contains an empirical evaluation of the 2008 Queensland forced amalgamation program. Chapter 3 ends in section 3.4 by drawing some policy lessons for the current *Fit for the Future* NSW from the two earlier amalgamation episodes.

3.2 Assessment of 2000/2004 Council Mergers in New South Wales

3.2.1 Jeff Tate Consulting Pty Ltd Analysis

The Panel provided Jeff Tate Consulting Pty Ltd (2013, p.1) with the following terms of engagement:

- 'Review relevant research into the processes and outcomes of Council amalgamations in NSW and other states over the last 20 years;
- Identify relevant findings from the research to inform an assessment of the processes and outcomes of a sample of recent (2004) amalgamations in NSW;
- Assess the processes and outcomes of a sample of five Council amalgamations that occurred in 2004, considering the following matters:
  - whether each amalgamation has produced positive outcomes;
  - the circumstances, process and/or scale of change required for amalgamations to produce positive outcomes;
  - how significant and lasting the costs and disruption associated with amalgamations were, relative to any benefits;
  - the lessons that can be learned for managing implementation of any future amalgamations or major boundary changes;
  - the lessons that can be learned in terms of barriers and incentives for voluntary or 'guided' boundary changes;

- Prepare a report summarising findings from each case study and an overall report for the Panel, taking into consideration its terms of reference'.

Against this background, it should be noted that the 2004 NSW municipal merger program resulted in a fall in the number of local authorities from 174 to 152 entities. A thorough evaluation of the 22 merged entities would have compared their subsequent performance with unmerged councils falling in the same local government classification categories using official NSW local government data, especially the annual *Comparative Information on Local Government Councils*, which contains comparative data by council across a range of indicators. However, so acute was the lack of rigour in the Panel's terms of engagement surrounding the sample of councils, Jeff Tate Consulting Pty Ltd (2013, p.2) was simply instructed to examine the following five councils:

- 'Clarence Valley Council (amalgamation);
- Glen Innes Severn Council (amalgamation);
- Palerang Council (amalgamation and associated boundary changes);
- Greater Hume Shire (amalgamation and associated boundary changes); and
- City of Albury (boundary changes associated with the Greater Hume Shire amalgamation)'.

No explanation was advanced in Jeff Tate Consulting Pty Ltd.'s final report *Assessing processes and outcomes of the 2004 Local Government boundary changes in NSW* (2013) or in any of the Panel's published documents to account for the basis on which these five local authorities were

selected or on how reflective they were of the total population of merged municipalities in NSW. In addition, the discursive 'research technique' employed by Jeff Tate Consulting Pty Ltd (2013, p.22) was not only entirely qualitative, but also suffered severely from 'selection bias' as attested by the fact that the people 'interviewed' were drawn from the new post-amalgamation entities and thus most unlikely to criticise the process which had spawned their current positions:

> 'Over 50 people were interviewed either individually or in groups for the case studies of the five Councils selected by the Independent Review Panel. The Council representatives included Mayors, Deputy Mayors, Councillors, General Managers, Directors, middle managers and other staff who had either been through the amalgamation or boundary change process or who have been closely involved since in implementing the new structures and systems'.

Given the absence of rigour in its report *Assessing processes and outcomes of the 2004 Local Government boundary changes in NSW*, it is thus not at all surprising that Jeff Tate Consulting Pty Ltd (2013, p.40) was only able to draw highly imprecise conclusions which can hardly inform policymaking:

> 'The research and interviews both confirm that the costs associated with amalgamation are often underestimated. Poor planning and implementation processes combined with legal, industrial and Proclamation restrictions have increased costs, extended the negative impacts associated with amalgamations and hampered the achievement of positive outcomes…However, the 2004 amalgamations have achieved many positive outcomes

despite the restrictions and poor planning and implementation. The positive outcomes include improvements in infrastructure and service delivery, the capacity to tackle larger and more complex projects and issues, greater ability to access external funding, the capacity to speak with a unified voice on behalf of local communities and improved opportunities for staff of Councils'.

3.2.2 Analysis of 2000/2004 NSW Amalgamations

Table 1 provides details of the ten general purpose councils which were subject to amalgamation over the period from 2000 to 2004. Because most of the amalgamations involved the dismembering of constituent councils, many of the empirical evaluations possible for Queensland cannot be performed for this cohort of municipalities. However, we can gauge the success of the merger program by examining and comparing the performance of the cohort of general purpose amalgamated entities against (a) all councils in the jurisdiction and (b) a group of peers selected according to the NSW Office of Local Government classification system.

Table 3.1: NSW General Purpose Councils Merged over 200/2004

Amalgamated Council	Date	Constituent Councils
Albury	26 May 2004	Albury and Hume (part)
Armidale-Dumaresq	21 February 2000	Armidale and Dumaresq
Bathurst	26 May 2004	Bathurst and Evans (part)
Lithgow	26 May 2004	Lithgow, Evans (part), Rylstone (part)
Clarence Valley	25 February 2004	Copmanhurst, Grafton City, Maclean, Pristine Waters
Goulburn-Mulwaree	11 February 2004	Goulburn, Mulwaree (part)
Mid-Western Regional	26 May 2004	Merriwa (part), Mudgee, Rylstone (part)
Queanbeyan	11 February 2004	Queanbeyan, Yarrowlumla (part)
Richmond Valley	21 February 2000	Casino, Richmond River
Tamworth	17 March 2004	Barraba (part), Manilla, Nundle (part), Parry (part), Tamworth

Table 3.2 compares the Financial Sustainability Rating (FSR) of the ten general purpose NSW councils with the FSR for the entire NSW local government system. This comparison clearly demonstrates that the FSR assigned to the two cohorts by TCorp (2013) do not suggest any material difference in performance between the ten general purpose councils which experienced forced amalgamation and the rest of the NSW councils. In fact, the ten general purpose councils under consideration had a higher proportion of sub-standard performance (i.e., 'very weak' and 'weak') than the rest of NSW councils. By way of contrast, the remaining NSW municipalities had a slightly higher proportion of councils exhibiting acceptable levels of performance (i.e., 'moderate', 'sound', and 'strong'). Given the lofty claims made by proponents of municipal reform it is somewhat surprising that the performance of the ten general purpose councils amalgamated in earlier programs is slightly lower than the remainder of the jurisdiction. This data suggests that the 2000-2004 amalgamations may not have been as successful its architects had hoped.

Table 3.2: Comparison of Financial Sustainability Ratings

TCorp (2013) Financial Sustainability Rating	Amalgamated Councils	Rest of Jurisdiction
Very Weak	0	3.5%
Weak	30%	21.8%
Moderate	50%	52%
Sound	20%	21.1%
Strong	0	1.4%
Very Strong	0	0
Total	10	142

A more nuanced result is possible by comparing the individual financial ratio indicators over the three year period in the *Fit for the Future* assessments. In Chapter 3, four of the *Fit for the Future* ratios are defined and employed in exactly the same way as prescribed by the OLG

(2014): Operating Performance, Own Source Revenue, Building and Infrastructure Renewal, and Asset Maintenance ratios.

However, we examined the Infrastructure Backlog ratio over three years instead of one (as per the OLG Council Toolkit 2015) owing to existing evidence of significant 'gaming' by councils on this data (see Chapter 4 in this Report). The debt ratio has been dropped entirely owing to the logical flaws in the method adopted by the OLG (2014), which incidentally was in direct contradiction to the advice provided to them by the experts which the OLG had previously commissioned to measure financial sustainability (TCorp, 2013).

We have also altered the expenditure per capita ratio to reflect the functional unit most appropriate to municipal service provision (i.e. households) (see Chapter 4 of this Report). Finally, we have included a measure of staffing ratios which – in the absence of more sophisticated data envelopment analysis – is necessary for an elementary understanding of municipal efficiency (although we stress that this is an empirical compromise required by our efforts to conform to the OLG model).

Table 3.3 details the various ratios of the amalgamated cohort (previously set out in Table 3.1) and the fourteen councils which represent the peer group according to OLG classification. A cursory examination of the data suggests that there is very little difference in the performance of the amalgamated cohort with respect to the peer group (which is consistent with our examination of FSR detailed in Table 3.2).

Table 3.3: Comparison of Fit for the Future Performance

	Operating Performance Ratio			Own Source Revenue Ratio			Employees per Household			Expense per Household		
	2014	**2013**	**2012**	**2014**	**2013**	**2012**	**2014**	**2013**	**2012**	**2014**	**2013**	**2012**
Amalgamated												
Quartile 1	-11.3%	-10.0%	-11.4%	69.6%	67.0%	60.7%	23.6	23.1	23.7	5,263	5,457	5,535
Median	-7.5%	-5.3%	-4.4%	74.6%	71.8%	65.4%	24.3	24.7	24.9	5,451	5,700	5,717
Quartile 3	-6.4%	-1.5%	-3.0%	78.8%	74.9%	73.1%	25.8	26.3	26.3	5,713	5,884	6,341
Non-Amalgamated												
Quartile 1	-11.1%	-7.7%	-14.8%	73.9%	67.7%	62.3%	21.7	21.9	22.0	5295	5316	5368
Median	-7.3%	-4.9%	-1.4%	76.7%	69.2%	72.5%	24.9	24.5	24.6	5624	6088	5693
Quartile 3	-3.6%	2.5%	2.3%	78.6%	76.5%	75.0%	27.8	28.0	27.0	6366	6629	6532

	Building & Infrastructure Renewal Ratio			Infrastructure Backlog Ratio			Asset Maintenance Ratio		
	2014	**2013**	**2012**	**2014**	**2013**	**2012**	**2014**	**2013**	**2012**
Amalgamated									
Quartile 1	64.4%	42.5%	32.8%	0.04	0.05	0.05	0.85	0.77	0.63
Median	73.0%	55.9%	51.8%	0.07	0.06	0.12	0.94	0.90	0.95
Quartile 3	81.7%	91.3%	93.4%	0.11	0.11	0.19	1.03	1.09	0.99
Non-Amalgamated									
Quartile 1	39.6%	33.4%	36.5%	0.01	0.02	0.02	0.68	0.74	0.71
Median	57.5%	60.0%	62.8%	0.06	0.07	0.05	0.85	0.88	0.80
Quartile 3	73.7%	106.8%	82.7%	0.08	0.10	0.11	0.95	1.00	1.00

However, a superior way of evaluating whether there is a real difference in performance between the two cohorts is to conduct an analysis of variance (ANOVA). An ANOVA compares the spread of the various financial ratios of individual councils within cohorts (amalgamated and non-amalgamated peers) to the spread of the same financial ratio between cohorts and thus provides a robust statistical test to determine whether there are statistically important differences between the financial ratios of the two cohorts.

Table 3.4: ANOVA of 2014 Fit for the Future Indicators

	Amalgamated	Non-Amalgamated	Differences
Operating Performance Ratio	-0.07 (0.059)	-0.099 (0.116)	No statistically significant difference
Own Source Revenue Ratio	0.744 (0.063)	0.749 (0.073)	No statistically significant difference
Employees per Household	25.016 (3.836)	25.093 (4.401)	No statistically significant difference
Expense per Household	5563.34 (555.23)	5827.50 (698.52)	No statistically significant difference
Building & Infrastructure Renewal Ratio	0.765 (0.293)	0.602 (0.399)	No statistically significant difference
Infrastructure Backlog Ratio	0.084 (0.064)	0.061 (0.060)	No statistically significant difference
Asset Maintenance Ratio	0.947 (0.201)	0.820 (0.175)	No statistically significant difference

The standard deviations in parentheses in Table 3.4 provide an indication of the average variation in each financial ratio of individual councils to the mean financial ratio within the particular cohort. Somewhat predictably Table 3.4 – which details the ANOVA results – finds no statistically significant difference between the two cohorts for each and every one of the seven financial ratios. It should be noted that ANOVA deals with the possibility of sampling error and other statistical noise. What this means is that there is absolutely no empirical basis for supposing that the performance of the amalgamated cohort is in any way superior to their peers. It is worth stressing that this is an 'inconvenient' result for proponents of amalgamation, based on sustainability criteria.

Had the Independent Panel approached the question of the outcomes of the 2004 NSW mergers in a technically competent manner, as we have demonstrated in Chapter 3, instead of instructing Jeff Tate Consulting Pty Ltd to use a biased and unrepresentative five council sample, then it would have discovered that the earlier 2000/2004 council mergers did not produce local

authorities exhibiting superior performance as measured using *Fit for the Future* FSR. This would surely have given both the Panel and the NSW Government pause for thought on the desirability of yet more costly council mergers.

3.3 Assessment of 2008 Council Mergers in Queensland

The Queensland amalgamations occurred in 2008 and involved a reduction in the number of councils from 157 to just 73. Apart from similarities relating to the radical scale of reform, the Queensland mergers also shared a number of other aspects with *Fit for the Future*:

(a) The amalgamation proposals were created in haste with no publicly available empirical analysis to support the contentions of the Local Government Reform Commission (LGRC);

(b) The merger recommendations involved a significant degree of political subterfuge, notably the alleged 'independence' of the inquiry;

(c) The council consolidation proposals used highly optimistic predictions of economies of scale whilst neglecting the possibility of scale diseconomies; and

(d) The amalgamation proposals entirely ignored the weight of scholarly evidence on the likely success of municipal boundary reform through compulsory council consolidation (see, for instance, Dollery, Ho and Alin 2008; Dollery, Wallis and Crase 2007).

Given these commonalities, it is instructive to examine the lack of success realised by the Queensland forced mergers, particularly given that the TCorp (2013) financial sustainability ratios bear uncanny similarity to the Queensland Treasury Corporation financial sustainability

assessments utilised by the Commission in forming their recommendations for the Queensland councils (LGRC, 2007, p42).

Drew, Kortt and Dollery (2015) interrogated the financial data of Queensland councils pre- and post-amalgamation to determine whether the radical merger program in fact reaped the economies of scale promised by the LGRC. Table 3.5 details the measures of central tendency for the variables used in the regression analysis. They concluded that the municipal merger program actually resulted in a greater proportion of councils exhibiting diseconomies of scale arising from amalgamations (see Table 3.6 empirical results) which created entities which were simply too large to be run efficiently:

> 'Eight percent of councils in 2006/07 (ten councils) -representing 64% of the state's population - exhibited diseconomies of scale. For the 2009/10 data, the average cost curve remained almost stationary at 99,000 residents per council, but almost 25% of all councils (thirteen councils) were now found to exhibit diseconomies of scale. The compulsory merger program thus increased the proportion of Queensland residents in councils operating with diseconomies of scale to 84%.'

This finding lies in stark contrast to the claims made by the Queensland Reform Commission prior to the amalgamations. Moreover, when the data was categorised according to functional expenditure (roads, waste and parks), it was established that only one of the categories (parks) exhibited any evidence of economies of scale (see Table 3.7). Given that parks expenditure represented only around 5% of total Queensland municipal spending, this suggests that the most

effective public policy response would have been to concentrate on shared service arrangements rather than expensive, disruptive and divisive forced amalgamations. Finally, Drew, Kortt and Dollery (2015) noted the following outcomes three years on from the mergers:

- An increase in real operating expenditure (excluding the effects of inflation) in the order of 4.7% p.a.
- An increase in real council rates (excluding inflation) of 3.1% p.a.
- An increase in council rates of 4.9% p.a. (excluding inflation).

Taken as a whole this suggests that, far from the earlier claims of leaner more efficient local authorities, the Queensland forced mergers actually produced more expensive local government funded in part by higher municipal rates and fees. It is thus impossible to argue that this episode of municipal amalgamation was a success. This is particularly troubling given the similarities between the Queensland amalgamations and the proposed *Fit for the Future* mergers.

Table 3.5: Definitions and Means of Variables (2006/07 n=114; 2009/10 n=57)

Variable	Definition	Mean 2006/07	Mean 2009/10
Expenditure			
Total expenditure	Log of total per capita expenditure	7.59	8.07
Road expenditure	Log of road expenditure per capita	6.31	6.49
Waste expenditure	Log of waste expenditure per capita	3.69	4.05
Parks expenditure	Log of parks expenditure per capita	4.19	4.48
Demographic			
Population	Log of population	8.86	9.51
Population squared	Log of population squared	81.35	95.01
Population density	Population divided by council area (in km^2)	55.34	42.75
Population growth	Four year average population growth	0.01	0.04
Exogenous Controls			
Ha. of agriculture/1000	Hectares of agricultural land divided by 1000	1234.4	2541.36
Average wage	Average wage of taxable individuals	$35,048	$51,092
UnN%	Percentage of individuals unemployed	4.78	6.25
ATSI%	Percentage of ATSI individuals	7.06	10.43
NESB%	Percentage of NESB individuals	3.07	3.74
Urban Roads (km)	Distance of urban roads in kilometres	737.81	472.58
Rural Roads (km)	Distance of rural roads in kilometres	1147.15	2174.05
Adults (over 65)%	Percentage of individuals aged over 65	12.04	12.95
Children (under 15)%	Percentage of persons under 15 years of age	21.67	20.86

Table 3.6: Relationship between Queensland Council Expenditure and Population before and after Mergers

	2006/07	2009/10
Population (ln)	-1.641**	-2.101**
	(0.272)	(0.358)
Population squared (ln)	0.071**	0.091**
	(0.016)	(0.020)
Density		
Population growth	-1.620	0.610
	(2.170)	(0.760)
Control variables	Yes	Yes
N	114	57
R^2	0.92	0.95

Standard errors in parentheses.
+ p<0.10, * p<0.05, ** p<0.01
Note: Regression Model 2 controls for hectares of agricultural land, average wage, unemployment rate, ATSI and NESB rates, proportion of the population over 65 and under 15, and the kilometres of urban and rural roads.

Table 3.7: Type of QLD Council Expenditure and Population size before and after Mergers

	2006/07			2009/10		
	Roads	*Waste*	*Parks*	*Roads*	*Waste*	*Parks*
Population (ln)	-1.095	0.162	-2.383**	0.137	-0.335	-3.687**
	(1.128)	(0.615)	(0.539)	(0.897)	(0.556)	(0.757)
Population squared (ln)	0.042	-0.028	0.128**	-0.039	0.018	0.220**
	(0.067)	(0.036)	(0.032)	(0.050)	(0.031)	(0.042)
Density	-0.001	0.000	-0.000	0.001	0.000	-0.004*
	(0.001)	(0.000)	(0.000)	(0.002)	(0.001)	(0.002)
Population growth	5.054	-0.293	-2.551	-0.553	-1.393	2.813+
	(8.997)	(4.983)	(4.345)	(1.961)	(1.215)	(1.654)
Control variables	Yes	Yes	Yes	Yes	Yes	Yes
N	105	105	101	57	57	57
R^2	0.57	0.43	0.68	0.72	0.67	0.86

Standard errors in parentheses.
+ p<0.10, * p<0.05, ** p<0.01
Note: Regression Model 2 controls for hectares of agricultural land, average wage, unemployment rate, ATSI and NESB rates, proportion of the population over 65 and under 15, and the kilometres of urban and rural roads.

3.3.1 DEA Scale Estimates

A significant reason for the failure of municipal mergers is that they often result in municipal entities which are too large and operate with concomitant diseconomies of scale. Multiple regression analysis, such as the analysis conducted by Drew, Kortt and Dollery (2015) discussed above, can provide an estimate of the optimal scale on the basis of a single proxy for municipal output. This is a relevant technique given that merger architects generally cache recommendations in terms of a single functional unit (in the case of both the Queensland and NSW reforms the functional unit used was population).

However, no one proxy can accurately represent the entire set of outputs generated by councils and this is particularly evident when one considers the diversity of services provided by local authorities. Most services in the local government milieu relate specifically to property (either business or residential), such as rubbish collection, development applications, water and

sewerage provision (where applicable).[1] In addition, the highest single category of functional expenditure relates to municipal road construction and maintenance (PricewaterhouseCoopers, 2007), typically representing over a quarter of operating expenditure. Moreover, road infrastructure costs bear little association to measures of scale approximated by population or the number of households and businesses. Hence it is reasonable to contend that a much more accurate representation of municipal output would be made by consideration of the number of households, number of employing businesses and length of council maintained roads.[2]

Data envelopment analysis (DEA) is the most appropriate empirical technique for the estimation of municipal efficiency and scale on the basis of multiple proxies for council output. It measures the relative technical efficiency of individual councils with respect to the conversion of inputs (staff and capital) into outputs (number of households, businesses and length of municipal roads).

In addition to its ability to consider multiple outputs, DEA has a number of advantages over other techniques, such as multiple regression analysis:

[1] It is acknowledged that population may be associated with some services provided directly to individuals, such as library services. However, consideration of both population and households distorts the production frontier by effectively double counting (and hence implicitly weighting) certain services. Moreover, population data are estimates in inter-censal periods subject to significant error and volatility (see Drew, Kortt and Dollery (2015) for a thorough examination of DEA specification error).

[2] This is the preferred output specification adopted by Drew, Kortt and Dollery (2015) in a recent publication which specifically addresses the effect of alternate specification on municipal data envelopment analysis.

- Firstly, it provides point estimates of relative scale based on a consideration of the interactions of all inputs and outputs, rather than a simple population threshold above which diseconomies may occur. This means that analysts can obtain efficiency and scale estimates specific to each council or group of councils.
- Secondly, DEA is non-parametric rather than requiring *a priori* knowledge of a certain functional form, which means that there is little chance of spurious results arising from unknown or unknowable interactions between variables.

In common with Cooper, Seiford and Tone (2007) and Drew, Kortt and Dollery (2015), we estimated:

(a) The scale of the extant cohort of Queensland councils prior to the amalgamations.

(b) The scale of Queensland municipal entities subsequent to the amalgamations.

The analysis is based on 2007 financial year data which was the last full period of financial statements prior to the mergers.

Table 3.8 details the results arising from analysis of Queensland councils prior to amalgamation[3]. Looking at the entire state we can see that a significant proportion of the councils (just over 37%) were operating with large decreasing returns to scale[4] (DRS) prior to

[3] Results exclude Aboriginal and Torres Strait Islander land councils.
[4] Optimal scale is set at 1. The greater the difference between the scale estimate and 1, the greater the degree of DRS or IRS. For instance a council with DRS of 0.4 is far more over scale than a council with a DRS of 0.9. We present the mean (average) and median scale estimate as alternate measures of the typical scale of Queensland councils.

the amalgamation. However, there were also approximately 56% of Queensland councils which were under-scale immediately before the boundary reform. Similar proportions of scale are also apparent amongst the councils scheduled for amalgamation. Clearly this suggests that the Queensland reforms were unlikely to yield positive results given that just over a third of the councils scheduled for merger were already inefficient due to being over scale. Moreover, it is entirely possible that combinations of councils with increasing returns to scale (IRS) could in fact result in a merged DRS council.

Table 3.8: Scale Results – Pre-Amalgamation 2007

Amalgamation status	Scale	Number	Mean scale	Median scale	Stand. Dev.
Entire State	OS	8	1	1	0
	IRS	69	0.788	0.839	0.194
	DRS	46	0.837	0.862	0.125
Councils to be Amalgamated					
	OS	8	1	1	0
	IRS	56	0.8036471	0.850625	0.1918306
	DRS	33	0.831551	0.842058	0.0149962

Notes: OS = optimal scale; IRS = increasing returns to scale; DRS = decreasing returns to scale.

Table 3.9 details the scale results arising from DEA of 2007 financial year data based on the post-amalgamation structure of Queensland councils. We focus on the scale estimates for the merged councils which arose from the reform program. Of the 31 entities created by the Queensland municipal reforms, we can see that just over 58% exhibited decreasing returns to scale. This means that over half of the councils created by the LGRC were too large and exhibited inefficient service provision directly as a result of being over-scaled. This result is consistent with the evidence provided by Drew, Kortt and Dollery (2014), but is a more nuanced result since it is based on multiple outputs.

Table 3.9: Scale Results – Post-Amalgamation 2007

Amalgamation status	Scale	Number	Mean scale	Median scale	Stand. Dev.
Amalgamated	OS	2	1	1	0
	IRS	11	0.947	0.975	0.070
	DRS	18	0.889	0.934	0.123
Non-amalgamated Councils	OS	3	1	1	0
	IRS	20	0.691	0.780	0.231
	DRS	3	0.897	0.924	0.065

Notes: OS = optimal scale; IRS = increasing returns to scale; DRS = decreasing returns to scale.

3.3.2. Efficiency of Queensland Councils over Time

Seiford, Cooper and Tone (2007) also propose a technique which can be used to measure the technical efficiency of councils over time. This technique has been applied numerous times in the scholarly literature, including notable contributions by Halkos and Tzeremes (2008, 2009) and Asmild, Paradi, Aggarwall and Schaffnit (2004). It overcomes a limitation of DEA arising from its construction of relative efficiency based on its use of a static efficient frontier formed by peers, which means that cross-sections of DEA cannot otherwise be compared (because they relate to a specific frontier in a particular year). In essence, locally intertemporal DEA (or windows analysis) examines several analyses of indexed data which spans more than one period of time. A moving average is then created for the efficiency scores of each council, which allows for a seamless evaluation of technical efficiency over time.

Figure 3.1 is a graphical representation of the average efficiency over time for the two cohorts of interest in the evaluation of the success of the Queensland mergers. Figure 3.2 is a graphical representation of the alternate measure of typical performance (median) of Queensland councils over the same period.

Figures 3.1 and 3.2 show that (a) efficiency decreased for both cohorts by a significant degree in the period leading up to the mergers and that (b) a negligible difference in the mean efficiency of the two cohorts existed at the start of the amalgamation period. However, since that time the efficiency of the Non-Amalgamated cohort has increased markedly (by both measures of central tendency), whilst the efficiency of the Amalgamated cohort has in fact decreased. Moreover, the gap in performance between the two cohorts is startling and provides clear evidence that the mergers resulted in typically less efficient councils in Queensland.

Figure 3.1: Mean Efficiency of Queensland Councils, 2004-2013

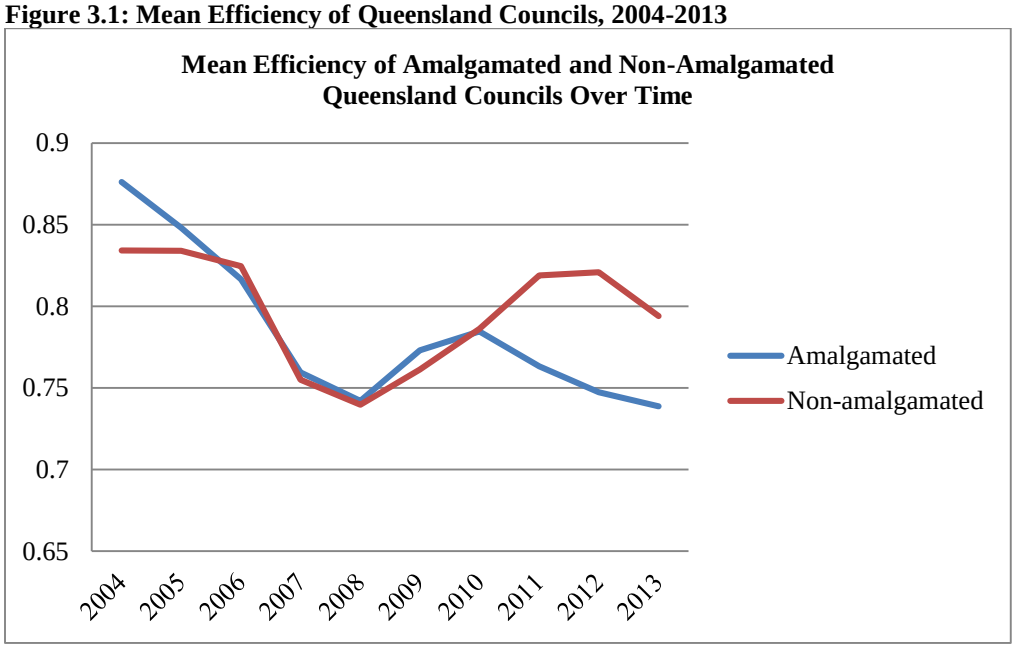


Figure 3.2: Median Efficiency of Queensland Councils, 2004-2013

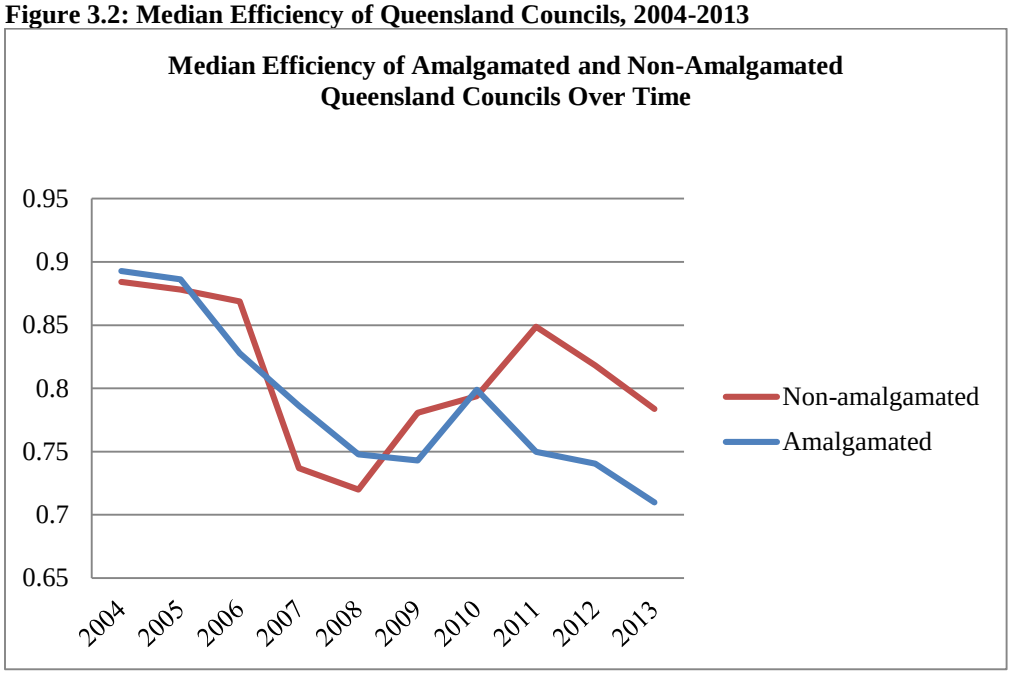
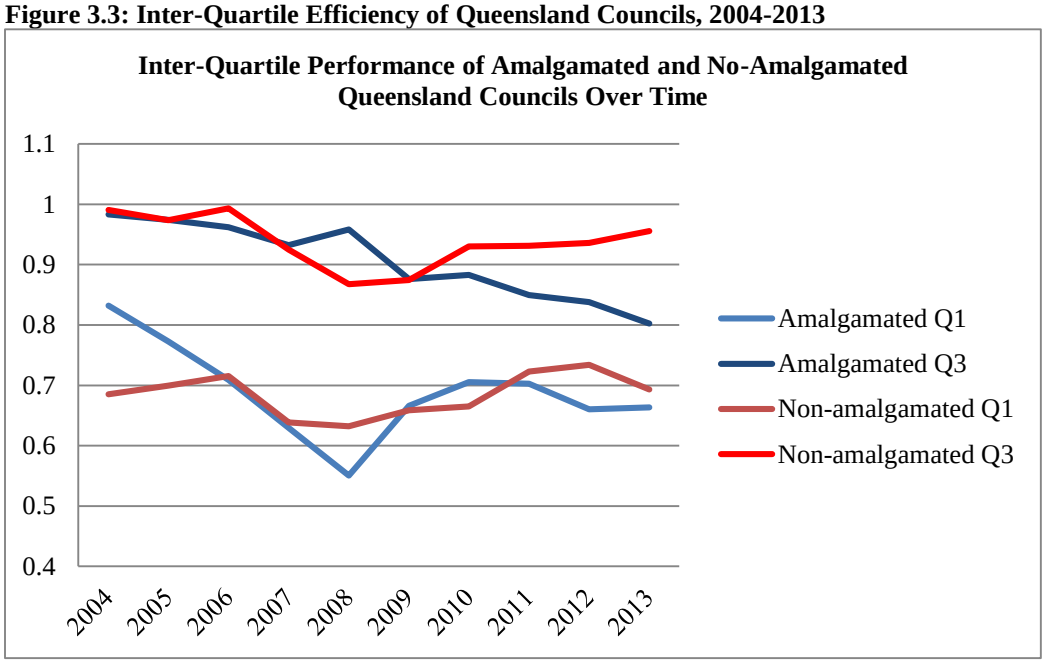


Figure 3.3: Inter-Quartile Efficiency of Queensland Councils, 2004-2013



Finally, Figure 3.3 presents graphical evidence of the efficiency of the top quartile (Q3) and lower quartile (Q1) for the Amalgamated and Non-Amalgamated cohorts. This shows clearly what has happened over the period since the amalgamations: the highest quartile of amalgamated

councils has experienced a marked decrease in efficiency, whilst the lowest quartile of amalgamated councils has improved somewhat, although it still lags behind the performance of Non-Amalgamated councils on this measure.

In essence, forced amalgamation has significantly diminished the performance of the most efficient councils, but has improved the performance of the worst performers. However, we need to be mindful that the typical performance - as measured by either the mean or median – of amalgamated councils is far lower than that of their Non-Amalgamated peers.

3.3.3 Post-Merger De-Amalgamation in Queensland

As we have seen, the empirical analysis presented in Chapter 3 demonstrates that the Queensland forced mergers represented a stunning failure of public policymaking. Moreover, many local residents clearly understood this even without the benefit of the empirical analysis presented in Chapter 3. Thus, after five years of ongoing public agitation and a change of state government, in a landslide win based in part on a promise to allow residents a vote on de-amalgamation, simmering anger over forced amalgamations resulted in four of the entities formed in the 2008 amalgamations receiving approval for de-amalgamation following the municipal referenda conducted in March 2013. In total, nineteen communities petitioned to be de-amalgamated, but only five of the petitions were put to the Boundaries Commissioner and only four de-amalgamation proposals were allowed to proceed to the referendum phase.

In a review of the earlier de-amalgamation of Delatite Shire (in Victoria) Drew and Dollery (2015, p.19) noted that:

> Consonant with Oates' (1999) Decentralism Theorem there seems to be a good case to suggest that boundary reform should focus on creating municipalities with as little heterogeneity as possible. Where this does not occur, then it is quite possible that residents from at least one of the former pre-merged entities will perceive a loss in welfare in at least one public service. The degree of diversity between pre-merged entities may predict the likelihood of subsequent de-amalgamation activism – motivation for de-amalgamation could be predicted to be proportional to loss in welfare which in turn is a function of the degree of homogeneity within and heterogeneity between pre-merged municipalities. It is also clear that subsequent de-amalgamation is promoted by having new municipalities constructed by whole portions of previous local government entities and providing even numbers of democratic representatives from previous entities.

It would appear that in most cases the NSW Independent Panel merger recommendations have failed to take note of this important finding. Most of the mergers involve whole entities and it is likely that the eventual political representatives from these former entities will vote as a block as per the experience in both Victorian and Canadian local government (see, for example, Spicer, 2012), thereby creating unstable and unproductive council representation.

Moreover the ILGRP (2013) recommended mergers have lumped together disparate groups of local residents, basically guaranteeing a loss in economic welfare (see Chapter 7 of this Report). This suggests that de-amalgamation is also a real possibility should the *Fit for the Future* program proceed, particularly given that, in common with Queensland, NSW residents have not been given a political voice on council mergers via referenda. Furthermore, the NSW Government has not campaigned for and received a mandate on municipal mergers. Indeed, the NSW Government studiously avoided any mention of local government amalgamation during the election campaign. This prepares the ground for de-mergers.

However, de-amalgamation is not inexpensive. In addition to bearing the original amalgamation costs, where the mean cost for Queensland was $8.108 million, the break-away councils were also required to wear the cost involved in returning to their former stand-alone state (Drew and Dollery 2014). For example, in the case of Noosa Council the Queensland Treasury Corporation estimated this cost to be $13.6 million, although it should be noted that the residual council (Sunshine Coast Regional Council) estimated the cost at just over $23 million (Drew and Dollery 2014).

Thus, excessive haste and poor public policymaking mean that the residents of the four Queensland councils so far de-amalgamated have incurred an entirely unnecessary and avoidable expense in the order of $20 million (considering both amalgamation and subsequent de-amalgamation costs).

3.4 Lessons for NSW Local Government Reform

A number of lessons can clearly be drawn from the empirical analysis of the 2000/2004 NSW mergers and the 2008 Queensland amalgamation process for NSW local government policymakers:

- Amalgamation proposals must be based on rigorous empirical analysis rather than preconceived ideological presumptions concerning council size and council performance.
- Policymakers must appreciate that optimal economies of scale are often unattainable and may only exist for a limited range of functional expenditure outlays (which can in any event be captured more effectively through shared service arrangements).
- Ill-conceived council mergers can create councils which are too large and thus operate with diseconomies of scale, as in Queensland.
- Well-developed empirical techniques exist to allow policymakers to determine whether proposed merged councils will operate efficiently.
- The financial sustainability assessments undertaken by the Queensland LGRC were seriously flawed.
- It is a thus a mistake to use the same flawed LGRC financial sustainability approach to inform the New South Wales *Fit for the Future* Program on council viability.
- Both the Independent Panel and the New South Wales *Fit for the Future* Program erred in ignoring the weight scholarly evidence on the efficacy of municipal amalgamation as a reform instrument.

- As Queensland mergers have has illustrated, poorly designed local government amalgamation could result in subsequent de-amalgamation.
- Local communities should be given a political voice in decisions regarding municipal boundary changes.
- Amalgamating heterogeneous communities results in a loss of economic welfare and encourages de-amalgamation campaigns.
- The real cost of misconceived public policy on local government created in haste and without regard to empirical evidence is borne by the community.

It is unfortunately evident that most of these lessons from the 2000/2004 NSW and 2008 Queensland amalgamation episodes have been neglected by the architects of the *Fit for the Future* program. If decisive action is not taken to mitigate these problems, then it is difficult to see how costly policy errors can be avoided in NSW. Chapter 4 now examines the specific problems associated with the OLG implementation of the *Fit for the Future* program.

CHAPTER 4: EVALUATION OF THE *FIT FOR THE FUTURE* PROGRAM

Chapter Summary

- A critical assessment of the *Fit for the Future* process found that it is flawed in a number of respects: (i) its arbitrary use of financial sustainability ratios; (ii) its problematic 'scale and capacity' approach; (iii) unreliable data employed in sustainability assessments; and (iv) an incorrect measure employed to assess the operational efficiency of councils.
- The NSW Office of Local Government should thus to halt the *Fit for the Future* process and solve these problems before proceeding with the reform program.

4.1 Introduction

As we have seen in Chapter 1 of this Report, the proposed municipal mergers in the Greater Sydney region, including the Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby amalgamation, derive from the recommendations of the Independent Panel which have largely been endorsed in the NSW Government's *Fit for the Future* program. Chapter 4 provides a critical assessment of the *Fit for the Future* process which demonstrates conclusively that it is seriously flawed in a number of respects.

Chapter 4 is divided into five main parts. Section 4.2 considers the multitude of problems which have arisen in the *Fit for the Future* criteria for evaluating councils which have derived from arbitrary and often illogical selection of financial sustainability ratios (FSRs) and the associated benchmark values and changes which have been made. Section 4.3 considers 'scale and

capacity' in *Fit for the Future* and demonstrates severe problems in its approach. Section 4.4 examines the deleterious effects that the use of unreliable data for sustainability assessments has had. Section 4.5 demonstrates that the OLG has employed an erroneous approach to the assessment of efficiency in local government which has serious adverse consequences. Chapter 4 ends with some brief reflections in section 4.6.

4.2 Shifting Goal Posts: Ratios and Thresholds

In its *Financial Sustainability of the NSW Local Government Sector*, TCorp (2013) summarised a total of ten financial ratios into a single financial sustainability rating (FSR) according to the weights detailed in Table 4.1. These FSRs and ratios were adopted without reservation by the ILGRP (2013a; 2013b) and formed the basis for a number of recommendations relating to financial sustainability of the sector, including potential municipal mergers. The (then) Division of Local Government NSW (now the OLG) also adopted the FSRs without reservation in both the 2011/12 and 2012/13 *Comparative Information on NSW Local Government* annual reports, although it only included seven of the TCorp financial sustainability ratios. Table 4.1 contains definitions of TCorp (2013) financial ratios and Table 4.2 provides details regarding how financial ratios have been subsequently adopted and altered.

Table 4.1: Definitions, Benchmarks and Weightings of TCorp Financial Sustainability Ratios

Variable	Weighting	Benchmark	Definition
Dependent			
Operating ratio	17.5%	>-4%	(Operating revenue † - Operating expenses) / Operating revenue †.
Own Source Revenue ratio	17.5%	>60%	Rates, utilities and charges / total operating revenue ‡.
Unrestricted Current ratio	10.0%	>1.50x	Current assets less restrictions / current liabilities less specific purpose liabilities.
Interest Cover ratio	2.5%	>4.00x	EBITDA / interest expense.
Infrastructure Backlog ratio	10.0%	<0.02x	Estimated cost to bring assets to a satisfactory condition / total infrastructure assets.
Debt Service Cover ratio	7.5%	>2.00x	EBITDA / (principal repayments + borrowing costs).
Capital Expenditure ratio	10.0%	>1.10x	Annual capital expenditure / annual depreciation.
Cash Expense ratio	10.0%	>3.0 months	(Current cash and equivalents / (total expenses - depreciation - interest costs)) x 12.
Buildings and Infrastructure Renewal ratio	7.5%	>1.00x	Asset renewals / depreciation of building and infrastructure assets.
Asset Maintenance ratio	7.5%	>1.00x	Actual asset maintenance / required asset maintenance.

† Revenue excludes capital grants and contributions
‡ Revenue includes capital grants and contributions

Table 4.2: Changes in Financial Sustainability Measures for NSW Local Government

Financial Ratio	TCorp Weighting	Comparative Information Report 2012/13	TCorp Threshold	Fit For The Future
Operating ratio	17.5%	Reported	>-4%	>0.0% over 3 years
Own Source	17.5%	Reported	>60%	>60% over 3 years
Cash Expense	10.0%	Reported	>3.0 months	Abandoned
Unrestricted Current	10.0%	Reported	>1.5	Abandoned
Debt Service	7.5%	Reported	>2.0	0 to 20% over 3 years[5]
Interest Cover	2.5%	Not reported	>4.0	Abandoned
Infrastructure backlog	10.0%	Reported	<0.02	<2% (unchanged) over just one year
Asset Maintenance	7.5%	Not reported	>1	>100% (unchanged) over 3 years
Building and Infrastructure Renewal	7.5%	Reported	>1	>100% (unchanged) over 3 years
Capital Expenditure	10.0%	Not reported	>1.1	Abandoned
Real Operating Expenditure per Capita	n/a	Reported in nominal terms only according to 8 functional categories	Not considered	No time or threshold in documentation

Source: TCorp (2013); Office of Local Government (2014a), Office of Local Government (2014b)

However, it appears that the OLG has shifted its position on municipal performance indicators. As we can see from Table 4.2, in its *Becoming Fit for the Future* (OLG 2014b) four of the TCorp FSR ratios have been abandoned, the time horizon for five of the remaining six ratios has been extended, thresholds for two ratios have been significantly revised, ratio weightings have been omitted, a new ratio has been added, and crucially all ratios have been subordinated under the concept of 'adequate scale and capacity'.

It is possible that the FSR assessments, Capital Expenditure and Cash Expense ratios were abandoned in response to scathing assessments, such as Drew and Dollery (2014a; 2014b), regarding lack of transparency, logical flaws and the corrosive effects of unreliable accrual data

[5] It is important to note that the OLG has radically altered the definition of this ratio.

on these measures of municipal performance. On the other hand, relinquishing the remaining two ratios appears to be a pragmatic response to the near universal achievement of the respective thresholds: in 2011 only twelve councils failed to meet the unrestricted current ratio, whilst just eight councils failed to achieve the benchmark for the Interest Cover ratio. It is noteworthy that the four omitted ratios had a combined weighting of 32.5% in the original TCorp (2013) FSR.

The second policy shift – involving an extension of the measurement time horizon for five of the six remaining ratios – is a positive initiative which will ameliorate some of the volatility associated with using annual financial statement data. However, there is substantial risk of 'gaming', given that 2013 and 2014 financial year report data is used, since these reports were compiled after the March 2013 TCorp Financial Assessments and April 2013 ILGRP report. The opportunities for gaming include depreciation accruals (Pilcher and Van der Zahn 2010; Drew and Dollery 2014b) and estimates on required maintenance and the cost to bring assets to a satisfactory standard contained in Special Schedule 7 and 8. Table 4.3 details the gaming that has occurred on depreciation, estimated cost to bring assets to a satisfactory standard and required annual maintenance estimates (the latter two being derived from Schedule 7).

To produce the estimates of unexpected financial statement items, we followed the general approach of Marquardt and Wiedman (2004) developed from the earlier work of Hribar and Collins (2002) and Mulford and Comiskey (2002). This approach is also consistent with the work of Pilcher and Van der Zahn (2010). In essence, we compared the quantum of the three financial statement items in the 2012/13 and 2013/14 financial statements, making adjustments for changes to the asset base or asset maintenance and renewal.

Table 4.3: Descriptive Statistics for Unexpected Financial Statement Items, 2013/14 Financial Year

Financial Statement Element	Smallest	Largest	Q1	Median	Q3
Entire NSW					
Depreciation	-70.5%	113.1%	-6.3%	0.2%	4.9%
Cost to Bring to Satisfactory Standard	-124.5%	462.8%	-48.6%	-13.5%	8.4%
Required Annual Maintenance	-151.6%	950%	-48.8%	-11.4%	14.1%
Greater Sydney					
Depreciation	-70.5%	27.7%	-6.5%	2.0%	7.1%
Cost to Bring to Satisfactory Standard	-124.5%	345.6%	-36.7%	-9.0%	9.7%
Required Annual Maintenance	-127.1%	723.3%	-29.4%	1.4%	32.9%
Outside Greater Sydney					
Depreciation	-65.5%	113.1%	-6.0%	-0.1%	3.8%
Cost to Bring to Satisfactory Standard	-102.6%	462.8%	-49.9%	-13.7%	8.2%
Required Annual Maintenance	-151.6%	950%	-51.3%	-13.3%	6.8%

Table 4.3 clearly demonstrates that a great deal of gaming has occurred, particularly in the unaudited schedule 7 items, where the typical (median) unexplained change to estimates is a reduction in excess of 10%. Moreover, the Q1 results demonstrate that a quarter of councils have reduced their estimates of the cost to bring assets to a satisfactory standard and required annual maintenance by almost half! It is clear that many local authorities may have manipulated data to enhance their *Fit for the Future* assessments and this is particularly concerning for the case of the Infrastructure Backlog ratio, which the OLG have decided to assess on the basis of a single year. As Bevan and Hood (2006, p.533) have noted, 'complete specification of targets and how performance will be measured almost invites reactive gaming by managers of service providing units'.

In this regard it is clear that the OLG and TCorp specified the target for this ratio and the benchmark for same well in advance of the production of the 2014 Financial Statements. It is equally clear that the majority of the councils participated in reactive gaming. The problems with

this are twofold. Firstly, the integrity and usefulness of the Infrastructure Backlog ratio has been completely undermined, and the integrity of three other ratios significantly diminished.

Secondly, the minority of councils that did not participate in reactive gaming may well be punished as a result of their integrity. As LeGrand (2003) has observed, performance targets implicitly assume that the service population is comprised of 'knights' rather than 'knaves' (LeGrand 2003). However, when pressure is brought to bear and opportunity is provided the balance of knights and knaves will change, and in this case the balance has shifted to such a degree that no confidence can now be placed in the Asset Maintenance ratio and Infrastructure Backlog ratio (Bevan and Hood, 2006). In sum, Schedule 7 estimates and depreciation accruals directly affect four of the retained ratios (Infrastructure Backlog, Operating, Asset Renewal and Asset Maintenance ratios).

The third policy shift – concerning changes to performance thresholds for the operating and debt service ratios – is more difficult to explain than the other changes. With respect to the Operating Ratio, a very large proportion of councils already failed to meet the existing benchmark: 55 councils in 2009, 57 in 2010 and 89 councils in 2011 (TCorp 2013). Accordingly, raising the benchmark to break-even would seem to cast doubt on the fitness of the great majority of councils (since 115 councils failed to achieve break-even status in 2011).

Two explanations seem plausible. Firstly, the OLG may be signalling to councils that expenditure reduction is an absolute imperative: it should be noted in this regard that property taxes in NSW are pegged, many fees are regulated and intergovernmental grant revenue has been

frozen for a period of three years. This obviously leaves little opportunity to address the ratio from a revenue perspective. Alternatively, the OLG may be seeking to restrict the number of councils which can access the benefits promised to *Fit for the Future* entities, such as access to low cost debt facilities, 'streamlined' development planning and 'unshackling' from the rate peg. In so doing, the OLG may be seeking to limit the pecuniary and potential political costs associated with *Fit for the Future* councils.

The second threshold to change is the Debt Service Ratio. However, this is only part of the story for a close examination of the *Fit for the Future Self-Assessment Tool* (2014) reveals a number of significant changes which are not disclosed in the other literature. Firstly, the OLG has changed the definition of the ratio. The ratio definition in the *Self-Assessment Tool* (2014) is 'cost of debt service (interest expense & principal repayments) / total continuing operating revenue (excluding capital grants and contributions')). Previously the cost of debt was the denominator and EBIDTA (Earnings before interest, depreciation and amortisation) was the numerator. In addition, the *Self-Assessment Tool* (2014) deems councils with no debt to be not financially sustainable as a result of the lower bound of the benchmark (greater than 0)!

Why exactly zero debt would be financially unsustainable is beyond logic and at complete odds with the entire scholarly literature. Apart from being illogical the lower bound of the threshold also produces some perverse results. Firstly, payables which are unsecured liabilities generally owed to suppliers are treated differently to debt, which is also classified as a liability and may be unsecured (but will generally be owed to a financial institution). Drawing this distinction means that the OLG believes that owing money to a financial institution is somehow preferable to

owing money to a supplier, even though the former will require the payment of interest, while the latter might be a prudent way of managing cash flows that avoids the payment of interest (although interest may be part of the supplier's terms).

Secondly, councils (such as Lane Cove) which miss the benchmark owing to an absence of debt could easily meet the benchmark by drawing up a secured loan for a nominal amount and paying it back the next week! Clearly, this would produce no benefit for the local community and achieve no material enhancement – in real terms – to the council's financial sustainability, yet such an act would suddenly mean that Lane Cove (and other councils like it) would be deemed *Fit for the Future* on this criterion.

We should also note that the change to the Debt Service ratio is in direct contradiction to the approach taken by TCorp(2013) which the OLG had earlier commissioned to assess financial sustainability (and which the ILGRP (2013) endorsed). It would be instructive to know why the OLG has decided against the expert advice provided to it by TCorp and instead produced an illogical and indefensible measure of debt serviceability. Moreover, the upper bound of the benchmark (20%) would also seem to punish councils which aggressively reduce debt through high principal repayments or which use debt wisely to manage the lumpy cash flows (grants and quarterly rates) associated with the local government sector. It is curious that the definition adopted by the OLG is at odds with definitions employed for comparable measures in most standard texts (see for instance, Horngren et al. 2006; Ross et al. 2009). In so doing, the OLG appears to be measuring the *proportion* of revenue employed to service and reduce debt rather

than the *ability* to service debt (measured by TCorp (2013)). Clearly, the *ability* to service debt is the most relevant ratio for assessing financial sustainability.

In addition, it appears that the OLG (2014b) has dispensed with the ratio weightings originally applied by TCorp (2013). This may not be problematical given that no justification was ever given for the arbitrary weights applied by TCorp (2013) (Drew and Dollery 2014a). Moreover, reallocating the abandoned 32.5% of FSR and adding a new performance indicator would have made the exercise difficult, whilst subordinating all indicators to the criteria of 'adequate scale and capacity' seems to make weightings rather redundant.

The new performance indicator seeks to measure efficiency and it is defined by the OLG as real operating expenditure over time. There are a number of problems associated with this measure, not least that it fails to measure efficiency. Accordingly, we consider this in more detail in Section 4.7 of Chapter 4 of this Report.

The final change to the OLG use of financial sustainability as a measure of council performance lies in its assertion that 'right scale and capacity' is the predominant concern which councils must address in assessing *Fitness for the Future* submissions and the OLG specifically refers councils to the Panel's recommendations in relation to this matter. Councils which do not have 'adequate scale and capacity' are required to prepare a council merger proposal (OLG 2014b). Councils which meet 'adequate scale and capacity' are referred to the seven performance criteria discussed above. It is thus clear that 'adequate scale and capacity' is the pivotal criterion in the *Fit for the Future* program. This presents an apparently insolvable dilemma for councils in the

position where adjacent municipalities are either deemed to be of adequate scale and capacity and/or *Fit for the Future,* or where adjacent councils are simply uninterested in merger. The OLG is yet to explain the rationale for having councils complete merger proposals where all potential merger partners are *Fit for the Future* or are not interested in 'voluntary' amalgamation.

4.3 Scale and Capacity

The ILGRP (2013b) recommendations for Greater Sydney metropolitan councils were couched in terms of 2036 population projections which *prima facie* make it difficult to assess present scale and capacity. However, the Panel's preferred scale for Greater Sydney councils can be gleaned from the mean population of the ILGRP (2013b) proposed mergers which was 323,072 (median 291,350) in 2036 projection terms. For rural councils, the Panel (2013b: 40) stated that 'populations of less than 5,000 will not normally be sufficient' and that 'councils with populations between 5,000 and 10,000 should be kept under review to ensure that they maintain the capacity required to be "standard" local governments'. These statements – along with the pre-eminence attributed to them by the OLG (2014b) – necessarily imply an empirically testable claim that economies of scale occur in the population domain proposed.

Table 4.4: Evidence of Economies of Scale, 2009-2013

	NSW	Urban Councils	Non-Urban Councils
Population squared[6]	-0.00006**	-0.00001	-0.0026
	(0.00002)	(0.00001)	(0.0116)
Population	0.0360**	0.0053	0.3196
	(0.0078)	(0.0080)	(0.4264)
Density	-1.4355**	0.3550	-3.4553*
	(0.3410)	(0.4781)	(1.4253)
Exogenous controls?	Yes	Yes	Yes
N	152	81	71
Coefficient of Determination	0.5925	0.3944	0.5685

Exogenous controls include: proportion of individuals over 65 or under 15 years of age, proportion of ATSI persons, average wage, unemployment rate, total length of roads (kms) and the percentage of NESB individuals.
+ p<0.10, * p<0.05, ** p<0.01

Table 4.4 presents a panel regression of total expenditure (less depreciation) per capita against population size and density over the five year period 2009-2013. The model specification is consistent with Drew, Kortt and Dollery, (2014a) and Drew and Dollery, (2014a). The empirical evidence for the entire NSW local government sector suggests the presence of a local *maxima* at 308,790 (significant at the 1% level): that is, per capita expenditure increases up to this population threshold and decreases after this point. However, density is also a statistically significant regressor (at the 1% level) which may suggest conflation leading to a spurious result (Holcombe and Williams 2009).

The accepted treatment of conflation is to stratify the data: in this case we have used the Australian Classification of Local Government urban/non-urban codes which are compatible with the OLG classifications. When the entire NSW population of councils is stratified into urban and non-urban municipalities, then all evidence of economies of scale disappears. This is

[6] Population and Population squared were scaled down by a factor of 1,000. Expenditure per capita and population density have been transformed (ln).

consistent with the findings of Drew, Kortt and Dollery (2014a) and Holcombe and Williams (2009), wherein stratifying councils according to categories associated with density disentangles its conflation with population, thus producing a more accurate picture of the presence of economies of scale. In this case it appears that *a priori* evidence of economies of scale may have been largely illusory. If this is the case, then the entire premise behind *Fit for the Future* is *void ab initio*.

It is hardly surprising that no robust evidence of economies of scale exists when NSW councils are stratified. This is largely because councils produce a heterogeneous mix of goods and services, some of which have no likely association with scale. For instance, 'labour-intensive services, such as council rangers and health inspectors, generate few scale economies due to their idiosyncratic work patterns in which an increased volume of services may simply require a correspondingly larger number of workers' (Drew, Kortt and Dollery 2014a: 635). Even for capital intensive services, such as road construction, where scale economies are more likely, it is not reasonable to expect that the optimal size for the various functions will be comparable: they may simply negate one another.

Finally, considerable doubt has been created as to whether population size is a suitable proxy for local government output in Australia (Drew and Dollery 2014c). The number of households aligns far better with the unit of actual service provision and it is less volatile and more accurate in inter-censal periods. Thus the OLG may well be conducting its structural reform agenda on an entirely fallacious unit of scale and capacity (Drew and Dollery 2014c).

4.4 Unreliable Data for Sustainability Assessments

From the outset TCorp (2013) has held significant reservations regarding the reliability of data critical to the financial ratios that it employed in measuring the financial sustainability of the local government sector. In relation to estimates used in the calculation of the asset maintenance and infrastructure backlog ratios, TCorp (2013: 66) noted that:

> 'TCorp's review process has shown an inconsistency in the approach of Councils to calculating the data included in these Schedules, particularly Schedules 7 and 8. Without a high level of confidence in the data presented, it is more difficult to make informed decisions.'

With respect to the depreciation data used, which is critical to the calculation of the operating ratio and asset renewal ratios, TCorp (2013, p.49) also expressed reservations:

> 'Councils with a higher FSR generally have a lower average rate of depreciation and depreciation represents a lower percentage of total expenses. These two observations are consistent across most of the rating groups so that the stronger the FSR rating, the lower the depreciation rate and the lower the proportion of depreciation as a percentage of total expenses.'

Drew and Dollery (2014a) conducted ANOVA which validated the suspicions expressed by TCorp (2013) and illustrated the constitutive implications of inconsistent depreciation accruals through a sensitivity analysis on the operating ratio. They found that:

> 'When depreciation accruals were adjusted to the median depreciation to infrastructure ratio, this resulted in 38 (out of 152) councils' benchmark status changing. In the case of adjusting depreciation accruals to the median depreciation to IPPE ratio, the status of 42 councils was altered…The results were largely consistent with expectations: 'weak' and 'very weak' councils tended to move up to benchmark levels whereas 'sound' councils moved down. Movements in the 'moderate' councils were approximately even.'

Accordingly, it seems likely from both the scholarly evidence and the concerns expressed by TCorp (2013) that four of the six ratios retained by the OLG (2014b) are distorted by unreliable data. Moreover, two of the three financial statement periods chosen by the OLG to assess *Fit for the Future*[7] were produced after the TCorp (2013) and ILGRP (2013a) reports which largely revealed the structural reform implications arising from financial ratio data, thereby opening up the possibility of 'gaming' by municipal officials. This essentially represents an invitation to councils to distort the data via reactive gaming (Bevan and Hood 2006) – an invitation which Table 4.3 (presented earlier) demonstrates most councils grasped. There must thus be serious questions regarding the reliability of the data that forms the foundations of the *Fit for the Future* assessments, questions that the OLG (2014c: 13) acknowledge in its decision to assign a new

[7] For the OLG (2014) efficiency measure two of the five financial statements were produced after the initial TCorp (2013) and ILGRP (2013a) reports.

role to the Auditor General to ‘give communities the assurance they deserve on how councils are managed financially’.

However, these matters do not represent the entire set of problems associated with the data used to assess council fitness. Reviews to rating practices, grant allocations and problems with ABS statistical data also represent threats to the objective assessment of a council’s future prospects. The ILGRP (2013b, p.41) noted that the 36-year old rate-capping regime imposed on councils by the NSW Government had resulted in ‘a broader equity issue concern[ing] the wide variation between local government areas in the level of rates paid as a proportion of property values’ and that ‘the rate-pegging system in its present form impacts adversely on sound financial management’.

A measure of the extent of equity concerns can be established by reviewing Table 4.5 which examines the residential taxation effort according to the five broad categories of council described in the Australian Classification of Local Government system. Residential taxation effort measures the residential taxes levied by NSW municipalities as a proportion of the total income accruing to individuals residing in the municipal area. Data for residential rates was extracted from the notes to the Income Statement of each of the 2012 local council audited financial statements. Total annual income was obtained from the latest ABS data: the 2012 National Regional Profile. Residential taxation effort ranged from 0.209% to 2.497% with a median of 0.956% and a mean of 0.998%. Thus some council revenue is constrained to less than a tenth of their peers as a result of the rate-capping regime. The ILGRP (2013b) was thus correct

in highlighting the effect of rating practices (largely outside of the control of councils) on financial sustainability.

The OLG (2014c) seems to have accepted this argument and it has promised a review of rating practices. However, the question arises as to whether *current* assessments should be made on councils given that there is an accepted need for *future* rate revenue reform: after all three of the six ratios retained by the OLG will be directly affected by changes to rating practices.

Table 4.5: ANOVA Results for Taxation Effort All NSW Councils, 2012

	Prob>F	Agricultural (Ag)	Fringe (Fr)	Metropolitan (Met)	Regional (Reg)	Remote (Rem)	Differences
Taxation Effort (%)	0.000	0.807 (0.302)	1.201 (0.233)	0.844 (0.213)	1.422 (0.346)	0.551 (0.000)	Fr>Ag** Fr>Met** Reg>Ag** Reg>Met** Reg>Rem*

+ p<0.10, * p<0.05, ** p<0.01

A similar situation exists for intergovernmental grant allocations. Drew and Dollery (2014d) have demonstrated that grant transfers are not allocated on a full horizontal equalisation basis as legislated in the Local Government (Financial Assistance) Act 1995. Moreover, Table 4.6 demonstrates that municipal size is a statistically significant determinant of NSW Local Government Grant Commission allocations, despite the fact that size in itself is irrelevant to the principles of horizontal equalisation. In fact, the most relevant determinant – average wage of residents – is associated with an increase in the allocation of financial assistance grants which is the exact opposite of the horizontal equalisation principles enshrined in the federal legislation! The ILGRP (2013b, p.45) has suggested that 'consideration needs to be given to the option of redistributing more funds to the most needy councils and communities'.

The OLG (2014c, p.13) has promised to 'consider opportunities to direct Financial Assistance Grants to communities with the greatest need'. This essentially concedes that the NSW LGGC has not allocated grants according the existing commonwealth legislation and confirms the results detailed in Table 4.6. Given that NSW council own-source revenue averages less than 60%, changes to grant allocation methods would have a large effect on the financial sustainability of municipalities. It is clear that this problem is acute and must be addressed *before* an objective assessment of future fitness can be made.

Table 4.6: Determinants of Financial Assistance Grants Allocated by the NSW Local Government Grants Commission 2009-2013

	NSW
Households (ln)	0.4778**
	(0.0781)
Average wage (ln)	0.1861**
	(0.0173)
Road length (sqrt)	0.0096+
	(0.0056)
N	152
Coefficient of Determination	0.8071

Exogenous controls include: density, proportion of ATSI and NESB residents, proportion of individuals under 15 years of age, proportion of individuals over 65 years of age, number of employing businesses.
+ $p<0.10$, * $p<0.05$, ** $p<0.01$

Finally, problems with ABS population data inputs have the potential to seriously undermine the relevance and reliability of the OLG's (2014b) preferred measure of municipal efficiency for a number of reasons. Firstly, publication of ABS population data by local government area is typically delayed by a few years. For instance, as at mid-March 2015 the latest estimate of municipal population size available was for 2012, although the OLG used a *projected* estimate of 2013 population available in the April 2014 ABS Regional Population Growth report. However, the *projected* population data is clearly provided with the caveat that it is a '*preliminary* figure or series subject to revision' (ABS, 2015). Moreover, the revisions can be quite significant – for

instance in the latest release of the Regional Population Growth data (released on the 31st March, 2015) the 2013 *provisional* data has been revised. These revisions are important because they could easily change the linear trend result which the OLG erroneously uses to measure efficiency (see section 4.5 below). For example, Snowy River had its population estimate reduced by 1.7% in the recent revision and Cooma-Monaro had its population estimate increased by 0.89%.

What this means is that the OLG in their *Fit for the Future Toolkit* is using data which the ABS itself has revised after noting that it is not correct. It is also important to remain cognisant of the fact that even the revised population data in inter-censal periods is nothing more than an estimate: for instance, a recent study by the ABS identified errors in inter-censal estimates ranging from 15.2% (for statistical areas with less than 2,000) to 2.4% error (in statistical areas with populations greater than 20,000)[8] (Drew and Dollery 2014c). In fact, 'throughout 2013, the ABS conducted a one-off exercise to revise (recast) population estimates for a longer time period, back to 1991. This was necessary due to a significant improvement in the methodology used to estimate net undercount in the 2011 Census' (ABS, 2015). Finally, serious doubt has been cast on the practice of using population as a proxy for local government size in service provision of goods and services given that 'services to property' (i.e. households and businesses) dominate in the Australian municipal milieu (Drew and Dollery 2014c).

[8] The ABS uses statistical areas as the basis for calculating the populations of local government areas. Multiple statistical areas may be combined to arrive at the population size for a given municipality.

4.5 Incorrect Measure of Efficiency

Problems with the OLG (2014b) 'efficiency' ratio go far beyond the considerable obstacles presented by unreliable and untimely population inputs: there are also unresolved matters relating to the definition of efficiency, indexing of financial data, contraindications with other ratios, failure to control for service quality and service sufficiency and the use of a completely erroneous method to establish the direction of expenditure over time.

Perhaps the most alarming aspect of the OLG's (2014b) 'efficiency' measure is that it does not measure efficiency *per se*. Technical efficiency is a measure of how inputs (such capital and labour) are combined to produce a set of outputs. Major outputs must be specified carefully according to the local government services actually produced. As we have seen, population size as a proxy for council output is deficient in Australian local government context, given its focus on 'services to property' (i.e. households and businesses), with its core functions aimed at local planning, domestic waste removal, provision of local infrastructure (predominately local roads) and water and wastewater in some regional and rural municipalities (Drew and Dollery 2014c). The number of households and business entities is a superior measure of many types of service provision (such as solid waste disposal) than population. Moreover, given that road infrastructure is the single largest cost for Australian local government, representing approximately a quarter of functional expenditure, it is important that the length of roads be included as an output. As noted in Chapter 3, there is only a very weak association (Pearson correlation coefficient -0.266) between population and municipal road length and the direction of the association is in fact negative (i.e. higher population is associated with smaller road commitments). Thus any analysis

which employs population as the sole proxy for municipal output is likely to produce spurious results.

The appropriate statistical technique to assess technical efficiency for multiple inputs and outputs is data envelopment analysis (DEA) and to assess trends in technical efficiency over time locally inter-temporal DEA would be indicated. Real expenditure over time can only capture one output (which does not reflect the heterogeneous nature of local government services) and thus is best described as per capita expenditure containment. It is most certainly not a measure of efficiency.

The use of financial data from multiple time periods (five under the OLG model) also raises the thorny problem of converting nominal financial data into real quantum. The OLG uses data from the 2010, 2011, 2012, 2013 and 2014 financial years in its assessment of municipal efficiency. However, it has elected to deflate all five years of data: annualised CPI is used for years 2010 and 2011, whilst annualised Local Government Cost Index is used for 2012 through to 2014 (OLG 2014d) (all deflators are rounded to one decimal place).

This strategy presents a number of problems. Firstly, it was entirely unnecessary to deflate the 2010 financial year data and this decision simply introduces avoidable rounding and measurement error into the algorithm (which as we will see below is extremely important given the sensitivity of the OLG's flawed linear trends analysis). Secondly, it is not acceptable to use two entirely different indexes to deflate continuous data. Thirdly, for comparative purposes it would have been more useful to *inflate* data to 2014 dollars rather than *deflate* data (given the high leverage of the 2014 data it is particularly important that this data point be free of avoidable

error – inflating rather than deflating the data would have reduced the error on this leverage point[9]). Finally, use of annualised growth in indexes imputes and compounds rounding error: given the sums involved (measured in tens of millions of dollars), and the use of five compounding periods, the resultant error is likely to be very significant. A much better strategy would have been to employ the actual index numbers in calculations.

The OLG (2014b) 'efficiency' measure is contraindicated to the other ratios. In essence, in order to address Infrastructure Backlog, Asset Maintenance and Building and Infrastructure ratios, it is necessary to increase rates of expenditure. Yet in so doing, a council will record a reduction in the OLG preferred measure of efficiency. This obviously sets up an insolvable dilemma for municipal management. Moreover, the OLG (2014b) measure of efficiency fails to address service quality and service sufficiency. This is a significant problem given the potential for comparisons to be drawn between councils delivering vastly different levels of services. Furthermore, even within a given council, service quality is unlikely to remain static over a five year period thus making it very difficult to make reasonable comparisons of costs. With respect to service sufficiency, the measure of efficiency chosen sets up a perverse incentive to discontinue services. Taken in the extreme a council could – on this measure alone – demonstrate that it was *Fit for the Future* by producing no future services at all: a measure which would meet the OLG criterion but most certainly would not that of residents!

Finally, the methodological technique used to assess the trend in per capita expenditure is completely flawed. This is because the OLG has chosen to fit a linear regression (they may not

[9] This is particularly important given the fact that this last data point already contains material error attributable to the use of *provisional* data which has since been revised as well as the failure to continue the practice of using an average of the two boundary years for this last financial period.

have realised that this is what the Microsoft Excel command they used was doing) to the per capita expenditure data (which as we have seen already contains significant error). As any undergraduate text will attest, there are a number of assumptions which must be satisfied in order for a linear regression to be sensible. Of these, two rather obvious assumptions are most pertinent to the errors that the OLG has made. The first assumption 'is that the dependent variable can be calculated as a linear function of a specific set of independent variables' (Kennedy, 2003, p.48). The second assumption – implied by the former – is that the model has been specified correctly: that is, that all relevant independent variables have been included.

Unfortunately, neither of these key assumptions has been met and this produces results which are incoherent. To illustrate the point, consider the per capita expenditure data for a combined Hunters Hill, Ryde, Lane Cove, Willoughby, North Sydney and Mosman entity (Figure 4.1). Figure 4.1 was produced from the *Fit for the Future* toolkit output (see Chapter 5 for further details). Moreover, we note that similar distributions exist for Willoughby, Hunters Hill and North Sydney's individual *Fit for the Future* assessments (and thus the same comments apply to each of these councils). From Figure 4.1, one can clearly see that the fundamental assumption of linear regression – that the relationship is linear – is not satisfied by this (and we would contend, most other local authorities') data set. There is no doubt that the data is best described by a polynomial function. A measure of the explanatory power of the model is given by the coefficient of determination (0.007): that is, the model produced explains less than one percent of the data (see Figure 4.1)! Similarly, the model for Willoughby and Hunters Hill also explains less than one percent of the data, whilst North Sydney's model explains just 7.5%. It is thus undoubtedly incorrect to try to fit a linear model to these council's per capita expenditure data.

The first assumption of linear regression has not been met and it is thus completely incorrect to try to fit a linear trend to the data as the OLG has attempted to do. As a result the linear trend estimate is completely unstable.

Suppose we change the 2012 financial year result to something ridiculous, such as a zero per capita expenditure for the year. Because of the leverage values and the functional form of the distribution, the gradient of the trend line[10] does not budge even though the council's per capita expenditure has been significantly altered! However, by contrast, if we lift the first data point by just 0.6%, then the amalgamated entity is suddenly deemed to have decreasing expenditure over time and is *Fit for the Future* on this criteria. This is particularly disturbing given the errors in the population data, compounded rounding errors, truncation errors and errors in the indexing of financial statement data that plague the OLG Toolkit!

Moreover, the second assumption is also invalid. If one conducts a statistical test for specification error – often referred to as the F test or 'junk' regression statistic – all four regressions indicate specification error (i.e. that the regression is junk). This is hardly surprising because as we have demonstrated above councils do not produce people: they produce a heterogeneous mix of services which is best represented by the number of households, number of employing business and length of council maintained roads. Accordingly, the OLG 'efficiency' measure is indisputably mis-specified, or in econometric parlance simply 'junk'.

[10] The OLG uses the gradient of the trend line to assess whether a council is fit. If the gradient is positive the council does not meet the benchmark. However, if the gradient is negative the council is deemed to have met the benchmark. Curiously, no importance is place on the magnitude of the gradient or the dependent intercept – which is in itself a flaw of the OLG approach.

There are many other flaws in the evaluation of per capita trend conducted by OLG which would take volumes to elaborate. However, it is not necessary to spend further time on the matter given the failure of the OLG model to conform to fundamental assumptions of econometric theory which are expounded on in every undergraduate econometrics text.

Figure 4.1: Distribution of Expenditure Per Capita for the Amalgamated Entity, 2010-2014

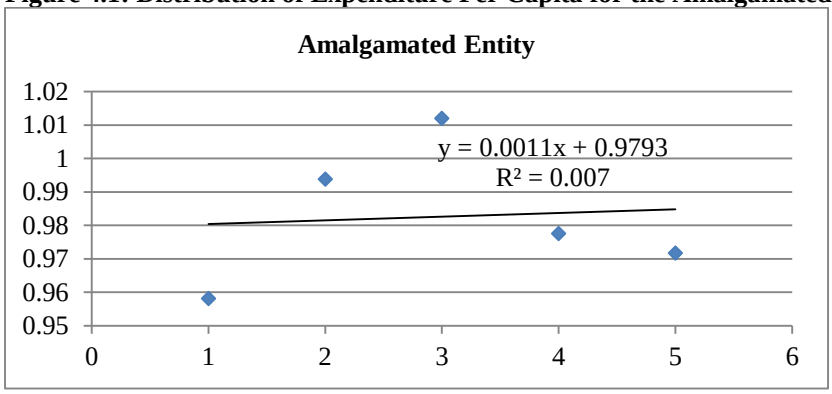


Figure 4.2 Illustrating the Instability of the Amalgamated Linear Trend, 2010-2014

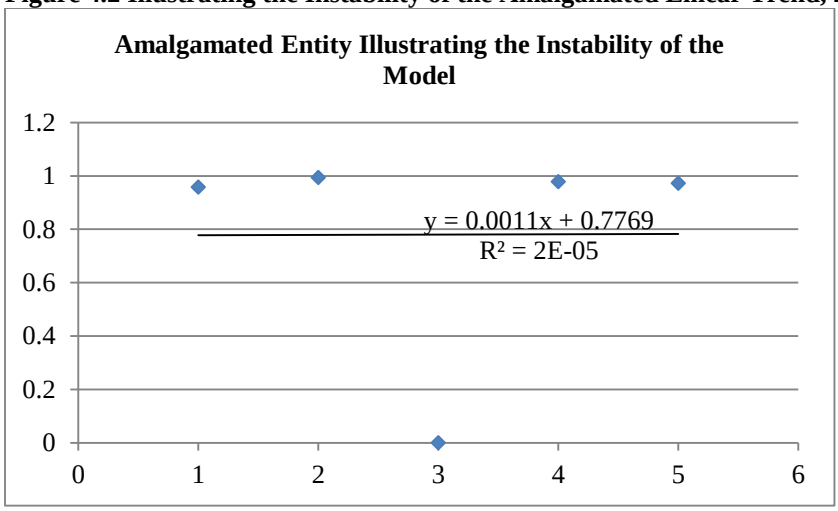
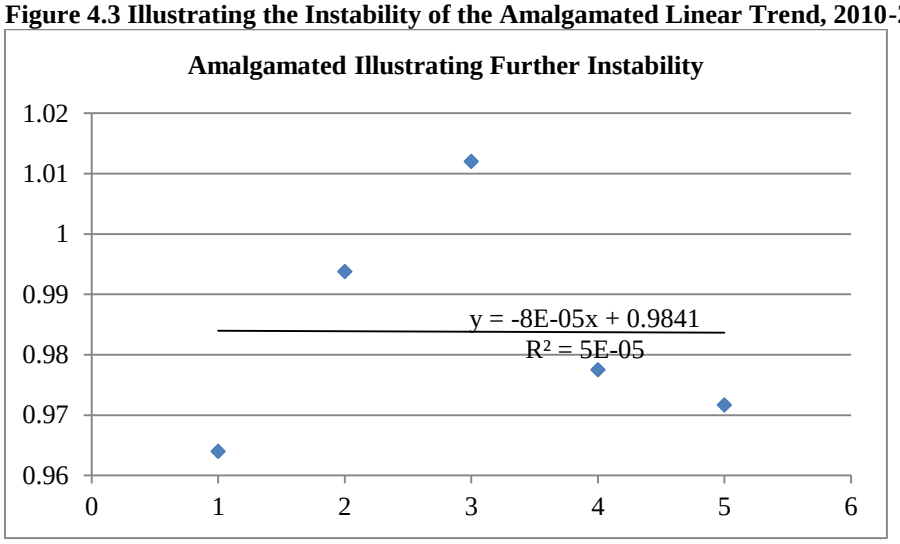


Figure 4.3 Illustrating the Instability of the Amalgamated Linear Trend, 2010-2014



4.6 Recommendations

The OLG (2014b; 2014c; 2014d) *Fit for the Future* documentation creates the distinct impression that the program has been rushed in the aftermath of a shock change of Premier in early 2014 and subsequent Cabinet reshuffle in order that the new Premier be well placed to implement structural reform plans after the March 2015 election. If this assumption is correct, then the NSW Government is intent on following the oft-trod path of previous state governments in NSW, Victoria, Western Australia and Queensland in which forced mergers have been implemented early in the respective term of office. It seems this is done to abate political damage by putting as much time as possible between unpopular structural reform and subsequent state polls. However, in the present case in NSW, in its rush to get a structural reform framework out in time, the NSW Government has blundered badly in its *Fit for the Future* program, as we have demonstrated in Chapter 4.

We have identified a number of errors which seem to derive from the harsh time constraints imposed on the OLG by the NSW Government. For instance, the efficiency measure hastily employed does not measure efficiency. Moreover, the method for indexing nominal data is clearly flawed and the approach taken to establishing the direction of the trend over time is ridiculous. The haste made in responding to the ILGRP (2013b) inquiry has also meant that no empirical evidence has been tendered to substantiate the Panel's assertion that substantial scale economies exist in NSW local government service provision, much less its claim that current municipal size is 'under-scale'. Likewise, the rush to articulate the criteria adopted in *Fit for the Future* has meant little time or appetite to investigate recent developments in the scholarly literature which clearly demonstrate that population size is not a suitable proxy for local government output.

Had this been done thoroughly, then it would have become evident that the population data which forms the foundation of both the OLG (2014b) scale and capacity criteria and efficiency measurement is not sufficiently reliable for public policy making purposes (particularly in inter-censal years) in NSW local government. It would also have uncovered the pernicious effects of unreliable accounting accruals on the financial sustainability ratios employed by the OLG. Finally, had sufficient time been available, remedial action might have been taken on Schedule 7 and 8 data which TCorp (2013) had already identified as problematic.

The rush to press forward with structural reform of local government also means that decisions will be taken without knowing the outcome of 'unfinished business'. This relates principally to reviews of local government rating and grant allocation practices which will result in significant changes to the revenue streams of NSW local authorities. It is hard to understand how a council's *Fitness for the Future* can be assessed without reference to significant changes to revenue policies.

CHAPTER 5: FINANCIAL ANALYSIS OF PROPOSED MERGERS

Chapter Summary

- An analysis of the proposed mergers identified a range of problems associated with: (i) significant disparities in rates, fees and charges among the six councils; (ii) complications in determining democratic representation post-merger; (iii) apportioning the burden of liabilities inherited by a newly merged council; (iv) complications derived from the dismemberment of the City of Ryde; (v) the Commonwealth financial assistance grants post-merger, and (vi) information disclosure to local residents.
- The key finding from this analysis is that almost all of the North Shore group of councils would be less financially sustainable under the *Fit for the Future* criteria than they had been pre-merger.

5.1 Introduction

As we have seen in Chapter 1 of this Report, in line with the recommendations of the Panel in *Revitalising Local Government* (2014), under the *Fit for the Future* program, the 'eastern two-thirds' of Ryde is supposed to merge with Hunters Hill, Lane Cove, Mosman, North Sydney and Willoughby, with the remaining 'western third' to amalgamate with Auburn, Parramatta and the 'North Parramatta area of the Hills'. No empirical analysis was undertaken by either the Panel or the NSW OLG to support these proposed mergers, despite repeated claims by the Panel that it would adhere to 'evidence-based' policymaking.

Chapter 5 seeks to undertake the empirical analysis of the proposed mergers which the Panel should have done had it been competently run. As we will demonstrate in Chapter 5, should these proposed municipal mergers progress, they will generate a number of severe difficulties for decision makers and affected councils alike. With respect to the proposed Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby amalgamation, Chapter 5 will establish that revenue structures, political representation, liabilities and infrastructure burdens all differ significantly amongst these six councils proposed for amalgamation. A merger will clearly create winners and losers, and the distribution of gains and losses attendant upon amalgamation must necessarily be decided as a result of a political process, with local residents having little direct say in the matter. In addition, there are also significant problems associated with merger proposals which dismember Ryde council. Once again, the result will be winners and losers. Finally, by the OLG's own reckoning[11], an amalgamation of the six councils into a North Shore group– as per the Panel's recommendation – will result in a *less Fit for the Future* entity (when compared to existing municipal structures) in all but one instance. In fact it is fair to say that the proposed merger would result in an amalgamated entity that is – by the OLG's own criteria – clearly *unfit* for the future!

Chapter 5 is divided into seven main parts. Section 5.2 considers the difficulties posed the existence of significant current disparities in rates, fees and charges, and capacities to pay across the six councils which were simply ignored by both the Panel and the OLG in the merger recommendations. Section 5.3 discusses the many difficult decisions which must be made regarding changes in democratic representation which will occur should amalgamations proceed.

[11] The OLG Toolkit was used to evaluate the *Fitness for the Future* of the proposed amalgamated entity.

Section 5.4 tackles current and non-current liabilities of each of the six local councils targeted for a North Shore group merger, the total liabilities likely to be inherited by any proposed new amalgamated municipality, and its probable impact on local residents. Section 5.5 assesses the complication derived from the question of how to dismember the City of Ryde financially. Section 5.6 probes the question of the allocation of Commonwealth financial assistance grants post-merger and the difficulties this poses. Section 5.7 considers other problems attendant upon forced mergers, notably the need for full information disclosure in a transparent and democratic manner given the inevitability winners and losers amongst local residents post-amalgamation. Section 5.8 analyses whether merged combinations of the North Shore group of councils would be more financially sustainable under the *Fit for the Future* criteria than they had been pre-merger. Chapter 5 ends with some brief concluding remarks in section 5.9.

5.2 Differences in Rates, Charges and Capacity to Pay

Table 5.1 details the average residential and business rates levied by each of Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby. Table 5.1 clearly demonstrates that there is a significant difference in extant municipal taxation, arising in part from the cumulative effects of an almost four decade long rate pegging regime. However, for more meaningful comparison one needs to compare the municipal rates with respect to the value of the land, although comparisons are confounded by the problem of high rise residential developments (see ILGRP (2013, p.40)[12]. When this is done it is clear that in order for the same rate revenue to be generated from the lowest rating council (Mosman) as the highest (Ryde), there would need to be an increase in the revenue generated per dollar of land of just over 70%.

[12] It is acknowledged that many councils use a combination of base rate and *ad velorum*. However, for comparative purposes the tax paid per dollar value of land is the appropriate quantum.

Depending on the approach taken to redistribute the land based taxation burden following the proposed amalgamation, there will certainly be winners and losers. On the basis of this analysis, it would appear that the residents of Hunters Hill and Mosman will likely be in the latter category. Moreover, there will also need to be adjustments made to the fee structure for a range of services. For instance, the average domestic waste charge in North Sydney would need to be raised by over 67% to bring it in line with the charge incurred by Willoughby residents.

However, the question naturally arises as to the capacity of residents to bear additional municipal tax and fee burdens. Because of the incidence of high-density residential developments, and the fact that municipal taxation in Sydney has been regressive for a number of years owing to the property bubble, it is necessary to construct a different measure in order to accurately assess local resident's capacity to bear municipal burdens. In this regard, residential revenue effort measuring the proportion of municipal taxes and fees expressed as a percentage of income accruing to residents in the local government area gives a good sense of the ability of residents to bear increases to rates and charges. The importance of this sort analysis is evident if one compares the fourth and fifth columns of Table 5.1. Thus whilst Hunters Hill council extracts a much lower rate of taxation per dollar value of land[13] than North Sydney council, it is clear that the residents of Hunters Hill do not have the same capacity to bear increases in their local government tax burden as do their neighbours in North Sydney.

[13] Based on OLG data appearing in the 2012-2013 comparative report. It should be borne in mind that the rates quoted will be different to the actual rate charged to individual land owners owing to the confounding effect of base rates, high-density residential complexes and *ad velorum* charges (where applicable).

Table 5.1: Differences in the Rates, Charges and Capacity to Pay in Targeted Councils

Council	Avg Residential Rate	Avg Business Rate	Total Rate Revenue/ Total Land Value ($000)[14]	Avg Domestic Waste Charge	Residential Revenue Effort[15]
Hunters Hill	1379.15	863.51	1.666	416.01	0.9088
Lane Cove	1130.89	4157.15	2.507	370.52	1.1049
Ryde	645.62	6992.46	2.509	363.38	1.1177
Willoughby	828.97	5941.70	2.472	439.10	0.9296
Mosman	1181.45	2593.59	1.452	432.79	0.8143
North Sydney	513.40	2961.57	2.298	262.00	0.6563

Source: Office of Local Government Measuring LG Performance 2012-13.

The point is that the question of how to re-distribute municipal burdens in an amalgamated local authority is far more complex than simply ensuring all residents pay the same taxation rate (per dollar value of land). One also needs to consider how other fees and charges add to the total municipal burden and the capacity of residents to pay. All of these difficult decisions have been blithely ignored by both the Panel and the OLG. However, the outcome of any amalgamation must necessarily involve winners and losers and it is not unreasonable to suggest that the losers are at least informed about the extent of the likely losses and have a say as to whether they are prepared to accept same.

5.3 Changes in Political Representation

It is also apparent that there are many weighty decisions to be made regarding changes in democratic representation which is likely to occur should amalgamation proceed as per the

[14] We have inverted the OLG data to make for more meaningful comparisons. This data is derived from the OLG 2012-13 report and we cannot guarantee its accuracy. Moreover the figure will be different to the actual rate charge levied per dollar value of land owing to the confounding nature of high rise development rate charges, base rates and *ad velorum*. However, irrespective of the individual methods which councils use to charge rates the quantum expressed in the table represents the total rate revenue extracted as a function of the value of land and is thus the fairest unit of comparison between municipalities. Differences in the approach taken to levy rates thus simply reflect the relative distribution of the charges amongst individual residents within the existing council boundaries.
[15] 2012 Residential revenue effort owing to ABS data limitations.

Panel's recommendation. Table 5.2 details the number of councillors and rate of democratic representation for each of the six municipalities.

Table 5.2: Political Representation in Target Councils

Council	No. of Councillors	Population per Councillor
Hunters Hill	7	2020
Lane Cove	9	3747
Ryde	12	9233
Willoughby	13	5533
Mosman	7	4229
North Sydney	13	5209

Source: Office of Local Government Measuring LG Performance 2012-13

With respect to Table 5.2, the first observation relates to the surprising degree of variation in political representation that exists under the current municipal structure. For instance, the residents of Hunters Hill have over four times the democratic representation as the residents of Ryde. Clearly there will thus need to be some adjustment to the democratic representation which the residents of a potential amalgamated entity might expect. The question is how much adjustment is reasonable?

If we were to adopt the entirely reasonable proposition that the residents of an amalgamated entity should have the same average level of democratic representation as existed under the previous municipal structures, then this would require a staggering 61 councillors and result in a council chamber about two-thirds of the size of the NSW Legislative Assembly! On the other hand, if we believe that residents should receive the level of representation currently afforded to the citizens of Hunters Hill, then we would finish with a council comprising 145 councillors! This serves to underline the point that unless the NSW Government believes that local democracy should be diminished, a merged entity would be unwieldy and, if previous scholarly work is a guide, it will also prove politically unstable (Spicer, 2015).

Since it is highly unlikely that the NSW Government would ever allow 61councillors, it follows that if the Government presses ahead with amalgamations, then it is implicitly endorsing lower levels of democracy. This policy implication doesn't even appear to have been considered by the architects of *Fit for the Future,* much less clearly articulated.

5.4 Liabilities and the Local Infrastructure Backlog

Table 5.3 details the current and non-current liabilities of each of the six local councils targeted for the North Shore group merger, as well as the total liabilities likely to be inherited by any proposed new amalgamated municipality. In order to facilitate easy comparison, we have also expressed each of the items in per household terms. Financial data is derived directly from the 2014 audited Financial Statements. One again it is evident that there is a good deal of variation between the six existing councils and, yet again, this means that any proposed amalgamation will necessarily create winners and losers. For instance, the total liability per household of Willoughby residents will *decrease* by about $1,500, whilst residents of Ryde will find themselves with over $600 per household of *additional* liabilities following amalgamation.[16]

[16] Current assets and non-current assets may offset this increase in liabilities a little. However, the experience from previous municipal boundary change suggests that non-current assets often require significant write downs, or cannot be used or sold due to obsolescence (for example previous municipal IT assets). Moreover non-current assets can exert a lasting negative cash flow due to maintenance and renewal needs (see, for instance, Drew and Dollery 2015).

Table 5.3: Differences in Liabilities in Targeted Councils ($000)

Council	Current Liabilities	Current Liabilities per Household[17]	Non-Current Liabilities	Non-Current Liabilities per Household	Total Liabilities per Household
Hunters Hill	5,317	1.151	182	0.039	1.19
Lane Cove	16,030	1.303	128	0.010	1.313
Ryde	30,312	0.773	4,958	0.126	0.899
Willoughby	28,057	1.107	49,264	1.944	3.051
Mosman	14,134	1.306	9,380	0.867	2.173
North Sydney	28,734	0.984	278	0.010	0.994
Amalgamated Entity	122,584	1.009	64,190	0.528	1.537

Source 2013-14 Audited Financial Statements.

This serves to underline the problems with the proposed merger on equity grounds. It can hardly be described as 'fair and reasonable' for some local residents to have their share of municipal liabilities almost doubled as a result of a decision arbitrarily made by a higher tier of government to compulsorily consolidate their council! Moreover, in some instances the liabilities have been accrued as a result of paying for services which existing residents have already consumed. A merger would thus mean that the costs of these services have been 'exported' to people outside of the municipality which elected to consume the services.[18] Finally, the fact that most residents do not have access to this information[19] and will probably not be given a direct democratic voice in the decision to assume higher liabilities seems particularly wrong in a western democratic society, such as Australia.

However, other financial burdens will also be assumed by the residents of the existing municipalities under the proposed amalgamation structure. For instance, Special Schedule 7 of the most recent Financial Statements details the infrastructure backlog which residents will be

[17] Estimated households based on 2011 census adjusted for subsequent new dwelling approvals.
[18] Although where debt is associated with non-current assets future residents of the amalgamated entity may get to consume some portion of the assets they have been forced to partly fund.
[19] Due to high information costs or lack of accounting skills.

burdened with under any amalgamation arrangement. In a recent press release, Minister Toole claimed that it was 'plainly ridiculous' to consider the cost to bring assets back to a satisfactory standard as a liability for residents associated with council mergers[20]. However, this statement by the Minister can only be true if he does not expect the assets in any merged council to ever be brought to a satisfactory standard, or if he believes the data in Schedule 7 of the Financial Statements to be untrue[21]. If the Minister has no expectation that assets will ever be brought to a satisfactory standard in amalgamated entities, then this suggests that he does not expect amalgamated entities to be in a position to address their infrastructure backlogs. Given that the Minister has justified the *Fit for the Future* program in part on the grounds that it is required to address critical infrastructure backlogs, this would seem to be an extraordinary position to take. The statement by the Minister is thus either illogical or a further example of the pains which the NSW Government has gone to in order to ensure local residents do not become aware of the inconvenient facts which underlie municipal amalgamation.

We present the relevant data obtained from the financial statements in per household terms in Table 5.4 to facilitate comparison. Two important conclusions can be drawn from the estimates of the cost required to bring assets to a satisfactory standard. Firstly, the proposed merger would result in winners and losers. For instance, residents of Lane Cove will find themselves firmly in the latter category should the amalgamation proceed, with an almost doubling of their household infrastructure burden. Secondly, the data clearly falsifies the OLG claim that inadequate levels of debt result in infrastructure, given that the two councils which fail the debt ratio on the basis of

[20] Western Advocate, March 4, 2015.
[21] As noted in Chapter 4 there are good grounds for doubting the veracity of many estimates – however, if the figures need to be revised then they would undoubtedly need upward revision.

having no relevant debt are also the two councils with the lowest per household levels of costs to bring municipal assets to a satisfactory standard![22]

Table 5.4: Council Differences in Infrastructure Deficits and Maintenance Costs

Council	Cost to Bring to Satisfactory Standard	Cost to Bring to Satisfactory Standard per Household	Required Maintenance	Required Maintenance per Household
Hunters Hill	7,800	1.688	1,503	0.325
Lane Cove	7,028	0.571	10,254	0.834
Ryde	56,416	1.439	15,752	0.402
Willoughby	38,034	1.501	20,518	0.810
Mosman	8,639	0.798	3,097	0.286
North Sydney	15,310	0.524	12,363	0.423
Amalgamated Entity	133,227	1.097	63487	0.523

Source 2013-14 Audited Financial Statements

5.5 Problems and Challenges in Dismembering Ryde

One particularly thorny problem which both Panel and the OLG have ignored revolves around the question of how to dismember the City of Ryde should the Panel's recommendations be adopted. This is a difficult problem which will undoubtedly result in winners and losers. As noted by Drew and Dollery (2014; 2015), there are a number of approaches which can be taken. Moreover, each approach will have significant constitutive implications for the financial sustainability of the two separate entities which emerge from the dismembering of Ryde. Specifically decisions need to be made about the allocation of the following assets, liabilities and labour:

[22] The OLG in its notes to the Debt Service ratio – which incidentally, measures the proportion of revenue used to service and repay debt rather than the ability to service debt – also state that the inadequate use of debt may force councils to raise rates to higher levels. However, this is a rather strange assertion given that rates have been pegged for almost four decades! It should be noted that neither Lane Cove nor North Sydney have applied for special rate variations in the latest rounds of IPART determinations.

- Immovable municipal assets
- Movable assets
- Staff
- Liabilities associated with staff
- Other liabilities.

It has generally been presumed that immovable municipal assets are the simplest element to distribute. However, as the empirical literature on de-amalgamation has demonstrated, this is far from the truth. For example, the financial sustainability problems which Benalla experience following the de-amalgamation of Delatite Council in 2002 derived from the division of immovable assets. In the Delatite case immovable assets were simply allocated to the emerging council in which the asset geographically resided. However, this presents equity problems where assets are not equally dispersed in the same proportion as rateable property revenue was extracted, which is unlikely to ever be the case, or where 'greenfield' sites have been provided with relatively new infrastructure which was principally funded by the entire cohort of municipal residents. Furthermore, geographically uneven asset maintenance and infrastructure backlogs, which also undoubtedly exist, can create an uneven distribution of future infrastructure burdens unless great care is taken.

The distribution of moveable assets also presents problems for the *Fit for the Future* reform architects. As the designers of the Delatite Shire's de-amalgamation discovered, it is not as simple as dividing up the assets in proportion to the rate revenue extracted from the divided

council. This is because many assets' book values unfortunately do not reflect their actual fair value, many assets do not have a viable market (for example, IT software or hardware created specifically for Ryde), and some assets (such as artworks) are inextricably linked with fixed assets. For instance, Benalla Council was hit particularly hard by write downs on assets following de-amalgamation of Delatite which significantly affected its financial position (Drew and Dollery 2015).

Staffing also presents a thorny problem in the context of council dismemberment. Firstly, there is the pressing problem regarding *what proportion* of staff to allocate to which emerging entity, especially since any over allocation will prove detrimental to the financial viability of the emerging entity (Drew and Dollery 2014). Secondly, there is the much more sensitive matter of *which* staff members to allocate to which entity. For instance, it is entirely likely that differences in productivity, experience, seniority and future work intentions exist amongst staff and that a bias in allocation (whether intentional or not) could diminish the financial sustainability of one of the emerging councils. Moreover, if liabilities associated with these staff, such as leave entitlements, are not handled carefully, then this will also significantly affect future financial sustainability. Finally, the allocation of existing liabilities also presents formidable problems for the architects of Ryde's dismemberment. The difficulty arises chiefly because some of the liabilities will be associated with specific moveable and fixed assets, some with services already consumed and it is unlikely that accountants will be able to accurately identify which liabilities are associated with which asset or service. Even if this could be done, it is not at all clear how

anyone could determine what proportion of the quantum of principal repayments relates to which asset or service and whether the proportion previously allocated was equitably applied.[23]

Thus, we once again see that the thoughtless recommendations of the Panel yield potentially serious equity and sustainability questions unanswered. Moreover, the endorsement of the recommendations of the Panel by the NSW Government clearly demonstrates that it either does not understand the gravity of the decisions which must be made or it does not wish local residents to know whether they will be winners or losers as a result of the proposed merger.

5.6 Other Complications: Financial Assistance Act

An additional problem which the OLG has thus far failed to address is the question of the allocation of Commonwealth financial assistance grants. As at 7 February 2006, a variation under subsection 6(4) of the federal legislation has been in force. In essence the proclamation states that where two or more local governing bodies are amalgamated, the grant allocation for the subsequent four years must be equal to the sum of the quantum that the bodies would have received had they remained separate entities.

This presents a number of difficult problems for the NSW Government. Firstly, as we detailed in Chapter 4, the NSW Government has recently implicitly acknowledged its failure to allocate financial assistance grants in the past according to the federal legislation. As a result, it has asked for grants to be redirected to communities with the greatest need. However, the proclamation

[23] For instance the bulk of principal repayments made by a council in a given year might have been disproportionality allocated to a liability associated with a specific asset (on strategic considerations) which is geographically located in a certain emerging council. However, had the principal repayments been allocated in a different manner (perhaps in proportion to the fair value of the fixed assets) then an entirely different set of liability balances may have resulted.

under subsection 6(4) requires of the NSW Government that it is lawfully obliged to maintain current levels of grant funding for a large proportion of the councils in NSW[24]. This will thwart its attempts to finally distribute Commonwealth intergovernmental grants according to the legislated horizontal fiscal equalisation principles because a significant proportion of the grant allocations will have been legislatively pre-determined.

Secondly, the reason why the proclamation came in to force in the first place is because grant allocations to amalgamated councils were typically significantly lower than the sum of previous financial assistance grants their individual constituent councils. This means that in all likelihood grant revenue for merged entities four years out from amalgamation will be significantly less than that which they would have received had the amalgamation not proceeded. Given the reliance of councils on financial assistance grants, this has important implications for long term financial sustainability.

Finally, failure to flag this matter in financial sustainability assessments and the *Fit For the Future* literature represents further evidence of the rushed manner in which the Panel, the and the NSW Government have approached the weighty question of council mergers.

5.7 Other Complications: Too Little Information

There are significant additional problems which must be resolved through a political process, either in a transparent and democratic manner or an opaque process conducted behind closed doors. Moreover, there are no simple answers and there will undoubtedly be a number of winners and losers.

[24] Depending on how many of the recommended amalgamations proceed.

Our contention is that the high information costs and rushed process means that most local residents in the six targeted North Shore group of councils will not even know the implications arising from the proposed merger until they are sent a new and significantly higher rates assessment, try to contact a local councillor, observe lower levels of road and other infrastructure maintenance diverted to areas of greater need, or discover that their personal share of municipal non-current liabilities has increased by a factor of over 50 times[25]!

5.8 Simulation of Impact of Proposed Merger on Fit for the Future Ratios

Table 5.5 details the results arising from *Fit for the Future* assessments undertaken for this Report using the OLG Toolkit for all six existing councils in the North Shore group (Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby).

Table 5.5 Existing Council Fit for the Future Assessments

F4F Criteria	Hunters Hill	Lane Cove	Ryde	Willoughby	Mossman	North Sydney
Operating Performance	No	Yes	No	Yes	No	No
Own Source	Yes	Yes	Yes	Yes	Yes	Yes
Renewal	No	Yes	No	No	Yes	No
Backlog	No	Yes	No	No	No	No
Maintenance	Yes	Yes	No	No	No	No
Debt Service	Yes	No	Yes	Yes	Yes	No
OpEx per capita over time	No	Yes	Yes	No	Yes	No
Number of Yes	3	6	3	3	4	1

Table 5.6 provides details of *Fit for the Future* assessments for three alternate merger scenarios. Despite the fatal flaws which we have already outlined in relation to the OLG Toolkit in Chapter 4 of this Report, we elected to use it in order to conclusively demonstrate that on the OLG's own

[25] As per the scenario for existing residents of Lane Cove.

evaluation instrument an amalgamated entity will be less financially sustainable than the majority of existing local authorities.

Table 5.6: Fit for the Future Simulations of Merger Scenarios

F4F Criteria	Amalgamated All Six Councils[26]	Amalgamated (Five Councils Only)	Amalgamated (Five plus 2/3rds of Ryde)
Operating Performance	No (-0.001)	Yes (0.000)[27] Care should be exercised here – see footnote	No (-0.001)
Own Source	Yes (81.67)	Yes (83.71)	Yes (82.39)
Renewal	No (91.60)	No (89.26)	No (91.0)
Backlog	No (4.79)	No (4.13)	No (4.63)
Maintenance	No (86.75)	No (84.01)	No (85.99)
Debt Service	Yes (2.90)	Yes (3.65)	Yes (3.10)
OpEx per capita over time	No (0.0011)	No (0.0033)	No (0.0016)
Number of Yes	2	3	2

Table 5.6 has been constructed according to three scenarios:

(a) All six councils;

(b) Five councils (excluding Ryde); and

(c) The five councils plus two-thirds of Ryde.

This has been done to deal with the ambiguity associated with the Panel/OLG recommendations. A comparison of the results indicates that the amalgamated entity will be no more financially sustainable - according to the OLG's own flawed model - than the current local councils. Indeed, in all likelihood all but one council will experience a decrease in financial sustainability. This is

[26] Includes *Fit for the Future* amalgamation incentive and amalgamation expenditure (based on indexed costs from Queensland amalgamations). The amalgamation incentive offered under *Fit for the Future* exceeds the indexed amalgamation costs.

[27] Whilst the Toolkit Benchmark and Results page states that the operating performance ratio is the 'average over 3 years' this is actually not the case. What the OLG Toolkit actually calculates is the cumulative ratio over 3 years which comes to 0.000310368. The average ratio over 3 years is in fact -0.002333, which would fail to achieve this benchmark. The OLG needs to be clear about what it means to calculate and the reasons for their decision so that an accurate assessment can be made for this benchmark.

conclusive evidence refuting claims by both the Panel and the OLG that council mergers would improve financial sustainability.

It should be stressed that the estimates for the merged entity exaggerate its financial sustainability because (a) they do not embody the direct costs of the process of merging the constituent councils which will involve millions of dollars, as we know from the 2008 Queensland amalgamation process; (b) they do not contain the significant additional expense arising from the diseconomies of scale which our empirical analysis conclusively demonstrates in Chapter 6; and (c) nor do they include an estimate of the higher costs which will inevitably result from upward adjustments in service quality to 'harmonise' it across the new entity.

Previous empirical work in the scholarly literature has demonstrated that service quality is invariably raised to the level of the highest service quality amongst merging councils (see, for instance, Steiner 2003; Dur and Staal 2008). This makes intuitive sense given that it would be difficult politically to require citizens to accept lower service standards. If the expected increase in service quality occurs, then it will result in most services being provided at a higher unit cost (concomitant with higher unit quality). This will make the amalgamated entity even less *Fit for the Future* than it currently appears in our simulation. Finally, the amalgamated *Fit for the Future* assessment does not include the significant write-downs of asset values that have accompanied previous boundary changes (Drew and Dollery 2015e) nor does it include the reduction in grant revenues which will likely occur four years after the merger.

In sum, even under the OLG's own criteria an amalgamation will result in a less sustainable merged municipality. Moreover, in all likelihood the actual performance of an amalgamated entity will be far worse than indicated, for the reasons set out above. We can thus only wonder as to why the Panel or the OLG or ILGRP did not perform the simulation analysis presented in Chapter 6 before recommending council mergers involving the North Shore group.

5.9 Conclusion

Chapter 5 has examined the proposed council mergers associated with the North Shore group of councils from several different perspectives. We have pondered (a) the difficulties posed the existence of significant current disparities in rates, fees and charges, and capacities to pay across the six councils which were ignored in the OLG in the merger recommendations; (b) the many difficult decisions to be made regarding changes in democratic representation post-merger; (c) the total liabilities likely to be inherited by any proposed new amalgamated municipality and its impact on local residents; (d) the complications derived from the dismemberment of the City of Ryde; (e) Commonwealth financial assistance grants post-merger; (f) the need for full information disclosure to local residents; and most importantly (g) whether merged combinations of the North Shore group of councils would be more financially sustainable under the *Fit for the Future* criteria than they had been pre-merger.

It is dismaying that neither the Panel nor the OLG had even considered most of these problems, never mind offered sound solutions. However, our most important finding in Chapter 5 is that almost all of the North Shore group of councils would be less financially sustainable under the *Fit for the Future* criteria than they had been pre-merger!

CHAPTER 6: ECONOMIC MODELLING OF PROPOSED MERGERS

Chapter Summary

- Economic modelling demonstrates that: (i) the Independent Panel's claim about scale economies proved false and that forced amalgamations will not produce cost-savings; and (ii) the Sydney amalgamations would yield over-scaled councils too large to efficiently provide local services.
- Taken together, the economic modelling shows that there is no empirical justification for the proposed merger of the Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby councils.

6.1 Introduction

As we noted in Chapter 3 and Chapter 4 of this Report, there are two main methods employed in the scholarly literature to assess municipal merger proposals. The 'standard' approach is to conduct a multiple regression analysis of expenditure per capita against population, whilst controlling for relevant exogenous factors. The more recent and more nuanced approach is to conduct a data envelopment analysis (DEA) of the existing and proposed municipal structures in order to ascertain relative scale and efficiency estimates. In Chapter 6, we produce a separate analysis following each approach in order to form robust conclusions on the likely results arising from the proposed merger of the North Sydney group of councils.

Chapter 6 is divided into four main parts. Section 6.2 discusses the inter-relationship between population size and population density in local government and conducts estimations which finds that when councils are stratified as either urban or non-urban, all evidence of scale effects (predicated on population size) disappears. Section 6.3 focuses on a data envelopment analysis of the proposed mergers recommended by the Panel and finds that over two-thirds of the amalgamated entities would be operating with decreasing returns to scale, and just two of the amalgamated entities would be operating at optimal scale if the ILGRP (2013) recommendations were enacted. Section 6.4 examines the proposed North Shore merger and finds that five of the six existing councils currently operate with increasing returns of scale at varying levels of TE and an amalgamated entity would operate with decreasing returns to scale. Chapter 6 ends with some brief concluding remarks in section 6.5.

6.2 Regression Technique for Estimating Optimal Council Size

Drew and Dollery (2014) provide a useful explanation of scale economies in the context of local government service provision:

> 'In essence, scale economies examine how the average total cost changes as the level of production increases (Drew et al. 2012). If the average total cost decreases as output increases, then economies of scale are said to be in existence. Conversely, if average total cost increases with greater output, then diseconomies of scale are in evidence… In the context of local government, economies of scale occur largely as a result of specialization, improved purchasing power, and greater utilization of capital plant. However, as a local

government entity expands difficulties coordinating and monitoring service provision mount, often resulting in increased average costs (Drew et al. 2013).'

Multiple regression analysis of per capita expenditure seeks to identify the domain of economies of scale with respect to municipal size. There is good reason to believe that the best proxy for Australian municipal size might be the number of households within the council boundary (Drew and Dollery 2014). However, because the ILGRP (2013) recommendations have been couched in terms of population, we have decided to use this as the proxy for municipal output so that we can engage fully in the current public policy debate.

Table 6.1 provides details of the regressand and regressor for the five year fixed-effects multiple regression analysis. Time invariant regressors have been excluded from Table 6.1 given that fixed effects regression does not provide output for them. Fixed-effects regression is widely considered to be the most plausible regression model when the sample exhausts the entire population (as it does in the present case) (Brooks, 2008). Moreover, the fixed-effects model has an advantage over other techniques given that it controls for unknown and unknowable omitted time invariant variables (Stock and Watson, 2011). Thus fixed effects regression is resistant to the two principal concerns in cross-section regression: omitted variable bias and the possibility of drawing the sample from an unrepresentative year.

The model specification employed in our econometric analysis can be expressed as follows:

$$E_{it} = \alpha i + \beta_1 P_{it} + \beta_2 X_{it} + \mu_{it} \qquad t=1...5$$

Where E is the natural log of expenditure per capita[28], P is a vector of population variables (i.e. population size, population sized squared and population density), X is a vector of exogenous control variables (i.e. average income of taxable individuals, percentage of persons over 65 years of age, proportion of persons under 15 years of age and total length of local government roads) and μ is an idiosyncratic error. The subscript *it* refers to the i^{th} council entity and the t^{th} year. Log transformations were employed to counter skewness in expenditure per capita, population density and average wage data.

Population density was included in recognition of the effects of density on economies of scope and scale (Drew and Dollery, 2014). Controls for age demographics (the proportion of persons under 15 years of age and over 65 years of age) were included in recognition that certain age groups are observed to place greater demands on different types of local government services, such as playgrounds and libraries. Average taxable income was included as a proxy for socioeconomic status, consistent with the literature (see, for instance Drew, Kortt and Dollery, 2015). Finally, the total length of local government roads was included on the basis that road expenditure represents the largest single component of Australian municipal expenditure (PricewaterhouseCoopers 2006, p.63).

[28] Depreciation and loss on disposal of asset costs have been excluded owing to the chaotic nature of depreciation accruals in NSW local government (Pilcher 2002; Drew and Dollery 2015).

Table 6.1: Definitions and Measures of Central Tendency for Regression Variables

Variable	Definition	Mean
Expenditure per capita (ln)	Expenditure less depreciation and asset disposals divided by the municipal population (transformed by natural log)	0.3418
Population	Number of residents residing in the council area scaled down by a factor of 1,000	46.928
Population Squared	Scaled population data squared	5553.93
Under 15	Percentage of individuals residing in the council under the age of 15	19.5612
Over 65	Percentage of individuals residing in the council over the age of 65	16.1913
Population density (ln)	Number of people per square kilometre (transformed by natural log)	2.9437
Average wage (ln)	Average wage of individuals residing in the local government area (transformed by natural log)	10.6326
Length of roads (sqrt)	Length of council maintained roads (transformed by square root)	29.1095

Three fixed-effects regressions were conducted and their results are detailed in Table 6.2. The first model examines data from the entire state and predicts diseconomies of scale up to a maxima of 308,790 residents, after which time per capita expenditure is predicted to decrease. However, population density is also highly significant (at the 1% level). This suggests conflation between population size and population density (which also explains the presence of a local maxima rather than a local minima as expected). This is hardly surprising when one considers that, in general, as population size increases population density also increases. For example, rural councils, such as Uralla (population 6,281; population density 1.94 people per square kilometre), tend to have low populations and low population density, whereas inner city municipalities, like Blacktown (population 317,598; population density 1323.32 people per square kilometre) tend to have the reverse situation. As a result, it is difficult to know whether the statistically significant data arising from an unstratified regression are a reflection of scale economies or economies of density.

Following Holcombe and Williams (2008) and Drew, Kortt and Dollery (2014), we thus conducted a further two regressions, stratified according to the Australian Classification of Local Government schema which is broadly consistent with the OLG classification groups. What we found was that when councils were stratified as either urban or non-urban, all evidence of scale effects (predicated on population size) disappeared. Thus the econometric evidence is at odds with the unsubstantiated assertions of the ILGRP (2013) that larger councils (predicated on population size) are 'more robust organisations that can generate increased resources through economies of scale and scope, and then "plough back" efficiency gains into infrastructure, services and other benefits for their communities' (ILGRP 2013, p.32).

The empirical evidence that we have presented in section 6.2 of Chapter 6 is not surprising given the heterogeneous range of services and goods produced by NSW councils. Since each service has a different capital and labour intensities, it is thus highly unlikely that the optimal service size for any two services (such as libraries and garbage collection) will coincide. As a consequence, economies of scale in one service may simply be negated by diseconomies of scale in other services.

However, as we noted in Chapter 4, regression analysis is a rather blunt empirical instrument. It is thus informative to conduct a data envelopment analysis (DEA) on NSW municipal data in order to (a) better approximate the actual council outputs; (b) assess the scale effects of the proposed ILGRP amalgamations; and (c) understand the efficiency implications of the proposed North Shore group merger.

Table 6.2: Evidence of Economies of Scale, 2009-2013

	Model 1 - NSW	Model 2 - Urban Councils	Model 3 - Non-Urban Councils
Population squared[29]	-0.00006**	-0.00001	-0.0026
	(0.00002)	(0.00001)	(0.0116)
Population	0.0360**	0.0053	0.3196
	(0.0078)	(0.0080)	(0.4264)
Density	-1.4355**	0.3550	-3.4553*
	(0.3410)	(0.4781)	(1.4253)
Exogenous controls?	Yes	Yes	Yes
N	152	81	71
Coefficient of Determination	0.5925	0.3944	0.5685

Exogenous controls include: proportion of individuals over 65 or under 15 years of age, proportion of ATSI persons, average wage, unemployment rate, total length of roads (kms) and the percentage of NESB individuals.
+ p<0.10, * p<0.05, ** p<0.01

6.3 Data Envelopment Analysis

Data Envelopment Analysis (DEA) allows for a more nuanced estimation of municipal scale and efficiency. Unlike regression analysis, DEA can accommodate multiple outputs, it does not require *a priori* specification of functional form, and it specific point estimates for each council or amalgamated entity. Technical efficiency (TE) is assessed in terms of the ability of a council to convert inputs (staff and capital) into a set of outputs (number of households, number of employing businesses and length of municipal roads) (see Drew, Kortt and Dollery (2015) for the justification of the DEA specification employed). The actual calculation employs linear programming to create an efficient frontier (comprised of the councils which most efficiently convert inputs into outputs) and then estimates relative efficiency of councils lying in the interior of the efficiency frontier according to their distance from the frontier. Two estimations of TE are commonly employed in the literature: the constant returns to scale (CRS) model and the variable returns to scale (VRS) model. The latter model adjusts efficiency estimates to account for scale effects: that is, the VRS model ensures that an inefficient council is only evaluated against

[29] Population and Population squared were scaled down by a factor of 1,000. Expenditure per capita and population density have been transformed (ln).

councils of a similar size. As a result, VRS scores are greater than or equal to CRS estimates of TE.

The constant returns to scale (CRS) algorithm is detailed below:

$\min \theta,\lambda\ \theta,$

s.t. $-yi + Y\lambda \geq 0,$
$\theta xi - X\lambda \geq 0,$
$I1'\lambda = 1$
$\lambda \geq 0$

where yi is a vector of outputs and xi is a vector of inputs, θ is a scalar (the efficiency score for each council) and λ a vector of constants. The subscript *i* refer to the *i*th council and the inequalities ensure non-negative weights. The CRS specification evaluates inefficient councils against any peer on the frontier, irrespective of size. The variable returns to scale (VRS) algorithm is achieved by adding the convexity constraint $I1'\lambda = 1$ so that inefficient councils are only evaluated against municipalities of a similar size. Under both estimates efficient councils are given a score of 1 and inefficient councils assigned a score between 0 and 1. Scale estimates are simply the quotient of CRS and VRS efficiency scores and a third estimate (non-increasing returns to scale (NIRS)) is made by imposing the restriction $I1'\lambda \leq 1$ so that the nature of the scale inefficiency can be determined.

Table 6.3 presents the measures of scale for the existing municipal structures calculated according to 2013 data (the extent of ABS data on employing businesses). The first set of scale estimates summarise all NSW councils and the second set of estimates refer to the subset of councils proposed for amalgamation (ILGRP, 2013). What is interesting is that five of the

councils proposed for amalgamation are already at optimum scale, whilst all councils proposed for amalgamation currently exhibit decreasing returns to scale (i.e. their technical efficiency is diminished by being too large). Moreover, where two or more councils exhibiting increasing returns to scale are merged, it is entirely possible that the resultant entity will be over-scaled.

Table 6.3: Scale Results: Pre-Amalgamation 2013

Amalgamation status	Scale	Number	Mean scale	Median scale	Stand. Dev.
All NSW councils	OS	10	1	1	0
	IRS	107	0.913673	0.961648	0.10653
	DRS	35	0.908377	0.942027	0.090211
Councils to be Amalgamated					
	OS	5	1	1	0
	IRS	50	0.900444	0.96389	0.119421
	DRS	7	0.941517	0.965585	0.058392

Notes: OS = optimal scale; IRS = increasing returns to scale; DRS = decreasing returns to scale.

Table 6.4 details the scale results based on DEA estimates in which it is presumed that all of the ILGRP (2013) amalgamation recommendations proceed (this approach follows Drew, Kortt and Dollery (2015) and Cooper et al. (2007)). We have summarised the results for 'amalgamated' and 'non-amalgamated' entities separately in order to facilitate comparisons. What we find is that over two-thirds of the amalgamated entities would be operating with decreasing returns to scale, and just two of the amalgamated entities would be operating at optimal scale if the ILGRP (2013) recommendations were allowed to proceed as planned. This result should serve as a warning against the presumption that larger councils will necessarily be more efficient.

Table 6.4: Scale Results: Post-Amalgamation 2013

Amalgamation status	Scale	Number	Mean scale	Median scale	Stand. Dev.
Amalgamated	OS	2	1	1	0
	IRS	5	0.984367	0.989982	0.014536
	DRS	15	0.874822	0.883753	0.067295
Non-amalgamated Councils	OS	5	1	1	0
	IRS	60	0.903707	0.92987	0.091257
	DRS	24	0.911952	0.95821	0.090048

Notes: OS = optimal scale; IRS = increasing returns to scale; DRS = decreasing returns to scale.

6.4 Efficiency Comparison for Proposed North Shore Merger

The techniques employed above generate a good understanding of the deleterious results that might be expected for the NSW local government sector if the ILGRP (2013) recommendations based on ideological presumption – rather than sound empirical analysis – are allowed to proceed. However, because the two sets of DEA estimates are constructed according to relative efficiency frontiers, it is not possible to make direct comparisons between pre- and post-amalgamation municipal structures.

One way of dealing with the relative frontier problem is to examine the pre- and post-amalgamation structures for a specific proposal within a single DEA (see, for instance, the pioneering work of Cooper *et al*. 2007). Table 6.5 compares the TE for the stand-alone and amalgamation scenarios for the six North Shore group of councils which have been the focus of this Report. Thus, the DEA conducted to produce the results in Table 6.5 utilises data for 153 councils: the 152 existing NSW councils plus an additional entity formed from the proposed North Shore group amalgamation (ILGRP 2013). Under this method we can compare the

efficiency implications arising from the specific case of amalgamating the six councils into a putative North Shore group.

What we find is that five of the six existing entities currently operate with increasing returns of scale at varying levels of TE. The sixth council (North Sydney) lies on the efficient frontier and it is operating at optimal scale. An amalgamated entity (along the lines proposed by the ILGRP (2013)) would operate with decreasing returns to scale and an efficiency of just over 0.797. The proposed merger would result in a significant decrease in efficiency for the Ryde and North Sydney councils and a slight decrease in efficiency for the Lane Cove municipality. Put differently, amalgamation would result in lower levels of efficiency for three of the councils and a barely perceptual improvement for a fourth council (Hunters Hill). Given the high transformation costs, disruption to services, decrease in democracy, the redistribution of council liabilities, and the decrease in financial sustainability which will accompany the proposed amalgamation, it is more than a little disconcerting that the proposed merger will only result in a material improvement in efficiency for two of the councils involved (Mosman and Willoughby).

Table 6.5: Comparison of Technical Efficiency and Scale under Non-Amalgamation and Amalgamation Scenarios

Council	Technical Efficiency[30]	Scale	Returns to Scale
Hunters Hill	0.788491	0.788491	Increasing
Lane Cove	0.826471	0.931865	Increasing
Ryde	0.96163	0.992882	Increasing
Willoughby	0.742302	0.987825	Increasing
Mosman	0.621084	0.901788	Increasing
North Sydney	1	1	Optimal
Amalgamated Entity	0.797484	0.797484	Decreasing

[30] These TE scores are CRS estimates as it is important that we do not make upward adjustments to mitigate the effect of scale – the whole purpose of this analysis is to determine whether a larger municipal structure would be more efficient.

6.5 Concluding Remarks

We have conducted analysis of the likely outcomes arising from amalgamation according to the two principal techniques employed in the empirical literature on local government: multiple regression analysis and data envelopment analysis. The results of the multiple regression analysis suggests that the ILGRP's (2013) unsubstantiated assertions of economies of scale – according to their preferred functional unit of population size – are completely illusory. Moreover, our DEA (using the multiple outputs of number of households, number of employing businesses and length of municipal roads) provides empirical evidence that the vast majority of proposed amalgamations will result in over-scaled councils which are too large to efficiently provide municipal goods and services. Finally, our DEA of the efficiency and scale implications arising from the proposed amalgamation of the North Shore group of councils suggests that there would be deleterious implications for three of these local authorities' efficiency should the proposed merger proceed.

In sum, there is no empirical justification for the proposed merger. Indeed, were the amalgamations to proceed as proposed by the Panel, the people of NSW can expect less efficient municipal services arising from ill-informed mergers resulting in councils which are too large to make the best use of capital and labour inputs.

CHAPTER 7: SOCIO-ECONOMIC CHARACTERISTICS OF THE HUNTERS HILL, LANE COVE, MOSMAN, NORTH SYDNEY, RYDE AND WILLOUGHBY COUNCILS

Chapter Summary

- This chapter presented a detailed analysis of the socio-economic characteristics of Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby councils.
- This analysis shows that there are noticeable differences in the socio-economic profiles among these councils.
- Given the differences between these councils the proposed merger cannot be mounted on 'community of interest' arguments.

7.1 Introduction

In Chapter 7, a descriptive analysis will be undertaken to examine the socio-economic characteristics of Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby. More specifically, the analysis will centre on comparing: age distributions and population projections, birth and fertility rates, labour force characteristics, family dynamics, income support, education levels, overweight and obesity, mental health conditions, health risk factors and health service utilisation.

Arguments in favour of council amalgamation are often based on the notion of 'community of interest'. However, the empirical analysis presented in Chapter 7 indicates that these local communities have sharply different characteristics. This means that the proposed merger of

Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby cannot be based on 'community of interest' considerations.

Chapter 7 is comprised of two main parts. Section 7.2 provides a socio-economic overview of Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby. Chapter 7 concludes in Section 7.3 with a discussion of 'community of interest' based on community characteristics and argues that Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby should not be merged.

7.2 Council Characteristics

There are 38 metropolitan NSW councils based on the current local government boundaries in Sydney. These 38 councils, which constitute 'Greater Sydney', can be divided into:

- 17 outer Sydney councils (Figure 7.1) of which Ryde council is a member; and
- 21 inner Sydney councils (Figure 7.2) of which Hunters Hill, Lane Cove, Mosman, North Sydney, and Willoughby are members.

Figure 7.1: Outer Sydney Councils (n = 17)

Source: NSW Government, Department of Premier and Cabinet.

Figure 7.2: Inner Sydney Councils (n = 21)

Source: NSW Government, Department of Premier and Cabinet.

An overview of council characteristics in terms of population, land area, population density, and for Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby is reported in Table 7.1.

Table 7.1: Overview of Council Characteristics

Council	Population	Area sq. km	Population Density
Hunters Hill	14,663	6	2,444
Lane Cove	33,976	10	3,398
Mosman	29,414	9	3,268
North Sydney	65,318	10	6,532
Ryde	107,307	40	2,683
Willoughby	70,705	22	3,214
Greater Sydney	**4,003,847**	**3,694**	**1,084**

Source: PHIDU (2015)

With respect to population, Ryde has the largest population with 107,307 people followed by Willoughby (70,705 people), North Sydney (65,318 people), Lane Cove (33,976 people), Mosman (29,414 people) and then Hunters Hill (14,663 people). In terms of land area, Ryde council accounts for 40 square kilometres, followed by Willoughby (22 square kilometres), Lane Cove and North Sydney (both 10 square kilometres), Mosman (9 square kilometres) and then Hunters Hills (6 square kilometres). With respect to population density (i.e., the number of people divided by the land area in square kilometres, North Sydney has the highest population density at 6,532 persons per square kilometre, followed by Lane Cove (3,398 persons per square kilometre), Mosman (3,268 persons per square kilometre), Willoughby (3,214 persons per square kilometre), Ryde (2,683 persons per square kilometre) and then Hunters Hill (2,444 persons per square kilometre).

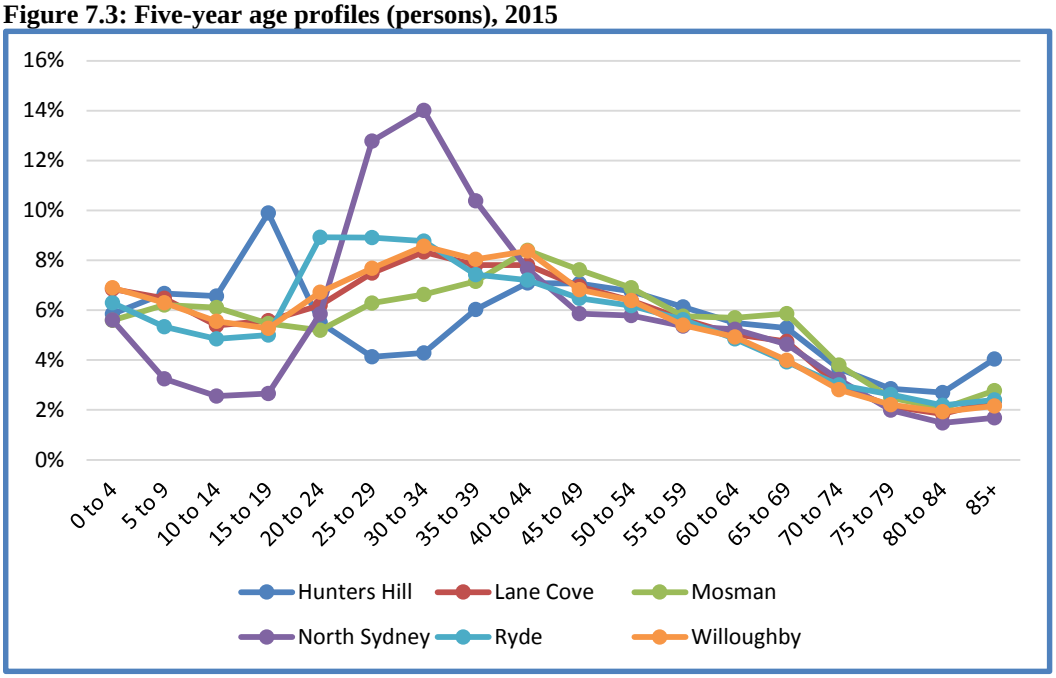
In considering Table 7.1, it is worth noting that Ryde is by far the largest councils in terms of both population size and geographical area (and the second smallest in terms of population density). At first blush, this suggests that Ryde council is significantly different from the other councils (at least in terms of population size and geographical area).

7.2.1 Age Distributions and Population Projections

The five-year age profiles for Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby councils are presented in Figure 7.3. With respect to the age distribution in Figure 7.3 the following points are noteworthy:

- North Sydney has the greatest proportion of people in the age groups spanning **25** to **39** and the lowest proportion of people in the age groups spanning **5** to **19**;
- Hunters Hill has the greatest proportion of people in the age group **15** to **19** and the lowest proportion in proportion of people in the age groups spanning **25** to **39**; and
- Ryde has the highest proportion of people in the age group **20** to **24**.

Figure 7.3: Five-year age profiles (persons), 2015

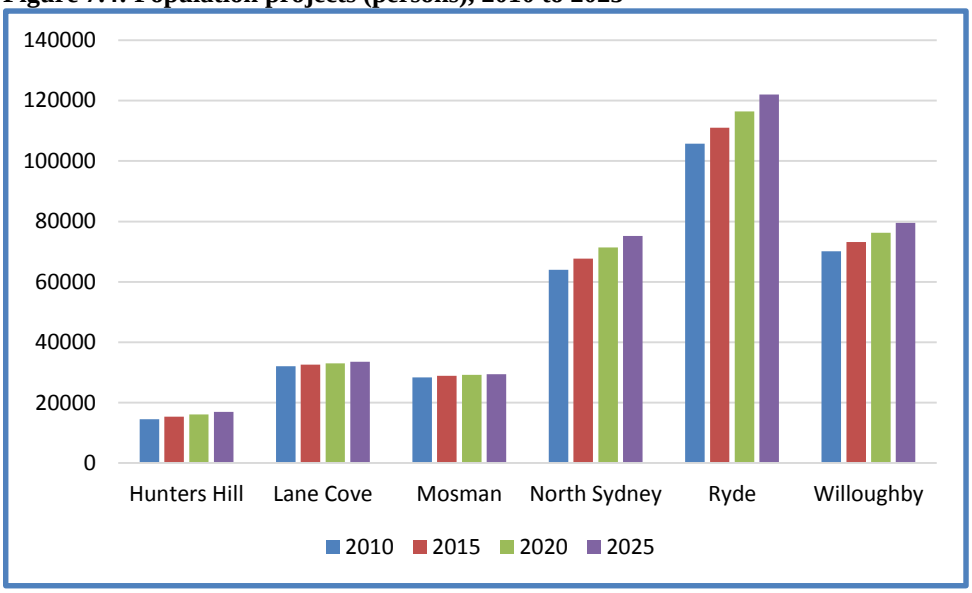


Source: PHIDU, Social Health Atlas of Local Governments Areas (2015)

Knowledge of these different age profiles is particularly important from a planning and service delivery perspective. Different age profiles require different planning and service delivery strategies. In other words, the requirements of North Sydney and Hunters Hill differ markedly from the needs of the other councils targeted in the proposed merger.

However, it is important to note that these age profiles may change over time due to changing population structures and growth rates at the local government area level. For planning and service delivery purposes it is often informative to consider population projections at the local government level (Figure 7.4).

Figure 7.4: Population projects (persons), 2010 to 2025



Source: PHIDU, Social Health Atlas of Local Governments Areas (2011)

For Hunters Hill, it is projected that between 2010 and 2025 the population will increase by 17%, which equates to an annual growth rate of 0.9%. For Lane Cove, it is anticipated that population will increase by 5%, which equates to an annual growth rate of 0.29%. For Mosman, it is

expected that the population will increase by 4%, which equates to an annual growth rate of 0.23%. For North Sydney, it is projected that the population will increase by 17%, which equates to an annual growth rate of 1.01%. For Ryde, it is estimated that the population will increase by 15%, which equates to an annual growth rate of 0.89%. Finally, for Willoughby, it is anticipated that the population will increase by 13%, which equates to an annual growth rate of 0.79%. Thus, Lane Cove and Mosman have the lowest annual population growth rates (at 0.29% and 0.23% respectively), while North Sydney and Ryde have the highest annual population growth rates (at 1.01% and 0.89% respectively).

However, it is possible that the population projections for Hunters Hill and Lane Cove may, over time, be reversed. This is because Lane Cove is currently experiencing unprecedented growth having recently approved 3,200 units with an average occupancy rate of 1.9 persons (or an additional 6,080 people). This, in turn, could substantially raise the population growth rate for Lane Cove over the period 2010 to 2025 so that it is greater than the current Hunters Hill population projection of 17%.

Although these local population projections provide useful insights, it is important to emphasise that these estimates need to be viewed with caution. Population projects are based on extrapolating current trends and are best viewed as ‘what if’ scenarios (i.e. what would happen to the local population if current growth rates persisted in the absence of any external factors). It is important to note that population projections do not take account of current or future local government policy initiatives, which may stimulate or inhibit local population growth.

7.2.2 Birth and Fertility Rates

Two factors underpinning population growth are the number of births and the fertility rate. According to the Population Health Development Unit at the University of Adelaide, the total fertility rate (birth rate) for Australia from 2011 is 1.88 children. Estimates of the number of births and the fertility rate for Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby from 2011 are reported in Table 7.2

Table 7.2: Births and Fertility Rates, 2011

Council	2011	
	Births	**Total fertility rate**
Hunters Hill	147	1.85
Lane Cove	446	1.69
Mosman	364	1.65
North Sydney	1,084	1.39
Ryde	1,375	1.60
Willoughby	981	1.65
Australia	**301,617**	**1.88**

Source: PHIDU, Social Health Atlas of Local Governments Areas (2015)

While the fertility rates for Hunters Hill (1.85 children) is broadly similar to the Australian rate of 1.88 children, the fertility rates for Lane Cove (1.69 children), Mosman (1.65 children), Ryde (1.60 children) and Willoughby (1.65 children) are noticeably lower. Finally, it is worth highlighting that the fertility rate for North Sydney (1.39 children) is well-below the Australian average (1.88 children).

7.2.3 Labour Force Characteristics

Details of the labour force characteristics for Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby are reported in Table 7.3. Looking across Table 7.3, there are some noticeable differences between the unemployment rates and labour force participation rates. In the first instance, the unemployment rates for Lane Cover (3.3%), Mosman (2.9%) and North Sydney (2.9%) were well below the national unemployment rate of 6%. Comparatively low unemployment rates were also observed for Hunters Hill (4.6%) and Willoughby (4.3%). On the other hand, the unemployment rate for Ryde (6.2%) was considerably higher, but nonetheless comparable to the national unemployment rate (6%).

With respect to labour force participation rates, the participation rates for Lane Cove (70%), Mosman (67%), North Sydney (77%), Ryde (68%) and Willoughby (69%) were higher than the national labour force participation rate of 65%. On the other hand, the labour force participation rate for Hunters Hill (62%) was noticeably lower than the national labour force participation rate (65%). Finally, the highest rates of female labour force participation were observed for North Sydney (67%) and Lane Cove (63%), whereas the lowest female labour force participation rate was observed for Hunters Hill (52%).

Table 7.3: Labour Force Participation, 2014

2014 **Unemployment**	**Number**	**Labour force**	**% unemployed**
Hunters Hill	340	7,324	4.6
Lane Cove	647	19,350	3.3
Mosman	475	16,601	2.9
North Sydney	1,361	47,393	2.9
Ryde	3,952	63,859	6.2
Willoughby	1,761	40,962	4.3
Australia	**732,709**	**12,277,789**	**6.0**

2014 **Labour force participation**	**Number**	**Population aged 15 years and over**	**% labour force participation**
Hunters Hill	7,324	11,726	62
Lane Cove	19,350	27,635	70
Mosman	16,601	24,615	67
North Sydney	47,393	61,339	77
Ryde	63,859	93,992	68
Willoughby	40,962	59,449	69
Australia	**12,277,789**	**18,760,524**	**65**

2014 **Female labour force participation**	**Number**	**Females aged 15 years and over**	**% female labour force participation**
Hunters Hill	2,878	5,521	52
Lane Cove	8,491	13,386	63
Mosman	6,713	12,184	55
North Sydney	19,520	29,173	67
Ryde	25,470	44,782	57
Willoughby	16,859	28,719	59
Australia	**4,971,658**	**8,857,519**	**56**

Source: PHIDU, Social Health Atlas of Local Governments Areas (2015)

7.2.4 Family Dynamics

Family dynamics is another socio-economic dimension that can be used to better understand the characteristics of local communities. The data contained in Table 7.4 is based on the most recent estimates prepared by the Population Health Development Unit at the University of Adelaide. While these estimates are from 2011, they can nonetheless foster some broad insights into the

characteristics of family dynamics Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby.

Table 7.4: Family Dynamics, 2011

Council	% single parent families	% jobless families
Hunters Hill	11.1	5.8
Lane Cove	11.5	4.0
Mosman	12.6	5.4
North Sydney	14.0	4.9
Ryde	13.0	7.1
Willoughby	11.2	6.2
Australia	21.3	13.3

Source: Social Health Atlas of Local Governments Areas (2015)

In Australia as a whole, it was estimated that single parent families with children aged less than 15 years accounted for 21.3% of *all* total families with children under 15 years. Across all six local government areas in Table 7.4, the percentage of single parent families was considerably lower than the national average. Among these six councils, North Sydney (14%) and Ryde (13%) had the highest rates of single parent families, while Hunters Hills (11.1%) had the lowest rate.

A further conventional measure of family dynamics is the number of 'jobless families' (i.e. parent(s) not employed with children under 15 years). In 2011, it was estimate the 13.3% of Australian families were classified as being jobless. Across all six councils, the rate of 'jobless families' was again well below the national average. The rate of 'jobless families' was highest for Ryde (7.1%), but noticeably lower for North Sydney (4.9%) and Lane Cove (4%).

7.2.5 Income Support

Table 7.5 presents the percentage of residents in Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby receiving income support in 2012/2013. The following income support categories are covered in Table 7.5: (i) Age Pension (AP), (ii) Disability Support Pension (DSP), (iii) Long-Term Unemployed Benefit (LTUB), and (iv) Youth Unemployment Benefits (YUB).

Table 7.5: Income Support, 2012/2013

Council	% AP	% DSP	% LTUB	% YUB
Hunters Hill	42.3	2.5	1.0	n.a.
Lane Cove	37.3	1.6	1.0	0.6
Mosman	25.7	1.1	0.7	n.a.
North Sydney	33.9	1.3	0.9	0.6
Ryde	63.8	3.1	1.7	0.7
Willoughby	42.8	1.6	1.1	0.5
Australia	**72.5**	**5.5**	**4.0**	**4.0**

Source: Social Health Atlas of Local Governments Areas (2015)
Notes: (i) Age pension (AP); (ii) Disability Support Pension (DSP); (iii) Long term unemployed (LTUB) 16-64; and (iv) Youth unemployment benefits (YUB) 16-24.

In 2012/2013, an estimated 72.5% of Australians of pensionable age received the Age Pension. While considerably lower than the national average, the Age Pension rate in Ryde (63.8%) was substantially higher than the other councils listed in Table 7.5. At the other end of the spectrum, Mosman (25.7%) had by far the lowest Age Pension rate among this group of councils.

In Australia, the proportion of people receiving a Disability Support Pension (DSP) was 5.5%. While considerably lower than the national average, DSP rates for Ryde and Hunters Hill were noticeably higher than the DSP rates for Lane Cove, Mosman, North Sydney, and Willoughby.

In Australia as a whole, the proportion of individuals in receipt of long-term unemployment benefits (LTUB) was 4.0%. Across all six councils, the LTUB rate is broadly comparable and considerably lower than the national average. Finally, whereas the proportion of all Australians on Youth Unemployment Benefits (YUB) was 4.0%, all six councils in Table 7.5 had extremely low rates of persons on Youth Unemployment Benefits.

7.2.6 Participation in Education

Details of the most recently available analysis of educational participation for Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby are reported in Table 7.6.

Table 7.6: Participation in Education, 2011/2012

Full-time participation in secondary school education at age 16	**Full-time participation at age 16**	**People aged 16**	**% full-time participation at age 16**
Hunters Hill	272	286	95
Lane Cove	344	377	91
Mosman	254	285	89
North Sydney	282	350	81
Ryde	892	1,031	87
Willoughby	607	679	89
Australia	**225,238**	**284,761**	**79**
Participation in vocational education and training	**Number**	**Rate per 100**	**SR**
Hunters Hill	466	3.4	40
Lane Cove	1,169	3.6	42
Mosman	801	2.9	35
North Sydney	2,158	3.1	37
Ryde	5,994	5.2	62
Willoughby	2,560	3.6	43
Australia	**1,909,544**	**8.4**	**100**

Source: Social Health Atlas of Local Governments Areas (2015)

Of particular interest in Table 7.6 is the: (i) percentage of full-time participation in secondary school education at age 16, and (ii) the standardised ratio (SR) for participation in vocational education and training. In 2011, the proportion of all Australians aged 16 and engaged in full-

time secondary school education was 79%. The participation rate in full-time second school education was not only similar across all six local government areas, but also substantially higher than the national average.

The standardised ratio (SR) is 'benchmarked' against the Australian average, which is set at 100. The SR is relatively easy to interpret. For example, consider the Hunters Hill SR of 40. This means that participation in vocation education and training in Hunters Hill is 60% *lower* than the Australian average [i.e., (40/100-1)*100]. Comparable interpretations can be made for the other councils listed in Table 7.6. However, it needs to be borne in mind that while all six councils fall below the national average, the vocational education and training participation rate for Ryde (5.2 per 1,000) is noticeably higher than the participation rates for the other five councils.

7.2.7 Overweight and Obesity

The prevalence of overweight and obesity is another important dimension that can be used to understand the local characteristics and health services needs of local communities (Table 7.7). The medical literature has clearly demonstrated that overweight and obesity are independent risk factors for a range of serious medical conditions, including Type 2 diabetes, elevated cholesterol levels, hypertension, coronary heart disease, musculoskeletal disorders, and several cancers.

Looking across Table 7.7 it is worth noting that the proportion of Australian men who were classified as either being overweight or obese was 42.2% and 27.5% respectively. The proportion of Australian women who were classified as either being overweight or obese was 28.2% and 27.5% respectively.

Table 7.7: Overweight and Obesity 2011-13 (estimates)

Council	Overweight males, 18+		Obese males, 18+		Overweight females, 18+		Obese females, 18+	
	Rate per 100	SR	Rate per 100	SR	Rate per 100	SR	Rate per 100	SR
Hunters Hill	44.9	106	22.0	80	27.0	96	15.4	56
Lane Cove	42.9	102	17.1	62	25.6	91	9.4	34
Mosman	43.6	103	16.7	61	26.9	95	10.9	40
North Sydney	41.9	99	16.4	60	25.5	90	10.1	37
Ryde	42.2	100	23.6	86	24.5	87	14.2	52
Willoughby	42.8	101	18.1	66	24.6	87	9.0	33
Australia	**42.2**	**100**	**27.5**	**100**	**28.2**	**100**	**27.5**	**100**

Source: Social Health Atlas of Local Governments Areas (2015)

Across all six councils, the proportion of overweight weight was comparable to the national average. While the proportion of obese men across all six councils is considerably lower than the national average (27.5%), Hunters Hill (22%) and Ryde (23.6%) have a noticeably higher proportion of obese men compared to other councils. A similar for pattern is also observed for overweight and obese women across these six councils.

7.2.8 Mental Health

Mental health costs Australia a great deal. There are the human costs, such as time lost to disability; financial costs to the economy as a result of lost productivity brought on by mental health conditions; and also expenditure by governments and individuals to combat the illness. In 2002-03, the total expenditure on mental health services across all levels of government and the private sector totalled $3.3 billion (Senate Select Committee on Mental Health, 2006).

The data presented in Table 7.8 are estimates based on self-reported survey responses that have been compiled by the Population Health Development Unit. While these estimates are based on

self-diagnosis rather than clinical assessment by a health professional, these data nonetheless provide a useful insight into the impact of mental health conditions in local communities.

Table: 7.8: Mental Health 2011-2013 (estimates)

Council	Males with mental and behavioural problems		Females with mental and behavioural problems	
	Rate per 100	SR	Rate per 100	SR
Hunters Hill	12.3	102	12.0	79
Lane Cove	12.1	100	12.0	80
Mosman	12.0	100	12.6	83
North Sydney	12.9	108	13.0	86
Ryde	13.1	109	13.0	86
Willoughby	12.6	105	12.2	81
Australia	**12.0**	**100**	**15.1**	**100**

Source: Social Health Atlas of Local Governments Areas (2015)

In 2011-13, the proportion of Australian men and women who identified themselves as having mental and behavioural problems was 12% and 15.1% respectively. For men, the rate of mental and behavioural problems was comparable to the national average for the majority of councils listed in Table 7.8, although the rates for Ryde (13.1%) and North Sydney (12.9%) were noticeably higher. For women, the rate of mental and behavioural problems across all councils was considerably lower than the national average (15.1%).

7.2.9 Health Risk Factors

Lifestyle factors, such as smoking and alcohol consumption, can lead to an increased risk of a variety of chronic diseases including cancer, diabetes and heart disease. The data presented in Table 7.9 presents the estimates for: (i) current smokers 18 years and over; and (ii) alcohol consumption at levels considered to be a high risk to health for persons 18 years and over.

Table 7.9: Health risk factors 2011-13 (estimates)

Council	Current smokers, persons 18 years and over		Alcohol consumption at levels considered to be a high risk to health, persons aged 18 years and over	
	Rate per 100	SR	Rate per 100	SR
Hunters Hill	11.5	64.1	4.5	97.2
Lane Cove	8.7	48.3	4.0	85
Mosman	9.0	50.1	3.9	84.1
North Sydney	10.0	55.5	4.4	95.5
Ryde	10.6	59.3	4.1	89.2
Willoughby	8.7	48.2	4.0	85
Australia	**18.0**	**100**	**4.7**	**100**

Source: Social Health Atlas of Local Governments Areas (2015)

In relation to smoking rates, the 2011-13 smoking rate in Australia was 18% for persons 18 and over. Across all local government areas listed in Table 7.9, the smoking rate was considerably lower than the national average. Lane Cover and Willoughby had the lowest proportion of smokers (8.7%), while the highest rates of smokers was observed for Hunters Hill (11.5%) and Ryde (10.6%). Alcohol consumption at levels considered to be a high risk to health is the second health risk factor presented in Table 7.9. Across all local government areas, the 'high risk' alcohol consumption estimates were well below the national average.

7.2.10 Health Service Utilisation

Health care services utilisation for Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby is reported in Table 7.10. More specifically, Table 7.10 shows (i) the number of GP services utilised per 100,000 people and (ii) the standardised ratio (SR) for each local government area.

Table 7.10: Health Service Utilisation, 2009/2010

Council	GP services	
	Rate per 100,000	**SR**
Hunters Hill	441903.3	81
Lane Cove	457873.8	84
Mosman	454592.4	83
North Sydney	440845.1	81
Ryde	546602.2	100
Willoughby	484900.2	89
Australia	545012.2	100

Source: Social Health Atlas of Local Governments Areas (2015)

Looking across Table 7.10, the following points are worth noting. First, GP service utilisation for Ryde is consistent with the national rate of service utilisation. Second, all other local government areas listed in Table 7.10 have GP service utilisation rates well below the national average.

7.3 Conclusion

Arguments presented in support of council mergers are often grounded on the notion of 'community of interest', which according to Fulcher (1989, p.7) encompasses: (i) a 'sense of belonging to an area or locality which can be clearly defined', (ii) the ability to meet the community's 'physical and human services', and (iii) the ability of the 'elected body to represent the interests' of its members. Thus, councils with similar 'community of interest' profiles represent a stronger rationale for council amalgamation compared to those councils with markedly dissimilar 'community of interest' profiles.

However, given the differences between Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby the proposed merger cannot be mounted on 'community of interest' arguments. For instance, it is worth noting that – when compared to the other councils – **Ryde** has:

- The **largest** population;
- The **largest** geographic area;
- The **highest** proportion of people in the age group **20** to **24**;
- The **highest** level of unemployment;
- The **highest** percentage of jobless families;
- The **highest** percentage of people of pension age receiving the Age Pension;
- The **highest** rate of participation in vocational education and training; and
- The **highest** rate of GP service utilisation.

Thus, the observed differences in the socio-economic profiles between Ryde and the other local government areas means that different planning and service delivery strategies will need to be implemented for each local government area. In other words, the community needs and priorities for Ryde will differ significantly from the community needs and priorities for the other councils. Thus, given these differences, there is no 'community of interest' imperative to proceed with a merger, which may also inadvertently lead to a widening of these socio-economic differences if 'inner-Sydney' local government strategies are pursued at the expense of 'outer-Sydney' local government strategies.

CHAPTER 8: EMPIRICAL EVIDENCE ON SHARED SERVICES IN LOCAL GOVERNMENT

Chapter Summary

- A detailed review of the empirical literature finds strong evidence that shared services could yield significant benefits (and cost-savings) to participating councils.
- Successful shared services arrangements typically include IT services, human resources and waste management.
- However, it need to be borne in mind that not all local services are amenable to regional provision through shared service arrangements.

8.1 Introduction

Chapter 8 summaries the extant empirical evidence on shared services in terms of both cost-savings and other economic benefits, as well as identifying which specific local government functions and services may benefit most from shared services arrangements.

Chapter 8 is divided into four main parts. Section 8.2 provide a synoptic account of the empirical evidence on shared services in Australia. Section 8.3 provides a summary of the empirical evidence on shared services internationally. Chapter 8 concludes in section 8.4, which considers the policy implications associated with body of evidence.

8.2 Empirical Evidence on Shared Services in Australian Local Government

It is somewhat surprising that there are a limited number of empirical studies that have investigated the economic effects of shared services arrangements in the Australian context. To date, the existing empirical literature is comprised of evidence drawn from three surveys, four case studies, and a literature review undertaken by KM Management Consulting (KMMC) (2005) for the Local Government Association of Queensland (LGAQ). However, this small body of empirical evidence still suggests that shared services may offer a range of economics and social benefits to participating councils in the Australian milieu. For convenience, this empirical evidence is summarised in Table 8.1.

Table 8.1: Australian Empirical Evidence on Shared Services Arrangements

Publication	Method	Sample	Summary of Main Findings
Lawson (2007)	Survey	34 South Australian Councils	Identified seven service areas with the greatest resource sharing opportunities, as well as some impediments to implementation of shared services.
Burow Jorgensen & Associates (2006)	Survey	55 WA Local Councils	92% of councils were engaged in resource sharing in various areas, including waste collection, recycling and disposal, human resource, information technology, road works, library facilities and so on.
Byrnes (2005)	Survey	19 NSW Metropolitan and Regional Councils	Identified eight services most suitable for resource sharing and seven services that should be provided locally.
Dollery & Byrnes (2006)	Case study	Walkerville Council, SA	Listed nine regional co-operative agreements Walkerville had entered into and provided estimates of benefits.
Dollery, Burns & Johnson (2005)	Case study	Armidale Dumaresq, Uralla, Guyra and Walcha Councils, NSW	Strategic Alliance of the Councils brought substantial benefits/savings through collaboration in the number of areas.
Local Government Association of Queensland (2005)	Case study	Wellington, Blayney and Cabonne Strategic Alliance, NSW	The Alliance achieved $720,000 savings in first ten month of operation through co-operative arrangements, joint purchases and staff and resource sharing.
Dollery, Marshall, Sancton & Witherby (2004)	Case study	Riverina Eastern Regional Organisation of Councils (REROC), NSW	REROC achieved savings of $4.5 million through reduced duplication, joint tendering, regional lobbying and co-operative sharing of resources.
KMMC (2005)	Literature Review	Not applicable	Identified six services most able to be successfully delivered through regional services units and three services most suited to delivery on a shared regional basis

Source: Adapted from Dollery and Akimov (2008).

The first study listed in Table 8.1 is a survey conducted by Lawson (2007). In this study, Lawson (2007) collected data from 34 South Australian councils regarding their participation in the delivery of local services. In the analysis of survey responses, Lawson (2007) found that:

1. Although the prospect of financial benefits was a main reason for entering into shared services agreements, only a small number of councils actually realised cost-savings; and
2. Expected financial benefits were not the only reason for entering into shared services agreements (other reasons included the prospect of securing access to a wider range of services).

Moreover, the six most common areas for shared services that were identified by Lawson (2007) included:

- Waste management
- Town planning
- Joint purchasing of physical assets
- 'Back-office' operations
- IT services
- Financial services.

In a 2006 survey of metropolitan and rural councils in WA, Burow Jorgensen and Associates (BJA) reported that 92% of councils surveyed had participated in shared services arrangements and that such arrangements were more commonplace among regional and remote councils. The authors of the report also identified that the most common shared services arrangements included:

- Waste management
- IT services
- Personnel resources
- Health and planning
- Library services
- Land management services.

In another survey of NSW councils, Byrnes (2005) identified the following local services that were considered suitable by respondents for shared delivery. These local service included:

- Fire protection
- Emergency services
- Health and planning
- Toxic plants and weeds
- Waste management and water
- Local markets and sale yards.

Furthermore, Byrnes (2005) also identified the following areas that respondents considered were best provided ‘in-house’ by councils. These services included:

- Public toilets
- Public halls

- Parks and gardens
- Property development.

The four case studies presented in Table 8.1 provide tangible examples of successful shared services arrangements between councils that have resulted in cost-savings. The first case study listed in Table 8.1 by Dollery and Byrnes (2006) examined that situation of SA Walkerville Council and its experience with shared service delivery involving neighbouring councils. More specifically, the Walkerville Council entered into nine agreements with a number of municipalities to jointly provide the following services:

- Waste collection
- Home care
- Crime deterrence
- Library service
- Health and planning
- Inspections.

Dollery and Byrnes (2006) reported – at the time – that the CEO of the Walkerville Council had estimated that the shared services arrangements entered into by the Council had resulted in an annual cost-saving of $138,180. In another case study, Dollery, Burns and Johnson (2005) also assessed the NSW Strategic Alliance Model that was developed by the Armidale Dumaresq, Guyra, Uralla and Walcha councils. In essence, the authors of this study concluded that:

> "The movement to shared services should generate economies of scale and reduce duplication. The Strategic Alliance has estimated that in the administrative core services areas, such as IT, finance, human resources, payroll, records, supplies, stores, plant and GIS, some 10 positions (representing 2.3 per cent total employment) could be abolished in the first instance and redeployed into other value adding positions, realizing around $800k in additional savings. Over the longer term, 18 positions were believed initially achievable yielding $1,450k in savings. However, it has been learned thus far in implementing the organizational development projects that even greater savings will be achieved that can be reinvested into value adding areas" (Dollery, Burns and Johnson, 2005, p.18).

However, the major drawback with this case study is that it only presented *potential cost-savings* as opposed to *actual cost-savings* that could have been achieved under the NSW Strategic Alliance Model. Nevertheless, this case study still serves to highlight that potential cost-savings could be substantial.

The third case study listed in Table 8.1 is the 2005 Queensland Local Government Association discussion paper entitled *Size, Shape and Sustainability*. In this discussion paper, the strategic alliance between three rural NSW councils – Wellington, Blayney, and Cabonne was identified as a successful example of a shared services arrangement. The discussion paper reported that cost-savings of $720,000 has been achieved during the first ten months of that the strategic alliance was in operation.

The final case study listed in Table 8.1 was conducted by Dollery, Marshall, Sancton and Witherby (2005). In this paper, the authors examined the Riverina Eastern Regional Organisation of Councils (REROC) resource sharing arrangements. Under this shared services arrangement it was estimated that $4.5 million in cost-saving accrued to the 13 participating NSW councils between 1998 and 2003.

The final study in Table 8.1 is a literature review conducted by KMMC (2005). This report argued in support of the provision of shared services by Queensland councils based on its review of the literature. However, the report failed to realise the difference between shared services models in local governments *per se* and all levels of government. This omission resulted in a large number of peripheral references and a deficiency of concrete examples to highlight the potential benefits of shared services arrangements in milieu of local government.

8.3 International Empirical Evidence on Shared Services in Local Government

Internationally there is a growing corpus of empirical evidence on the shared services arrangements. Table 8.2 summarises a representative selection of studies from the UK and US that highlight the numerous benefits that may accrue to councils that participate in shared services arrangements.

Table 8.2: International empirical evidence on shared services arrangements

	United Kingdom		
Publication	**Method**	**Sample**	**Summary of findings**
Murray et al. (2008)	Case studies	15 English Councils	Some smaller councils benefited from shared services arrangements
CLG [England] (2006a; 2006b; 2006c; 2006d; 2006e)	Case studies	73 Local Councils 81 Local Councils 69 Local Councils 80 Local Councils 64 Local Councils	Shared services arrangements were one of the approaches to efficiency gains.
PWC (2005)	Case studies	Two rural councils	Councils achieved top quartile performance and achieved cost-savings.
United States			
Publication	**Method**	**Sample**	**Summary of findings**
Hawkins and Feiock (2011)	Logistic regression	75 US municipalities	Joint ventures are more likely when: (i) local benefits are combined with a 'mayor-council' form of government or (ii) when wider benefits are sought under a 'manager-council' form of government.
LeRoux and Carr (2010)	Quantitative case study	44 local governments in Wayne County, Michigan	Municipalities cooperate more extensively on local public services such as waste disposal. Councils are also likely to enter into inter-local agreements when senior managers belong to the same professional associations.
LeRoux and Pandey (2011)	OLS regression	134 large US municipalities	Municipalities with managers motivated by career advancement are more likely to pursue inter-local service delivery.
Chen and Thurmaier (2010)	Ordered logistic regression	US municipalities in the Iowa	Inter-local agreements increase the effectiveness and efficiency of local services.
Hawkins (2010a)	Logistic regression	206 US municipalities	Cooperation on joint ventures for economic development between local governments is influenced by range of factors including high levels of social capital and frequent communication.

Table 8.2 (cont.)			
United States			
Publication	**Method**	**Sample**	**Summary of findings**
Hawkins (2010b)	Multinomial logistic regression	206 US municipalities	Evidence indicates that 'mayor-council' forms of local government as opposed to 'council-manager' form of government are more likely to pursue and form 'developmental' joint ventures (e.g. two local councils agree to develop vacant land spanning the councils' borders).
Kwon and Feiock (2010)	Heckman probit regression	Various US local municipalities	Intergovernmental services agreements can be characterised as a two-step process. First, communities consider whether to collaborate or not. Second, the likelihood of entering into an inter-local agreement is conditional upon the likelihood that a community has a preference for collaboration.
Hawkins (2009)	Descriptive and inferential statistical analysis	206 US local government municipalities	Identifies prospects/barriers for the establishment of joint ventures.
LeRoux and Carr (2007)	Logistic regression	Municipalities in Michigan	Local economic factors, policy and planning, networks, population growth, and characteristics of communities in the area adjoining the local government may help explain cooperation.

Source: Adapted from Dollery and Akimov (2008).

To begin with many British councils have reported that the introduction of shared services has reduced cost and led to improvements in service, particularly in the areas of 'back office' functions (Communities and Local Government [England] 2006a; 2006b; 2006c; 2006d; 2006e). In a similar vein, the consultancy report prepared by PriceWaterhouseCoopers (2005) on the Anglia Revenue Partnership – a shared services hub established for citizens in two rural councils – reported that these councils not only performed better but had accumulated considerable cost-

savings. Finally, the study by Murray, Rentell and Geere (2008) examined the benefits of procurement shared services arrangements for 15 councils and found that some smaller councils benefitted from shared services arrangements, particularly with respect to joint procurement.

A wide range of studies have empirically examined shared services arrangements in the United States. To begin with, Hawkins (2009) identified that the most common reasons for establishing a shared services arrangement include: (i) improving a council's competitive advantage; (ii) securing resources that would not otherwise be obtainable; and (iii) taking advantage of economies of scale. In similar vein, it not surprising that Chen and Thurmaier (2010) reported that the equitable sharing of benefits among partaking councils was crucial to the success of shared services arrangements.

Additional studies conducted by Hawkins (2010a, 2010b) have examined: (i) the circumstances under which councils were likely to establish shared services arrangements; and (ii) the role that institutional arrangements play in encouraging the establishment of shared services arrangement. For example, Hawkins (2010a) identified that cooperation on economic development shared services arrangements between councils is influenced by a whole host of factors, which include regular communication and high levels of social capital. With respect to institutional arrangements, Hawkins (2010b) found that a 'mayor-council' form of government is more likely to participate in 'developmental' joint ventures (as opposed to a 'council-manager' form of government). One possible reason for this finding is that such arrangements may provide 'a way for elected officials to claim for the benefits that can be directed to certain constituent groups' (Hawkins, 2010b, p.382). In another study, Hawkins and Feiock (2011) found empirical

evidence to substantiate the proposition that previous shared services arrangement positively influence on the probability of entering into a future cooperative venture.

Shared services arrangements in the US have also been examined by LeRoux and Carr (2007), LeRoux and Pandey (2011) and LeRoux and Carr (2010). To begin with, LeRoux and Carr (2007) examined cooperative practices on public service (like sewerage) among Michigan municipalities. In their study, LeRoux and Carr (2007) argued that cooperation among councils is motivated by a whole host of factors including: (i) the attributes of neighbouring communities, (ii) population growth, and (iii) economic factors. In a subsequent study, LeRoux and Carr (2010) examined cooperative arrangements among 44 Michigan councils. In their study, the authors found that councils were more likely to participate in cooperative arrangements for the provision of local public services like water management (as opposed to provision community-based activities like 'parks and recreation'). In another study, LeRoux and Pandey (2011) discovered that larger councils were more likely to pursue shared services arrangements if their senior bureaucrats were motivated by career advancement.

Finally, the study by Kwon and Feiock (2010) examines shared services arrangement as a two stage process. More specifically, Kwon and Feiock (2010) use a two-part regression model to consider with communities wish to partake in shared services arrangements and, in the second stage, consider the probability of entering into such an agreement conditional upon the likelihood that a community has a predilection for such an arrangement. The authors report that – in the first stage – inter-local cooperation is 'likely to be considered in relatively affluent cities experiencing population declines and economic conditions' while in the second stage, 'at large' election of

councillors and former agreements were predictive of communities entering into such arrangements (Kwon and Feiock, 2010, p.881).

Thus, by way of summary, the findings from the empirical literature suggest that shared services arrangements can lead cost-savings and improve service delivery although some services appear to be more conducive to shared services arrangements than other (Dollery, Grant and Kortt, 2012).

8.4 Implications of the Empirical Evidence on Shared Services

While the findings summarised above differ in their scope, it is still possible to draw some broad inferences:

- Shared services arrangements can enhance local service delivery;
- Some services seem to be more conducive to shared services arrangements;
- Successful shared services arrangements typically include IT services, human resources and waste management;
- Successful shared services arrangements can vary significantly;
- Barriers to shared services arrangements can be challenging to address; and
- Barriers to shared services arrangements include: (i) loss of control, (ii) competing objectives, (ii) uncertain benefits, (iv) and increasingly complex management and administrative processes.

Thus, from a policy perspective, a critical question arises: which local service are best suited to shared services arrangements? While the empirical literature provides some guidance on this matter, it nonetheless important to consider the common aspects of local services, give the plethora of services that are produced by the local government sector. A useful starting point is the extensive work that was conducted by Allan (2001; 2003) and the NSW Independent Inquiry into Local Government (NSW LGI, 2006) led Allan to identify the following six aspects:

(i) 'Low core capability';

(ii) 'High supplier availability'

(iii) 'Low task complexity'

(iv) Significant scale economies;

(v) 'Specialized technology'; and

(vi) 'Low asset specificity'.

'Core capability' refers to the 'steering' and not 'rowing' capacities of councils like service monitoring. Without this core capability, councils may not in a position to properly discharge their statutory requirements. Thus, shared services arrangements should only be considered for low core capabilities. In addition, the absence or presence of potential contractors is another aspect that needs to be considered since if shared services arrangements fail, then an appropriate exist strategy is needed. Along similar line, Allan (2001, 40) has stated that 'complex tasks are difficult to monitor, hard to measure for inputs and require unique expertise to monitor' and are therefore not generally suitable for shared services arrangements. The question of economies of

scale also comes into play on whether to enter into a shared services agreement. For example, the costs of purchasing an IT system makes these particular services well-suited to shared services arrangements. Finally, Allan (2001: 40) also recommends that 'where a task requires an expensive and specific asset it may be more cost effective for the council to provide the asset' and thus an suitably designed shared services model can assist in apportioning high fixed costs.

With respect to which services are best suited to shared services arrangements, Allan (2001: 46) contends that 'there is no reason as to why most core community services', such as road maintenance and domestic waste as well as 'backroom support services', including finance and IT should not be 'delivered or arranged by a central administration unit owned and controlled by several councils'. However, Allan (2001) added two vital qualifications to this conclusion: (i) that each council should secure performance agreements which detail 'specific rights and obligations' and (ii) that the shared service entity should be overseen by a board of directors comprised from all councils.

CHAPTER 9: COUNCIL COLLABORATION THROUGH JOINT REGIONAL BODY

Chapter Summary

- Shared services represent a superior alternative to forced amalgamation to improve the performance of the Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby councils.
- The best method of delivering shared services lies in a variation of the successful Hunter Councils model.

9.1 Introduction

In this Report we have considered in detail the empirical evidence on the efficacy of municipal mergers as an instrument of local government reform. Given the weight of empirical evidence in the international and Australian scholarly literature, together with the unanimity found in the Australian national and state inquiries into local government sustainability, we conclude that forced mergers have not met expectations.

In addition, as we saw in Chapter 4, the *Fit for the Future* process is severely flawed in a number of respects, not least in its approach to the evaluation of financial sustainability and council efficiency. Furthermore, as we have demonstrated in Chapter 5, the *Fit for the Future* merger proposals involving Hunters Hill, Lane Cove and Ryde will not improve financial sustainability under the *Fit for the Future* criteria, nor will they generate scale economies, as we show in Chapter 6. Indeed, a merged North Shore group of councils would produce diseconomies of

scale. Furthermore, demographic, socio-economic and other data emphatically underline the absence of an overarching community of interest amongst these councils, as Chapter 7 demonstrated. In sum, we have seen that there is an overwhelming evidential basis for rejecting the proposed council mergers and instead pursuing more promising alternative approaches to improving council performance, notably regional council collaboration through a joint regional body.

Chapter 8 provided a detailed discussion of the Australian and international empirical evidence on both scale economies and shared services in local government. While the empirical evidence shows that scale and scope economies do exist in selected municipal functions and services, these are concentrated in comparatively few services, which are mostly capital intensive. In a similar vein, although shared services are preferable to forced amalgamation, the empirical evidence demonstrates that they are not a 'silver bullet' which can cure all the ills of local government. Indeed, financial constraints, especially rate-pegging in NSW and a large local infrastructure backlog, necessarily imply that more funding be made available to local government, in the form of additional 'own-source' revenue, greater inter-governmental transfers, and more borrowing for capital investment.

Against this background, Chapter 9 considers the optimal approach to inter-council collaboration involving Hunters Hill, Lane Cove and Ryde, other local authorities comprising the North Shore group of councils, as well as a few additional spatially aligned councils. In Australian local government, literally dozens of different kinds of shared service arrangements have been implemented across the country, many displaying a high degree of ingenuity, often in trying

circumstances in remote areas (see Dollery, Grant and Kortt (2012) for a detailed analysis of these arrangements).

However, shared service delivery models differ considerably in terms of the success they have enjoyed in terms of cost effectiveness, the range of services offered, and the quality of these services. In Chapter 9 we consider the conceptual foundations for council collaboration through regional entities, we examine the Hunter Councils model as a relevant successful case study for designing a joint regional organisation suitable for the Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde, and Willoughby group of councils, and then we set out a draft joint regional body structure for these councils along the lines of the model already discussed by NSROC and SHOROC councils.

Chapter 9 is divided into four main parts. Section 9.2 considers the broad implications of the conceptual literature on shared services in local government for the selection of functions to be provided by a joint regional organisation for Hunters Hill, Lane Cove and Ryde and the other North Shore group of councils. Section 9.3 outlines the Hunter Councils model as a desirable design for a joint regional organisation for the councils in question. Section 9.4 sets out a proposed design for a joint regional organisation for these councils drawing on the draft model previously considered by the NSROC and SHOROC groups of councils. Section 9.5 tackles the thorny question of which local functions and local services could be collaboratively delivered by a regional body and provides a survey instrument which can be employed to determine which services to provide. Chapter 9 ends with some brief concluding comments in section 9.6.

9.2 Conceptual Foundations for Council Collaboration and Shared Services

In his pioneering *Governing Local Public Economies*, Oakerson (1999, p.7) distinguished between local service *provision* and local service *production* and demonstrated that different criteria apply to these conceptually different functions. The *provision* of local services involves determining whether to provide a particular service, the regulation of local activities, the accretion of adequate revenue to pay for the service, the quantity and quality of local services to be provided, and how these services should be produced. By contrast, *production* involves the actual creation of a product or the rendering of a service rather than its financial provision.

In local government, the main implication of the conceptual separation of provision from production resides in the fact that local authorities enjoy a choice between different vehicles for producing local goods and local services. Oakerson (1999, p.17/18) has identified seven generic possibilities for linking provision with production in local government service delivery:

1. '*In-house production'* occurs where a local council arranges its own production. For example, a council organises its own production along traditional 'in-house' grounds.
2. '*Coordinated production'* takes place where two or more local councils coordinate production activities. For instance, the health inspection departments of two adjoining councils cooperate on activities affecting both jurisdictions.
3. '*Joint production'* where two or more adjacent councils organise a single production unit as in, for example, invoice processing or joint printing.

4. '*Intergovernmental contracting'* takes the form of one council horizontally contracting local services from a separate council or vertically with a state or national government agency, such as work undertaken on road maintenance for the NSW Government by councils.
5. '*Private contracting'* where a private for-profit firm undertakes production for a council, as in the contracting out of domestic waste collection.
6. '*Franchising*' where a council gives a commercial producer the exclusive right to produce a given service from which local residents can purchase the service.
7. '*Vouchering*' where a council sets quality standards as well as the level of provision, but allows households to select their own producer using a municipal voucher.

In addition to these possibilities, Warner and Hefetz (2008) have added l*ocal services provided by unpaid local volunteers*. This often occurs in the form of co-production where unpaid volunteers use council resources, such as vehicles, to provide a service, like caring for environmentally sensitive wetlands or cleaning up garbage in public parks and waterways.

While the voluminous empirical literature on council collaboration and shared services is varied, as we have seen in Chapter 8, it is nevertheless possible to draw some broad inferences:

(a) Whereas shared services arrangements can enhance the efficiency of local service delivery, some local services are more adaptable to shared services arrangements.
(b) Successful shared services arrangements commonly include 'back-office' services, IT services, human resources and waste management.

(c) Successful shared services arrangements can vary significantly from case to case, even where the same services are produced, and there is thus not a single optimal model.

(d) Barriers to shared services arrangements can be difficult to surmount and include the 'loss of control', competing objectives, ill-defined or uncertain benefits, and expensive and convoluted management and administrative processes.

These general considerations should thus be taken into account when developing policies that are intended to advance the efficiency of local government service delivery. However, a vital question that arises is which local services are most suited to shared service arrangements? While the empirical literature provides the necessary information to answer this question, it is also informative to consider the generic attributes of local services, given the variety of services produced by local authorities.

For instance, the work conducted by Allan (2001; 2003) and the NSW Independent Inquiry into Local Government (NSW LGI, 2006) led by him identified the following six attributes: 'Low core capability'; 'high supplier availability'; 'low task complexity'; significant scale economies; 'specialized technology'; and 'low asset specificity'. 'Core capability' refers to the 'steering' and not 'rowing' capacities of local municipalities like service monitoring. In the absence of this core capability, local municipalities may not in a position to fittingly discharge their statutory obligations. Shared service arrangements should thus only be considered for low core capabilities. Moreover, the absence or presence of prospective contractors is another factor that needs to be considered since if shared services arrangements fail, then an appropriate exist strategy needs to be put in place. However, in large cities, such as Sydney, the absence of

prospective contractors is unlikely to be a problem. Allan (2001, 40) has also made the case that 'complex tasks are difficult to monitor, hard to measure for inputs and require unique expertise to monitor' and are therefore not generally not deemed suitable for shared services arrangement. The question of scale economies also comes into play on whether deciding to enter into a shared services agreement. For instance, the costs of purchasing and upgrading IT systems make these particular services well-suited to shared services arrangements. Finally, Allan (2001, p.40) also suggests that 'where a task requires an expensive and specific asset it may be more cost effective for the council to provide the asset' and thus an appropriately designed shared services model can assist in allocating high fixed costs.

With regard to which services and functions are most suited to shared services arrangements, Allan (2001, p.46) argues that 'there is no reason as to why most core community services', such as road maintenance and domestic waste, as well as 'backroom support services', including finance and IT, should not be 'delivered or arranged by a central administration unit owned and controlled by several councils'. Nevertheless, Allan (2001) added two vital caveats to this generic conclusion: (a) that each participating council should secure performance agreements which detail 'specific rights and obligations' and (b) that the shared service entity should be overseen by a board of directors comprised of mayors or general managers from all participating councils.

9.3 Hunter Councils

9.3.1 Genesis and Structure of Hunter Councils

Hunter Councils - more formally termed the Hunter Regional Organisation of Councils - is a regional organisation of councils in NSW comprising the Cessnock, Dungog, Gloucester, Great Lakes, Lake Macquarie, Maitland, Mid-Western Region, Muswellbrook, Newcastle, Port Stephens, Singleton and the Upper Hunter councils, with almost 700,000 residents. Hunter Councils engages in various regional advocacy and shared services initiatives. At a more detailed level, Hunter Councils engages in political advocacy through the operation of the Board of Hunter Councils, which consists of the Mayors of its eleven member councils. In addition, Hunter Councils has a number of business units managed by the general managers of member councils.

Shared service entities under the Hunter Councils include: Environmental programs; training and development through the Local Government Training Institute; large-scale purchasing by the Regional Procurement Division Records Management; film and television attraction and approval services managed by Screen Hunter Central Coast; consultancy services, such as economic development strategies; legal services; and engineering and project management services.

Hunter Councils (2013, pp.11/12) attributes its success to the fact that its shared service activities have been run on strictly commercial lines and member councils ‘have not been asked to provide

up-front capital'. Furthermore, its focus 'has always been on reducing costs to member councils', while concurrently ensuring the 'timeliness, quality and relevance' of its services. In addition, because of the commercial success of Hunter Councils, 'member contributions were eliminated some years ago with the only exception being a minor contribution to grant funded environmental programs that are invariably valued at more than $5 million per annum'. Moreover, Hunter Councils has constantly sought new business opportunities, but only where there has been a 'clear business case for each opportunity and growth/investment has only occurred when the organisation has a demonstrated capacity to fund in the long-term any debt that might be generated'. Finally, Hunter Councils contends it has offered 'value for money and access to services and expertise not necessarily available to larger councils let alone one of our small regional councils', which has been a 'critical factor in guaranteeing commitment and in establishing and maintaining credibility with stakeholders'.

9.3.2 Council of Mayors Model

In structural terms, Hunter Councils presently consists of two entities: Hunter Councils Ltd and Hunter Councils Inc. Each operates under an entirely different organisational structure. Thus Hunter Councils Ltd is a company limited by guarantee under the *Corporations (New South Wales) Act 1990* whereas Hunter Councils Inc. is an incorporated association under the *Associations Incorporation Act 2009*.

Hunter Councils Inc. is controlled by a Board consisting of the Mayors from each of its member councils. The Board of Mayors controls its policy-making, strategic and advocacy functions.

However, as we shall see, while Hunter Councils Inc. has long run some business entities, these will be transferred to the Hunter Councils Ltd under plans presently afoot.

By contrast, Hunter Councils Ltd is controlled by a Board consisting of the General Managers from each of the member councils. The Board of General Managers controls the remaining business and operational functions and reports formally to the Mayors at Hunter Councils Inc. Hunter Councils Ltd is thus subject to direction from Hunter Council Inc. Hunter Councils Ltd is the umbrella entity for a series of limited companies established under the *Corporations (New South Wales) Act 1990* to provide a range of beneficial services, mostly on a commercial basis, enabling shared services and strategic alliances to develop as required. Hunter Councils Ltd also provides these services outside the Hunter region.

Both Hunter Councils Inc. and Hunter Councils Ltd are self-funding. This includes all employee and operational costs. At present approximately sixty people are employed by Hunter Councils in total.

9.3.3 Proposed Restructured Hunter Council Model

Under plans to restructure Hunter Councils, the entity would adopt a 'Council of Mayors' model (Hunter Councils, 2013). The existing Hunter Councils Inc. would be closed and its assets transferred to Hunter Councils Ltd. A Hunter Council of Mayors would be formed under the *Associations Incorporation Act 2009* as an Incorporated Association. It would focus largely on high-level policy, regional strategy, regional decision-making, and regional advocacy. Hunter

Councils Ltd would continue the operational arm of Hunter Councils and fund the Hunter Council of Mayors, to which it would report on a formal basis.

At a more specific level, the restructuring process would enable the Hunter Council of Mayors to control the following functions:

- Ten year planning based on each of the member councils' community strategic plans;
- 'Whole of region' advocacy and intergovernmental relations;
- Strategic regional and subregional planning;
- Regional and subregional infrastructure and transport planning;
- Regional economic development strategy;
- Regional waste strategy;
- Regional social and cultural strategy; and
- Regional high end corporate services provision.

By contrast, Hunter Councils Ltd would manage the following functions:

- An annual business plan formally endorsed by the Council of Mayors;
- Local Government Training Institute;
- Environment Division operations;
- Local Government Legal;
- Engineering,

- Asset Management and Land Use Planning Services;
- Regional Procurement;
- Strategic Consultancy Services;
- Visitor Economy Hunter;
- Hunter Records Storage; and
- Council capacity building and support services.

Under the restructuring proposal, it is hoped that enabling legislation will be introduced through the *Local Government Act 1993* to establish the Council of Mayors model. This revised Act would then specify the following:

- The roles adopted by councils collaboratively and at a regional and/or sub-regional level;
- Underpin the formation of a regional body by a grouping of clusters of councils to fulfil regional and sub-regional roles; and
- Establish the foundations for formal agreements between regional bodies and the NSW Government on regional roles.

9.4 Northern Sydney Metropolitan Regional Body

As we have seen in section 9.3 of this Report, the existing Hunter Councils structure has performed well, not only in terms of its regional advocacy and coordination role, but also in economic terms through its subsidiary business entities. Furthermore, the proposed restructuring of Hunter Councils represents a promising avenue for preserving the current

strengths of Hunter Councils, whilst improving its governance structure and enhancing its relationship with the NSW Government. This suggests that a joint regional body for the North Shore group of councils, including additional neighbouring municipalities, should follow the Hunter Council model. Indeed, ongoing discussions along these lines have already been held between NSROC and SHOROC, which together represent the majority of councils in the Northern metropolitan region of Sydney.

The Northern Sydney Regional Organisation of Councils (NSROC) comprises the Hornsby, Hunter's Hill, Ku-ring-gai, Lane Cove, North Sydney, Ryde and Willoughby local authorities. NSROC itself consists of a Board with 14 members consisting of the Mayor and one other nominated Councillor from each NSROC council; an Executive comprising a President and two Vice-Presidents nominated by the Board, a General Managers Advisory Group (GMAC), and the NSROC secretariat consisting of an Executive Director and Executive Assistant.

The Shore Regional Organisation of Councils **(**SHOROC) consists of the Manly, Mosman, Pittwater and Warringah councils. SHOROC itself comprises a Board of Mayors and General Managers of the four member councils, supported by the SHOROC Executive Director and its secretariat.

Earlier discussions between NSROC and SHOROC had seen the emergence of a proposed 'Northern Sydney Council Collaboration Model' which has many of the characteristics of the Hunter Council model. However, discussions on the progression of this model had

become dormant, no doubt in part due the fact that the 'Joint Organisation' model proposed by the Independent Panel had not been defined or its proposed characteristics made public. However, the envisaged draft Northern Sydney Council Model would possess the same basic governance structure as the Hunter Council model: A North Sydney Council of Mayors would operate as the overall strategic regional decision-making body, alongside a Northern Sydney Regional Services Group overseen by General Managers of the member councils, and supported by a Northern Sydney Council secretariat.

The proposed North Sydney Council of Mayors would focus on 'whole-of-region' advocacy and intergovernmental relations; strategic sub-regional land use and infrastructure planning; regional Community Strategic Planning; Regional Action Plans; Regional economic development, waste and environment, social and cultural strategies.

The Northern Sydney Regional Services Group would run collaborative projects aimed at improved financial sustainability and enhanced council capacity of voluntarily participating councils. It would offer a specific range of shared services on a commercial basis to member councils, as well as other local authorities, public sector entities and private firms, which willingly wish to participate.

The structural separation of the North Sydney Council of Mayors from the Northern Sydney Regional Services Group facilitates the separation of regional strategic and advocacy functions (which would be obligatory for all member councils), from regional resource sharing, shared services and joint service delivery functions (where council participation is voluntary on an 'opt-

in opt-out' basis). It also enables the Northern Sydney Regional Services Group to operate on a commercial for-profit basis without any constraint from member councils which do not want to use particular services which may be offered.

The actual establishment of the Northern Sydney Council Collaboration Model with its North Sydney Council of Mayors and the Northern Sydney Regional Services Group has been placed in abeyance pending the outcome of the *Fit for the Future* program which will formalize the structure of local government in NSW, including the north Sydney metropolitan region. In addition, further clarity is required from NSW Government regarding its specific plans for Joint Organisations, especially with regard to any planned legislative changes.

However, the success of the Hunter Council model has demonstrated that the Northern Sydney Council Collaboration Model should also consider adopting its financial self-sufficiency platform. Under an arrangement of this kind, surpluses generated by the Northern Sydney Regional Services Group should in the first instance be used to support the costs associated with the operation of the North Sydney Council of Mayors and the Northern Sydney Council Collaboration Model secretariat. Any remaining surplus should then be distributed amongst member councils, after funds have been deducted to support new initiatives and attendant investments.

9.5 Suitable Functions and Services for Collaborative Service Provision

Chapter 8 of this Report provided a comprehensive empirical evaluation of the benefits which could flow from shared service arrangements between groups of local authorities derived from

the empirical literature. Moreover, as we have seen in section 9.3 of Chapter 9, highly successful shared service models already exist in NSW local government, especially Hunter Councils, which can be used as the basis for the design of a model of council collaboration among the north Sydney councils.

However, while this provides valuable insights into successful shared service arrangements elsewhere, it cannot simply be transplanted into the precise circumstances facing north Sydney municipalities since local factors typically play a key role in determining which services are suitable for resource-sharing, shared service agreements and other modes of council collaboration in a given regional area. Furthermore, it should be emphasised willing voluntary participation by member councils is an essential ingredient of success, as we have seen in the case of Hunter Councils.

For these reasons, it is recommended that north Sydney councils which will join the proposed Northern Sydney Council Collaboration Model be invited to participate in a survey of all General Managers and Mayors of its member councils. This survey would seek to determine:

(a) The extent of existing resource-sharing and shared service arrangements between member councils and how well they operate.

(b) The views of General Managers and Mayors on possible future resource-sharing, shared service and other collaborative initiatives which could prove successful if offered through a Northern Sydney Council Collaboration Model.

(c) The views of General Managers and Mayors on which specific functions and services offer the greatest prospects of success if they were provided through the Northern Sydney Council Collaboration Model on a collaborative basis.

To this end, a well-developed survey instrument is provided in Table 9.1 which can be used for this purpose. It has previously been successfully applied to other constellations of councils in other Australian state jurisdictions. The results of the survey can then be employed by the Northern Sydney Council Collaboration Model Board to identify promising avenues for collaboration and to plan further resource-sharing and shared service initiatives.

Table 9.1: Products and Services Review for Suitability of Shared Services Instrument

Products and Services Review for Suitability of Shared Services												
Section	**Product/Service**	**High Potential for early success**	**Suitable for Shared Services? *(Mark "E" for existing shared services)***				**How the service delivery is best performed?**				**Where the policy management should be controlled?**	
			High	**Med**	**Low**	**No**	**Local**	**Sub - Regional**	**Regional**	**External**	**Local**	**Regional**

By way of a concrete example of how the survey instrument outlined in Table 9.1 should be employed, Table 9.2 lists some generic service categories, such as ‘Ranger Services’, ‘Community Safety Crime Prevention (CSCP)’, ‘Health Services’ and ‘Community Services’, and the sub-categories associated with each of these generic service functions. In this way, the instrument contained in Table 9.1 can be tailored to suit the specific circumstances of particular groups of councils, including the ‘Northern Sydney Council Collaboration Model’.

Table 9.2: Products and Services Review for Suitability of Shared Services: Example

Products and Services Review for Suitability of Shared Services - Community Development (1)												
Section	**Product/Service**	**High Potential for early success**	**Suitable for Shared Services? *(Mark "E" for existing shared services)***				**How Service Delivery is best performed?**				**Where Policy Management should be controlled?**	
			High	**Med**	**Low**	**No**	**Local**	**Sub - Regional**	**Regional**	**External**	**Local**	**Regional**
Ranger Services	Education, compliance and enforcement of Local, State and Federal Laws (Dog Act, Litter Act, Bushfires Act, Off-road Vehicles Act, Parking Local Laws, Fines Enforcement Regulation, Emergency Management Act).	Y	X						X			X
	Emergency Management Plans/Recovery Plan, Testing Plans - scenario based, Stakeholder relationships, LEMC & DEMC representation (SES, FESA, POLICE)	Y	X						X		X	
	Investigations / Prosecutions, non-compliance of Laws, illegal dumping, dog attacks, illegal burning, fire prevention contraventions, parking, barking dogs.			X					X			X
	Dog Pound					X	X					X
Community Safety Crime Prevention (CSCP)	Support FESA / SES / Police emergency management/recovery		X						X			X

Products and Services Review for Suitability of Shared Services - Community Development (2)												
	Provide crime prevention advice to residents			X				X				X
	Reporting of maintenance issues				X			X			X	
	Support community based activities and events			X				X			X	
	Community Safety Crime Prevention Plan											
	Graffiti Strategy and Management					X			X			X
	Neighbourhood Watch Program			X					X			X
	Community based events / workshops on various crime prevention topics (leavers presentations, parents seminars, safety for seniors, CCTV, home security talks, shopping centre displays).				X				X		X	
Health Services	Food management services											
	Food hygiene controls/audits		X						X			X
	Food sampling program		X						X			X
	Food safety and hygiene education		X						X			X
	Approval of new premises		X						X			X
	Compliance											

Products and Services Review for Suitability of Shared Services - Community Development (3)												
	Noise management				X		X				X	
	Hazardous materials		X						X			X
	Monitor contaminated sites		X									X
	Public building audits	Y	X						X			X
	Notifiable disease investigations		X							X		X
	Disease and pest control											
	Resident rat bait program			X						X		X
	Midge control/treatment			X						X	X	
	Mosquito management/monitoring			X						X	X	
	Public swimming pool audits	Y	X						X			X
	Provision and management of facilities for child health clinics					X				X		X
	Health promotion services (resource development, program design and delivery)		X							X		X
	Approval for black & grey water systems		X						X			X
Community Services	Home and Community Care				X			X			X	

Products and Services Review for Suitability of Shared Services - Community Development (4)												
	Immunisation (infant)				X					X		X
	Library Services											
	Library Reference & Information Service			X					X			X
	Library Resources					X	X				X	
	Housebound Library Delivery Service			X					X			X
	Regional Library Service			X					X			X
	Library - common server and software		X							X		X
	Museums & Local History											
	Local History Service			X				X			X	
	Gallery Exhibitions				X				X			X
	Collections Management - Museums & Local History				X			X			X	
	Local Museums				X		X				X	
Community Development	Community Event Management			X			X				X	
	Community Calendar of Festivals and Events		X						X			X
	Events Package to assist community groups with events			X				X				X

Products and Services Review for Suitability of Shared Services - Community Development (5)												
	Volunteer Recognition / Information & Referral Service			X			X					X
	Family Support Programs			X					X			X
	Coordination of various Youth programs. Events & forums			X				X			X	
	Senior Citizen Support and activities			X				X			X	
	Publication of Senior Information Directory			X				X			X	
	Coordinate Aged Services Provider Network			X				X			X	
	Document and Review Disability Access and Inclusion Plan	Y	X						X			X
	Provision of ID Profile (demographic information)			X					X			X
	Aboriginal liaison and information			X				X				X
	Community Development			X				X			X	

9.6 Conclusion

Chapter 9 has built on the review of the empirical literature on shared services in Chapter 8 to consider council collaboration as the main structural alternative to forced mergers for Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde, Willoughby and other northern Sydney councils wishing to participate in resource-sharing, shared services and other forms of regional collaboration. Section 9.2 demonstrated that sound analytical foundations exist for separating service provision from service production in contemporary local government, with several different available modes of delivering local services, including inter-council collaboration. However, work by Allan (2001; 2003), the NSW Independent Inquiry into Local Government (NSW LGI, 2006) and others has shown that not all local services are amenable to joint provision or production.

The question of the most appropriate organisational design for inter-council collaboration amongst Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde, Willoughby and other northern Sydney councils was tackled in section 9.3 of Chapter 9, which examined the structure of the current Hunter Council model, as well as plans to restructure Hunter Councils. Given the success of the Hunter Councils model, together with the fact that it services a comparable aggregate population to that which would be served by as north Sydney cooperative entity, it was argued that the Hunter Council model be taken as a broad template for the design of a north Sydney regional body.

Section 9.4 of Chapter 9 evaluated the draft Northern Sydney Council Collaboration Model which had been drawn up after discussions between the NSROC and SHOROC groups of councils, but had become dormant pending the outcome of the *Fit for the Future* process. It was argued that the Northern Sydney Council Collaboration Model represented a close approximation of the Hunter Council model and thus represented a suitable regional collaborative model for the northern Sydney group of councils. However, section 9.5 argued that the optimal selection of council functions and services to be provided collaborate was not furnished by simply establishing a designated organisational model.

To this end, section 9.5 provided a survey instrument in Table 9.1 which could be used by a Northern Sydney Council Collaboration Model Board to (a) pinpoint promising avenues for inter-collaboration and to (b) plan further resource-sharing and shared service initiatives. Table 9.2 demonstrated by way of example how the survey instrument could be applied in practice.

CHAPTER 10: COMMUNITY CONSULTATION BY LANE COVE, HUNTERS HILL AND RYDE COUNCILS

Chapter Summary

- All three local authorities initiated ongoing and extensive community engagement processes from the early stages of the *Destination 2036* reform.
- Local residents of Lane Cove, Hunters Hill and Ryde overwhelmingly oppose council mergers.
- Local communities prefer the 'joint organisational' (JO) approach to achieving the benefits of scale and capacity.

10.1 Introduction

Given the strong democratic foundations of Australian local government, local authorities govern with the consent of local communities and attempt to provide local services in accordance with local community demand. In this respect, the Local Government Act empowers local councils to plan and manage local services in consultation with their respective local communities. It is thus obvious that extensive community consultation should occur prior to local authorities submitting *Fit for the Future* submissions to the OLG for adjudication by IPART under its *Methodology for Assessment of Council Fit for the Future Proposals.*

The need for extensive community consultation has been emphasised at every stage of the current NSW local government reform process. For example, in its final report *Revitalising Local Government,* the Independent Panel (2013b, p.56) observed that 'all services provided

by a council must meet defined performance outcomes and quality and cost standards developed by the council in consultation with local communities and key stakeholders'. The Panel (2013b, p.74) also contended that while 'the State government's currently unfettered right to impose amalgamations and major boundary changes more or less at will should be limited', and it was essential that 'any amalgamation or major boundary change should be preceded by careful analysis of the issues to be addressed and all the options available', there must be 'full community consultation'.

The NSW OLG (2014) also stressed the need for comprehensive community consultation. It observed that 'all councils are encouraged to work with their community, including council staff, in preparing their Proposals'. This meant that 'councils that are preparing a Template 1 Merger Proposal will need to explain how they have discussed the potential benefits and costs of the proposal with their community and considered their concerns', with a minimum 28 day public exhibition period required for merger proposals'. Similarly, 'councils preparing a Template 2 or 3 Proposal may wish to draw on consultation that have recently completed for their Integrated Planning and Reporting requirements, or undertake a specific consultation', adding that 'it is up to each council to decide, based on the details of their Proposal'.

By contrast, in its *Methodology for Assessment of Council Fit for the Future Proposals*, IPART (2015, p.36-37) explicitly noted that it would formally evaluate community consultation by local authorities as part of its overall assessment of council submissions under the *Fit for the Future* process. Furthermore, IPART set out its approach to evaluate community consultation. Against this background, Chapter 10 outlines IPART methodology for assessing community consultation and then considers the community consultation undertaken by Lane Cove, Hunters Hill and Ryde councils.

Chapter 10 is divided into three main parts. Section 10.2 provides a synoptic review of the approach to evaluating community consultation in *Methodology for Assessment of Council Fit for the Future Proposals.* Section 10.3 summarises the community consultation undertaken by Lane Cove, Hunters Hill and Ryde. Chapter 10 ends with some brief concluding remarks in section 10.4.

10.2 Community Consultation in IPART's (2015) Methodology

In its *Methodology for Assessment of Council Fit for the Future Proposals*, IPART (2015, p.36) notes that it's Terms of Reference 'ask us to include an assessment of the consultation process undertaken by the council as part of our assessment of council FFTF proposals. It goes on to observe that the Independent Panel 'considered that a policy on boundary changes based on evidence based assessments should include full community consultation'. Furthermore, the 'OLG's FFTF guidance material also identifies how councils may use findings from community consultation to assist in identifying benefits and costs for proposals', with the OLG specifically requiring councils to 'provide evidence on community consultation regarding any proposed merger or new 'rural council' structures'. This should involve 'evidence of council resolutions' which support amalgamation and the public exhibition of merger proposals 'for at least 28 days as part of their community consultation'.

On its part, IPART (2015, p.36) formally declared that it would adopt the following approach:

> ‘We will assess a council’s consultation process with reference to the OLG guidance materials. We will also consider how balanced was the information that is provided to the community. That is, whether it promoted only the benefits or only the costs of a particular option, or instead informed the community about both the costs and benefits of one or more options’.

However, IPART (2015, p.36) explicitly acknowledged a variety of methods could be employed in community consultation in order to secure community views. Different approaches included the following:

- ‘Exhibiting options or proposals for comment
- a mail-out to all ratepayers with a reply-paid survey
- fact sheets and media releases
- an online survey or a random survey of ratepayers, appropriately stratified to capture the population characteristics of the LGA, and
- public meetings, listening posts, or resident workshops’.

Given the multitude of alternative approaches, IPART (2015, p.36-37) recommended that ‘councils should choose methods that reflect the issues that need to be consulted upon’. For instance, a Merger Proposal would ‘require input from residents in multiple councils regarding the implications of change, whereas a Council Improvement Proposal, where the ILGRP recommended that a council already had sufficient scale and capacity, would require more limited consultation, if any’. In essence, ‘the nature and extent of the consultation should be commensurate with the significance of the changes involved in the proposal and

the possible impacts on the community'. In addition, IPART (2015, p.37) noted that it will 'also consider the resources of the council in assessing consultation'.

10.3 Community Consultation by Lane Cove, Hunters Hill and Ryde Councils

We now consider in detail the community consultation undertaken by Lane Cove, Hunters Hill and Ryde.

10.3.1 Lane Cove

Lane Cove has undertaken extensive consultation with its local community. Table 10.2 provides a summary of these community consultation efforts:

Table 10.1: Community Consultation by Lane Cove

Date	Action Taken	Outcome	Comment
May 2013	Special Edition newsletter mailed to ratepayers highlighting local government reform and promoting community information session.	Delivered to 10,000+ ratepayers.	Lane Cove began its conversation with the community in 2013. It was one of the few councils that provided direct communication to all residents regarding the proposed reforms in 2013 meaning that this has been on the agenda within the community for some time.
12 June 2013	Community information session and community consultation.	100+ residents attended.	Residents raised concerns regarding potential loss of democracy, sense of community and engagement and impact on the quality of facilities and services. This was reflected in Council's response to the *Future Directions* consultation paper.
July 2014	New Council website launched.	Local government reform on website homepage under 'Hot Topics' providing access to *Future Directions* paper etc.	Members of the community could access to shortcuts to all relevant information on the NSW Government's plan.
15 September 2014	Council Meeting.	Council resolution to oppose forced amalgamation and request meeting with Minister for Local Government.	
26 September 2014	E-newsletter invitation to public meeting.	7,600+ emails sent. 34% open rate = 2,590 residents read email.	
3 October 2014	Reminder e-newsletter to public meeting.	7,600+ emails sent. 33% open rate = 2,510 residents read email.	
8 October 2014	Public meeting.	100+ residents attended.	Similar themes as 2013 – local democracy, loss of sense of

			community, impacts on efficiencies and access to staff/Councillors.
13 October 2014	Council Meeting.	Resolution included to initiate a public awareness campaign that highlights the most important issues for our community and reasons for Council's decisions.	
16 October 2014	Meeting with Minister for Local Government.	Copy of the presentation made to the Minister available on Council's website.	
29 October 2014	E-newsletter Update to the community on Local Government Reform.	7,500+ emails sent. 35% open rate = 2640 residents read email.	
October 2014	Council website – *Fit for the Future* page.	*Fit for the Future* logo, details and link to State government reports provided to the community.	Council has continued to ensure that the community has access to State government resources to inform their decisions on the issue.
October 2014	Article in *The Village Observer* on *Fit for the Future*.	Distribution to 19,000 people monthly.	Council works with the Editor on articles which are of significant interest to the community.
January 2015	E-newsletter notification of Extraordinary Council Meeting regarding *Fit for the Future*.	7,100+ emails sent. 40% open rate = 2,800 read email.	
21 January 2015	Extraordinary Council Meeting re *Fit for the Future*	13 members of the public attended to speak on the matter. Council resolved to involve and engage the community in a communications campaign.	
January 2015	*North Shore Times* coverage on the Council meeting.	Keeping local residents informed of the reforms.	Council liaises with the media on issues of importance to the local community.
March 2015	Keep Councils Local.	Council updated its website and provided an update on the recent activities of Council including meeting with other Councils.	This campaign reflected the concerns expressed by residents during earlier public meetings.
March 2015	Mayoral Column update in *The Village Observer*.	Distribution to 19,000 people monthly. Updating the community on Council's upcoming activities re *Fit for the Future.*	A Lane Cove-based publication that has a high readership amongst the local community.
March 2015	Article in *The Village Observer* on *Fit for the Future.*	Distribution to 19,000 people monthly. Raising community awareness of the issue.	Council works with the Editor on articles which are of significant interest to the community.
25 March 2015	Letter to ratepayers.	The Mayor wrote to over 10,000 ratepayers to provide them with information on the *Fit for the Future* campaign and Council's upcoming consultation process including public meeting on 7 May 2015.	
April 2015	Mayoral Column update in *The Village Observer*.	Distribution to 19,000 people. Updating the community on Council's upcoming activities re *Fit for the Future.*	A Lane Cove-based publication that has a high readership amongst the local community.

April 2015	Quarterly Newsletter.	Front page update on proposed reforms. Sent to 10,000+ ratepayers and distributed online and in hardcopy at local facilities.	
29 April 2015	E-newsletter to residents regarding public meeting.	7,100+ emails sent. 25% open rate = 1,775 read email.	
20-17 April 2015	Recruitment for Deliberative Poll.	600 participants agreeing to take part in Deliberative Poll.	Aim is to produce a snapshot of the wider community's views.
7 May 2015	Public Meeting on *Fit for the Future.*		
8 May 2015	Public Survey launched.		This is an opt-in survey that includes the same information as the deliberative poll i.e. all options. The information will be kept separate to the poll results.
15 May 2015	Letters to ratepayers.	The Mayor wrote to over 10,000 ratepayers to provide them with information on the *Fit for the Future* campaign and Council's upcoming consultation process including public meeting on 7 May 2015.	
18/25 May 2015	Deliberative Poll conducted.		

It is obvious from Table 10.1 that Lane Cove has taken concerted and vigorous action with respect to community consultation from the outset of the NSW local government reform process. Indeed, Lane Cove was one of the few local authorities which began a 'conversation' with its local community as far back as October 2013. In the initial stages, Lane Cove prepared and distributed a special edition newsletter for its residents. Since then Lane Cove has held two council public information sessions – one in 2013 and one in 2014 – with a further public meeting held on 7 May 2015 to provide an overview of the options available to the Lane Cove community. No less than five Lane Cove Council resolutions have been made during this time reflecting Lane Cove Council's consistent rejection of forced amalgamations and directing Lane Cove staff to engage with the community on the *Fit for the Future* package.

Electronic newsletter distribution has provided information to the Lane Cove community with an average of 2,400 local residents opening emails directly associated with *Fit for the Future*. There have been at least five e-newsletters distributed to date. In addition, the Lane Cove Council website has provided consistent updates on the *Fit for the Future* package and Lane Cove has secured a regular presence in the local monthly newspaper *The Village Observer*. Lane Cove also joined the *Keep Councils Local* campaign which aimed to engage the local community on questions surrounding the *Fit for the Future* package so that the local community was aware of the proposed changes.

More recently, Lane Cove has been providing its local community with an opportunity to express its views, with the Lane Cove Mayor writing to ratepayers to encourage them to participate during May 2015 in a public meeting and an online survey. Lane Cove Council is also running a deliberative poll to capture the wider views within the community.

In adopting its approach to community consultation, Lane Cove was mindful that it should first fully inform its local community of the *Fit for the Future* program, present it with alternative possibilities and then canvass local opinion. In this spirit, Lane Cove continued to update its local community on the progress of Lane Cove Council's actions in response to the NSW Government's initiative. With community feedback at two public meetings (held in 2013 and 2014) highlighting the community's concerns around local representation and reduced services under the proposed model by the NSW Government, Lane Cove sought to find an alternate solution that brought together the scale and efficiencies of the NSW Government's proposal while retaining the local community's interest in keeping Lane Cove as an independent local authority.

Lane Cove did not to survey its local community until it could provide alternative solutions which addressed the concerns raised by its residents. Accordingly, Lane Cove Council waited until it had expert analysis of the options available to the community before asking for their response on all proposals. In the interim, Lane Cove kept a steady presence in the community from newsletters, direct mail-outs and media coverage to ensure that the local community is aware and engaged in the reform process. Lane Cove's website has always included the NSW Government's information to ensure that the local community had ready access to the proposed changes. Lane Cove also joined the *Keep Councils Local* campaign as a means of generating interest in the *Fit for the Future* changes so that when it was time to run the community consultation the local community would be well aware of the questions at hand.

With expert information to hand, Lane Cove will be running both an opt-in survey and a deliberative poll. The information will be the same in both surveys with the results analysed separately so that they can provide a more robust snapshot of the wider community and those keen to have their say on the matter. Both surveys will require respondents to read through each of the options presented to ensure they are making an informed decision about their Lane Cove Council's future. The results will be available in June 2015 following the deliberative polling and online survey.

10.3.2 Hunters Hill

In Common with Lane Cove, Hunters Hill has also undertaken extensive consultation with its local community. Table 10.2 provides a summary of these community consultation efforts:

Table 10.2: Community Consultation by Hunters Hill

Date	Action Taken	Outcome	Comment
06/15/2015	Public Consultation Meeting.	The community group *Save Hunters Hill Municipality Coalition* outlining their positive involvement and attendance at key community meetings.	Information and data catch session. Key questions to be asked at this meeting regarding *Fit for the Future* options.
April/May 2015	Radio Interviews.	Council's Mayor responding to key questions regarding likely impacts on residents as a result of the Independent Review Panel recommendations.	Building community awareness.
June 2014 – May 2015	1. Advertisements and editorials in local newspapers. 2. Website updates.	Raising awareness of *Fit for the Future* criteria and deadlines. Providing current updates on State Government requirements.	Building community awareness and understanding about what 'Fit for the Future' means. Ensuring the community realise the resource impacts of the Independent Panel Report and Fit for the Future requirements.
March/April	Letter to every household from the Mayor providing background information and inviting residents to attend the Public Consultation Session on 6 May 2015 and published on Council web site.	Awareness raised on the issues facing Hunters Hill should a merger take place.	
March 2015	Council Newsletter distributed to every household in Hunters Hill and published on Council web site.	Awareness raised of the State Government's proposal for voluntary mergers.	Building community awareness and understanding about what '*Fit for the Future*' means.
March 2014	Newsletter to every household and published on Council web site.	Advising that the final reports of the Independent Local Government Review Panel and the Local Government Acts Taskforce were released in January 2014 and that the reports are available at www.localgovernmentreview.nsw.gov.au Both the Government and report say 'no change' IS NOT an option. The report recommends the merger of the following Councils into a larger regional council: 1. Hunters Hill 2. Lane Cove	Council made a submission as did a number of community members. In responding to this report the focus then is on alternatives such as collaboration and joint organisations, consistent with Council's previous

		3. Mosman 4. North Sydney 5. Ryde (part) 6. Willoughby Council has taken the view (supported by the community), that a merger or amalgamation is not an appropriate outcome of the local government reform agenda.	position. Urgent consideration of two principal recommendations relating to mergers and regional collaboration and joint organisations therefore take on a more significant role. These are: Recommendation 41: Evidence based response to merger proposals; and Recommendation 43: Establishing Joint Organisations (JOs).
July 2013	Newsletter to every household advising outcome of public meeting and update. Published on Council web site.	Council holds to its position and resolutions: • No forced amalgamations. • Work with other councils through. NSROC to deliver services on a regional basis (e.g. waste collection and disposal) and to create greater economies of scale.	Building community awareness.
June 2013	Public meeting (250 in attendance).	A gathering of 250 people attended the meeting resulting in the following resolutions being passed by an overwhelming majority. 1. That Hunters Hill Municipality retains its independence and historic boundaries. 2. That the NSW Government recognises and protects the significant character and heritage values of Hunters Hill Municipality and the whole of the State. 3. That the NSW Planning 'White Paper' and draft Bill, the Metropolitan Strategy and the Local Government Review Panel final discussion papers do not reflect the following goals in the NSW Government's State Plan 'NSW 2021': Goal 32 'People to have a real say and be Involved in localised decision making'; and	Building community awareness.

		Goal 27 'Recognising and protecting the State's most significant heritage places and values', and that these discussion papers should be withdrawn, given their current flawed content. The Municipality of Hunters Hill must indeed retain its independence and historic boundaries and the NSW Government should recognise and protect the significant character and heritage values of this historic Municipality and many others in accordance with its own State Plan (Goal 27). Government should recognise and protect the significant character and heritage values of this historic Municipality and many others in accordance with its own State Plan (Goal 27). Government should recognise and protect the significant character and heritage values of this historic Municipality and many others in accordance with its own State Plan (Goal 27).	
March 2013	Newsletter to every household and published on Council web site.	Advice to residents that Hunter's Hill Council is firmly opposed to any proposed amalgamations and recently joined with our regional partners at the Northern Sydney Regional Organisation of Councils (NSROC) in adopting in part the following position: **Point 1** Local government reform should include mechanisms that allow councils to undertake cooperative activities more easily and efficiently. Our Councils hold the NSW Government to its pre-election promise of no forced amalgamations. We believe that reform should introduce changes that enable real improvements, without the need for mandatory amalgamations. **Point 2** Mandatory amalgamations may not be the best solution for better local councils. Amalgamations may not solve the fundamental problems facing us. A larger council will still face the pressures of increased service demand from a restricted financial base. Amalgamation experiences in other jurisdictions have created great upheaval. As councils are merged, service levels, contracts, wages and technologies must be harmonised, creating substantial transitional costs.	Building community awareness.

		Point 3 A key element for successful change is support by the community. If communities of interest are either fractured or pushed together in artificial groupings this will diminish community well-being. Reshaping councils into standard populations or geographic areas will not correspond to the uneven distribution of infrastructure, economic and employment centres. Nor will it create alignment with inconsistent State and Federal agencies' operational boundaries. **Point 4** In the NSROC region there are historically established communities with continuing separate identities. The financial management of our councils is sound, as recently verified by the NSW Treasury Corporation. As a Regional Organisation of Councils we have a history of successful collaboration and have achieved valuable outcomes for our communities through cooperation. **Point 5** We seek and support reform that will strengthen our capacity as individual councils to engage in collaboration that delivers improved value for money and is in the best interests of our communities. …With greater flexibility we can improve our operations while maintaining local participation and democracy to our constituents under our existing boundaries (a full copy of the statement is available at www.nsroc.com.au). For detailed information on the current state of play visit the following web site: www.savehuntershill.org To have your say please visit the Local Government Independent Review web site: www.independentreview.nsw.gov.au Updates on the review process can also be found on Council's web site: www.huntershill.nsw.gov.au	
2012 December	Newsletter to every household and published on Council web site.	The Independent Local Government Review Panel is responsible for providing recommendations to Government on key actions relating to governance, structure and financial sustainability to improve the strength and effectiveness of Local	Building community awareness.

		Government in NSW. The recently released publication 'Better, Stronger Local Government - The Case for Sustainable Change', was tagged by media as a means for the State Government to embark on metropolitan amalgamation that included Hunter's Hill Council. It is vital that Council and the Hunters Hill community participate and respond to any discussion papers put out by the Independent Review Panel, or Local.	
2012 May	Newsletter to every household and published on Council web site.	A review of local government in NSW - have your say! The NSW State Government has appointed an Independent Local Government Review Panel to develop options to improve the effectiveness of local government in NSW. The review will drive key directions identified in the Destination 2036 initiative. The panel will investigate and identify options for: 1. Governance models 2. Structural arrangements 3. Boundary changes. In considering the above options, needs of local communities, delivery of services and infrastructure, financial sustainability, local representation, decision making and boundary changes will all be reviewed. The panel will spend the next 12 months holding discussions with the widest possible range of people and organisations throughout NSW. The panel will consult widely with the local and broader community. For further information and to have 'your say' visit: www.localgovernmentreview.nsw.gov.au Submissions close on 14 September 2012. The Panel will make its final report in July 2013.	Building community awareness.
2012	Resident Telephone Survey.	83.5% of residents felt renewing and maintaining footpaths, kerbs and roads was of high importance in maintaining current Council service levels.	This survey was conducted to determine whether residents would support a SRV for infrastructure

			maintenance and renewal.
2009	Resident Survey	>90% of residents were satisfied or very satisfied with waste, aging & disability & cultural services, community building, environmental education & council information. Footpaths, road maintenance, traffic, street cleaning building & development were rated by >30% of residents as not satisfied.	This survey was conducted to update surveys undertaken in 2001, 2002, 2003 & 2004.
2003	Resident Survey.	80% of residents said 'No' to a proposed merger with Ryde City Council.	This survey was undertaken to determine if residents of Hunter's Hill Council would agree to merge with Ryde City Council.

It is abundantly clear from Table 10.2 that Hunters Hill Council has taken the view (supported by the community and draft independent reports) that an amalgamation is not an appropriate outcome of the *Fit for the Future* process for Hunters Hill.

In responding to the Independent Panel (2013b) Revitalising Local Government report, Hunters Hill considered alternatives such as 'standing alone', merging, collaboration and Joint Organisation (JO) models. However, in Hunters Hill's response to the *Fit for the Future* criteria, it was resolved to pursue both regional collaboration in determining the viability of mergers and a Joint Regional Authority model based on maintaining existing boundaries using a shared services model with neighbouring councils. These two options are listed below:

- During October and November 2014, Mayors and General Managers of the Northern Sydney Councils recommended for a merger(s) in *Revitalising Local Government* agreed in principle with the draft collaboration model for the purpose of ongoing discussion with neighbouring councils. Hunters Hill Council further endorsed this strategy and the engagement of consultants – on a joint basis – to undertake a business

case analysis of the Independent Panel's recommendation for Hunters Hill, Lane Cove, Mosman, North Sydney, Willoughby and Ryde to merge (with costs to be on a shared funding basis). Independent consultants Morrison Low were subsequently appointed to assess the likely social, environmental, financial and governance outcomes that merging of Hunters Hill, the eastern two thirds of Ryde, Lane Cove, North Sydney, Willoughby and Mosman Councils would have.

- Simultaneously, Hunters Hill, Ryde and Lane Cove agreed to appoint consultants – on a joint basis – to further investigate options for an alternate Joint Regional Authority model. It is envisaged that this will benefit the business case to meet the 'scale and capacity' criteria set out by the Independent Panel, as well as providing high level financial efficiencies via shared funding to each participating council.

The exploration of an alternative proposal to form a Joint Regional Authority (JRA) of neighbouring councils has indicated that Hunters Hill Council will be well positioned to achieve the NSW Government's key objectives.

Hunters Hill Council is one of the initial local government areas in New South Wales (1861), and the only one of the original councils to have essentially kept its historic boundaries. In 2011, it celebrated 150 years with its community. Hunters Hill Council contains more heritage listed items per head of population than any other area in NSW, and many significant natural areas, including Boronia Park and Kelly's Bush. The historic boundaries of the Parramatta and Lane Cove Rivers, as well as Punt, Victoria and Pittwater Roads, remain today as Hunters Hill's natural and relevant boundaries. The 'community of interest' and 'sense of belonging' are extremely strong in Hunters Hill Council. This is evidenced by the

large number of local community and cultural groups, and the great spirit and determination of its residents to save it from amalgamation, as witnessed by the Save Hunters Hill Municipal Coalition.

Due to its strong history, heritage and community of interest Hunters Hill Council felt strongly about examining each option in detail to assess and understand the likely impacts that the NSW Government's recommendations would have at a local level. To this end reports by Percy Allen and Associates, Professor Brian Dollery, SGS Economics and Morrison Low made it clear that Hunters Hill Council's performance would best be enhanced by a Joint Regional Authority. In this regard, SGS Economics (2015) observed that 'the Joint Regional Authority scenarios can achieve efficiency advantages by getting the most return (relative to cost) out of the resources used in strategic planning, decision making and through operation of the organisation.'

The Hunters Hill community have a history of strong public demonstration and support of no forced amalgamations. As far back as 2003, over 80% of residents opposed a proposed forced amalgamation. Council received survey feedback, over 200 telephone calls and 100 protestors opposing the possible merger of Hunters Hill. A similar community sentiment exists in 2015 with a strong and vocal community group *Save Hunters Hill* launching a website and supporting Hunters Hill Council in developing a strong Joint Regional Authority model, which would see the heritage of its natural and built environment maintained.

In broad terms the economic advantages that could be achieved by a Joint Regional Authority can be characterised by the following:

- Enhanced strategic plans for land and infrastructure with the same or fewer staff, administrative and capital resources;
- Savings from economies of scale in the joint use of development decision making resources;
- Achieving economies of scale and scope from the operation of a shared services facility (managing rates, shared procurement, major facilities charging and management); and
- Rapidly and accurately achieve targeted subregional land use, infrastructure, social and economic development outcomes.

At a local level some of the key benefits to Hunters Hill using this model would be:

- Improved utilisation of existing local facilities;
- More efficient urban development patterns as better plans are made and investment decisions are more consistent with these plans;
- Amplified benefits from pooled grant funding;
- More effective achievement of social plan outcomes;
- Enhanced policy and grant funding success (leading to a more rapid achievement of funding priorities);
- Delayed or avoided new capital expenditure for planned state infrastructure;
- A more rapid adjustment towards identified objectives or alleviating social exclusion; and
- Free up Council to focus on services that are done best locally.

Across Sydney, there is growing community concern about the impact of forced council amalgamations. 'Mega-councils' mean loss of representation on planning, which ultimately takes local decision-making away from crucial community matters. By contrast, there is a consensus that a Joint Regional Authority will provide a superior method of improving council performance to deal with local issues and boost our capacity to tackle subregional priorities.

10.3.3 Ryde

In common with Lane Cove and Hunters Hill, the City of Ryde has actively engaged and communicated with its local community since the Independent Panel was commissioned by Minister for Local Government Page in June 2012 as a result of the *Destination 2036* initiative.

Following the Panel's request for feedback on their *Future Directions* report in April 2013, Ryde has communicated extensively and consulted vigorously with its local community to ensure it 'listened' to the community's views.

With respect to *Future Directions*, Ryde undertook the following consultation in May/June 2013 in formulating its response:

- Survey conducted on Ryde's website which received 255 responses;
- Telephone survey of 600 Ryde residents; and
- Community Meeting on 3 June 2013 with 140 attendees.

The results of the surveys and community consultation undertaken were as follows:

Telephone Survey: 56% of residents were not very or not at all supportive of amalgamations. If required to give a response of their preferred amalgamation preference, 48% preferred a merger to the east, with 38% still opposing amalgamations.

On Line Survey: 65% of residents were not very or not all supportive of amalgamations. If required to give a response of their preferred amalgamation preference, 47% preferred a merger to the east, with 36% still opposing amalgamations.

Community Meeting: 71% were not very or not at all supportive of amalgamations. If required to give a response of their preferred amalgamation preference, 47% preferred a merger to the east, with 27% still opposing amalgamations. In addition, 57% did not support the western third of Ryde being merged with Parramatta, Auburn and Holroyd Councils. The meeting also did not accept as true the Panel's recommendation that the amalgamation proposed with Parramatta, Holroyd and Auburn Councils would enable Ryde to become more financially sustainable, with 86% disagreeing. Finally, 79% of attendees disagreed with the Panel that mergers would result in greater efficiencies in the delivery of services to Ryde.

Based on this feedback from the community, Ryde Council endorsed its submission to be lodged back to the Panel, opposing the proposed mergers. Ryde Council also resolved to engage an appropriate external party to undertake a 'desktop review' of all publicly available information in critically evaluating the Panel's proposed mergers. This review was undertaken by SGS Economics which concluded that the City of Ryde remained strongest by

‘standing alone’ and clearly demonstrated a lack of ‘community of interest’ in the proposed merger with councils to the west of Ryde.

Between August 2013 and June 2014, the City of Ryde internally undertook a rigorous review of its operations together with an education program for councillors of Ryde’s financial position. This comprised 9 councillor workshops and three reports to Ryde Council. It also included a number of internal cost control measures being taken, which resulted in an annual ongoing saving of $1.9 million from its operations. This was mainly achieved through the reduction of 14 full-time positions. A further $0.6 million was projected in future revenue that projected annual ongoing efficiency savings at $2.5 million.

In June 2014, due to a better understanding of its projected financial position, Ryde Council authorised the Acting General Manager to undertake a comprehensive community engagement program with the local community to explain its financial position, as well as the likely impacts on Ryde’s services and service standards, if its financial position was not addressed. This ‘conversation’ with the community included the option of a possible Special Rate Variation (SRV) application over the rate-peg.

The Community Engagement Program occurred over August and September 2014. As a result of Ryde Council’s adoption of the Community Engagement Plan to meet the requirements of a proposed SRV application, it implemented the engagement strategy. The consultation program also included details of the proposed impacts of each option and that any proposed SRV application would be complemented by an annual efficiency saving totalling $2.5 million in generating adequate annual funding for Ryde’s asset renewal and

maintenance requirements. It should be noted that no funds from any of the SRV options would be used to address the refurbishment of the Civic Centre.

The key options that were included in the Community Engagement program were as follows:

Option A: DECLINE IN SERVICES (Approximate 3% rate-peg increase): Option A would be no additional rate increase for the next 4 years, commencing 2015/16 other than the estimated rate-peg increase of 3% each year. This would mean no additional investment in local infrastructure or facilities and would thus lead to a reduction in service levels and possible cuts in services.

Option B: MAINTAIN SERVICES (Approximate 7% increase (including rate-peg)): Option B would be an average annual 7% rate increase for the next 4 years, commencing 2015/16 (including the rate peg increase of around 3%) to maintain services at their current level, and provide additional money for renewing Ryde's infrastructure. It would not be sufficient to undertake all maintenance required, but would be enough to renew all assets that are rated as 'Condition 5' and some assets that are in 'Condition 4.'

Option C: UPGRADE SERVICES (Approximate 12% increase (including rate-peg)): Option C would be an average annual 12% rate increase for the next 4 years, commencing 2015/16 (including the rate peg increase of around 3%) to maintain services at their current level and provide further money for renewing the Ryde's infrastructure. It would still not be sufficient to undertake all repairs and maintenance needed, but would be enough to renew all assets that are rated as 'Condition 5' and most assets that are in 'Condition 4'

Summary of Community Survey Results: The community survey results are a combination of both the voluntary votes (i.e. votes lodged either through the reply-paid postcard or the online portal) and the random telephone survey. Due to the difference in the base size of the two survey methods (i.e. voluntary votes n=2,883 and random telephone survey n=655), the random telephone survey result was weighted up in order to provide a true representation of the average. This means that results from both survey methods are evenly represented in Table 10.3.

Table 10.3: Survey Results

Option A:	Supporting no increase at all in the rates over and above the rate peg	42.3% Community support
Option B & C:	Supporting either a 7% or 12% increase, inclusive of the rate peg	57.7 % Community support

In preparing the community engagement strategy for this proposed SRV, Ryde referred to Criterion 2 of the IPART SRV application guidelines indicates what councils must undertake in ensuring that 'the community is aware of the need and extent of a rate rise'. In essence, 'councils should canvas alternatives to a rate rise, the impact of any rises upon the community and the council's consideration of the community's capacity and willingness to pay rates'.

To this end the community engagement strategy addressed the following areas in line with the IPART requirements:

- Community's awareness of the proposal;
- Level of community engagement in the proposal;
- Community's willingness to pay increased rates; and
- Community's capacity to pay the proposed increase.

To provide further validity to the data, comparisons against neighbouring councils which have received an SRV approval from IPART in recent years were also included.

Ryde Council referred to the IPART guidelines which state that all SRV applications must demonstrate that 'the council has demonstrated an appropriate variety of engagement methods to ensure community awareness and input into the special variation process'. In addition, IPART expects local councils to select and execute methods which reflect the size and impact of the proposed rate increase and the resources of the council.

To this end, Council developed and executed a comprehensive eight week strategy that included:

- A 12-page information brochure mailed directly to over 30,000 residential ratepayers;
- Soft copies of the brochure emailed to over 200 real-estate agents for distribution to non -residential ratepayers (which totals approximately 5,000 properties);
- Brochure translated in to the Ryde's top five languages;
- A dedicated website that included an online Q&A portal;
- A dedicated phone number for community enquiries;
- 3 town hall community meetings, where the proposed SRV options were presented and workshopped with the community; and
- 16 information booths at various times and days during the eight week consultation period.

Local community members could provide feedback in a variety of ways including:

- Return of the reply paid postcard;
- Online vote through the dedicated engagement portal; and
- Contacting customer service to register a vote over the phone.

Comparison of Engagement Strategy against other Councils

An analysis of the engagement approaches and statistics of other councils which have undertaken an SRV process have been compared to the City of Ryde's approach and are detailed in Table 10.4.

Table 10.4: Engagement approaches, City of Ryde

	City of Ryde	Ku-ring-gai (2011)& (2013/14)	Lane Cove (2011/12)	Holroyd (2014/15)	Auburn (2010/11)	Warringah (2014/15)	Parramatta (2011/12)	North Sydney (2011)	Willoughby (2012/13)	Hunters Hill (2012/13)	Against the other Councils
Mail out	**30,211**			36,000		6,000		32,813		5,092	***Above Average***
Mail In	**2,408**			2017		151		3163		0	***Above Average***
Postal Response Rate (%)	**8%**			6%		3%		10%			***Above Average***
Online Response	**475**	37	174			419	37		911	160	***Above Average***
Random phone survey respondents	**655**	400	400	400	400	400	505	600		400	***Above Average***
Awareness (%)	**61%**	50% /37%		42%							***Above Average***
Support (%) for proposed SRV*	**57.7%**			37.2%			77.9%			40.2%	***Within the acceptable range***

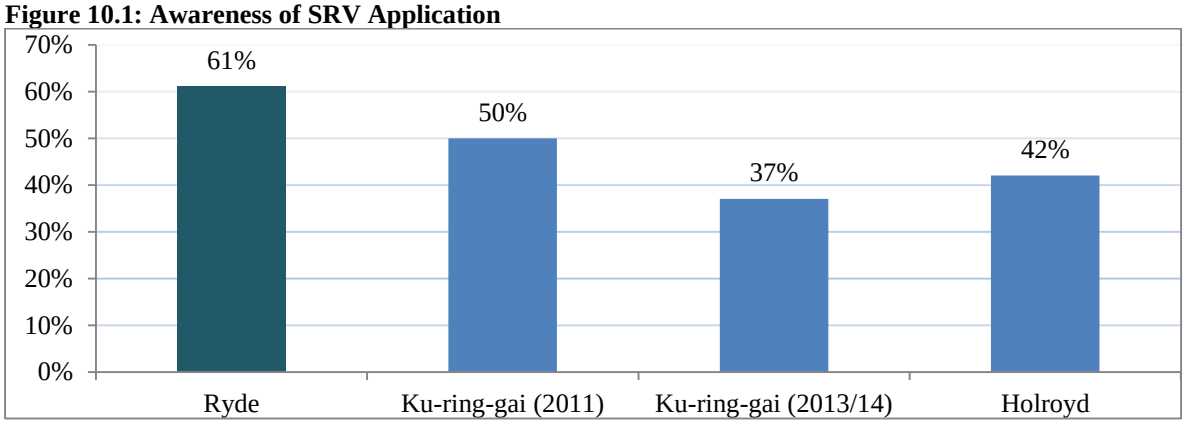
**** Average value of voluntary and random survey results***

Table 10.4 shows that the City of Ryde's approach compares favourably on how it has engaged with its community on this matter. The 57.7% support represents those members of the local community which support either Option B or Option C. In general, Table 10.4 indicates a significantly high awareness of the SRV proposal in the City of Ryde community.

According to the random telephone survey, with 95% confidence and ±3.8% margin of error, the majority (61%) of the rate payers in Ryde are aware of the SRV proposal.

The City of Ryde strongly compares with other councils on the local community's awareness of a proposed SRV application as detailed in Figure 10.1.

Figure 10.1: Awareness of SRV Application



As at 30 September 2014, Ryde received over 2,883 voluntary votes (2,408 postal votes and 475 online votes) with 655 telephone survey respondents, reflecting a high level of community engagement. In comparison to the neighbouring councils, Ryde has achieved the most responses by telephone surveys, second highest response rate via postal votes, and third most votes via online (Figures 10.2 to 10.7 below).

Figure 10.2: Number of Mail-Outs (Brochures, Letters, Booklets)

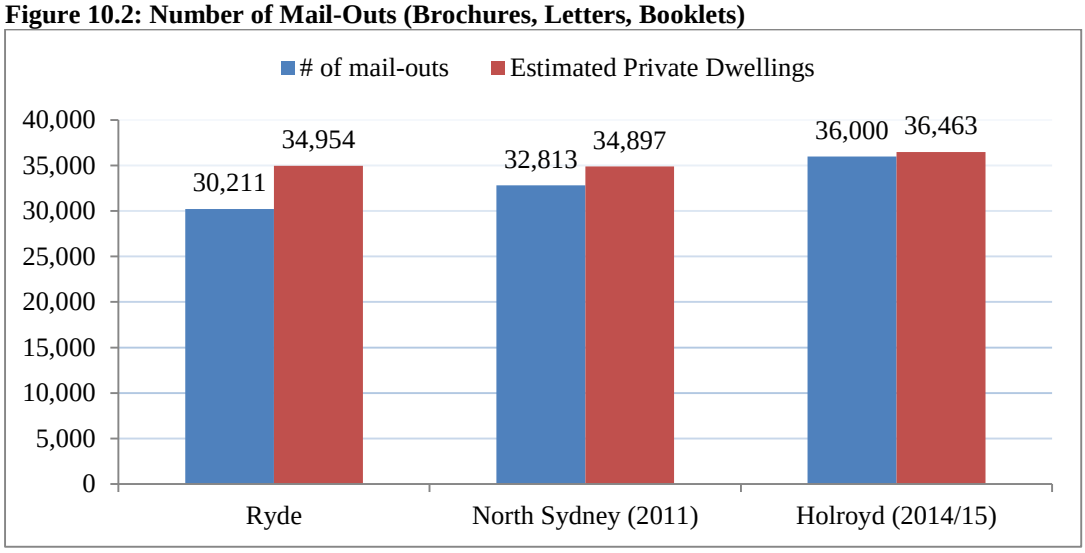


Figure 10.3: Number of Postal Votes Received

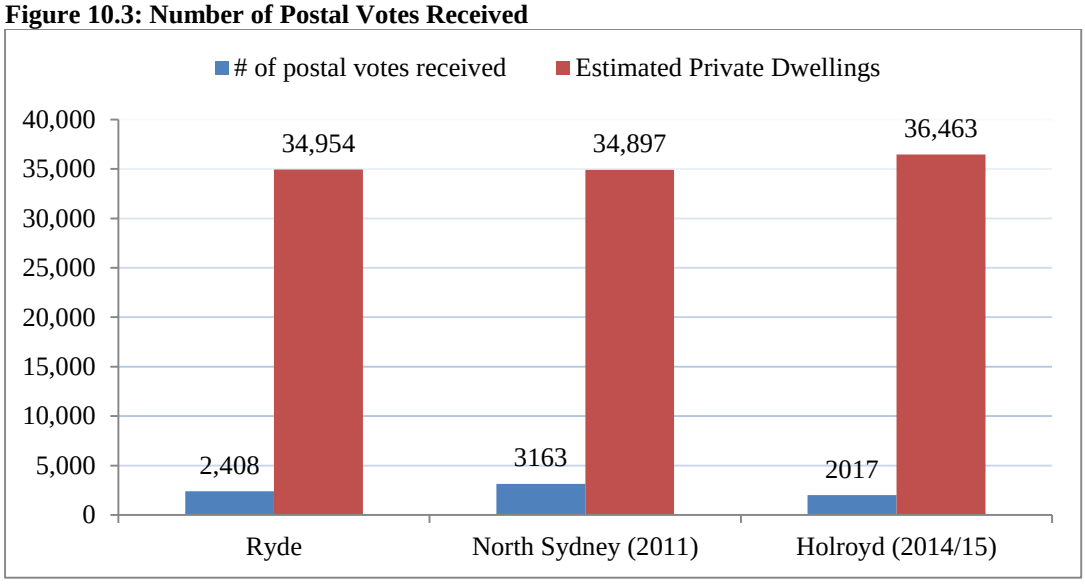


Figure 10.4: Response Rate by Mail

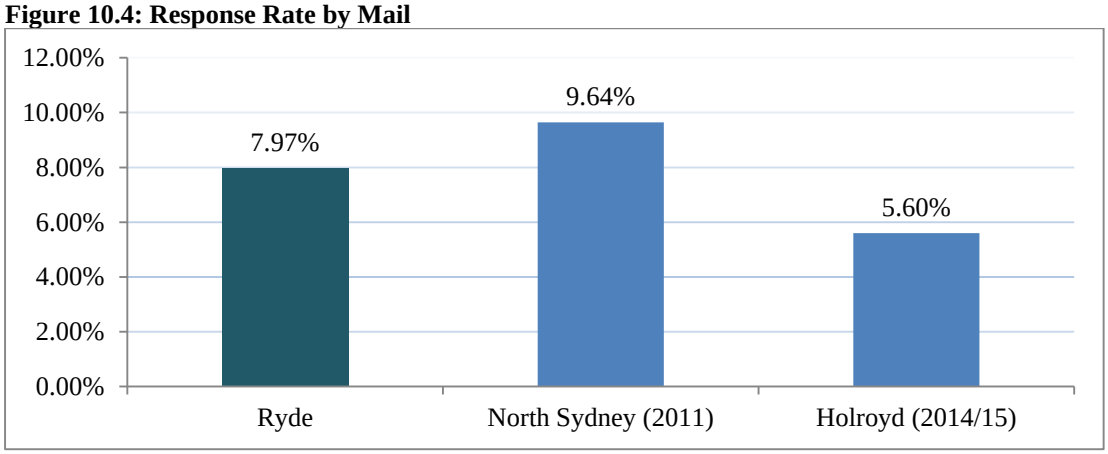


Figure 10.5: Online Votes

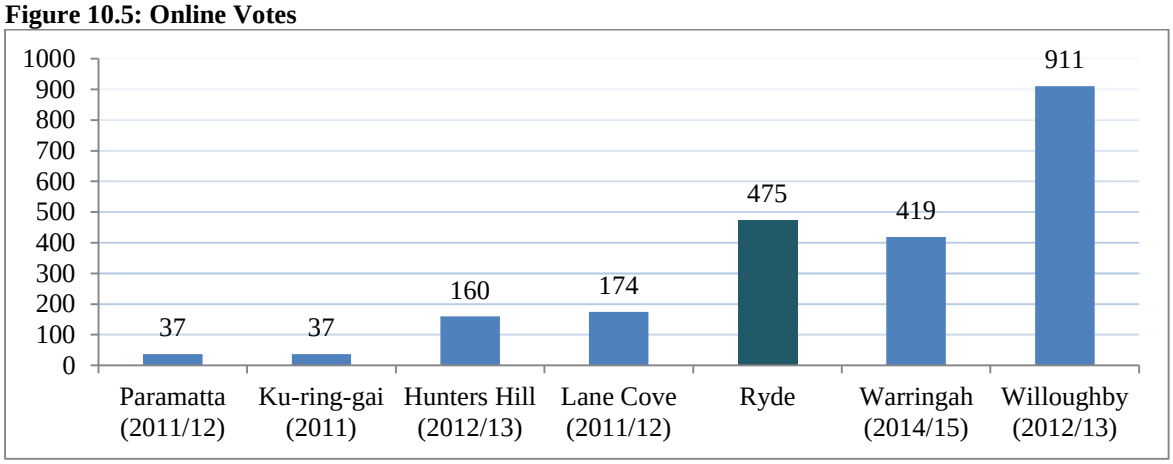
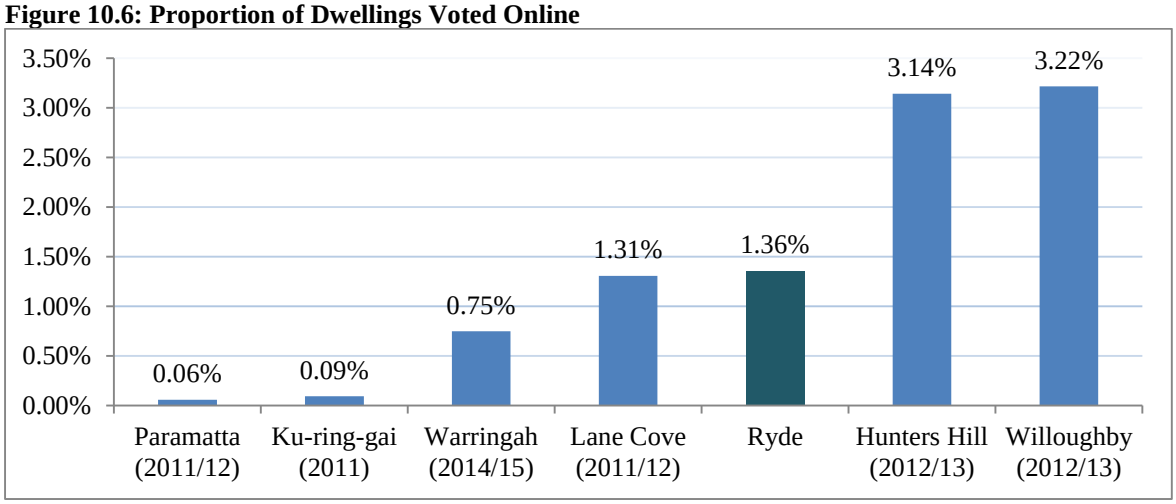
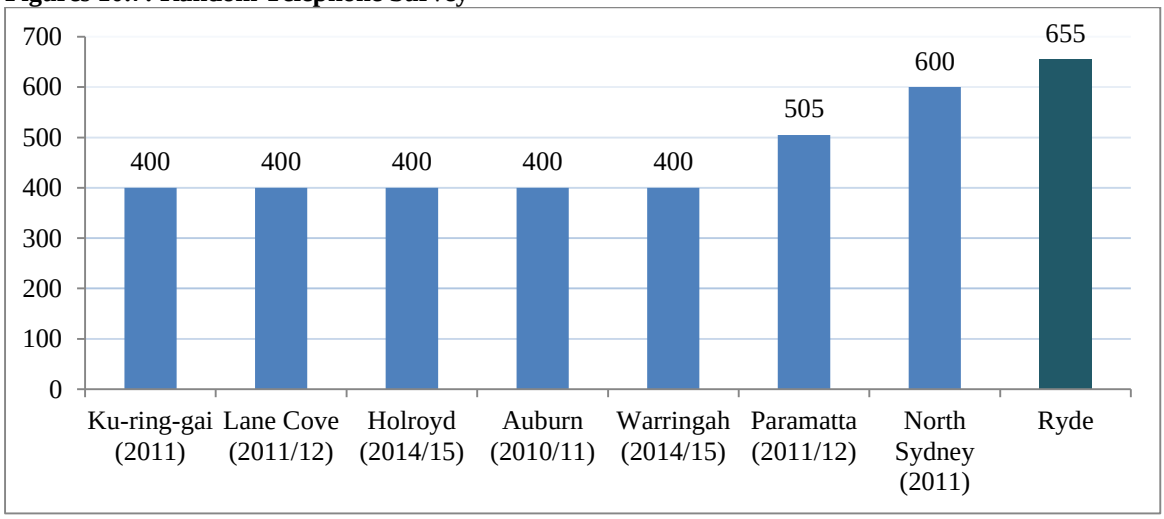


Figure 10.6: Proportion of Dwellings Voted Online



Figures 10.7: Random Telephone Survey



Reviewing community support and willingness to pay, the comparison pool was reduced from the original nine councils to three councils: Holroyd, North Sydney and Hunters Hill. These three councils were chosen for this comparison due to the similarity in both the type of submission and also the community engagement strategy undertaken.

As can be seen from Table 10.5, Holroyd, North Sydney and Hunters Hill undertook similar engagement strategies. Whilst Warringah also undertook an equally comprehensive strategy, its voting methods differed from Ryde and the other three councils. It was difficult to make accurate comparisons against the Warringah results.

Table 10.5: Community Support and Willingness to Pay

	City of Ryde	Ku-ring-gai (2011)& (2013/14)	Lane Cove (2011/12)	Holroyd (2014/15)	Auburn (2010/11)	Warringah (2014/15)	Parramatta (2011/12)	North Sydney (2011)	Willoughby (2012/13)	Hunters Hill (2012/13)	Against the other Councils
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Mail In	**2,408**			2017		151		3163		0	***Above Average***
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Random phone survey respondents	**655**	400	400	400	400	400	505	600		400	***Above Average***
Awareness (%)	**61%**	50% /37%		42%							***Above Average***
Support (%) for proposed SRV*	**57.7%**			37.2%			77.9%			40.2%	***Within the acceptable range***

**** Average value of voluntary and random survey results***

The comparison councils made the following applications as shown in Table 10.6:

Table 10.6: Council Applications

COUNCIL	SRV APPLICATION/IPART DETERMINATION
Hunters Hill Council (2012/13)	Applied and received IPART approval for SRV of 10.4% for 10 years in 2012/13.
Parramatta Council (2011/2012)	Applied and received approval from IPART to increase its general income by: • 4.3% in 2011/12 • 4.3% in 2012/13 • 9.2% in 2013/14.3. These increases represent a cumulative increase of 18.79% for these 3 years.
Holroyd Council (2014/2015)	Applied and received IPART approval for SRV of 8% for 3 years then 7% for 2 years, or a cumulative increase of 44.22% over the next 5 years.

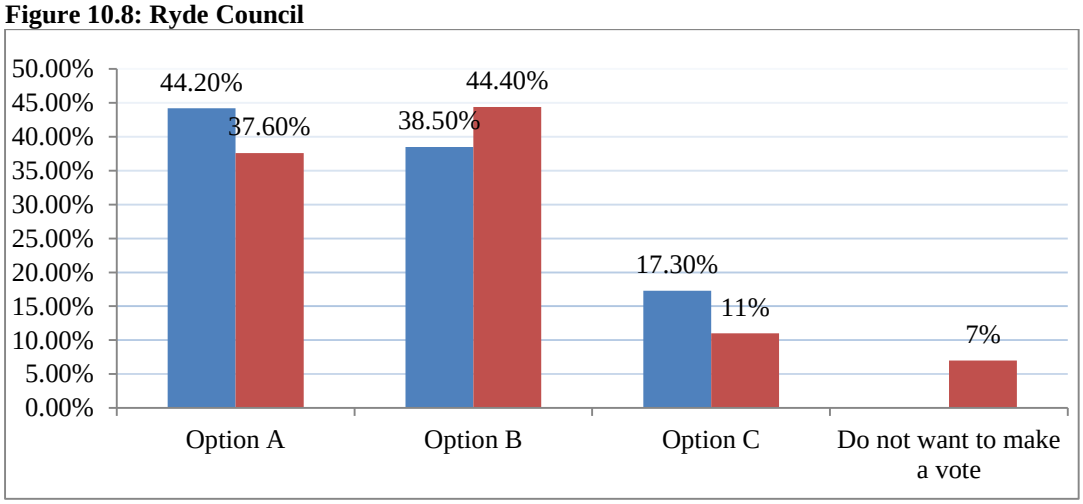
In general, councils showed similar trends from the random telephone surveys, receiving more support for the SRV in contrast to the voluntary votes (via postal and online voting). This is due to the non-biased measure of the random sampling that allows a more representative view of the wider community.

Using an average of the two measures (voluntary votes and random sampling), 57.7% of the community, would support either of Ryde's Option B or C, with 41.5% supporting Option A (i.e., SRV of 7% per year for 4 years). These results are in line with the comparable councils' range of 37% to 77.9%, previously approved by IPART, as shown in Table 10.7 below. Additional details are provided in Figures 10.8 to 10.11.

Table 10.7: Proposed Options

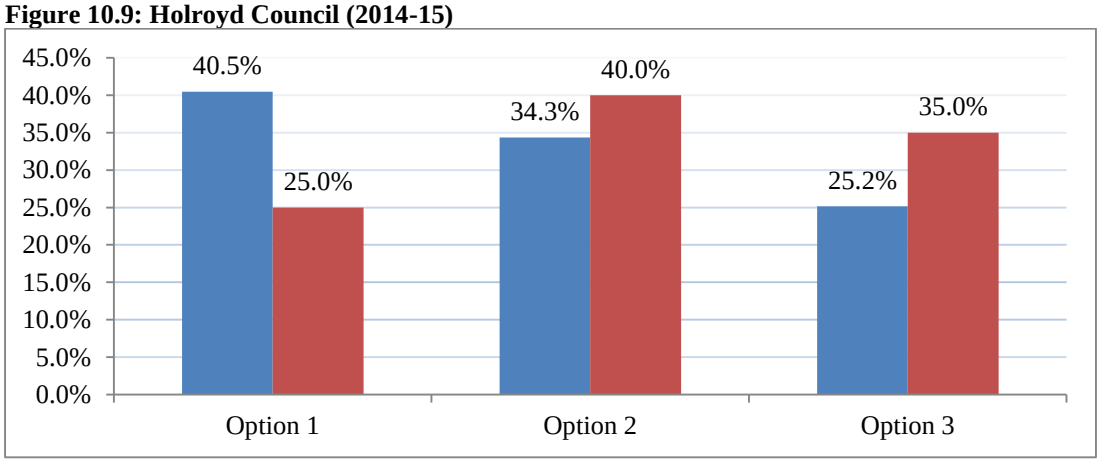
COUNCIL	PROPOSED SRV OPTIONS
Hunters Hill Council (2012/13)	Option 1 - Against the continuance of infrastructure levies. Option 2 - Rate peg increase and continuance of special rates. Option 3 - Support a rate peg increase, continuance of special rates and an operations catch-up increase to the general rate of 2%.
Parramatta Council (2011/2012)	Option 1 – Reduction in community services and infrastructure. Option 2 - Modest increase in Council ordinary rates (on average $10 per year over four years).
Holroyd Council (2014/2015)	Option 1 - Not in support of a SRV. Option 2 - Special Variation of 8% for 3 years then 7% for 2 years. Option 3 - Special Rate Variation of 9% for 6 years.

Figure 10.8: Ryde Council



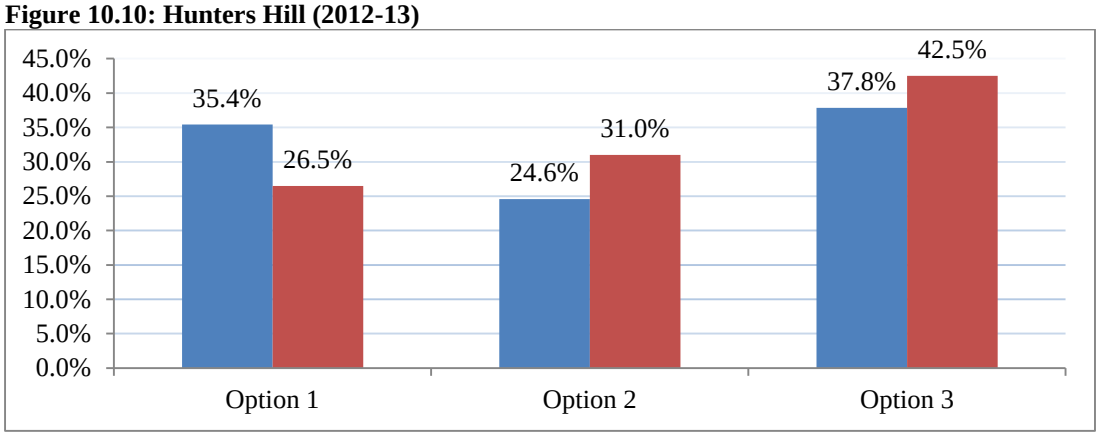
Voluntary (blue) = 2732; Random (red) = 655

Figure 10.9: Holroyd Council (2014-15)



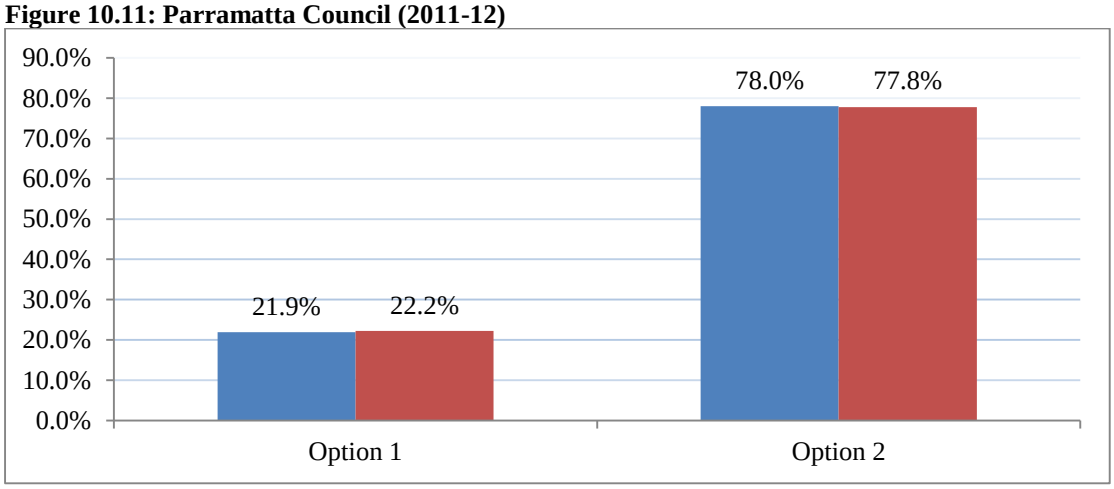
Voluntary (blue) = 2096; Random (red) = 400
Note: IPART approved Option 2- SRV of 8% for 3 years then 7% for 2 years.

Figure 10.10: Hunters Hill (2012-13)



Voluntary (blue) = 175; Random (red) = 416
Note: IPART approved Option 3 – 10.4% for 10 years in 2012/13. This option was presented to the community as "Rate peg increase, a new levy equivalent to the previous levy and operations catch up increase to the general rate of 2".

Figure 10.11: Parramatta Council (2011-12)



Voluntary = 664 (blue); Random (red) = 505
Note: IPART partially approved Option 2 – An accumulative increase of 18.79% for 3 years. This option was presented to the community as a "Modest increase in Council ordinary rates" (increase of average $10 per year over four years).

In general, while there are variations between the councils compared, the Ryde's results of 57.7%% of the community supporting an SRV to 42.3% for no change are positive and in line with the results of the other councils surveyed.

As a result of the results from the Community Engagement Program, Ryde approved making an SRV application to IPART in February 2015. It is presently awaiting the outcome of its application.

In respect of *Fit for the Future*, the Ryde determined its position and how it would respond at its Extra-Ordinary Council meeting on the 17 February 2015. Since this resolution, Ryde Council has taken the following initiatives, either exclusively to its own community or jointly with Lane Cove and Hunter's Hill on the Joint Regional Authority (JO) option.

These initiatives were to ensure the Ryde community fully understood the proposed implications for Ryde Council: it is proposed that Ryde be split into two 'mega-councils' to the east and west, if the recommendations in the *Fit for the Future* program are implemented by the NSW Government.

As a result of Lane Cove and Hunter's Hill joining Ryde to investigate the JO proposal, a number of joint initiatives were taken as part of a joint community engagement strategy, including

- Letters to the community by the Mayors with a supporting brochure;
- Publicity campaign on forced amalgamation;
- Community Meetings – Coordinated by the City of Ryde and facilitated by
- Urbis; and
- Joint Community survey that will be commenced on 18 May 2015.

In addition, the Mayors of each council were interviewed by the *Northern District Times*, followed by articles and press releases in the *Northern District Times* relating to key components of the *Fit for the Future* program. The Mayors of both Ryde and Hunter's Hill were also recently interviewed by 2RRR.

Following the Ryde community meeting, with an attendance of approximately 100 residents, the results from the meeting were as follows:

- How supportive are you of the City of Ryde Council being split and merged: 11.0%;
- How supportive are you of the City of Ryde standing alone: 84.0%; and
- How supportive are you of Council exploring the possibility of a Joint Organisation: 83.8%.

These results show strong opposition to Ryde being split and merged and for Ryde to 'stand alone'. While the vote was strong, the participants at the meetings were also supportive of Ryde exploring a JO.

Ryde's results at the community meeting also are consistent with the results that it has received to its on-line survey which has been running since 10 March 2015. A total of 1,153 responses have been received which shows 81% do not support the NSW Government's *Fit for the Future* program which would split Ryde into two 'mega-councils'. Ryde's results are strikingly similar to the results at both the Hunter's Hill and Lane Cove community meetings.

Table 10.8: Community Meeting Results

	Hunter's Hill (%)	Lane Cove (%)
How supportive of being merged	17.8	7.0
How supportive of standing alone	73.4	85.5
How supportive of exploring a JO	86.0	82.2

As can be seen from Table 10.8, both Hunter's Hill and Lane Cove results are consistent with the results achieved by Ryde. All support each council 'standing alone' and to explore the possibility of a JO.

In addition to this communications/engagement strategy, Ryde has also undertaken extensive initiatives in further informing its community of the proposal to dismember Ryde. These included:

- Direct mailing all ratepayers on 10 March 2015 with a letter from the Mayor and supporting brochure;
- Advertising in the Northern District Times on 3 March, 11 March and 18 March 2015;
- Banners on buildings and at locations throughout the City of Ryde;
- 2 week campaign at the end of April for advertising in Adshel Bus Shelters;
- Dedicated placement on Council's website on home page and landing page;
- Place the 'Ryde Says No Campaign' to all email signatures from 20 March 2015;
- Placed 'Ryde Says No' on 70 banner poles from 23 March 2015 in Ryde and Macquarie Park;
- Published articles in the e-Newsletter from March that were distributed on 2 February 2015 and 3 March 2015;

- Also forwarded e-Newsletter to extended list of people who had signed up for Fit for the Future updates on Ryde website (14,955 people);
- Various Mayoral radio interviews on Sydney Metropolitan radio stations during March and April;
- General Manager has sent regular updates to all staff;
- This initiative has been prominent in Council's social media, both on Facebook and Twitter;
- Various media releases in Local and National press during the months of March and April; and
- Various speaking engagements by the Mayor and General Manager during March and April.

In sum, the evidence presented under section 10.3.3 demonstrates conclusively that the extensive Community Engagement program that Ryde has initiated with its community since 2013 that has included the Independent Panel's reports, Ryde's *Financial Future* initiative that resulted in Council approving a SRV application and responding to the NSW Government's *Fit for the Future* program. Table 10.9 summarises the efforts taken by Ryde Council:

Table 10.9: Community Consultation by Ryde

Date	Action Taken	Outcome	Comment
May 2013	Community Survey (Telephone)	450 respondents When prompted, 54% of the community supported as a first preference for City of Ryde Council to develop a long term resourcing strategy that would maintain services and facilities, and increase rates sufficiently to cover increased provision of these to serve the growing population. 24% supported a strategy that would enhance services and facilities, and increase rates. Only 22% of residents wanted to retain rates and	

		reduce Council services as a first option. 54% of residents nominated it their lowest preference.	
3 June 2013	Community Meeting Local Council Amalgamations	135 attendees Discussed Independent Local Government Review Panel's recommendations 44.6% of respondents not at all supportive of City of Ryde being amalgamated with other nearby Councils. If the community had to choose, 47.1% of respondents would prefer a merger with Willoughby, Lane Cove and Hunters Hill. 78.9% of respondents strongly agree that it is important to retain a sense of local identify within the City of Ryde. 67.8% think that an amalgamation will have a negative impact on services in their local area. 83.1% have the opinion that it is important that their local representatives are familiar with their area and its specific needs.	
25 June 2013	Council Report Response to Independent Local Government Review Panel's Report	Council endorsed Council's response to the Independent Local Government Review Panel's Report. Council also endorsed for a consultant to be engaged to undertake a desktop review of the Panel's amalgamation proposal.	
August 2013 – June 2014	9 x Councillor Workshops City of Ryde's Financial Future, using TCorp's financial sustainability ratings as a basis of discussions	In April 2014: • Council resolved to proceed with the Action Plan, including Stage 1 of the Community Engagement Program; and • Council resolved to engage an independent organisation to undertake an assessment of the City of Ryde's performance against other similar sized Councils and industry benchmarks In June 2014: • Council endorsed completing a comprehensive Community Engagement Program, which included the possibility of an SRV application	
October 2013	Independent Local Government Review Panel Revitalising Local Government Final Report	Independent Local Government Review Panel issues final report	
25 February 2014	Council Report - SRV	Council resolved for the GM to report back on short, medium and long term propositions in regards to the City of Ryde's financial future and to detail the proposed community engagement strategy	
22 April 2014	Council Report – SRV	Council resolved to proceed with the Action Plan, including Stage 1 of the Community Engagement	PWC was engaged

<table>
<tr><td></td><td></td><td>Program

Council also resolved to engage an independent organisation to undertake an assessment of the City of Ryde's performance against other similar sized Councils and industry benchmarks</td><td></td></tr>
<tr><td>24 June 2014</td><td>Council Report - SRV</td><td>Council endorsed for the GM to complete the remaining stages of the community engagement program, and for the results of the engagement to be reported back to Council.</td><td></td></tr>
<tr><td>July – September 2014</td><td>Community Workshops / Interactions Various locations, within the City of Ryde, including 3 public community forums</td><td>57.7% of the community supported an increase of up to 12% to ensure Council maintains services, service standards and address the annual funding shortfall for asset renewals

3,538 responses received:

<table><tr><td></td><td>SERVICE LEVEL</td><td>RATE</td><td>Rate Payer Support</td></tr><tr><td>OPTION A</td><td>DECLINE IN SERVICES</td><td>3% rate peg</td><td>42.3%</td></tr><tr><td>OPTION B</td><td>MAINTAIN SERVICES</td><td>7% including rate peg</td><td>43.1%</td></tr><tr><td>OPTION C</td><td>UPGRADE SERVICES</td><td>12% including rate peg</td><td>14.6%</td></tr></table></td><td></td></tr>
<tr><td>October 2014</td><td>Minister for Local Government released the Fit for the Future Initiative</td><td></td><td></td></tr>
<tr><td>11 November 2014</td><td>Council Report SRV Application – including updated information relating to Council's Infrastructure Assets</td><td>Council endorsed for IPART to be notified of Council's intention to make a SRV application.</td><td></td></tr>
<tr><td>November 2014 – February 2015</td><td>A number of discussions between Northern Sydney Councils – Fit for the Future</td><td>Meeting of Mayors, General Managers across Northern Sydney Councils.

Received Councillor feedback</td><td></td></tr>
<tr><td>10 February 2015</td><td>Council Report Draft Four Year Delivery Plan 2014-2018 (including One Year Operational Plan 2014/2015)</td><td>Council endorsed making an SRV application</td><td></td></tr>
<tr><td>17 February 2015</td><td>Extraordinary Council Meeting Council Report "Fit for the Future – City of Ryde's Response"</td><td>Council resolved to reject the Panel's recommendations and to investigate a Joint Organisation alternative.

RESOLUTION: (Moved by The Mayor, Councillor Pickering and Councillor Salvestro-Martin)</td><td>Extraordinary Council Meeting</td></tr>
</table>

		(a) That the City of Ryde reaffirm its rejection to the recommendations as detailed in the Independent Panel's final report that proposes to split the City of Ryde partly between Parramatta, Holroyd and Auburn Councils with the balance being amalgamated with Councils to the east and north, comprising Hunters Hill, Lane Cove, Mosman, North Sydney and Willoughby Councils; *(b) That the City of Ryde complete Template 2 – Council Improvement Proposal, to demonstrate that the City of Ryde is sustainable in its own right;* *(c) That in addition to completing Template 2, Council also endorse investigating a modified Joint Organisation (regional body) proposal to meet the State Government's scale and capacity criteria, on the basis that there are other Councils in northern Sydney interested in participating in this proposal with the City of Ryde;* *(d) That the City of Ryde endorse undertaking a shared community engagement strategy with those Councils that confirm interest in exploring a modified Joint Organisation (regional body) proposal as detailed in part (c) above;* *(e) That Council endorse the General Manager writing to the Mayor and General Manager of the Councils that attended the Symposium, to confirm their Council's position by Wednesday 18 March 2015, in respect of parts (c) and (d) above;* *(f) That the City of Ryde endorse a business case (cost benefit analysis) being undertaken of the Independent Panel's recommendation for the Councils of Hunters Hill, Lane Cove, Mosman, North Sydney, Willoughby and Ryde to amalgamate (costs to be on a shared funding basis); and* *(g) That the General Manager write to the Mayor and General Manager of Parramatta, Auburn and Holroyd Councils to formally advise that the City of Ryde rejects the Independent Panel's recommendations for the western area of the City of Ryde to*	

		merge with Parramatta, Auburn and Holroyd Councils and to advise that Council is exploring other options as detailed above. *(h) That the City of Ryde, as soon as possible, commence a community information strategy to bring the specific predicament of this Council to the attention of our community.*	
March 2015	Community Telephone Survey *Fit for the Future* Initiative	450 respondents.	
March – April 2015	Awareness Campaign	City of Ryde issues letters to residents, increased media presence, banners across the City of Ryde LGA.	
March 2015	Community Poll Online	1,100 residents to date have responded: • 81% against amalgamations • 19% support amalgamations	
May 2015	Community Meetings	Community meetings to gain community feedback on Fit for the Future plus Council's response, including a Joint Organisation proposal: • City of Ryde – 5 May 2015 • Hunters Hill – 6 May 2015 • Lane Cove – 7 May 2015	
May 2015	Joint Council Community Survey Telephone	Proposed to be undertaken mid May 2015: • 450 City of Ryde residents • 450 Lane Cove residents • 250 Hunters Hill residents	

10.4 Conclusion

Chapter 10 has considered the efforts by Lane Cove, Hunters Hill and Ryde to engage extensively with their respective local communities on the options confronting them under the NSW Government's *Fit for the Future* program. We have demonstrated that all three local authorities instigated ongoing community engagement processes from the initial stages of the Destination 2036 reform initiative. These community engagement processes have not only been extraordinarily thorough and comprehensive, but also provided striking evidence that the local residents of Lane Cove, Hunters Hill and Ryde overwhelmingly oppose council mergers. It also provided compelling evidence that these communities much preferred the JO approach to achieving the benefits of scale and capacity.

In its *Methodology for Assessment of Council Fit for the Future Proposals*, IPART (2015, p.36/37) set out criteria against which local authorities community engagement efforts would be assessed, including clear evidence of comprehensive engagement, 'evidence of council resolutions' on amalgamation, the public dissemination of merger proposals, and the use of a variety of methods, such as disseminating options or proposals for comment, mail-outs, fact sheets and media releases, online surveys, random surveys of ratepayers, public meetings, listening posts, and workshops. We have seen in Chapter 10 that Lane Cove, Hunters Hill and Ryde easily meet these criteria.

CHAPTER 11: IPART'S *METHODOLGY FOR ASSESSMENT OF COUNCIL FIT FOR THE FUTURE PROPOSALS*

Chapter Summary

- The publication of IPART's (2015) *Methodology for Assessment of Council Fit for the Future Proposals* on 27 April 2015 added a further twist to the local government reform process in NSW.
- Not only will IPART now replace the Panel of Experts promised in the OLG's (2014) *Fit for the Future* documentation as the assessor of council submissions due on 30 June 2015, but *Methodology for Assessment of Council Fit for the Future Proposals* also introduces significant changes to the basis of the assessment process.
- The most important change resides in the differentiation between 'non-rural', 'rural' and 'merged' councils in IPART (2015) and the 'one size fits all' approach in *Fit for the Future.*
- In this chapter we demonstrate that not only due these changes fail to address the difficulties in the *Fit for the Future* performance criteria and benchmarks, but they also contain additional flaws.

11.1 Introduction

As we have spelled out in this Report, the NSW local government *Fit for the Future* reform program has become increasingly convoluted with ongoing and significant changes being made to the criteria with which local authorities are to be assessed. Indeed, Chapter 4 in this Report considered in detail the nature of many of these earlier changes, which had occurred between the publication of the Independent Panel's (2013a; 2013b) *Future Directions* interim

report, its *Revitalizing Local Government* final report and the NSW OLG's (2014b) *Fit for the Future* documentation, and demonstrated numerous problems with the criteria employed and their associated benchmarks. Chapter 4 also demonstrated how rushed and ill-considered the reform process had become. Under the *Fit for the Future* process all NSW local councils have to submit a merger proposal, 'council improvement' proposal, or a Rural Council proposal to the NSW OLG by 30 June 2015 using templates issued by the NSW OLG.

In yet another abrupt and startling twist to an already convoluted and rushed reform process, the Independent Pricing and Regulatory Tribunal's (IPART) (2015) *Methodology for Assessment of Council Fit for the Future Proposals; Local Government Consultation Paper April 2015* was released on 27 April 2015, a mere two months before the 30 June 2015 deadline for proposals to be submitted to the NSW OLG. The NSW OLG's (2014b) *Fit for the Future* program had earlier set out the six criteria and associated benchmarks which local authorities had to address in the submissions to the OLG. *Fit for the Future* had also specified that an Expert Panel would be established to assess all submissions from local councils and make recommendations to the OLG.

The sudden and entirely unexpected publication of IPART's (2015) *Methodology for Assessment of Council Fit for the Future Proposals* rendered much of the *Fit for the Future* process obsolete. For example, IPART – together with South Australian commercial consultant John Comrie – would now replace the proposed Expert Panel as the assessor of council submissions. In addition, the criteria contained in *Fit for the Future* were modified and augmented in *Methodology for Assessment of Council Fit for the Future Proposals*!

At a stroke, *Methodology for Assessment of Council Fit for the Future Proposals* thus placed NSW local government in invidious circumstances. Across NSW, local authorities, including Hunters Hill, Lane Cove and Ryde councils, have spent many months and millions of dollars consulting with their local communities and preparing merger, 'council improvement' and Rural Council proposals on the basis of the *Fit for the Future* process and its criteria.

Many of these efforts were now rendered obsolete. Furthermore, too little time now remained for councils to once again go through a thorough community engagement process and carefully prepare submissions using the new *Methodology for Assessment of Council Fit for the Future Proposals.*

Against this background, Chapter 11 sets out the new process and criteria embodied in IPART's (2015) *Methodology for Assessment of Council Fit for the Future Proposals*, differentiating it from the OLG's (2014a) *Fit for the Future* program, and then providing a critical assessment of *Methodology for Assessment of Council Fit for the Future Proposals*. In so doing, Chapter 11 demonstrates that *Methodology for Assessment of Council Fit for the Future Proposals* not only fails to remedy the severe problems in the *Fit for the Future* program, but also is awash with further deficiencies itself.

Chapter 11 is divided into three main parts. Section 11.2 briefly summarises *Methodology for Assessment of Council Fit for the Future Proposals*, sets out its evaluative criteria, and compares these with the criteria originally developed by TCorp (2013) and modified in *Fit for the Future.* Section 11.3 considers the numerous problems inherent in the *Fit for the*

Future criteria and the IPART (2015) *Methodology for Assessment of Council Fit for the Future Proposals* assessment technique:

- IPART (2015) assessment methodology for scale;
- IPART (2015) assessment methodology for sustainability;
- IPART (2015) assessment methodology for infrastructure and delivering services; and
- IPART (2015) assessment methodology for efficiency.

Chapter 11 ends with some brief concluding remarks in section 11.4.

11.2 *Methodology for Assessment of Council Fit for the Future Proposals* Structure

IPART (2015, p.43) have been instructed in its terms of reference to assess each council's fitness with 'consistency, fairness and impartiality'. However, the terms of reference also require IPART (2015, p.43) to 'be consistent with the Government's local government reform agenda, as outlined in the *Fit for the Future* documentation'. This last requirement places great constraints on IPART because the *Fit for the Future* (FFTF) program has severe deficiencies, as we demonstrated in Chapter 4 of this Report.

Table 4.2 in Chapter 4 of this Report set out the performance criteria developed by TCorp (2013), employed by the Independent Panel and then modified in the *Fit for the Future* process. Table 4.2 is reproduced as Table 11.1 below:

Table 11.1: Changes in Financial Sustainability Measures for NSW Local Government

Financial Ratio	TCorp Weighting	Comparative Information Report 2012/13	TCorp Threshold	Fit For The Future
Operating ratio	17.5%	Reported	>-4%	>0.0% over 3 years
Own Source	17.5%	Reported	>60%	>60% over 3 years
Cash Expense	10.0%	Reported	>3.0 months	Abandoned
Unrestricted Current	10.0%	Reported	>1.5	Abandoned
Debt Service	7.5%	Reported	>2.0	0 to 20% over 3 years
Interest Cover	2.5%	Not reported	>4.0	Abandoned
Infrastructure backlog	10.0%	Reported	<0.02	<2% (unchanged) over just one year
Asset Maintenance	7.5%	Not reported	>1	>100% (unchanged) over 3 years
Building and Infrastructure Renewal	7.5%	Reported	>1	>100% (unchanged) over 3 years
Capital Expenditure	10.0%	Not reported	>1.1	Abandoned
Real Operating Expenditure per Capita	n/a	Reported in nominal terms only according to 8 functional categories	Not considered	No time or threshold in documentation

Source: TCorp (2013); Office of Local Government (2014a), Office of Local Government (2014b)

As we noted in Chapter 4, the performance indicators in Table 11.1 changed significantly between the TCorp (2013) and the *Fit for the Future* process: some indicators were simply abandoned, and weightings, thresholds and benchmarks modified, often with little or no explanation.

Table 11.2 illustrates the differences between the *Fit for the Future* performance indicators and those proposed in *Methodology for Assessment of Council Fit for the Future Proposals.*

Table 11.2: *Fit for the Future* and IPART (2015) Performance Criteria

Criteria and measure	Benchmark	IPART Non-Rural	IPART Rural	IPART Merged
Scale and Capacity	ILGRP recommendations	ILGRP recommendations or merger broadly consistent with ILGRP or Sound argument for no structural change	Demonstrates it has considered merger option and has strategies to enhance capacity.	Not applicable.
Sustainability				
Operating Performance Ratio	Greater or equal to break-even over 3 years	Must meet within 5 years.	Plan to meet within 10 years	Must meet within 5 years (non-rural). Plan to meet within 10 years (rural).
Own Source Revenue Ratio	Greater than 60% over 3 years	Must meet within 5 years.	Plan to improve within 5 years & consideration of FAGs	Must meet within 5 years (non-rural). Plan to improve within 5 years & consideration of FAGs (rural)
Building and Asset Renewal Ratio	Greater than 100% over 3 years	Meet or improve within 5 years.	Met or improve within 5 years.	Meet or improve within 5 years.
Effective infrastructure and service management				
Infrastructure Backlog Ratio	Less than 2% over 3 years	Meet or improve/inform within 5 years	Meet or improve/inform within 5 years	Meet or improve/inform within 5 years
Asset Maintenance Ratio	Greater than 100% averaged over 3 years	Meet or improve/inform within 5 years	Meet or improve/inform within 5 years	Meet or improve/inform within 5 years
Debt Service Ratio	Greater than 0% but less than or equal to 20% over 3 years	Meet within 5 years	Meet within 5 years	Meet within 5 years
Efficiency				
Real Operating Expenditure	A decrease in Real Operating Expenditure per capita over time	Must demonstrate operational savings (net of IPR supported service improvements) over 5 years.	Must demonstrate operational savings (net of IPR supported service improvements) over 5 years.	Must demonstrate operational savings (net of IPR supported service improvements) over 5 years but may not be practical in short term

Source: IPART (2015)

Just as significant differences exist between TCorp (2013) and the *Fit for the Future* performance criteria, so too substantial differences are evident between *Fit for the Future* and IPART (2015), as we see can see from Table 11.2. A major difference resides in the

differentiation between ‘non-rural’, ‘rural’ and ‘merged’ councils in IPART (2015) and the ‘one size fits all’ approach in *Fit for the Future.* In addition, the benchmarks which must be met diverge widely between IPART (2015) and *Fit for the Future.*

This presents obvious and acute problems for councils which have already undertaken *Fit for the Future* analysis of their performance on existing *Fit for the Future* criteria and associated benchmarks. Quite apart from the procedural problems derived from ‘changing the rules of the game’ towards the end of the process, it also means that local authorities have a bear two months to assess their performance under the new IPART (2015) benchmarks. It need hardly be noted that this is a chaotic way of conducting public policymaking.

11.3 Problems in *Methodology for Assessment of Council Fit for the Future Proposals*

In addition to these problems there are severe problems embedded in the *Fit for the Future* program which are replicated in *Methodology for Assessment of Council Fit for the Future Proposals.*

In the first place, in common with the *Fit for the Future*, the IPART (2015) *Methodology for Assessment of Council Fit for the Future Proposals* is characterised by an absence of any controls for the external constraints facing councils over which they can exercise no control. Put simply, external constraint refers to the exogenous challenges which a municipality faces in providing local services (Andrews et al. 2005). Since local authorities typically face different external circumstances, they are nonetheless judged according to the same performance benchmarks. For instance, it is ridiculous to suggest that Manly (with 105km of roads, an average wage of $87,682, indigeneity at 0.3% and average density of 3,097 individuals/km^2) faces the same problems as Penrith (with 970km of roads, an average wage

of $49,046, indigeneity at 3% and density of 462 individuals/km^2). Yet this is the approach taken in the *Fit for the Future* program and now *Methodology for Assessment of Council Fit for the Future Proposals.*

Secondly, as we saw in Chapter 4 of this Report, both the *Fit for the Future* program and *Methodology for Assessment of Council Fit for the Future Proposals* use data fraught with problems. IPART (2015, p.26) recognised these data problems and observed that 'we consider some flexibility is required when considering some benchmarks more than others to take account of particular issues, e.g., data integrity issues'. However, more than 'flexibility' will be required to make any reliable assessment of 'fitness for the future' given the extent of the problems in the data. The corrosive nature of the data distortions have been demonstrated in the scholarly literature (Drew and Dollery, 2015a). At least two significant additional sources of error are introduced by the OLG's (2014) use of population data for its so-called 'efficiency' ratio: (i) population estimates in inter-censal years are simply estimates and not objective data and (ii) the *Fit for the Future* toolkits use 2013 *projected* population data which the Australian Bureau of Statistics (ABS) had clearly labelled 'preliminary figure[s] or series subject to revision' (ABS, 2015).

In addition, errors in logic continue to plague some *Fit for the Future* ratios, as we saw in Chapter 4. IPART (2015, p.31) recognised the logical flaws in at least one ratio when it observed that 'we should note that the benchmark for the Asset Maintenance Ratio is based on the underlying assumption that previous underspending has occurred, which has resulted in the infrastructure backlog for councils being greater than 2%'. Thus 'should a council continuously exceed the Asset Maintenance target by spending more on maintenance than is

required (i.e., the ratio is > 100%), this may also indicate the council is not efficiently managing its assets'.

There are a number of difficulties raised by this acknowledged logical flaw. Firstly, there are a large number of councils which claim to have an infrastructure backlog ratio of less than 2% and indeed to be 'fit for the future' councils must demonstrate that this is the case. It thus follows that – according to this statement – a council demonstrating 'fitness' on the Infrastructure Backlog Ratio will simultaneously demonstrate inefficient Asset Management if they also meet the latter benchmark! Secondly, IPART/OLG propose to use the *Fit for the Future* ratios as a long-term performance management device, even after the ratios have served their purpose of providing an ersatz rationalisation for a politically motivated forced amalgamation program. However, by IPART's (2015) own admission the continual achievement of this ratio benchmark will actually indicate that councils are not 'efficiently managing' their assets.

A further problem resides in the fact that the architects of *Fit for the Future* – the OLG (2014) and ILGRP (2013a; 2013b) – have still not provided a satisfactory empirical evidence that amalgamation is the panacea to the NSW municipal 'sustainability crisis' that they claim it to be. Consequently, it may well come as a surprise to most NSW residents that the NSW Government has embarked on the 'most significant investment the State has ever made in the local government sector' (Toole 2014) - predicated on enhancing the sustainability of the local government sector through mergers - without actually conducting a rudimentary examination of whether amalgamations do enhance sustainability!

However, as we saw in Chapter 3 of this Report, an examination of a stratified sample of the 2000/2004 Carr Government amalgamated councils found that there was no statistically significant difference in the sustainability of merged and unmerged councils. Moreover, Drew, Kortt and Dollery (2013) conducted an empirical examination of the outcomes from the Queensland (Qld) 2007/8 amalgamations and found evidence to suggest that the forced amalgamations were generally deleterious for Queensland local government. Moreover, Chapter 3 provided compelling evidence that the efficiency of Queensland merged councils was lower than their unmerged peers over the period under review.

IPART (2015, p.32) acknowledged that mergers of NSW councils will *reduce* efficiency when it stated that 'some discretion will apply to Merger Proposal councils in the short term as this measure may be affected by the transition to new arrangements that may require additional spending to achieve future efficiencies'. The obvious question raised by this statement is how long should local residents wait to see an improvement in efficiency subsequent to a merger? The rather convenient answer for the NSW Government is that residents should wait for at least five years, placing expected improvement into the period *after* the next state election! However, empirical evidence by Drew, Kortt and Dollery (2015b) suggests that residents will never see any improvement in efficiency arising from the proposed amalgamations.

According to IPART's (2015) methodology, different types of councils are held to different standards of 'fitness'. In particular, rural councils are held to a lower standard of 'fitness for the future' than their metropolitan cousins. For instance, IPART (2015, p.8) has extended the time horizon for the Operating Performance Ratio by 5 years for rural councils and even then

rural councils are only required to 'plan to meet' the benchmark. Moreover, on the critical matter of scale, rural councils will be assessed as having met the criterion where 'the council's clearly demonstrates the strategies to enhance its capacity to a more sustainable level' (IPART 2015, p.25). Simultaneously, IPART (2015) provide 'flexibility' for merged councils on Capital Sustainability and note that improvement in efficiency of merged councils 'may not be practical' in the short term. It is thus puzzling that IPART (2015) repeatedly claims that it will assess council's *Fit for the Future* proposals in a 'consistent' manner! This may well suggest political imperatives at play to ensure the continued political support of the National Party for the NSW Government. Politics aside, this raises the question as to why residents of metropolitan councils deserve a higher standard of municipal 'fitness' than the residents of rural councils.

At the technical level, serious questions have been raised as to whether the rural/urban distinction has any meaning in terms of environmental constraint in local government. In this regard, Drew and Dollery (2015c) note that empirically robust methods for categorising councils combine nominally urban and rural councils when forming homogenous groups. This indicates that the distinction between rural and urban councils has little public policy meaning. The OLG (2014) has sought to list a number 'rural council characteristics' as if a clear distinction can be made, or indeed can be meaningful. However, this list lacks quantitative measures and many nominally urban municipalities equally fit a number of the criteria. We list the rural characteristics in Table 11.3 below, along with some of the decidedly odd implications which flow from the application of these criteria:

Table 11.3 Characteristics of Rural Councils

Characteristic	Implication
Small and static or declining population spread over a large area	What is a large area? Does a council cease to be rural simply because it's population has grown marginally (assuming of course that the population estimates are reliable)
Local economies that are based on agricultural or resource industries.	How exactly does one conceive 'based'. In terms of geographical area dominated by the select industries, or by the proportion of people employed directly or indirectly in the industry?
High operating costs associated with a diverse population and limited opportunities for return on investment?	Once again, the criteria lack quantitative measures. For instance Penrith is almost seven times less dense than Manly, yet few would categorise Penrith as rural (we assume 'diverse' is meant to refer to density rather than ethnic or religious diversity)! How is return on investment conceived – in terms of community satisfaction, projected savings or actual ROI? If the latter this raises the thorny question as to whether municipalities should be producing private goods (such as child care).
High importance of retaining local identity, social capital and capacity for service delivery	Firstly, many urban councils have made the argument that amalgamation will destroy local identity and social capital (see, for instance, Holroyd). Secondly, the OLG and Sansom (2015) have argued that amalgamation is necessary to *increase* capacity – so how can *retaining* capacity also be used as an argument by IPART and the OLG for not merging rural councils?
Low rate base and high grant reliance	As Abelson and Joyeux (2015) have argued this is an erroneous measure of financial sustainability because councils have had their rate revenue pegged for well over three decades! Moreover, the OLG has recently conceded that grant allocations have not been made according to the horizontal equalisation principals enshrined in federal legislation (see also Drew and Dollery 2014a). Therefore, how can this be regarded as a valid criteria for deciding whether a council is rural or not? Moreover, the logic flaws contained in the indicator apply equally to urban councils.
Difficulty in attracting and retaining skilled and experienced staff	Firstly, this presumes that rural councils do in fact have difficulty with staffing (despite there being no empirical data to support the claim). Secondly, if this is to be taken as an indicator that a council is rural it implicitly assumes that urban councils do not face difficulty with staffing – once again, a claim made in the absence of empirical evidence.
Challenges in financial sustainability and provision of adequate services and infrastructure.	This is a rather curious criteria for determining whether a council is rural or not given that the ILGRP (2013), OLG (2014) and Minister Toole have been loudly proclaiming that the entire NSW municipal sector is facing a financial sustainability and infrastructure crisis! If, as implied by this statement, the government believes that the challenges apply only to rural councils then there is clearly no longer a case for urban amalgamation!
Long distance to major (or sub) regional centre	Once again this criterion suffers from a lack of detail. How does IPART/OLG conceive 'long' – in terms of kilometres or travelling time? The criterion also exhibits a circuitous argument given that it is first necessary to identify non-rural councils before rural councils can be definitively recognised.
Limited opportunities for mergers	Yet another criterion which applies equally to rural and urban councils and lacks sufficient detail for judgements to be made. All councils in NSW have neighbours and therefore all councils in NSW have more or less equal opportunities for merger. Moreover, if the criterion is conceived in terms of willing partners, or merger partners which would enhance sustainability, then all urban *and* rural councils face limited opportunities.

Forecasts of performance are problematic. Both the 'council improvement' and 'Rural Council' templates require councils to make specific forecasts of performance for each of the subsequent four years. In addition, IPART (2015, p.34) makes the following rather odd request of all councils:

> We consider councils should provide as much relevant information or data as is required to support the proposals. Therefore, we consider it would be helpful if a longer time series of data to include 2014-15 and 2015-16 is provided by all councils lodging proposals (no matter the type of the proposal). We consider that the additional two years of data would provide us with a better picture of the trend in council performance relative to the benchmarks. *The additional two years of data should be available from councils' annual reporting requirements and could be provided without imposing an unreasonable burden* (emphasis added).

We agree that a longer time series may assist with assessment of some ratios, assuming that data distortions could be corrected. However, it appears that either IPART is not aware that 2014/15 and 2015/16 reports cannot exist at present or it has inordinate faith in the budgeting forecasting ability of councils. Moreover, as we have seen, the *Fit for the Future* templates imply a touching faith in forecasting and budgeting practice accuracy. It further implies an empirically testable claim that budget data in NSW municipalities contains a relatively low degree of error.

Table 11.3 details the accuracy of budget projections made by councils in both the 2013 and 2014 financial statements. What is immediately clear is that the average council (i.e. median result) has an absolute budget error of around 8% of actual revenue. Furthermore, there is evidence of a wide variation from the average. For instance, 25% of councils had errors in excess of 16% in 2013 and one council missed the mark by 60%! It should be noted that many of the ratios employed by IPART (2015) are extremely sensitive to variation (particularly the 'efficiency' ratio). Moreover, it should be borne in mind that these errors are for forecasts which are made *only one year in advance*. It is thus not unreasonable to suggest that the accuracy of forecasts made two years in advance (to provide IPART with its requisite longer time series), or four years in advance (for the *Fit for the Future* templates) will have errors so large as to make the forecasts effectively worthless. Moreover, according to 'Goodhart's Law', 'any observed statistical regularity will tend to collapse once pressure is placed on it for control purposes' (Bevan and Hood, 2006, p.521). This means that forecasts made in the current atmosphere of 'target terror' (Coulsen 2009) will be extremely unreliable. If IPART does require a longer time series of data, then the sensible approach would be to use data from earlier periods (i.e. the 2011 and 2010 financial years) for most ratios.

Table 11.2: Accuracy of NSW Municipal Budget Projections (Deviance of Actual Result to Budgeted Item)*

Budget Item	Smallest	Largest	Quartile 1	Median	Quartile 3
Entire State 2013					
Operating Revenue Budget Error	-29.903	68.282	3.768	9.958	18.353
Operating Expenditure Budget Error	-24.513	60.798	-1.873	2.059	7.927
Operating Result Budget Error*	0.006	60.017	3.646	7.487	16.029
Entire State 2014					
Operating Revenue Budget Error	-32.337	40.563	-0.890	4.931	11.414
Operating Expenditure Budget Error	-31.788	41.738	-3.341	0.799	6.096
Operating Result Budget Error*	0.105	76.412	4.003	8.273	13.862

* This budget error is expressed as a percentage of actual revenue and is reported in absolute terms.

The ILGRP ‘preferred options’ -now referred in IPART (2015, p.15) as ‘merger recommendations’ - were based in large part on the Department of Infrastructure (2013) report *NSW in the Future: Preliminary 2013 Population Projections* (ILGRP 2013). This raises an important question as to whether it is wise to base decision-making on *preliminary* forecasts made 18 years into the future, especially given the low rate of accuracy inherent in ABS population estimates for inter-censal base years.

Unfortunately, very little work has been done in assessing the accuracy of local government area (LGA) forecasts. An exception to this is Wilson and Rowe (2011) who examined Queensland LGA forecasts. They found a mean absolute percentage error for three separate 15 year forecasts of Queensland’s entire set of LGA’s in the order of 14.6%, suggesting that it is not wise to place too much confidence in long-term population forecasts. It follows that the basis for the ILGRP’s (2013) deliberations on NSW metropolitan councils is not sound. It is thus concerning that the Panel’s ‘preferred options’ are now being cast as ‘merger recommendations’ by IPART (2015, p.15). Moreover, it is entirely likely that the ILGRP ‘preferred options’ and subsequent OLG and IPART endorsements of the preferred options as ‘merger recommendations’ have been made on the incorrect functional unit for municipal goods and service production.

Drew and Dollery (2014d) have established that household and business data is more reliable, less volatile and more relevant than population data. This follows from the fact that the preponderance of municipal functions focus on ‘services to property’ rather than ‘services to people’. Moreover, use of a population measure of scale and capacity implies that business entities do not contribute to revenue or place demands on local services! The neglect of

business – particularly for regional centres – also means that spill-over effects are not being adequately considered. In addition, population is negatively correlated with the length of council-maintained roads (since the Pearson correlation coefficient equals -0.2659). The use of population data thus not only ignores the single largest expenditure function of NSW municipal government (PriceWaterhouseCoopers, 2006), but actively discriminates against councils with a large road infrastructure. Finally, it is the number of households and employing businesses that a council has control over (through development applications and economic development efforts) and not organic population growth.

Even if we were to concede that population was the appropriate functional unit for NSW local government policy purposes, there is still the inconvenient fact that neither TCorp (20913), the ILGRP (2013a; 2013b), the OLG (2014) nor IPART (2015) have provided any evidence to suggest that there is an association between population size and the various measures of municipal sustainability which have been employed to date.

As we have seen in Chapter 6 of this Report, panel regression of the 2009/2011 TCorp financial sustainability ratios only indicates associations for population size for non-Sydney councils (and then only for two of the ten ratios examined). There is in fact no evidence of an association between population size and financial sustainability for Greater Sydney councils when a time series analysis is conducted. Thus, this is further evidence against the ideologically imposed scale criteria.

Drew and Dollery (2015d) have also empirically demonstrated that there is no association between population size and municipal expenditure. Hence, it has now been empirically demonstrated that the assumption of economies of scale pervading the Panel's (2013a;

2013b) reports are completely illusory. This recent empirical evidence is consistent with the earlier work of Drew, Kortt and Dollery (2014c) which was available to the Panel at the time that it prepared its final report).

According to IPART (2015), its sustainability criteria include the operating performance, Own Source revenue and building and infrastructure renewal ratios, which are set out in Table 6.1 of this Report. Two of these ratios are heavily dependent on data which is still the subject of 'unfinished business', whilst the integrity of the data relating to the third ratio is under serious question. It is important to note these deficiencies given IPART's (2015, p.29) assertion that it will 'consider that ensuring councils are financially sustainable, and being able to show this will occur into the future, is fundamental to demonstrating a council is FFTF'.

Yet future revenue flows from both rates and FAGs cannot be predicted with any degree of confidence given that the outcomes from the proposed review of rating practice and changes to ensure FAGs are distributed to councils with the greatest need are still to be completed. As Abelson and Joyeux (2015) note, it is not reasonable to hold councils accountable for revenue streams for which they have very little control. Local government residential taxation effort[31] lacks inter-municipal equity and has constrained an important stream of own-source revenue as noted by the ILGRP (2013) and illustrated in Table 7.2 in this Report. In fact, residential taxation effort ranged from 0.209% through to 2.497% with a mean of 0.998%. Thus the long-standing rate-capping regime has constrained the local tax revenue of some councils to just one tenth of their peers. This suggests that if rate-capping is removed – a likely outcome

[31] Residential taxation effort is defined as the proportion of residential rates levied by a municipality expressed as a percentage of total annual incomes accruing to residents residing in the council boundary and is the preferred measure of municipal fiscal burden in the literature – see, for instance Ladd and Yinger 1989.

of the NSW Government's review – then the Operating Performance and own-source ratios of some councils might be altered quite significantly.

It also seems unreasonable to suggest that FAG revenues 'provide a stable income for rural councils' (IPART, 2015, p.29) but not urban municipalities. FAGs will not be a stable source of revenue for *any* NSW council owing to (a) the 'unfinished business' relating to more equitable allocations and (b) the fact that the Commonwealth Government has frozen FAGs for a period of three years, which means FAGs will be reduced in real terms for each of the subsequent three years. Moreover, there is no certainty that the Commonwealth Government will not attempt to extend the freeze or make further cuts to FAGs given the pressures on the Commonwealth's budget. In addition, the reasoning behind the Own Source ratio seems to be that 'a council's ability to raise its own revenue insulates it from a fall in revenue from sources that are outside its control' (IPART, 2015, p.29). .Thus for IPART (2015, p.29) to argue that rural councils can rely on an external source of income seems to contradict the entire purpose of the ratio.

Finally 'sustainability' ratios also present significant problems for IPART if it is to assess councils with 'consistency, fairness and impartiality' (IPART, 2015, p.43). This is largely because the data relied on for the ratio has been the subject of 'earnings management' and it is thus not reliable (Pilcher and Van der Zahn 2010; Drew and Dollery 2015a). In addition, climatic factors and natural disasters may affect the ratio, thus requiring very careful analysis given little comparability across the sector. It is also clear that municipal efforts to address this ratio will have negative implications for the Operating Performance ratio which presents a rather difficult problem for councils seeking to demonstrate future fitness.

As we have seen earlier in Chapter 11, the ratios employed to assess Infrastructure and Delivery of Services are subject to enormous levels of data distortion. It is thus hard to imagine that any methodology could be used to assess these criteria with 'consistency, impartiality and fairness' (IPART 2015, p.3). Of greatest concern is the Infrastructure and Backlog ratio which was compiled according to just a single year of data well after it had become known that the data would be used as an important ratio for the assessment of 'future fitness'. Moreover, the data is unaudited (as is the data for the Asset Maintenance ratio) and thus it cannot be claimed that there is any basis for reasonable assurance.

It is hardly surprising that auditors have deliberately excluded Special Schedule 7 from their opinions in the past given that it relies on completely subjective assessments. For instance, the following definitions are employed to determine what a 'satisfactory standard' and what is 'required maintenance': 'Satisfactory refers to estimated cost to bring asses to a satisfactory condition as deemed by Council. Required Maintenance is what should be spent to maintain assets in a satisfactory standard'.

The definition falls far short of Bird et al. (2005) requirement for a competent performance management program and invites 'reactive gaming' owing to the fact that (a) it does not commit the council to any particular future action, (b) it is defensible given that it is based on professional judgement, (c) it does not require a 'real' transaction with second parties (Copeland, 1968, p.102). Moreover, the breadth of municipal infrastructure, along with the detailed engineering knowledge required to assess maintenance needs, suggests that it would be extremely difficult for an audit team to provide reasonable assurance on the Schedule 7

items. Without some sense of assurance of accuracy in the data, the two ratios which depend upon it are worthless.

In addition, the Asset Maintenance Ratio is subject to an obvious flaw in logic. To achieve benchmark status a council must demonstrate that it is spending more on asset maintenance than what is required! We have already noted this problem earlier, along with the unconvincing attempt by IPART to try to justify it. If IPART (2015) is successful in extending the *Fit for the Future* assessments to include an additional two years of data (taking this ratio up to five years of data), then the unsatisfactory nature of the benchmark will be further highlighted. Perpetual reporting of the Asset Maintenance Ratio against the existing benchmark clearly would not make any sense.

The Debt Service Ratio is problematic. It should be noted that the OLG (2014) disregarded NSW Treasury Corporation advice on the definition of this ratio and thereby eroded the ratio's utility. It no longer measures the ability to service debt as indicated by its formal name, but rather measures the proportion of revenue that a council devotes to principal and interest repayments.

This is most unsatisfactory for several reasons. Firstly, this discourages councils from reducing interest expenditure through high principal repayments even though councils are being directed by the 'efficiency' ratio to reduce expenditure. Secondly, the ratio in its current form actively insists that councils not currently in debt take on debt! However, this lower bound benchmark for the ratio (0.0%) encourages some rather perverse behaviour for councils which currently have no debt. For instance, a council with no debt may become 'fit for the future' by taking out a loan large enough to be recognised in the financial statements

and either (a) make interest only repayments and take no action to employ the capital for productive purposes or (b) repay the loan the next week!

The reasoning employed by the OLG (2014) for requiring councils which have no need for debt to take on debt is that councils should 'use debt wisely to share the life-long cost of assets and avoid excessive rate increases' (IPART, 2015, p.31). However, as we have demonstrated, councils can meet the benchmark without using debt according to the IPART (2015) prescription.

Moreover, if the object is to use debt with the aim of intergenerational equity on long-lived assets then this presents a number of problems. Firstly, requiring councils to share intergenerational costs henceforth imposes inequities on previous generations which paid for assets which continue to have a useful life beyond this point in time. Secondly, it assumes that debt will be used for capital projects rather than operational expenditure without any assurance that this will be the case. Third, the OLG/IPART objective assumes that the life of the asset will be closely correlated with the term of the debt without any reason to suppose this will be the case!

There are a number of other problems which plague the OLG/IPART 'efficiency' ratio (which does not measure efficiency). These problems include the population data employed in the calculations, the method used to deflate data and the method used to assess the direction of expenditure trend. With respect to the population data, the OLG (2014) have introduced significant and avoidable error by using 2013 *projected* population estimates. Firstly, as we have seen earlier, population data in inter-censal periods already have significant error associated with them and this error typically increases with temporal

distance from the last census (2011). Secondly, the projected population estimates were never meant to be anything other than a guide and were clearly labelled 'preliminary figure[s] or series subject to revision' (ABS, 2015). Thirdly, the figures have in fact been revised and many of the revisions are quite significant. Given the high leverage of 'efficiency' data points even a very small error could result in a completely different assessment on this criterion.

The OLG/IPART 'efficiency' ratio is also deficient as a result of the method used to deflate the nominal expenditure data. Firstly, it is not acceptable to use two entirely different indexes to deflate continuous data. Secondly, use of annualise growth in calculations imputes and compounds rounding error (given the sensitivity of the empirical method erroneously used to calculate the trend in expenditure per capita even relatively small errors could result in the wrong conclusions being drawn from the data). Thirdly, it was entirely unnecessary to deflate the 2010 financial year data and this decision simply introduced avoidable rounding error. The final – and fatal – problem associated with the OLG/IPART efficiency measure is the empirical method chosen to establish the direction of expenditure/capita trend. The OLG toolkit employs linear regression to establish whether expenditure per capita is rising or falling. Unfortunately, the use of linear regression to establish the direction of the trend is completely flawed owing to the fact that it breaks the key assumption of linear regression that the data association has a linear functional form!

11.4 Conclusion

As we have seen in Chapter 11, the surprise publication of IPART's (2015) *Methodology for Assessment of Council Fit for the Future Proposals* on 27 April 2015 added a further twist to an already convoluted local government reform process in NSW. Not only will IPART now replace the Panel of Experts promised in the OLG's (2014) *Fit for the Future* documentation

as the assessor of council submissions due on 30 June 2015, but *Methodology for Assessment of Council Fit for the Future Proposals* also introduces significant changes to the basis of the assessment process. The most important change resides in the differentiation between 'non-rural', 'rural' and 'merged' councils in IPART (2015) and the 'one size fits all' approach in *Fit for the Future.* In addition, the benchmarks which must be met diverge widely between IPART (2015) and *Fit for the Future.* In Chapter 11 we have demonstrated that not only due these changes fail to address the difficulties in the *Fit for the Future* performance criteria and benchmarks, but they also contain additional flaws.

Apart from the procedural inequities inherent in 'changing the rules of the game' towards the end of the reform process, local councils now have only two months to assess their performance under the new IPART (2015) benchmarks. It goes without saying that this is a chaotic way of conducting public policymaking. It also means that councils which have cooperated fully with the *Fit for the Future* process, undergone self-assessment using the requisite OLG (2014) templates, and engaged in extensive and *bona fide* community consultation, such as Hunters Hill, Lane Cove and Ryde, now find that all their efforts have been largely in vain.

CHAPTER 12: CONCLUSION

12.1 Introduction

This Report has considered in detail the proposed merger of Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby local authorities, which had been recommended by the Panel in both its *Future Directions* and *Revitalising Local Government* reports, under the NSW Government's *Fit for the Future* program. Chapter 12 seeks to provide a brief summary of the major findings of the Report, together its chief recommendations.

Chapter 12 is divided into two main parts. Section 12.2 outlines the key findings of the Report whereas section 12.3 briefly considers its major policy implications.

12.2 Major Findings of the Report

The Report comprised a short introductory Chapter 1, followed by ten substantive chapters, each examining a different dimension of the recommended municipal mergers affecting the Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby local councils.

Chapter 2 considered the available empirical evidence on municipal mergers in local government against the historical background that Australian local government policymakers have traditionally relied heavily on council amalgamation as an instrument of reform. Chapter 2 demonstrated that the weight of both the Australian and international scholarly literature was decidedly sceptical of the ability of compulsory consolidation to improve council performance. Indeed, the empirical literature is awash with evidence that municipal

mergers are expensive and frequently counterproductive in terms of improving the operational performance of local authorities. Section 2.4 of Chapter 2 considered the effects of these structural changes on the financial viability of local government through the prism of a series of Australian state-based and national public inquiries into financial sustainability in local government. Given the popularity of forced amalgamation in the Australian milieu, the most interesting feature of the deliberations of these inquiries resides in the fact that they echo scepticism in the academic literature on compulsory council consolidation. Indeed, the weight of opinion in the public inquiries contends that the traditional Australian stress on council mergers has been seriously misplaced. For example, in NSW the Allan Report (2006) found that population density – and not population size – represented a pivotal component of council cost structures. It recommended that policy instruments other than amalgamation should be employed, notably shared service arrangements.

Chapter 3 of this Report provided detailed empirical analyses of two recent Australian forced amalgamation episodes: The 2004 NSW compulsory council consolidation program and the 2008 Queensland forced amalgamation program. The analysis of the NSW council mergers considered ten general-purpose councils which were subject to amalgamation over the period from 2000 to 2004. Chapter 3 compared the performance of this cohort of general purpose amalgamated entities against (a) all councils in NSW and (b) a group of peer councils selected according to the NSW Office of Local Government classification system using the TCorp (2013) Financial Sustainability Rating (FSR) employed in the *Fit for the Future* program. This comparison yielded no significant statistical differences in performance between merged and unmerged councils demonstrating that, despite all the expense and disruption, the 2000/04 mergers made no material difference to council performance on the *Fit for the Future* criteria. Chapter 3 also examined the 2008 Queensland amalgamations

which involved a reduction in the number of councils from 157 to just 73. Drew, Kortt and Dollery (2015) conducted an econometric analysis and concluded that the mergers had resulted in a greater proportion of councils exhibiting diseconomies of scale arising from amalgamations, which created entities which were simply too large to be run efficiently. Chapter 3 employed a DEA analysis to examine scale and found that – of the 31 entities created by the Queensland mergers – over 58% exhibited decreasing returns to scale. This result is consistent with the evidence provided by Drew, Kortt and Dollery (2015), but is a more compelling result since it is based on multiple outputs. Finally, Chapter 3 compared the efficiency of non-amalgamated with amalgamated Queensland councils through time. It found that the latter group performed worse than the non-amalgamated councils providing clear evidence that the mergers had resulted in typically less efficient councils in Queensland!

Chapter 4 provided a critical assessment of the *Fit for the Future* process. It found that the criteria for evaluating councils had been derived from an arbitrary and often illogical selection of financial sustainability ratios (FSRs) and the associated benchmark values. Moreover, Chapter 3 exposed severe problems with 'scale and capacity' approach in *Fit for the Future*. Section 4.4 laid bare the deleterious effects that the use of unreliable data for sustainability assessments had had. Finally, section 4.5 demonstrated that the OLG had employed an erroneous approach to the assessment of efficiency in local government which has had serious adverse consequences for its assessment of operational efficiency.

Chapter 5 empirically investigated the proposed council mergers associated with the North Shore group of councils from several different perspectives. It found numerous problems, including (a) the difficulties posed the existence of significant current disparities in rates, fees and charges, and capacities to pay across the six councils which were ignored in the OLG

merger recommendations; (b) the many tough decisions which would have to be made regarding changes in democratic representation post-merger; (c) the total liabilities likely to be inherited by any proposed new amalgamated municipality and its impact on local residents; (d) the complications derived from the dismemberment of the City of Ryde into two parts; (e) Commonwealth financial assistance grants post-merger; (f) the need for full information disclosure to local residents; and most importantly (g) almost all of the North Shore group of councils would be less financially sustainable under the *Fit for the Future* criteria than they had been pre-merger. Chapter 5 argued that it is dismaying that neither the Independent Panel nor the OLG had even considered most of these problems, never mind offered sound solutions.

Chapter 6 conducted an empirical analysis of the likely outcomes arising from amalgamation according to the two main econometric methods employed in the empirical literature on local government: multiple regression analysis and data envelopment analysis (DEA). The results of the multiple regression analysis showed that the Panel's (2013) unsubstantiated assertions of economies of scale – based on population size – are completely illusory. Moreover, the DEA analysis (using the number of households, number of businesses and road length) demonstrated that the vast majority of proposed amalgamations would yield over-scaled councils too large to efficiently provide local services. Finally, the DEA in Chapter 6 of the efficiency and scale implications arising from the recommended merger of the North Shore councils showed that it would reduce the efficiency of these local authorities should the merger proceed. In sum, the empirical analysis in Chapter 6 showed that there is no empirical justification for the proposed merger of the Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby local councils.

Chapter 7 examined the socio-economics of the Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby councils. This descriptive analysis, which was based on data compiled by the Population Health Information Development Unit at the University of Adelaide, identified some stark difference between some of these local authorities and thereby proving that no common 'community of interest' exists.

Chapter 8 summarised the key literature from Australia and abroad on shared services arrangements in local government. In summary, this literature provides strong evidence that shared services can yield substantial benefits to local government, although not all local government services are suitable to shared service provision.

Chapter 9 used the literature review on shared services in Chapter 8 to consider council collaboration as the main structural alternative to forced mergers. Section 9.2 demonstrated that sound analytical foundations exist for separating service provision from service production in contemporary local government, with numerous alternative modes of delivering local services, including inter-council collaboration. However, work by Allan (2001; 2003), the NSW LGI (2006) and others demonstrated that only some local services are open to joint provision. Section 9.3 examined the Hunter Council model as the most successful operational example of inter-council collaboration in NSW. It was argued that the Hunter Council model should be taken as a template for the design of a north Sydney regional body. Section 9.4 evaluated the draft Northern Sydney Council Collaboration Model which had been drawn up after discussions between the NSROC and SHOROC groups of councils, arguing that it represented a close approximation of the Hunter Council model and was thus a suitable regional collaborative model. Finally, section 9.5 provided a survey instrument which could

be used by a Northern Sydney Council Collaboration Model Board to determine promising avenues for inter-collaboration and plan further initiatives.

Chapter 10 considered the question of community engagement by local councils with their local communities on alternatives under the *Fit for the Future* process. Both the *Fit for the Future* process and the later IPART (2015) *Methodology for Assessment of Council Fit for the Future Proposals* require local authorities to consult widely with their local communities. In addition, IPART explicitly noted that it would formally evaluate community consultation by local authorities as part of its overall assessment of council submissions under the *Fit for the Future* process. Furthermore, IPART set out its approach to evaluate community consultation. Chapter 10 examined the IPART methodology for assessing community consultation, considered the extensive community consultation undertaken by Lane Cove, Hunters Hill and Ryde councils, and found that they had all easily met the IPART criteria for community consultation.

Chapter 11 provided a detailed evaluation of the IPART (2015) *Methodology for Assessment of Council Fit for the Future Proposals* approach. It compared the *Methodology for Assessment of Council Fit for the Future Proposals* evaluative criteria and performance benchmarks against the criteria originally developed by TCorp (2013) and modified in *Fit for the* Future and found that significant differences had emerged. Furthermore, Chapter 11 considered the numerous problems inherent in the *Fit for the Future* criteria identified in Chapter 4 of the Report and found that the IPART (2015) *Methodology for Assessment of Council Fit for the Future Proposals* assessment technique had failed to remedy these problems. In addition, Chapter 11 found that severe problems existed with the following elements in the IPART evaluation approach: its methodology for the assessment of scale, its

methodology for the assessment of sustainability, its methodology for infrastructure and delivering services assessment, and its assessment methodology for efficiency.

12.3 Major Policy Implications of the Report

The analysis performed in this Report has eight major policy implications for local government policymakers.

(a) The weight of empirical evidence on municipal mergers in the scholarly literature and the Australian national and state public inquiries into local government falls overwhelmingly against forced amalgamation. This body of evidence holds that shared services and other forms of council collaboration provide a superior method of securing the advantages of greater scale.

(b) Comprehensive empirical analysis of the 2000/2004 NSW compulsory council consolidation program in the Report demonstrated that there is no statistical difference in the performance of merged and unmerged councils under the *Fit for the Future* criteria. Similarly, a detailed investigation of the outcomes of the 2008 Queensland forced amalgamation program demonstrated that a majority of amalgamated councils now operated with diseconomies of scale. These two analyses thus provide convincing empirical case against proceeding with a further round of municipal mergers in NSW in 2015.

(c) Detailed critical assessment of the *Fit for the Future* process found it severely flawed in numerous respects, not least its arbitrary use of financial sustainability ratios (FSRs) and associated benchmark values, significant problems with its ‘scale and capacity’ approach, problems with unreliable data employed in sustainability assessments, and an incorrect

measure employed to assess the operational efficiency of councils. This provides a powerful argument for the NSW Office of Local Government to halt the *Fit for the Future* process and deal with these problems before proceeding.

(d) IPART's (2015) *Methodology for Assessment of Council Fit for the Future Proposals* – only released on 27 April 2015 – add a further twist to a convoluted reform process. IPART will replace the Panel of Experts promised in *Fit for the Future* as the assessor of council submissions and its new assessment methodology introduces significant changes to the process. In particular, 'non-rural', 'rural' and 'merged' councils in IPART (2015) replace the 'one size fits all' approach in *Fit for the Future.* Performance benchmarks also now diverge widely between IPART (2015) and *Fit for the Future.* However, the Report demonstrates that the IPART approach is badly flawed and does not correct the problems identified in *Fit for the Future*.

(e) By 'changing the rules of the game' IPART has rendered much hard work already done by local councils obsolete. Thus Hunters Hill, Lane Cove and Ryde, which have cooperated fully with the *Fit for the Future* process, undergone self-assessment using the requisite OLG (2014) templates, and engaged in extensive and *bona fide* community consultation, now find that much of this effort has in vain.

(f) A comprehensive empirically investigation the proposed Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby council mergers found numerous problems, including the challenges posed by significant current disparities in rates, fees and charges, and capacities to pay across the six councils, problems determining democratic representation

post-merger, the burden of the total liabilities inherited by a newly merged council, complications derived from the dismemberment of the City of Ryde, Commonwealth financial assistance grants post-merger, a lack of full information disclosure to local residents, and the critical fact that almost all of the North Shore group of councils would be less financially sustainable under the *Fit for the Future* criteria than they had been pre-merger. This underlines the foolishness of proceeding with the proposed merger.

(g) The Report conducted two modelling exercises to investigate the outcomes of the proposed mergers. The results of the multiple regression analysis showed that the Panel's (2013) claims about scale economies proved false. The DEA analysis also demonstrated that the vast majority of proposed amalgamations would yield over-scaled councils too large to efficiently provide local services. Taken together, these empirical analyses show conclusively that there is no empirical justification for the proposed merger of the Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby councils.

(h) The Report presented a detailed analysis of the socio-economic characteristics of the Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby councils. This demonstrated stark differences between some of these local authorities thereby proving that no common 'community of interest' existed.

(i) A detailed review of the literature on shared services in local government was undertaken in the Report which found strong evidence that shared services could yield significant benefits. However, not all local services are amenable to regional provision through shared service arrangements.

(j) The Report found that shared services represent a superior alternative to forced amalgamation to improve the performance of the Hunters Hill, Lane Cove, Mosman, North Sydney, Ryde and Willoughby councils. It investigated the best methods of delivering shared services and established that the Hunter Councils model represented an optimal approach. The draft Northern Sydney Council Collaboration Model - drawn up by the NSROC and SHOROC groups of councils - was based on the Hunter Councils model and it provided a sound institutional basis for council collaboration amongst the North Shore group. The Report presented an instrument which the Board of the proposed Northern Sydney Council Collaboration Model could use to determine which local services to provide collaboratively and which to retain 'in-house'.

(k) The Report thoroughly examined the community engagement programs conducted by Hunters Hill, Lane Cove and Ryde and found that they easily met the community engagement assessment criteria stipulated by IPART (2015) in its *Methodology for Assessment of Council Fit for the Future Proposals.*

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