BIGGER IS NOT ALWAYS BETTER: AN EVALUATION OF “FUTURE PROSPERITY OF THE HAWKES BAY REGION” AND “POTENTIAL COSTS AND SAVINGS OF LOCAL GOVERNMENT REFORM IN HAWKES BAY”

3 December 2013
CONTACTS:

Professor Brian Dollery  
Telephone: 61 2 6773 2500  
Email: bdollery@une.edu.au

Mr Wayne Jack  
Chief Executive  
Napier City Council  
Telephone: 06 834 4159  
Email: waynej@napier.govt.nz

Disclaimer
This Report was prepared by Brian Dollery and Michael Kortt on behalf of New England Education and Research Proprietary Limited for the Napier City Council. This Report was produced for the Napier City Council as a strictly independent Report. The opinions expressed in the Report are thus exclusively the views of its authors and do not necessarily coincide with the views of the Napier City Council or any other body. The information provided in this Report may be reproduced in whole or in part for media review, quotation in literature, or non-commercial purposes, subject to the inclusion of acknowledgement of the source and provided no commercial use or sale of the material occurs.
# TABLE OF CONTENTS

EXECUTIVE SUMMARY ......................................................................................................................... vi

CHAPTER 1: INTRODUCTION .................................................................................................................. 14
  1.1 BACKGROUND ............................................................................................................................... 14
  1.2 OUTLINE OF REPORT ..................................................................................................................... 16

CHAPTER 2: ANALYSIS OF FUTURE PROSPERITY OF THE HAWKES BAY REGION (PART 1: ISSUES AND OPTIONS) .............................................................................................................. 22
  2.1 INTRODUCTION ............................................................................................................................. 22
  2.2 SYNOPSIS REVIEW OF FUTURE PROSPERITY OF THE HAWKES BAY REGION ..................... 22
  2.3 IMPROVING LOCAL GOVERNMENT PERFORMANCE IN THE HAWKES BAY REGION .......... 27
    2.3.1 Shared Services .......................................................................................................................... 30
    2.3.2 More Effective Collaboration and a Hawkes Bay Plan ............................................................. 36
    2.3.3 Key Investments ....................................................................................................................... 37
    2.3.4 Increased Regional Role: Transfer of Responsibilities ............................................................ 38
    2.3.5 Rural Amalgamation ............................................................................................................... 40
    2.3.6 Regional Amalgamation .......................................................................................................... 42
  2.4 CONCLUDING COMMENTS ........................................................................................................... 47

CHAPTER 3: ANALYSIS OF POTENTIAL COSTS AND SAVINGS OF LOCAL GOVERNMENT REFORM IN HAWKES BAY ........................................................................................................... 48
  3.1 INTRODUCTION ............................................................................................................................. 48
  3.2 SYNOPSIS REVIEW OF POTENTIAL COSTS AND SAVINGS OF LOCAL GOVERNMENT REFORM ........................................................................................................................................... 50
  3.3 ASSESSMENT OF POTENTIAL COSTS AND SAVINGS OF LOCAL GOVERNMENT REFORM ........................................................................................................................................... 64
  3.4 ASSESSMENT OF ESTIMATED TRANSITION COSTS IN POTENTIAL COSTS AND SAVINGS ........................................................................................................................................... 66
  3.5 CONCLUDING REMARKS ................................................................................................................ 70

CHAPTER 4: CONCEPTUAL AND EMPIRICAL EVIDENCE ON AMALGAMATION ................................................................................................................................................................. 72
  4.1 INTRODUCTION ............................................................................................................................. 72
  4.2 LOCAL GOVERNMENT AMALGAMATION IN NEW ZEALAND AND AUSTRALIA ...................... 75
    4.2.1 New Zealand ............................................................................................................................ 75
    4.2.2 Australia .................................................................................................................................. 76
  4.3 EMPIRICAL EVIDENCE ON IMPACT OF AMALGAMATION .......................................................... 78
  4.4 ASSESSMENT OF AUSTRALIAN AMALGAMATION PROGRAMS .................................................. 81
    4.4.1 Hawker Inquiry (2003) ............................................................................................................. 82
    4.4.2. South Australian Financial Sustainability Review Board (FSRB) (2005) .............................. 84
    4.4.3 Financial Sustainability of NSW Local Government (‘Allan Report’) (2006) ....................... 85
    4.4.4 Queensland Size, Shape and Sustainability (SSS) Program (2006) ...................................... 86
    4.4.5 Western Australian Systematic Sustainability Study (2006) ............................................... 87
    4.4.7 Local Government Association of Tasmania (LGAT) (2007) ............................................... 88
    4.4.8 Queensland Local Government Reform Commission (2007) ............................................. 89
  4.5 CONCLUSION .................................................................................................................................. 90

CHAPTER 5: ECONOMETRIC ANALYSIS OF PROPOSED AMALGAMATIONS ................................................................................................................................................................... 93
  5.1 INTRODUCTION ............................................................................................................................. 93
  5.2 ECONOMIES OF SCALE IN LOCAL GOVERNMENT ...................................................................... 94
  5.3 DATA AND EMPIRICAL STRATEGY ............................................................................................... 96
    5.3.1 Dependent Variables ............................................................................................................... 97
    5.3.2 Independent Variables ............................................................................................................ 97
5.3.3 Empirical Strategy ................................................................. 98
5.4. DISCUSSION OF RESULTS .......................................................... 99
5.4.1 Summary Statistics ................................................................. 99
5.4.2 The relationship between per capita expenditure and population size ... 103
5.4.3 The relationship between per capita income and population size ...... 105
5.4.4 The relationship between per capita rates and population size .......... 106
5.4.6 Robustness Checks ............................................................... 109
5.5 CONCLUSION ........................................................................... 109
5.6 STATISTICAL APPENDIX ............................................................ 111

CHAPTER 6: GOVERNANCE AND ADMINISTRATION COSTS AND EFFICACY ........... 112
6.1 INTRODUCTION ........................................................................ 112
6.2 PROPOSED GOVERNANCE ARRANGEMENTS FOR THREE AMALGAMATION SCENARIOS .............................................................. 113
6.3 OPERATION OF LOCAL/COMMUNITY BOARDS IN NEW ZEALAND .............................................................. 115
6.4 EVALUATION OF COST ESTIMATES FOR COMMUNITY BOARDS ....................................................................................... 119
6.5 CONCLUSIONS ......................................................................... 122

CHAPTER 7: LOCAL GOVERNMENT COMMISSION REORGANISATION APPROACH .......... 123
7.1 BACKGROUND ......................................................................... 123
7.2 LOCAL GOVERNMENT BOARD AMALGAMATION PROCESS ................. 124
7.3 ASSESSMENT OF THE LOCAL GOVERNMENT BOARD NORTHLAND DRAFT PROPOSAL ................................................................. 130
7.3.1 Genesis of Draft Proposal .......................................................... 130
7.3.2 Nature of Draft Proposal ........................................................... 130
7.3.3 Efficiency Gains and Cost Savings ............................................... 136
7.3.4 Community Boards ................................................................ 141
7.4 CONCLUSION ........................................................................... 146

CHAPTER 8: CONCLUSIONS ................................................................... 148
8.1 INTRODUCTION ......................................................................... 148
8.2 SPECIFIC LIMITATIONS WITH FUTURE PROSPERITY OF THE HAWKE'S BAY REGION ............................................................ 148
8.3 SPECIFIC LIMITATIONS WITH POTENTIAL COSTS AND SAVINGS OF LOCAL GOVERNMENT REFORM IN HAWKE'S BAY .......... 149
8.4 OTHER LIMITATIONS ................................................................ 150
8.5 SPECIFIC LIMITATIONS WITH THE DRAFT PROPOSAL FOR REORGANISATION OF LOCAL GOVERNMENT IN NORTHLAND .............................................................. 152
8.6 CONCLUSIONS ........................................................................... 152

REFERENCES ................................................................................... 154
LIST OF TABLES

Table 2.1: Possible Initiatives for Hawkes Bay Region .............................................................. 24
Table 2.2: Characteristics of Local Government in Hawkes Bay Region .................................. 28
Table 3.1: Local council activities included in the financial model ........................................ 55
Table 3.2: Summary of Cost Estimates for Scenarios A, B and C ............................................. 63
Table 3.3: Amalgamation Queensland Council Estimates of Costs of Mergers ....................... 69
Table 4.1: Number of local councils in New Zealand, 1946 to 2012 ........................................ 76
Table 4.2: Number of local councils in Australia, 1910 to 2012 ............................................... 76
Table 4.3: An international comparison of average council size, 2007 ....................................... 78
Table 5.1: Summary Statistics for select New Zealand councils, 2003 to 2012 ....................... 100
Table 5.2: Effect of population size on council expenditure, 2003 to 2012 ............................. 103
Table 5.3: Effect of population size on council income, 2003 to 2012 ..................................... 105
Table 5.4: Effect of population size on rates, 2003 to 2012 ...................................................... 106
Table 5.5: Effect of population size on employee costs, 2003 to 2012 .................................... 108
Table 5.6: Robustness Check 1 – Inclusion of population squared term ................................. 111
Table 5.6: Robustness Check 2 -- Per capita expenditure in dollar terms and a quadratic in population .......... 111
Table 6.1: Estimated Governance and Management Cost for Scenarios A, B and C ............... 114
LIST OF FIGURES

Figure 3.1: Combined Local Authority Current Expenditure by Function, 2012/13 .................................................. 60

Figure 5.1: Summary Charts ................................................................................................................................. 101
EXECUTIVE SUMMARY

Bigger Is Not Always Better: An Evaluation of Future Prosperity of the Hawkes Bay Region and Potential Costs and Savings of Local Government Reform in Hawkes Bay examined the case for local government amalgamation in the Hawkes Bay Region as set out in the two related reports prepared by McGredy Winder & Co: (i) Future Prosperity of the Hawkes Bay Region and (ii) Potential Costs and Savings of Local Government Reform in Hawkes Bay. Bigger Is Not Always Better also considers the recently released Local Government Commission’s Draft Proposal for Reorganisation of Local Government in Northland given its striking resemblance to the dire recommendations in Future Prosperity of the Hawkes Bay Region. Together these reports proposed a single unity authority for their respective regions in the absence of any compelling empirical evidence that forced amalgamation would result in cost savings.

In essence, Future Prosperity of the Hawkes Bay Region provided a wide-ranging analysis of the various policy options which could be implemented to boost the economic prospects of the Hawkes Bay Region. It identified economic and other constraints on economic development in the Hawkes Bay Region and then examined 13 matters which could be addressed to enhance economic growth in the Hawkes Bay Region.

Chapter 2 of this Report provided an analysis of the Future Prosperity of the Hawkes Bay Region (Part 1: Issues and Options) which focused on option 9 ‘local government performance’ of the 13 alternative policy avenues.
With respect to local government, *Future Prosperity of the Hawkes Bay Region* advocated a radical amalgamation of Hawkes Bay Regional councils as a means of enhancing local government performance and fostering economic growth in the Hawkes Bay Region.

Chapter 2 found *Future Prosperity of the Hawkes Bay Region* seriously deficient in two main respects:

- *Future Prosperity of the Hawkes Bay Region* had ignored the voluminous literature on structural reform in local government, which includes a substantial body of thought on Australasian local government reform, including structural reform through council amalgamation. This neglect was most unfortunate since a wealth of material exists, which demonstrates that forced amalgamation seldom improves the performance of local authorities, especially in non-metropolitan areas.

- Shared services offer a promising alternative to compulsory consolidation, particularly in a regional context which should have been considered in detail in *Future Prosperity of the Hawkes Bay Region*.

- The authors of *Future Prosperity of the Hawkes Bay Region* should have been aware that effective regional leadership is best fostered through the establishment of regional development bodies rather than through bitterly divisive battles over forced amalgamation which typically results in the domination of regional areas by regional centres.

Chapter 3 of this Report provided an analysis of the *Potential Costs and Savings of Local Government Reform in Hawkes Bay* which offered estimates of cost savings attendant on
structural reform of local government within the Hawkes Bay Region through amalgamation. Its authors examined the cost implications of three specific models of council amalgamation:

- **Scenario A:** A single unitary authority as proposed by *A Better Hawkes Bay* to the Local Government Commission.
- **Scenario B:** A single territorial authority and the existing regional council.
- **Scenario C:** Two territorial authorities (a northern council including Napier City, Wairoa District and the part of Hastings District north of the Tutaekuri River, and a southern council comprising the balance of Hastings District and Central Hawkes Bay District and the existing regional council).

Using a host of assumptions, *Potential Costs and Savings of Local Government Reform in Hawkes Bay* employed financial modelling to determine potential costs and savings associated with these three scenarios and found that Scenario A generated the greatest cost savings.

Chapter 3 found that the cost savings estimates provided in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* were far from convincing. Four main problems were identified with the analysis:

- *Potential Costs and Savings of Local Government Reform in Hawkes Bay* entirely ignored claims made in *Future Prosperity of the Hawkes Bay Region* on the primacy of effective regional leadership as the main driver of regional development in the Hawkes Bay Region and made no attempt to provide empirical validation for this far-reaching claim.
• Potential Costs and Savings of Local Government Reform in Hawkes Bay nowhere sought external validation for the accuracy of its projected cost savings by examining previous amalgamation episodes in Australian and New Zealand local government and then comparing projected costs savings pre-amalgamation with actual realised cost savings post-amalgamation. Had this been done, Potential Costs and Savings of Local Government Reform in Hawkes Bay would have found that claims of cost savings and other pecuniary gains from amalgamation were almost never realised in practice.

• The robustness of the purported cost savings estimates in Potential Costs and Savings of Local Government Reform in Hawkes Bay cannot be assessed because its authors had failed to conduct a sensitivity analysis of their alternative cost savings scenarios. Thus policy makers have no estimate of either a ‘worst case’ or ‘best case’ scenario. The omission of a sensitivity analysis is a serious oversight given the inherent uncertainty surrounding the costs and benefits associated with local government consolidation.

• The cost savings presented in Potential Costs and Savings of Local Government Reform in Hawkes Bay are based on estimates of what would have happened in the absence of council amalgamations (‘base case’) which ignores cost savings which may have occurred without mergers. Thus the reported cost savings in Potential Costs and Savings of Local Government Reform in Hawkes Bay are based on a comparison of two uncertain forecast settings.

Chapter 4 considered the conceptual and empirical evidence on amalgamations in local government in order to assess the viability of the council amalgamation program proposed in
Chapter 4 found that the bulk of the scholarly literature had found that council amalgamation had not met its intended aims. Furthermore, the weight of opinion in a host of recent Australian national and state inquiries into the impact of amalgamation public inquiries agreed that the additional financial and emotional stress on council mergers has been seriously underestimated. Thus it was most unfortunate that the authors of *Future Prosperity of the Hawkes Bay Region and Potential Costs and Savings of Local Government Reform in Hawkes Bay* had entirely ignored the findings of this literature. In particular, these two reports had been remiss in neglecting the potential contribution of shared services to improving the performance of local government.

Chapter 5 conducted an econometric analysis to determine whether there is any statistically significant relationship between council population size and local government expenditure for Central Hawkes Bay District Council, Hastings District Council, Napier City Council, and Wairoa District Council. The econometric analysis reveals that there is no statistically significant relationship between council population size and per capita expenditure. Thus there is little, if any, reason to assume that the cost savings proclaimed in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* would be realised.

Chapter 6 considered the proposed governance arrangements for the Scenario A, Scenario B and Scenario C forced amalgamation models and demonstrated that *Potential Costs and Savings of Local Government Reform in Hawkes Bay* had taken a far too benign view of the
costs and efficacy of these arrangements, especially with respect to community boards. In particular, Chapter 6 found that:

- Despite extravagant claims in *Future Prosperity of the Hawkes Bay Region* on the crucial role of leadership in the development of Hawkes Bay Region, its authors had not consulted the relevant literature, especially on the operation of community boards. This was most unfortunate since the operation of community/local boards had been unsatisfactory. Indeed, Richardson (2008) had demonstrated that community/local boards were used less than when first established in 1989.

- The anticipated costs of community boards in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* had underestimated the real costs of establishing local boards in proposed amalgamated scenarios A, B and C. In particular, despite advocating Auckland-style community boards, no consideration was given to the costs of administrative personnel, office accommodation and the like.

Chapter 7 provides a critical evaluation of the new Local Government Commission (LGC) process. In particular, it examines the *Draft Proposal for Reorganisation of Local Government in Northland* prepared by the LGC as a salient and worrying example of how the revised process works. The *Draft Proposal for Reorganisation of Local Government in Northland* is important for local government reorganisation in the Hawke’s Bay Region because of its strong resemblance to the drastic recommendations in *Future Prosperity of the Hawkes Bay Region*: both propose a single unitary authority for their respective regions in place of existing functioning and financial viable district councils and regional councils.
Chapter 7 found that the Draft Proposal for Reorganisation of Local Government in Northland was badly flawed in several respects:

- Our appraisal of the Draft Proposal for Reorganisation of Local Government in Northland as a recent example of how the Commission approaches local government amalgamation revealed an almost entirely ‘evidence-free’ methodology on the part of the Commission. Given the pivotal importance of local government reorganisation and the need to prevent expensive and divisive errors, it is vital that proposed reorganisation proposals are based on extensive econometric modelling and the best available empirical evidence. This is unfortunately not the case with the Draft Proposal for Reorganisation of Local Government in Northland.

- This failing was especially concerning in the almost complete absence of any empirical or other justification for the extravagant claims in Draft Proposal for Reorganisation of Local Government in Northland centred on increased efficiency and cost savings from the proposed forced merger of Northland councils.

- The Commission’s recommendation for extended powers for community boards and its strong preference local boards, despite the threats this poses for regional infrastructure maintenance and investment, represent a worrying aspect of Draft Proposal for Reorganisation of Local Government in Northland.

Finally, chapter 8 drew together the various arguments in this Report to present a case against forced council amalgamation. Chapter 8 also recommended that:
1. The proposed amalgamations scenarios advocated in: (i) *Future Prosperity of the Hawkes Bay Region*, (ii) *Potential Costs and Savings of Local Government Reform in Hawkes Bay* and (iii) *Draft Proposal for Reorganisation of Local Government in Northland* are not supported by available empirical evidence and past experience of compulsory council mergers; and

2. Shared service arrangements should be considered as an alternative option to forced council amalgamations.
CHAPTER 1: INTRODUCTION

1.1 Background

In common with almost all Australian state local government systems, New Zealand local government is no stranger to council amalgamation, having experienced radical restructuring in 1989, when about 700 councils and special purpose bodies were merged into 86 local authorities. Across the world, advocates of forced amalgamation have adduced numerous advantages purportedly flowing from larger local government entities, which have changed over time (Dollery, Crase and Johnson, 2006). For example, whereas exponents of compulsory council consolidation previously emphasised cost reductions and other efficiency dividends allegedly attendant upon amalgamation, the observed failure of consolidated councils to achieve these claimed savings targets has seen more recent municipal mergers premised on their ability to increase the administrative and technical capacity of local authorities. However, some contemporary campaigns aimed at forced amalgamation, such as A Better Hawkes Bay (ABHB) council consolidation campaign, have centred their principal arguments on the purported ability of regional leadership based on large merged regional local authorities to drive faster regional growth and development.

The concerted campaign aimed at compulsory council consolidation in the Hawkes Bay Region rests on argumentation presented in two related reports prepared by commercial consultants McGredy Winder & Co. Future Prosperity of the Hawkes Bay Region (Part 1: Issues and Options) which sets forth thirteen different policy instruments for boosting economic growth and regional development in the Hawkes Bay Region, and examines option 9 ‘local government performance’ in some detail. While the main thrust of Future Prosperity of the Hawkes Bay Region hinges on the vital importance of regional leadership derived from
a single amalgamated local authority in the Hawkes Bay Region, it also contains subsidiary
claims regarding cost savings and other monetary benefits which would flow from a forced
amalgamation of existing local authorities.

Whereas *Future Prosperity of the Hawkes Bay Region* made no attempt to calculate or
substantiate these claims, a second report entitled *Potential Costs and Savings of Local
Government Reform in Hawkes Bay*, also produced by McGredy Winder & Co., examined
three alternative scenarios for council amalgamation in the Hawkes Bay Region. It sought to
compute the pecuniary consequences of these three structural models using a host of different
assumptions of varying degrees of plausibility in a financial modelling exercise.

More recently, the Local Government Commission itself has weighed into the debate with the
recent release of its *Draft Proposal for Reorganisation of Local Government in Northland*.
This draft proposal is of particular importance in the current context given its striking
resemblance to the ominous recommendations in *Future Prosperity of the Hawkes Bay
Region*. Together these reports proposed a single unity authority for their respective regions
in the absence of any compelling empirical evidence that forced amalgamation would lead
cost savings, improved service delivery, or enhance community well-being.

Against this background, this Report assesses the claims made in: (i) *Future Prosperity of the
Hawkes Bay Region*, (ii) *Potential Costs and Savings of Local Government Reform in
Hawkes Bay*, and (iii) *Draft Proposal for Reorganisation of Local Government in Northland*
on the financial and other implications of compulsory council consolidation, with particular
reference to the Hawkes Bay Region.
1.2 Outline of Report

*Bigger Is Not Always Better: An Evaluation of Future Prosperity of the Hawkes Bay Region and Potential Costs and Savings of Local Government Reform in Hawkes Bay* is divided into seven chapters:

Chapter 2 provides an analysis of the *Future Prosperity of the Hawkes Bay Region* concentrating on policy option 9 ‘local government performance’ of the 13 alternative policy avenues advanced in the report.

Chapter 2 is divided into three main parts:

- Section 2.2 provides a synoptic overview of *Future Prosperity of the Hawkes Bay Region*.
- Section 2.3 critically considers the six proposed alternative policy instruments under option 9 ‘local government performance’ in more detail.
- Chapter 2 ends with some brief concluding comments in section 2.4.

While Chapter 2 provided a detailed critique of *Future Prosperity of the Hawkes Bay Region*, Chapter 3 focuses exclusively on *Potential Costs and Savings of Local Government Reform in Hawkes Bay* also prepared by commercial consultants McGredy Winder & Co on behalf of the Hawkes Bay Regional Council. *Potential Costs and Savings of Local Government Reform in Hawkes Bay* attempts to calculate the cost savings associated with three different structural reform ‘scenarios’ for the Hawkes Bay Region:
• **Scenario A**: A Single Unitary Authority.

• **Scenario B**: A single territorial authority and the existing regional council (i.e. Wairoa, Central Hawkes Bay and Hastings District Councils combined with Napier City Council).

• **Scenario C**: Two territorial authorities and the existing regional council (a northern council combining Napier City, Wairoa District and the part of Hastings District north of the Tutaekuri River, and a southern council merging the balance of Hastings District and Central Hawkes Bay District Council).

Chapter 3 is divided into four main parts:

• Section 3.2 provides a synoptic overview of *Potential Costs and Savings of Local Government Reform in Hawkes Bay*.

• Section 3.3 provides a critical assessment of the approach adopted in *Potential Costs and Savings of Local Government Reform in Hawkes Bay*.

• Section 3.4 considers the estimates made of transition costs by the authors of the report in the light of recent experience of similar constellations of forcibly amalgamation councils in Queensland.

• Chapter 3 ends with some brief concluding remarks in section 3.5.

Whereas Chapter 2 examined *Future Prosperity of the Hawkes Bay Region* in detail and Chapter 3 concentrated on *Potential Costs and Savings of Local Government Reform in Hawkes Bay*, Chapter 4 ‘steps back’ and considers the available conceptual and empirical
evidence on amalgamation in local government as a means of assessing the viability of the
council amalgamation program proposed in *Future Prosperity of the Hawkes Bay Region*.

Chapter 4 is divided into four main parts:

- Section 4.2 describes the historical scale of municipal mergers in New Zealand and
  Australia and compares the current size of Antipodean councils with their
  counterparts in other advanced countries.
- Section 4.3 provides a synoptic account of the international and Antipodean scholarly
  research on local government consolidation.
- Section 4.4 considers the effects of 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.
- Chapter 4 ends with some brief concluding remarks in section 4.5.

Chapter 5 conducts an econometric modelling analysis to determine whether there is any
statistically significant relationship between council population size and local government
expenditure for Central Hawkes Bay District Council, Hastings District Council, Napier City
Council, and Wairoa District Council. This is done to ascertain whether scale economies
exist. If economies of scale are not present, then it follows that the argument for
amalgamation is seriously weakened. Furthermore, it terms of public policy, if scale
economies do not exist, then there is little reason to presume that the proposed cost savings
claimed in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* would
be realised.
Chapter 5 employs a 10 year panel data set for Central Hawkes Bay, Hastings, Napier, and Wairoa for the period 2003 to 2012. The econometric analysis reveals that there is no statistically significant relationship between council population size and per capita expenditure.

Chapter 5 is comprised of four main parts:

- Section 5.2 provides a synoptic review of the concept and measurement of economies of scale.
- Section 5.3 describes the data source, econometric model, and the empirical strategy employed.
- Section 5.4 presents the statistical estimates obtained using the econometric model.
- Chapter 5 concludes with some brief remarks in section 5.5.

While Chapter 3 critically examined the cost calculations in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* and found numerous problems with its cost estimates, Chapter 6 considers in more detail the proposed governance arrangements for the Scenario A, Scenario B and Scenario C. It demonstrates that *Potential Costs and Savings of Local Government Reform in Hawkes Bay* have taken too benevolent view of the costs and efficacy of these arrangements, especially with respect to community boards.
Chapter 6 is divided into four main parts:

- Section 6.2 briefly sets out the assessment of governance arrangements undertaken in *Potential Costs and Savings of Local Government Reform in Hawkes Bay*, especially regarding its Auckland-style community boards.
- Section 6.3 critically evaluates the performance of community boards as sub-council representative structures in New Zealand local government.
- Section 6.4 assesses the cost estimates of the operation of community boards in *Potential Costs and Savings of Local Government Reform in Hawkes Bay*.
- Chapter 6 ends with some brief concluding comments in section 6.5.

Chapter 7 provides a critical analysis of the new Local Government Commission process. In particular, we examine the *Draft Proposal for Reorganisation of Local Government in Northland* prepared by the LGC as a striking and worrying example of how the revised process is interpreted to work by the LGC. The *Draft Proposal for Reorganisation of Local Government in Northland* is important for local government reorganisation in the Hawke’s Bay Region because of its remarkable similarity to the dire recommendations in *Future Prosperity of the Hawkes Bay Region*. Both reports propose a single unitary authority for their respective regions in place of existing district councils and regional councils.

Chapter 7 is divided in three main parts:
• Section 7.2 briefly sets out the new Local Government Commission (LGC) process of determining local government reorganisation.

• Section 7.3 critically examines the LGC Draft Proposal for Reorganisation of Local Government in Northland as the most recent example of how the LGC is approaching local government consolidation.

• Chapter 7 ends with some brief concluding remarks in section 7.4.

Bigger Is Not Always Better: An Evaluation of Future Prosperity of the Hawkes Bay Region and Potential Costs and Savings of Local Government Reform in Hawkes Bay concludes with Chapter 8 which sets out its main conclusions and recommendations.
CHAPTER 2: ANALYSIS OF FUTURE PROSPERITY OF THE HAWKES BAY REGION (PART 1: ISSUES AND OPTIONS)

2.1 Introduction

*Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a) provides a broad analysis of the various policy options which could be invoked to improve the economic prospects of the Hawkes Bay Region. It attempts to identify the major economic and institutional constraints impeding economic development in the Hawkes Bay Region and then examines 13 matters which could be addressed to enhance economic growth. Chapter 2 of this Report provides an analysis of the *Future Prosperity of the Hawkes Bay Region* which focuses on option 9 ‘local government performance’ of the 13 alternative policy avenues.

Chapter 2 is divided into three main parts. Section 2.2 provides a synoptic overview of *Future Prosperity of the Hawkes Bay Region*. Section 2.3 critically considers the six proposed alternative policy instruments under option 9 ‘local government performance’ in more detail. Chapter 2 ends with some brief concluding comments in section 2.4.

2.2 Synoptic Review of Future Prosperity of the Hawkes Bay Region

*Future Prosperity of the Hawkes Bay Region* represents the first of two reports commissioned by the Hawkes Bay Regional Council. It not only seeks to identify the major problems facing the Hawkes Bay Region, but also to pinpoint various ‘broad initiatives that could be pursued to improve prosperity’ (McGredy Winder & Co., 2013a, p.18).
In terms of its overall performance, *Future Prosperity of the Hawkes Bay Region* contends that whereas the Hawkes Bay Region has significant natural resources, it has nevertheless performed below average for New Zealand. *Future Prosperity* argues that given the Hawkes Bay Region resource base, it has the capacity to perform much better. Various factors account for the comparatively poor economic performance of the Hawkes Bay Region. For instance, *Future Prosperity* holds that while the Hawkes Bay economy is driven by primary production, if its agri-business sector is decomposed into its constituent parts, then it appears that it contains a number of agricultural industries which have performed poorly over the last decade. Along analogous lines, the structure of Hawkes Bay Region economy is focused on relatively few industries, which has made it vulnerable to external economic factors, such as falling international commodity prices.

Within these broader constraints, *Future Prosperity of the Hawkes Bay Region* contends that the Hawkes Bay Region faces several specific growth inhibiting factors. In particular, the availability and security of water available for agricultural purposes is inadequate. Similarly, the Hawkes Bay Region not only has an ageing labour force, a comparatively poorly educated population, and significant unemployment, but also a significant proportion of people experience unemployment, deprivation and poverty.

Against this background, *Future Prosperity of the Hawkes Bay Region* argues that the Hawkes Bay Region nonetheless has a well-developed public sector, made up of both central and local government entities, which should be able to foster much faster economic growth and development in the region. However, *Future Prosperity of the Hawkes Bay Region* claims that serious concerns exist over the performance of local government in the Hawkes
Bay Region, especially relating to the capacity of the Wairoa District Council and the Central Hawkes Bay District Council to effectively tackle the multi-dimensional problems confronting their local communities. In particular, *Future Prosperity of the Hawkes Bay Region* holds that as presently constituted, local government in the Hawkes Bay Region is unlikely to act as the catalyst for more rapid economic growth.

In aggregate, *Future Prosperity of the Hawkes Bay Region* identified 13 ‘possible initiatives’ which could serve to ‘improve the economic and social development’ of the Hawkes Bay Region. These are reproduced in Table 2.1.

**Table 2.1: Possible Initiatives for Hawkes Bay Region**

<table>
<thead>
<tr>
<th>Initiative</th>
<th>Timeframe</th>
<th>Likely Cost</th>
<th>Degree of Difficulty</th>
<th>Likely Return</th>
<th>Importance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Water storage and increased intensive primary production</td>
<td>5+ years</td>
<td>5+ years</td>
<td>High</td>
<td>Very High</td>
<td>Critical</td>
</tr>
<tr>
<td>Maximising the value add from increased production</td>
<td>5+ years</td>
<td>High</td>
<td>High</td>
<td>High + Risk</td>
<td>Critical</td>
</tr>
<tr>
<td>Transforming the sale and distribution of produce</td>
<td>5+ years</td>
<td>High</td>
<td>Very High</td>
<td>Uncertain - High</td>
<td>High</td>
</tr>
<tr>
<td>Skills, improving educational achievement and pathways to employment</td>
<td>3-5 years</td>
<td>Low - Moderate</td>
<td>Moderate</td>
<td>High</td>
<td>Critical</td>
</tr>
<tr>
<td>Maori participation and economic performance</td>
<td>5+ - 20 years</td>
<td>Low</td>
<td>High</td>
<td>Very High</td>
<td>Critical</td>
</tr>
<tr>
<td>Transforming primary production – applied research and development</td>
<td>2-3 years</td>
<td>Low - Moderate</td>
<td>Moderate</td>
<td>Very High + Risk</td>
<td>Moderate</td>
</tr>
<tr>
<td>Tourism and the visitor industry</td>
<td>2-3 years</td>
<td>Low</td>
<td>Moderate</td>
<td>Moderate - High</td>
<td>High (short term gain)</td>
</tr>
<tr>
<td>Community development initiatives</td>
<td>2-5 years</td>
<td>Low - Moderate</td>
<td>Moderate</td>
<td>Moderate - High</td>
<td>High</td>
</tr>
<tr>
<td>Performance of local government</td>
<td>3-5 years</td>
<td>Moderate</td>
<td>Moderate - High</td>
<td>Moderate</td>
<td>Critical</td>
</tr>
<tr>
<td>Contribution and alignment of central government investments</td>
<td>Less than 2 years</td>
<td>Low</td>
<td>Moderate - High</td>
<td>High</td>
<td>Critical</td>
</tr>
<tr>
<td>Retirement destination</td>
<td>3-5 years</td>
<td>Low - Moderate</td>
<td>Moderate - High</td>
<td>Moderate - High</td>
<td>Moderate</td>
</tr>
<tr>
<td>Harnessing regional assets – the Hawkes Bay Power Consumers’ Trust</td>
<td>Less than 1 year</td>
<td>Low</td>
<td>Moderate - High</td>
<td>Very High</td>
<td>High</td>
</tr>
<tr>
<td>Oil and Gas</td>
<td>5 – 20 years</td>
<td>High</td>
<td>Moderate + Risk</td>
<td>Uncertain – Very High</td>
<td>High</td>
</tr>
</tbody>
</table>

Source: *Future Prosperity of the Hawkes Bay Region* (2013, Table 1, p.16)
With respect to the 13 options contained in Table 2.1, the authors of *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, p.48/49) have advanced a number of caveats. They are at pains to stress that ‘some of these initiatives reflect well-advanced thinking and planning from within the region’, whereas ‘others are more speculative, and indeed may not be achievable’. In addition, ‘other than the water storage initiative all others would require further work to develop specific and implementable recommendations’.

Moreover, the authors underline the fact that ‘there is no set recipe for driving or encouraging change’ nor is there a ‘single silver bullet that will transform the fundamentals of an economy or a community to deliver different outcomes’. The authors stress that while it is ‘comparatively easy to identify things that could be done to improve economic and social outcomes’, it is much ‘more difficult to drive change at the scale of the regional economy’ since ‘economies and communities are complex, organic systems that reflect the decisions and actions of a large number of individuals, businesses and groups, both within the region and elsewhere’. Furthermore *Future Prosperity of the Hawkes Bay Region* warns that although ‘change will be the result of these people and groups making conscious decisions to invest, to take risks, to work differently, and to pursue new opportunities’, only ‘some of those decisions will be successful, others will not’ and ‘there will always also be significant groups that benefit from the status quo and will work to protect that’.

It is apparent from the 13 options listed in Table 2.1, that the authors of *Future Prosperity of the Hawkes Bay Region* have not only estimated a feasible timeframe, the likely costs of implementation, the ‘degree of difficulty’, and the ‘likely return’, but they have also ranked the importance of the 13 options in terms of their probable impact on the future growth prospects of the Hawkes Bay Region. The latter ranking is noteworthy in the sense that 6 of
the 13 options (or 46 per cent) are regarded as ‘critical’ for future economic development, even though the probability of all 6 options being adopted and fully implemented must be remote!

Despite listing 13 options and then ranking them in terms of significance, the authors of *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, p.48) nonetheless view ‘leadership’ as by far the most important ingredient for a prosperous future for the Hawkes Bay Region:

If there is one thing that above all else can make a difference, it is leadership and vision. Communities that are able to build a shared vision of the future, and the confidence to invest to make it happen, will drive change. Leadership is not just about the role of the public sector and the recognised elected representatives of the community. Leadership within the business community and more broadly within society is critical. However, public sector leadership has a particular and important role in facilitating vision, and in harnessing the region’s public resources to support the vision for the future.

In sum, the *Future Prosperity of the Hawkes Bay Region* has argued that the Hawkes Bay Region would become more prosperous if it could bring about the following ‘wish-list’ of changes: ‘diversify and significantly deepen its economy’; ‘insulate itself to some degree from the cyclical nature of primary production’; engage in value-added production to a greater extent; establish a pattern of employment centred on skilled well-paid jobs; at the same time ‘provide increased employment opportunities and greater depth in the labour market’, especially for younger people; provide incentives for people to remain in Hawkes
Bay; to remove ‘unnecessary barriers or impediments to making the changes that are necessary’; develop local communities in Hawkes Bay Region imbued with ‘pride, a real sense of inclusion, connection and achievement’; ‘address the poverty and disadvantage within the region’; enable people to develop ‘a real stake in the future and contribute meaningfully to their community’; and establish the vital leadership in the Hawkes Bay Region essential for growth and development.

2.3 Improving Local Government Performance in the Hawkes Bay Region

Despite the fact that the authors of *Future Prosperity of the Hawkes Bay Region* have advanced 13 policy options for improving economic growth and development in the Hawkes Bay Region, the main thrust of the *Future Prosperity of the Hawkes Bay Region* centres on the purportedly urgent need to improve the performance of local government and ensure that it provides innovative regional leadership.

Local government in the Hawkes Bay Region is comprised of five local authorities. Given the heterogeneous nature of the Hawkes Bay Region, significant differences exist between these five councils. Whereas Central Hawkes Bay District Council, Hastings District Council, Napier City Council and Wairoa District Council focus largely on ‘traditional’ local government service provision, such as local roads, water and wastewater, waste collection and disposal, as well as local regulation, by contrast the Hawkes Bay Regional Council deals mainly with natural resources and environmental policy, especially flood control, land management, sediment control and water management land management issues in the headwaters of the rivers, as well as air quality, biosecurity, and pest control.
Table 2.2 summarises the chief characteristics of local government in the Hawkes Bay Region.

<table>
<thead>
<tr>
<th>Local Authority</th>
<th>Central Hawkes Bay District Council</th>
<th>Hastings District Council</th>
<th>Napier City Council</th>
<th>Wairoa District Council</th>
<th>Hawkes Bay Regional Council</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population (2010)</td>
<td>13,500</td>
<td>75,100</td>
<td>57,600</td>
<td>8,440</td>
<td>154,800</td>
<td>154,800</td>
</tr>
<tr>
<td>Area (km²)</td>
<td>3,332</td>
<td>5,226</td>
<td>522</td>
<td>4,077</td>
<td>14,138</td>
<td>14,138</td>
</tr>
<tr>
<td>Operating Revenue ($000)</td>
<td>29,700</td>
<td>83,602</td>
<td>79,662</td>
<td>20,633</td>
<td>35,630</td>
<td>249,227</td>
</tr>
<tr>
<td>Operating Expenditure ($000)</td>
<td>27,233</td>
<td>89,282</td>
<td>71,947</td>
<td>20,160</td>
<td>35,098</td>
<td>243,720</td>
</tr>
<tr>
<td>Rates ($000)</td>
<td>15,121</td>
<td>57,867</td>
<td>43,799</td>
<td>9,415</td>
<td>13,583</td>
<td>139,785</td>
</tr>
<tr>
<td>Fixed Assets ($000)</td>
<td>700,736</td>
<td>1,540,424</td>
<td>1,262,020</td>
<td>185,196</td>
<td>246,753</td>
<td>3,935,129</td>
</tr>
<tr>
<td>Total Equity ($000)</td>
<td>704,083</td>
<td>1,472,620</td>
<td>1,326,032</td>
<td>204,177</td>
<td>409,150</td>
<td>4,116,062</td>
</tr>
<tr>
<td>Term &amp; Current Debt ($000)</td>
<td>11,446</td>
<td>58,434</td>
<td>4,036</td>
<td>0</td>
<td>11,352</td>
<td>85,268</td>
</tr>
<tr>
<td>Current Equity &amp; Investments ($000)</td>
<td>23,135</td>
<td>13,665</td>
<td>83,825</td>
<td>23,790</td>
<td>182,483</td>
<td>326,898</td>
</tr>
<tr>
<td>Mayors &amp; Councillors</td>
<td>8</td>
<td>14</td>
<td>12</td>
<td>6</td>
<td>8</td>
<td>48</td>
</tr>
<tr>
<td>Councillor Rem. ($000)</td>
<td>251</td>
<td>657</td>
<td>536</td>
<td>207</td>
<td>513</td>
<td>2,164</td>
</tr>
<tr>
<td>Staff Complement (2009)</td>
<td>40</td>
<td>368</td>
<td>441</td>
<td>38</td>
<td>179</td>
<td>1,066</td>
</tr>
<tr>
<td>Employee Costs ($000)</td>
<td>3,171</td>
<td>24,775</td>
<td>24,652</td>
<td>2,706</td>
<td>12,416</td>
<td>67,720</td>
</tr>
<tr>
<td>Rates per Person ($)</td>
<td>1,120</td>
<td>771</td>
<td>760</td>
<td>1,116</td>
<td>88</td>
<td>903</td>
</tr>
<tr>
<td>Rates per Km² ($)</td>
<td>4,538</td>
<td>11,073</td>
<td>83,858</td>
<td>2,309</td>
<td>961</td>
<td>9,887</td>
</tr>
<tr>
<td>Equity per Person ($)</td>
<td>52,154</td>
<td>19,609</td>
<td>23,021</td>
<td>24,192</td>
<td>2,643</td>
<td>26,590</td>
</tr>
<tr>
<td>Current Equity / Person ($)</td>
<td>51,906</td>
<td>20,512</td>
<td>21,910</td>
<td>21,943</td>
<td>1,594</td>
<td>25,421</td>
</tr>
<tr>
<td>Debt per Person ($)</td>
<td>848</td>
<td>778</td>
<td>70</td>
<td>0</td>
<td>73</td>
<td>551</td>
</tr>
<tr>
<td>Ratio of Debt to Equity</td>
<td>0.02</td>
<td>0.04</td>
<td>0.00</td>
<td>0.00</td>
<td>0.03</td>
<td>0.02</td>
</tr>
<tr>
<td>Ratio of Debt to Rates</td>
<td>0.76</td>
<td>1.01</td>
<td>0.09</td>
<td>0.00</td>
<td>0.84</td>
<td>0.61</td>
</tr>
</tbody>
</table>

Source: *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, Table 3, p.29)

It is evident from Table 2.2 that a great deal of variation exists between the five local authorities in terms of size, especially between the numerically small Central Hawkes Bay District Council and Wairoa District Council on the one hand and the much larger Hastings District Council and Napier City Council on the other hand. In addition, it is clear that the financial position of all five local organisations is sound. This point is readily conceded in the *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, p.30) which
acknowledges that ‘whilst the financial position of each council is clearly different, the overall position of the councils is very favourable’. As we shall see, this is a significant concession since it removes financial sustainability – often the major impetus behind structural reform in local government – as a rationale for local government restructuring in the Hawkes Bay Region.

The *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, p.73) considers six policy options for ‘improving the performance of local government’ in the Hawkes Bay Region:

- Shared Services;
- More Effective Collaboration and a Hawkes Bay Plan;
- Key investments;
- Increased Regional Role – Transfer of Responsibilities;
- Rural Amalgamation; and
- Regional Amalgamation’.

The authors of *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, p.73) are at pains to stress that not only do these policy options ‘vary in scale, complexity’, but the ‘benefits and costs of the local government reform options range from being quite small to being moderate’. We now critically examine the discussion in *Future Prosperity of the Hawkes Bay Region* on these six policy options.
2.3.1 Shared Services

In their assessment of shared services in local government, the authors of *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, p.67/69) contend that ‘there is considerable scope for shared services within local government’, with the best prospects in back-office functions and ‘service delivery functions that councils have in common’. However, to implement shared systems ‘councils must adopt an agreed framework for a shared systems platform, including the standards, operating philosophy, enterprise architecture and the protocols necessary for foundation information systems’. Furthermore, *Future Prosperity of the Hawkes Bay Region* stresses that ‘securing the potential benefits of shared services is difficult and requires the adoption of common management practice, common and standard business processes and systems, and ways of ensuring that the competing needs of the authorities sharing the service are all met effectively’.

*Future Prosperity of the Hawkes Bay Region* offers some pecuniary estimates of the kinds of savings which could be reaped. For instance, it notes that ‘back-office related services savings of between 3% and 9% per annum are possible if there is a real commitment to driving change’. In the specific case of Hawkes Bay local government, with its ‘combined council support expenditure of the councils is $35.7m per annum’ this would imply savings of around ‘$1m to $3.2m per annum’.

The authors of *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, p.69) draw pessimistic conclusions with respect to the potential offered by shared service models:
The opportunity for shared services has existed for many years. For many reasons little progress has been made to deliver significant shared services within the region. The incentives for collaboration are weak and for it to be successful organisations need to be willing to cede some of their independence and sovereignty. It is unlikely that the region could secure the potential benefits of shared services without a major and enduring commitment from both political leaders and Chief Executives.

However, the analysis of shared services in *Future Prosperity of the Hawkes Bay Region* is seriously deficient in a number of respects. In the first place, its authors contend that ‘there have been relatively few published assessments of the benefits that have been secured through shared services’. This claim is false. In fact, a voluminous literature exists on shared services in local government. An exhaustive summary of the empirical evidence on the results of shared services can be found in Dollery, Grant and Kortt (2012) *Councils in Collaboration: Shared Services in Australian Local Government*.

After their survey of the published empirical material on shared services, Dollery, Grant and Kortt (2012, p.152) observed that ‘shared service arrangements can be beneficial for councils both in terms of cost savings and enhanced service quality’. However, the ‘success of particular arrangements seems to vary depending on the specific local circumstances’. Six most popular broad areas are cited in empirical evidence: (i) procurement; (ii) human resources; (iii) governance, compliance and audit services; (iv) IT; and (v) waste management. They note further that the bulk of empirical work on shared services indicates that it is a useful cost-reduction and quality-enhancing tool rather than a general panacea for the financial ills of local government.
A second major weakness in the discussion of shared services in local government in *Future Prosperity of the Hawkes Bay Region* resides in the absence of any method of deciding upon which services to choose for sharing. In the literature, four criteria are proposed in order to identify ‘appropriate’ services for shared delivery (Dollery, Grant and Kortt, 2012):

- Strategic services requiring expert local knowledge should be retained ‘in-house’ in local authorities;
- ‘Non-strategic, low-risk, rule-based’ and ‘high volume transaction processing’ services could be shared;
- Services requiring access to the latest technology without ongoing significant capital investment or a requirement for specialist expertise could be shared; and
- Services in which expert skills not readily attainable by councils should be garnered through service sharing or outsourcing.

At a more specific level, Dollery, Grant and Kortt (2012) have identified the characteristics of services suitable for a shared service arrangement as follows: ‘Low core capability’ of councils; ‘high supplier availability’; ‘low task complexity’; substantial scale economies; ‘specialized technology’; and ‘low asset specificity’.

A third problem in *Future Prosperity of the Hawkes Bay Region* resides in its neglect of alternative models of shared services in local government. For example, a typology of shared service arrangements has been proposed by Tomkinson (2007) in his *Shared Services in Local Government*, which contains four alternative shared service models:
The Intra-Service Model includes limited shared services options, such ‘regional procurement models’ which provide procurement and purchasing services to member councils;

The Service Model embodies a degree of formality which enables the participating group of councils to cede control to the council which takes on the role of the ‘lead council’ in terms of budgetary control, service specification, statutory service responsibilities, etc.

The Corporatist Model involves two or more councils forming a joint arrangement to deliver a specific service or services at a mutually agreed standard in which both the costs and benefits are borne by all partner councils on a negotiated basis. In general, this means the creation of a joint governing body to sit between the sharing councils and the delivery body which is wholly owned by these councils.

The Supra-Corporate Model enables two or more participating councils to set up a separate ‘special purpose vehicle’ to deliver a specified service or services on behalf of member councils. This vehicle could take a variety of organisational forms, such as a joint venture company, a company limited by shares or by guarantee, a not-for-profit organisation and limited liability partnerships.

In addition, Dollery, Grant and Akimov (2010) developed a tripartite typology, which can help shed light on the characteristics of shared services amongst councils, such as the Hawkes Bay group of councils:
• The ‘Horizontal Shared Service Model’ is the most common form of shared services in contemporary Australian and New Zealand local government. These standard shared service arrangements involve partnerships between local councils, typically spatially bordering one another, which range from simple *ad hoc* resource sharing between two or more local councils to fully-fledged area integration models. While these shared service arrangements take a multitude of different forms, with widely varied governance models and patterns of ownership, they have in common that the shared services, shared resources, shared equipment and shared facilities involved are fully owned by member councils. Thus not only are the activities and procedures of the shared service entity completely controlled by its members councils, but all costs, income, profit and risk rest ultimately upon these councils. In other words, shared service arrangements falling under horizontal shared service models are wholly operated and owned by participating local councils.

• The ‘Vertical Shared Service Model’ involves cooperation between all or some local councils in a given national or state jurisdiction and the local government association in that country. Vertical shared service models usually involve the state local government association offering a defined service to member councils across its state jurisdiction, either as a normal part of its ongoing contribution to members or on a ‘fee-for-service’ basis.

• The ‘Intergovernmental Contracting Shared Service Model’ under which local councils *voluntarily* carry out various functions on behalf of public agencies from higher tiers of government. We can differentiate between various different types of intergovernmental contracting shared service models. For instance, the most common
form of this model occurs where individual councils contract on an *ad hoc* basis with national agencies to undertake specific tasks, such as highway maintenance.

In the context of the Hawkes Bay Region councils, all three models could be invoked to the benefit of local councils.

Finally, we contend that the pessimistic assessment of the prospects of successful shared services models in the Hawke’s Bay Region *Future Prosperity of the Hawkes Bay Region* is erroneous since its authors do not appear to understand the inextricable link between forced amalgamation and shared services as alternative methods of achieving structural change in local government. Several scholars have noted the link between structural reform through compulsory amalgamation and the imperatives it provides towards the introduction of shared service models. For example, Dollery, Crase and O’Keefe (2009) have shown that the threat of forced mergers has served to galvanise targeted councils into embarking on successful shared service initiatives as a means of avoiding compulsory consolidation. In other words, the threat of amalgamation provides adequate incentives for councils to overcome inertia and barriers to shared service arrangements. This strand in the literature has been entirely overlooked by the authors of *Future Prosperity of the Hawkes Bay Region*. Had they taken it into account, they would have realised that the threat of amalgamation *per se* is sufficient grounds for local authorities in the Hawkes Bay Region to begin discussions on shared service programs, provided the threat is credible.
2.3.2 More Effective Collaboration and a Hawkes Bay Plan

The authors of *Future Prosperity of the Hawkes Bay Region* proposed greater regional collaboration and an integrated Hawkes Bay Plan as a second approach to improving the performance of local government. The argument was set out as follows by its authors (McGredy Winder & Co., 2013a, p.69):

A second possible area for working to improve the delivery and impact of local authorities within the region would be to focus on a stronger collaborative approach to local governance. The cornerstone of this option would be to enhance co-ordination of regional strategy and policy and to ensure that a Hawkes Bay vision and plan is translated into both the regulations and the activities of the existing councils. One of the key requirements of this approach would be to ensure that council regulatory frameworks are responsive to development opportunities.

*Future Prosperity of the Hawkes Bay Region* goes on to concede that ‘there are a number of collaborative frameworks already within the region’, which include the Regional Land Transport Committee, the ‘regional council’s new Joint Committee’ and the ‘collaborative development of the Heretaunga Plains Urban Development Strategy’. However, its authors contend that further regional collaboration is necessary. For example, it is argued that ‘securing agreement and alignment of council efforts to implement a jointly agreed plan for the region would be significant step toward achieving the benefits of scale in local government without the cost of transition to new institutional arrangements’. However, the claim centring on the purported ‘benefits of scale’ has not been substantiated in any way.
In general, experience in local government systems around the world has shown that regional collaboration can be an effective method of enhancing regional growth and economic development. For example, Australian local government is replete with examples of successful Regional Organisations of Council (ROCs) and Regional Alliances which has engaged in successful regional development strategies. Part C of *Councils in Collaboration* (Dollery, Grant and Kortt, 2012) has undertaken a detailed analysis of the operation of several of these entities. It is thus most unfortunate that the authors of *Future Prosperity of the Hawkes Bay Region* did not consult this literature. Nevertheless, the *Future Prosperity of the Hawkes Bay Region* is broadly correct in concluding that ‘this option provides the greatest opportunity for the local authorities of the region to provide leadership and progress a truly regional development agenda’.

As *Councils in Collaboration* has demonstrated, successful regional collaboration has not only occurred in numerous local government systems, but much is known about the barriers to successful regional collaboration and how these can be overcome. It would therefore be advisable for Hawkes Bay local authorities to investigate this option further, and more particularly the question of forming a ROC to facilitate regional development though inter-council collaboration.

### 2.3.3 Key Investments

The authors of *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, p.70) take pains to stress the existing strong financial viability of the five local government entities in the Hawkes Bay Region:
The councils of the region collectively enjoy quite strong balance sheets. The regional council in particular has substantial assets and is now working to use the strength of its balance sheet to drive projects that will enhance the economic performance of the region. The sort of investment planned by the regional should provide substantial long-term returns to the region – both through increased production and through a direct return on the investment.

Other councils within the region have healthy balance sheets. Wairoa has no term debt and around one year’s worth of operating income held as current assets. Napier City has progressively paid down its external debt and also holds substantial current assets. Even Hastings District (which holds the highest level of debt of all of the councils) has quite modest levels of debt in relation to other New Zealand local authorities.

The *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, p.70) goes on to argue that ‘it would be possible for the councils of the region to make more active use of the resources that they have at their disposal’. However, unfortunately no specific details are provided as to how council financial resources should be deployed and what models should be used.

2.3.4 Increased Regional Role: Transfer of Responsibilities

The fourth option for improving the operation of local government in the Hawkes Bay Region canvassed in the *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, p.70) involves an upward functional reallocation of responsibilities from the territorial local authorities to the regional council. In particular, its authors argue that ‘the most pressing infrastructure issues in the region relate to the wastewater networks and
treatment facilities of Central Hawkes Bay and (in the future) Wairoa’. This could be addressed by a ‘transfer of responsibilities from territorial authorities to the regional council’.

*Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013, p.70) observes that ‘the advantages of such a transfer would be that it: aligns within one organisation greater responsibility for water management; provides a mechanism to spread or equalise the costs of providing wastewater over a larger constituency (including those who benefit from improved water quality); provides the ability to use the strength of the regional council’s balance sheet to support much needed infrastructure; and enables one organisation to deal with the environmental consequences of managing the impacts of the major sources of nitrogen within significant river systems’. In addition, it would enable the establishment of ‘a critical mass of professional skills and capabilities’ within the regional council which already contains significant ‘expertise related to water management and treatment’. It is further argued that ‘one of the benefits of this approach is that it has relatively little cost and can be achieved relatively rapidly within the existing framework of the Local Government Act without recourse to any external decision-making body’.

This suggestion has undoubted merit. In particular, had the authors of *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013, p.70) consulted the empirical literature on scale economies in local public service provision, they would have established that local government water and wastewater operations frequently exhibited scale economies, largely as a result of their capital intensive nature. For this reason, urban water and wastewater provision, storage and treatment is frequently undertaken by regional water authorities, such as the Sydney Water Corporation and Hunter Water in New South Wales.
However, it is necessary to add a critical caveat to the desirability of the proposed upward functional reallocation of responsibility for water from the territorial local authorities to the regional council in the Hawkes Bay Region. For example, in an analysis of proposed water ‘regionalisation’ in non-metropolitan New South Wales local government Dollery and Johnson (2012) have shown that it would have severely deleterious financial consequences on country councils by depriving them of a significant stream of revenue without a concomitant decrease in costs.

Dollery and Johnson (2012) have argued that water and sewerage functions are critical to the long-term financial sustainability of non-metropolitan New South Wales councils. An important reason for this is that income from these functions enables country councils to attract a variety of skilled staff that would not otherwise be available. These functions also make a significant contribution towards the cost of a council’s corporate and technical support services. Water and sewerage services thus significantly enhance a local council’s ability to achieve scale and scope economies in its overall operations. All this makes a substantial contribution to financial sustainability. Given these concerns, prior to any upward functional reallocation of responsibility for water from the territorial local authorities to the regional council in the Hawkes Bay Region, it would be essential to conduct a thorough evaluation of the financial and other consequences of such action.

2.3.5 Rural Amalgamation

The fifth option for improving the performance of local government in the Hawkes Bay Region considered in Future Prosperity of the Hawkes Bay Region (McGreedy Winder & Co., 2013a, p.71) centres on the compulsory consolidation of the Hawkes Bay Regional Council
with the Wairoa and Central Hawkes Bay District Councils to ‘create a council that was a unitary authority in those rural districts but continued to perform the role of a regional council’. The rationale for this suggestion apparently derives from the ‘major concerns that stakeholders identified with respect to the performance of local authorities and possible local government reform was the potential for the rural voice of the region to get lost’, with ‘a number of stakeholders cautioned strongly against changes that would diminish the strong rural focus of the regional council’. This fear stemmed from the fact that ‘despite its very large rural area, Hastings was in their eyes an urban authority, dominated by an urban population, where urban issues dominated politics and where it is difficult to remain connected to the primary economy that supports the region’. It was felt that ‘one way to drive improved local authority outcomes and ensure that there is a strong focus on rural issues would be to amalgamate the regional council with Wairoa and Central Hawkes Bay Districts’. *Future Prosperity* recognised several of these benefits, observing that not only would it generate ‘a strong rural focus for the region that can focus on both the region’s major environmental issues and on the primary economy that supports the region’, but it would also ‘address the areas of greatest weakness in capability and capacity amongst the local authorities and provide a platform for leadership’.

Despite these purported advantages, the authors of *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, p.71) are unconvinced. In the first place, while they noted that a rural amalgamation of this kind ‘has not previously been contemplated in New Zealand’, they nonetheless concede that ‘there would be no statutory impediment to reform of this nature’. However, they stress that a rural merger possesses ‘the same sorts of benefits and risks’ as a more general regional program of forced amalgamation of all Hawkes Bay regional local authorities without the correspondingly greater ‘scale of benefits that would be
possible through a substantial region-wide shared services approach, or a regional amalgamation’. Finally, a rural merger ‘would not deliver the quantum change in leadership that would be possible through the creation of a single Hawkes Bay Council’.

### 2.3.6 Regional Amalgamation

The final and by far the most draconian option for improving the performance of local government assessed of *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, pp.71/72) resides in the compulsory consolidation of the Hawkes Bay Regional Council with all of the district councils to form a single Hawkes Bay local government entity. This option ostensibly flows from the fact that a ‘large number of stakeholders advocated for the amalgamation of [all] local authorities’.

The rather confusing rationale for this purportedly popular sentiment is set out as follows in the *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, p.71):

> Interestingly, the focus of this discussion was Napier City, Hastings District and the regional council. One of the very strong conclusions that the project team has come to is that the region is far bigger than just Napier and Hastings. Central Hawkes Bay and Wairoa are an integral part of the regional economy. Whilst Wairoa may (with some justification) consider itself to be less closely linked to the region than Central Hawkes Bay, in a functional sense it is part of the Hawkes Bay economy. Local government reform that does not include the two small rural councils fails to address some of the most significant local government issues facing the region.
*Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, pp.71/72) contends that five advantages would flow from the establishment of a single Hawkes Bay Council:

i. A single Hawkes Bay Council would possess ‘a single voice and a focus of leadership for the region.’

ii. It would provide ‘the platform for a deeper and more manageable relationship with government and a means to align government expenditure with agreed regional priorities’.

iii. It would generate the ‘greatest scope to address the cost structure and performance of local government’.

iv. It would yield ‘the greatest scope to attract and retain highly skilled professionals’.

v. Finally, it would maximise ‘the scope to use the considerable, combined financial strength of the local authorities’.

By contrast, the authors of the *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, p.72) concede that a drastic forced merger of this kind would possess six main shortcomings:

i. The establishment of a single Hawkes Bay Council would involve costly ‘transition and harmonising business systems and processes’.

ii. It would entail ‘risks associated with the loss of key staff and institutional knowledge’.

iii. It would create ‘the potential for major service disruption during the change process’.
iv. It could result in ‘the potential loss of focus on rural issues’.

v. Resources would be absorbed in the merger process in terms of the ‘time and effort that is required to secure the benefits of change and the possible opportunity cost that [it] imposes on the region through [an] inability to concurrently address other issues’.

vi. Finally, ‘in the context of the Hawkes Bay one significant risk from an amalgamation process of this scale would be that the level of management time and engagement in transition detracts from, or compromises the delivery of the Ruataniwha water storage project’ since ‘the benefits to the region from the water storage project probably eclipse the potential hard measurable savings from amalgamation by a factor of 10’.

In addition to these specific advantages and disadvantages, the authors of *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, p.72) recognise further difficulties associated with forced amalgamation. For example, they readily conceded that ‘any merger is challenging’ and it would involve ‘on-going effort to secure benefits and to ensure that the new organisation is not simply the product of the highest cost and lowest productivity approaches of the original organisations’. However, these difficulties should be seen against the fact that ‘an amalgamation of the five Hawkes Bay Councils would be of a different scale than the Auckland amalgamation’ since ‘the combined staffing of the current councils is in the order of 1,000 and total annual operating expenditure is around $250m’ which would make a single Hawkes Bay Council ‘larger than the current Hamilton or Dunedin City Councils, but it would be smaller than Wellington City Council and the previous North Shore and Waitakere Cities’.
As we can see from Table 2.1, in their overall assessment of local government reform as one of 13 possible initiatives, the authors of *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, Table 5, p.82) contend that local government reform would take around ‘3/5 years’, the likely cost would be ‘moderate’, the ‘degree of difficulty’ involved would be ‘moderate/high’, the ‘likely return’ would be ‘moderate’ and its ‘importance’ is ranked as ‘critical’.

However, this synoptic summary of local government reform is not entirely consistent with the analysis in *Future Prosperity of the Hawkes Bay Region* on the benefits and costs of the proposed reform options. For example, the summary table on p.73 of *Future Prosperity of the Hawkes Bay Region* offers the following assessment of the ‘6 options for improving the performance of local government: Shared Services; More Effective Collaboration and a Hawkes Bay Plan; Key investments; Increased Regional Role – Transfer of Responsibilities; Rural Amalgamation; and Regional Amalgamation’:

These options vary in scale, complexity, costs and benefits. In comparison with the other development initiatives presented in this report the benefits and costs of the local government reform options range from being quite small to being moderate. All of the options presented would take between 3 and 5 years to deliver the full value of potential benefits. The possible longer-term financial returns that are possible are probably in the order of $3m to $25m per annum, depending on the option pursued. The costs of transition for the more complex amalgamation options, and for a significant shared services platform have not yet been identified but will below (sic) to moderate in comparison to the costs for the other possible development initiatives.
In addition, the authors of *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013a, p.83) take pains to stress that ‘improving the performance of local government is also considered critical – but not so much because of the potential for savings or efficiencies as because leadership and the resources of the local authorities are required as an enabler of the other critical initiatives’. In other words, all that is sought from local government reform is effective regional leadership rather than an improvement in the performance of local government functioning *per se!* As if to reinforce this observation, the authors (McGredy Winder & Co., 2013a, p.83) note further that while ‘there is scope for improving the efficiency and effectiveness of local government within the region, however, this is by no means a silver bullet and potential quantifiable savings will be modest compared to the potential benefits of a number of other initiatives’.

Moreover, the authors (McGredy Winder & Co., 2013a, p.83/4) go on to stress that whereas ‘generally local government has quite limited abilities to directly influence or drive economic development’, ‘effective and inspiring community leadership can make the difference between mobilising the community’s resources and capabilities to achieve common goals, or muddling along’. Put differently, in the view of the authors of *Future Prosperity of the Hawkes Bay Region* (McGredy Winder & Co., 2013, p.84) what is required is dynamic leadership rather than simply local government reform!

Finally, the cognitive dissonance between the prescription in *Future Prosperity of the Hawkes Bay Region* for radical local government restructuring through compulsory consolidation and its belated recognition that local government is seldom able to drive economic growth and development in the absence of other essential ingredients is further
underlined by the note of caution on the vital importance of water development, especially the Ruataniwha water storage project. The authors observe that ‘given the central importance of water management it is vital that any reform local government does not impede or compromise the ability to deliver the Ruataniwha and other water storage projects’. In the light of experience on the bitterly divisive nature of local government amalgamation on local communities, this caveat is important.

2.4 Concluding Comments

Chapter 2 of this Report has sought to provide a synoptic account of the analysis in *Future Prosperity of the Hawkes Bay Region* and critically assess its proposals for improving the performance of local government in the Hawkes Bay Region. Several conclusions can be drawn.

In the first place, it is clear that the authors of *Future Prosperity of the Hawkes Bay Region* have almost entirely ignored the voluminous literature on structural reform in local government, which includes a substantial body of thought on Australasian local government reform. This neglect is most unfortunate since a wealth of material exists. As we shall see in Chapter 4 of this Report, various lessons emerge from this literature, not least that forced amalgamation has not improved the performance of local authorities, especially in non-metropolitan areas. Secondly, shared services offer a promising alternative to compulsory consolidation, particularly in a regional contact. Finally, effective regional leadership is best fostered through the establishment of regional bodies, such as ROCs and Regional Alliances of Council, rather than by means of bitterly divisive battles over forced amalgamation which almost invariably results in the domination of regional areas by regional centres.
3.1 Introduction

Chapter 2 provided a detailed critique of *Future Prosperity of the Hawkes Bay Region*, which proposed 13 alternative policy avenues for fostering economic growth and development in the Hawkes Bay Region and then considered option 9 ‘local government performance’ in more detail. Various claims were made in *Future Prosperity of the Hawkes Bay Region* regarding the cost-savings and other benefits which would purportedly flow from a forced amalgamation of local authorities, but no effort was made to calculate or substantiate these claims.

By contrast, a second report *Potential Costs and Savings of Local Government Reform in Hawkes Bay* – also prepared by commercial consultants McGredy Winder & Co at the behest of the Hawkes Bay Regional Council – seeks to provide at least some substantiation for some of the claims made in *Future Prosperity of the Hawkes Bay Region* regarding the benefits and costs of structural change in local government in the Hawkes Bay Region. In particular, *Potential Costs and Savings of Local Government Reform in Hawkes Bay* (McGredy Winder & Co., 2013b, p.9) attempts to calculate the cost savings associated with three different structural reform ‘scenarios’ for the Hawkes Bay Region:
• **Scenario A**: A Single Unitary Authority

• **Scenario B**: A single territorial authority and the existing regional council (i.e., Wairoa, Central Hawkes Bay and Hastings District Councils combined with Napier City Council)

• **Scenario C**: Two territorial authorities and the existing regional council (a northern council combining Napier City, Wairoa District and the part of Hastings District north of the Tutaekuri River, and a southern council merging the balance of Hastings District and Central Hawkes Bay District Council).

On the basis of a host of assumptions of varying degrees of plausibility, the authors of *Potential Costs and Savings of Local Government Reform in Hawkes Bay* (McGredy Winder & Co., 2013b, p.1) sought to develop ‘a financial model that was able to support more robust estimates of the potential costs and savings’ associated with these three scenarios for structural reform of local government in the Hawkes Bay Region. The authors were at pains to underline the arbitrary nature of the cost savings estimates in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* (McGredy Winder & Co., 2013, p.1) by adding a number of caveats. While this report intended to ‘produce estimates of the potential costs and savings associated with local government reform in Hawkes Bay that are considerably more robust than the indicative, order of magnitude statements’ found in *Future Prosperity of the Hawkes Bay Region*, its estimates nonetheless ‘are based on assessments of the potential to achieve savings in each activity that the region’s local authorities undertake’. The authors stress that ‘the estimates reflect a medium level understanding of the cost structures and drivers for each activity’ and not ‘a detailed design of a new organisation, or the detailed
assessment of workflows, work processes, or systems that would be part of the detailed design of a new organisation’.

The net result is that the cost savings estimates ‘describe the likely level of savings that could be achieved’ rather than provide a more precise understanding of the actual costs involved. The authors of *Future Prosperity of the Hawkes Bay Region* contend that their estimates can be employed for three purposes: (a) ‘comparing the relative potential for savings between different reform options’; (b) ‘understanding the total potential savings from reform’; and (c) ‘understanding the key activities where savings may be possible and how critical those savings would be to achieving the total savings estimated’. Chapter 3 of this Report provides a critical examination of the analysis in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* on the three alternative structural reform options proposed for Hawkes Bay Region local government.

Chapter 3 is divided into four main parts. Section 3.2 provides a synoptic overview of *Potential Costs and Savings of Local Government Reform in Hawkes Bay*. Section 3.3 provides a critical assessment of the approach adopted in *Potential Costs and Savings of Local Government Reform in Hawkes Bay*. Section 3.4 considers the estimates made of transition costs by the authors of the report in the light of recent experience of similar constellations of forcibly amalgamation councils in Queensland. Chapter 3 ends with some brief concluding remarks in section 3.5.

**3.2 Synoptic Review of Potential Costs and Savings of Local Government Reform**

As we have seen, *Potential Costs and Savings of Local Government Reform in Hawkes Bay* (McGredy Winder & Co., 2013b, p.4) set out to provide estimates of any cost savings which
may eventuate from structural reform of local government entities within the Hawkes Bay Region. Its authors were requested by the Hawkes Bay Regional Council to examine the cost implications of three specific types of structural change to Hawkes Bay local government:

- **Scenario A**: A single unitary authority as proposed by *A Better Hawkes Bay* to the Local Government Commission.
- **Scenario B**: A single territorial authority and the existing regional council.
- **Scenario C**: Two territorial authorities (a northern council including Napier City, Wairoa District and the part of Hastings District north of the Tutaekuri River, and a southern council comprising the balance of Hastings District and Central Hawkes Bay District) and the existing regional council.

*Potential Costs and Savings of Local Government Reform in Hawkes Bay* (2013, p.4) aims to provide ‘a summary of the financial model that was developed and the assumptions that underpin it as well as the estimated costs and savings associated with the three reform options’. The objective of the exercise is threefold:

i. ‘Comparing the relative potential for savings between different reform options;

ii. Understanding the total potential savings from reform; and

iii. Understanding the key activities where savings may be possible and how critical those savings would be to achieving the total savings estimated’.

The *modus operandi* adopted by the authors of *Potential Costs and Savings of Local Government Reform in Hawkes Bay* centres on employing data derived from information taken from current Hawkes Bay council long-term plans rather than independently collected
data. Estimated cost savings are presented in the form of cost savings and ‘increased costs against the forecast levels of expenditure in the long-term plans’. These estimates are presented for the timeframe embodied in the period remaining in current council long-term plans and thus extends to 2012/22 from an anticipated start date beginning 2015 and they are supposed to ‘reflect both the timing and cost of transition and the time period over which savings might accrue’.

As we have seen, the authors of Potential Costs and Savings of Local Government Reform in Hawkes Bay (McGredy Winder & Co., 2013b, p.4/5) have added a number of caveats to the estimates they produced in the report. Thus, each structural reform scenario embodies transition costs towards embedding the new organisational arrangements. Without explanation or justification of any kind, it is held that transition costs ‘would generally fall in the first or second year of the transition process’, while ‘potential savings will be more difficult to secure’ and would ‘generally accrue later’. The magnitude of estimated transition costs follows the ‘Auckland experience’, with Potential Costs and Savings of Local Government Reform in Hawkes Bay (McGredy Winder & Co., 2013b, p.5) conceding that this approach might be problematical since ‘the scale of options under consideration in Hawkes Bay is substantially smaller than the Auckland amalgamation’.

A second major caveat concerns the presumption in Potential Costs and Savings of Local Government Reform in Hawkes Bay (McGredy Winder & Co., 2013b, p.4/5) that no ‘differences in, or changes to, the level of service provided’ will occur. Given widespread agreement in the literature that the composition, quality and quantity of local services are invariably affected by substantial structural reform, it is clear this assumption is unwarranted. Even the authors feel compelled to concede that future service provision will be determined
by ‘future political decision-making’, noting that it is ‘premature to second-guess what those decisions might be’.

Thirdly, the financial modelling undertaken in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* (McGredy Winder & Co., 2013b, p.5) has ignored the distributional consequences of structural change to the revenue-raising activities of the new local government entities. The authors note that the report ‘does not address the incidence of rates and what the redesign of a rating system might mean for the residents of the current local authorities’. This omission is also sharply at odds with real-world experience of rating following council amalgamations in Australia. For instance, in his study of the aftermath Moreton Bay Regional Council amalgamation in Queensland over the period 2008 to 2012, Dallinger (2013) found ‘rate harmonisation’ of the pre-merger council rating schedules meant that the new ‘harmonised’ schedules simply embodied the rating levels of the previous highest rating council!

The fourth caveat underlines the fact that cost savings estimates have not taken into account any changes to the capital works program of the merged councils even though they now form part of a new entity. Moreover, *Potential Costs and Savings of Local Government Reform in Hawkes Bay* (McGredy Winder & Co., 2013b, p.5) also leaves depreciation levels unaltered. This necessarily implies that its authors see no rationalisation of capital works expenditure in the new amalgamated entities, despite the fact that a new merged council would obviously require a single headquarters in a designated ‘capital’ centre! The justification for this approach rests on the arguments that if changes to capital work were embodied in the modelling, then this would necessitate ‘a detailed design process and an assessment of the need for each project’, which ‘has not been undertaken’.
More generally, the authors of *Potential Costs and Savings of Local Government Reform in Hawkes Bay* (McGredy Winder & Co., 2013b, p.5) caution that their cost saving estimates ‘have been built up from an activity-by-activity review of the costs of delivering current services and reflect both the scope for making savings and the likely level of costs associated with transition’. It is claimed that while it is ‘highly likely that for some activities there is little or no scope for savings’ in other activities ‘there is scope for savings in the number of people required to deliver the service, but little scope for changing the external costs of delivery’. Furthermore, whereas ‘some activities offer scope to secure savings in both personnel and direct costs’, other areas suggest ‘potential for savings across a number of overhead activities and in management associated with each of the options for reform’. Given that the authors have consulted no empirical literature on the cost savings involved in local government mergers, these assumptions have no empirical support at all and therefore remain mere supposition.

Perhaps as a means of deflecting criticism of their *a priori* approach, the authors (McGredy Winder & Co., 2013b, p.5) note that ‘there has been no authoritative review of the impact of local authority amalgamations within New Zealand’ and speculate that ‘the nature of local authority financial reporting prior to 1989 made it difficult to estimate what would have happened without amalgamations’. However, as we shall demonstrate in Chapter 4 of this Report, a voluminous empirical literature exists on the economic and financial consequences of amalgamation which has exhaustively examined real-world merger episodes across the world, including almost all Australian states, which have local government systems very similar to the New Zealand system. This literature provides invaluable insights into how amalgamation works in practice, as opposed to hypothetical estimates of future outcomes.
The financial model itself employed in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* (McGredy Winder & Co., 2013b, p.6) consisted of a spreadsheet constructed from the current long-term plans of the five Hawkes Bay local government entities. The model is based upon ‘assumptions as to the percentage change in costs for each activity, for each year in the long-term plan after the implementation of the re-organisation’, with different assumptions ‘made relating to the potential for savings in staff costs, non-staff costs, and overheads, in each year of the long-term plan after the commencement date of the reorganisation’.

The model considers 37 different local government activities drawn from the long-term council plans. These are set out in Table 3.1.

<table>
<thead>
<tr>
<th>Table 3.1: Local council activities included in the financial model</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Airports</strong></td>
</tr>
<tr>
<td>Animal control</td>
</tr>
<tr>
<td>Aquatic facilities/pools</td>
</tr>
<tr>
<td>Biosecurity</td>
</tr>
<tr>
<td>Building control</td>
</tr>
<tr>
<td>Bylaws general</td>
</tr>
<tr>
<td>Cemeteries</td>
</tr>
<tr>
<td>Community development</td>
</tr>
<tr>
<td>Economic development</td>
</tr>
<tr>
<td>Emergency management</td>
</tr>
<tr>
<td>Environmental health/food premises</td>
</tr>
<tr>
<td>Environment</td>
</tr>
<tr>
<td>Facilities/venues/halls/arts/museums</td>
</tr>
</tbody>
</table>

With respect to assumptions regarding potential cost savings, *Potential Costs and Savings of Local Government Reform in Hawkes Bay* (McGredy Winder & Co., 2013b, p.6/7) lists the basis for these assumptions as follows:
• ‘comparison of existing cost structure of each council;
• assessment of a number of cost drivers for each activity for each council, how they differ, and the possible scope to migrate toward a more cost effective delivery;
• comparison with the cost structure of other council operations in New Zealand;
• experience of the transition to establish the Auckland Council;
• observation of the issues and challenges that the Auckland Council has had to deal with following amalgamation;
• the management experience of the reviewer;
• the advice of key Hawkes Bay local authority staff from a workshop conducted in May 2013; and
• other research reflecting the potential for savings through scale and different approaches to the purchase of services. In particular, the input assumptions have drawn on the work by Rationale Ltd undertook for the NZTA Procurement Task Group’.

As we have noted, this list is seriously deficient since it does not include the substantial empirical literature on local government amalgamation outside of New Zealand which provides a wealth of material which can much more accurately assist in making plausible assumptions about costs savings.

The data employed in the spreadsheet was drawn from current Hawkes Bay council long-term plans in 2012 and thus extends to 2022. By contrast, ‘cost drivers’ were taken from a variety of sources with differing degrees of accuracy (McGredy Winder & Co., 2013b, p.8):
Cost drivers include the number of staff directly allocated to the activity, and for activities like roading, water and wastewater the length of the network being maintained. Councils were asked to provide a number of cost drivers for each activity. In practice it proved difficult to get a consistent set of cost drivers for each activity. In part this reflects the different business models used by the councils to deliver services (for instance where service delivery is contracted out as opposed to being undertaken by in-house staff). In part this reflects differences in the way that the current councils allocate both staff and costs to activities. Understandably, in the smaller councils where an individual or very small group may play a key role in supervising a number of activities it is difficult to allocate their costs to each activity.

The authors of Potential Costs and Savings of Local Government Reform in Hawkes Bay (McGredy Winder & Co., 2013b, p.8) contend that ‘the value of the cost driver information was to provide an understanding of the cost structure and business models of each of the councils’ which would yield ‘an understanding of the differences between councils, highlighting for instance differences in the cost of information technology systems, and in the cost of processing resource consents between the councils’. However, they point out that ‘the cost driver information is not used directly in the financial model’ but rather it is employed to ‘assist with the assessment of the potential costs and savings associated with reform where it would be possible to change the business model of the new council(s), rationalise activity, etc.’
The authors note a number of deficiencies with the data employed Potential Costs and Savings of Local Government Reform in Hawkes Bay (McGredy Winder & Co., 2013b, p.8). These include the fact that ‘each council has a different approach to the allocation of costs and the definition of activities’, ‘each council use different assumptions relating to inflation and interest rates in their long-term plan’, and for smaller councils overheads were arbitrarily allocated across different functions. The authors dealt with the problem of varying price inflation assumptions by simply using current prices, even though this could severely distort estimates since local government cost escalations seldom approximate consumer price inflation and thus analyses of future councils costs almost always use producer cost escalators, often related to the construction industry.

Potential Costs and Savings of Local Government Reform in Hawkes Bay (McGredy Winder & Co., 2013b, p.9) also experienced difficulties with the allocation of staff and staff costs to different functions. This was tackled by working with the councils to ‘ensure that there is a proper allocation of staff costs and non-staff costs to each activity’.

With respect overheads, the authors adopted the following approach:

Overheads have been grouped by council and dealt with in their own right. The approach to allocating overheads varies by council and the project has been dependent on the data provided by councils to calculate activity expenditure net of overheads and total overhead-related expenditure. Because overheads have been removed from the cost of each activity, the reported expenditure by activity will differ from that shown in the long-term plans.
The most critical foundation of the estimates of cost savings made in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* (McGredy Winder & Co., 2013b, p.10) resides in the 15 ‘key high-level assumptions’ it made. These can be summarised as follows:

6.1. No change to activities delivered by only one Council

6.2. No sale of assets

6.3. No change to capital works

6.4. No change to depreciation

6.5. No change to service levels

6.6. Parts of other councils ignored

6.7. New Councils operational 1 July 2015

6.8. Transition Board and transition costs

6.9. Governance Costs

6.10. Detailed design of new councils not attempted

6.11. Redundancy costs equal first year of salary savings

6.12. Savings in direct costs start in year 2 of operation – or later

6.13. No savings for some activities

6.14. Finance costs

6.15. Activity by activity assumptions

We shall examine the validity of these assumptions in section 3.3 below.
Potential Costs and Savings of Local Government Reform in Hawkes Bay (McGredy Winder & Co., 2013b, Figure 1, p.14) provides a useful breakdown of the composition of expenditure by Hawkes Bay councils by function for the 2012/13 financial year, which is replicated in Figure 3.1.

In addition to its 15 ‘key high-level assumptions’, Potential Costs and Savings of Local Government Reform in Hawkes Bay (McGredy Winder & Co., 2013b, p.14/15) makes a number of further assumptions regarding the transition process in the proposed three mergers scenarios. In general, the authors have presumed that the ‘new transition provisions of the Local Government Act 2002 would apply’ to all three amalgamation models which would involve ‘doing as much as possible in the year before the establishment of any new council to make the transition as smooth as possible’, an approach analogous to the Auckland experience. However, they note that ‘the major difference between the Auckland approach and the sequence proposed here is the timing of the appointment of the interim Chief Executive and the role of the Transition Board’. In terms of costing, it is assumed that ‘the
interim Chief Executive is appointed for each new council very early in the process, contributes to and/or develops the change management plan for approval of the Transition Board and then leads the implementation of the plan’.

In more specific terms, the transition process has been costed in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* (McGredy Winder & Co., 2013b, p.14/15) as follows:

i. The establishment of a Transition Board to supervise the transition process.

ii. Appointment of interim Chief Executive on annual salary.

iii. Development of a change management plan to guide transition process.

iv. Creating a human resources team to help design new entity, select and appoint staff, etc.

v. Select and migrate to one to a current council finance system.

vi. Select and migrate to other necessary business systems.

vii. Integrate records of merging councils.

viii. Appointment of ‘second-tier’ managers for merged entity.

ix. Recruitment of staff and payment of legal costs, branding, etc., for new entity.

x. 2% of the annual cost of staff as a one off and on-going change in remuneration ‘to harmonise staff salaries and conditions’.

xi. No allowance has been made for the costs of housing the Transition Board and its operation.
Potential Costs and Savings of Local Government Reform in Hawkes Bay (McGredy Winder & Co., 2013b, p.15) added an important caveat to its costing methodology for transitional costs, observing that ‘it is very difficult to estimate transition costs without fully understanding the nature of the existing staff, business systems and business processes within each council’. As a consequence, its estimates ‘are probably best regarded as indicative of the sort of costs that will be incurred and their order of magnitude’. We shall examine its transition cost estimation process in more detail in the light of the recent experience of comparable groups of forcibly merged councils in Queensland in section 3.4.

With respect to the estimation of governance costs in Potential Costs and Savings of Local Government Reform in Hawkes Bay (McGredy Winder & Co., 2013b, p.15), its authors identified two possible approaches:

Apart from the number of elected representatives there are two possible approaches to estimating the levels of remuneration that would be paid. One approach would be to assume that the governance role within the region does not change under any of the scenarios and to therefore leave the current pool of funds allocated by the Remuneration Authority unchanged. The second is to assume levels of remuneration for the governance roles that reflect the sort of payments that the Remuneration Authority makes to members in similar roles in similar sized councils. The estimated costs here reflect the second approach.
Chapter 6 will examine in more detail the estimated governance costs in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* and more particularly its claims surrounding the costs and representational equity of community boards.

After applying its methodology and relisted plethora of assumptions, *Potential Costs and Savings of Local Government Reform in Hawkes Bay* (McGredy Winder & Co., 2013b, Table E1, p.3) produced cost estimates for the three structural change scenarios A, B and C which are summarised in Table 3.2.

**Table 3.2: Summary of Cost Estimates for Scenarios A, B and C**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Combined Total Expenditure from LTPs (Uninflated) ($000s)</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Scenario A</td>
<td>283,861</td>
<td>287,720</td>
<td>296,763</td>
<td>298,305</td>
<td>296,300</td>
<td>300,610</td>
<td>302,758</td>
<td>296,694</td>
<td>350,610</td>
<td>301,857</td>
<td>2,147,196</td>
</tr>
<tr>
<td>Scenario C</td>
<td>283,861</td>
<td>287,720</td>
<td>302,393</td>
<td>293,472</td>
<td>297,588</td>
<td>299,728</td>
<td>293,697</td>
<td>347,646</td>
<td>298,847</td>
<td>2,131,113</td>
<td></td>
</tr>
</tbody>
</table>

| **Combined Total Expenditure by Scenario ($000)** |         |         |         |         |         |         |         |         |         |         |             |
| Scenario B           | 283,861 | 287,720 | 302,068 | 287,972 | 292,064 | 294,204 | 288,203 | 342,120 | 293,339 | 2,098,986 |
| Scenario C           | 283,861 | 287,720 | 302,393 | 293,472 | 297,588 | 299,728 | 293,697 | 347,646 | 298,847 | 2,131,113 |

| **Combined Total Net Savings by Scenario ($000)** |         |         |         |         |         |         |         |         |         |         |             |
| Scenario A           | 0       | 0       | -6,575  | -3,840  | 10,337  | 10,390  | 10,627  | 10,569  | 10,648  | 10,597  | 59,328      |
| Scenario B           | 0       | 0       | -5,305  | -2,780  | 8,329   | 8,546   | 8,555   | 8,491   | 8,551   | 8,518   | 48,210      |
| Scenario C           | 0       | 0       | -5,630  | -1,830  | 2,828   | 3,022   | 3,030   | 2,997   | 3,025   | 3,010   | 16,083      |

**Combined Total Net Savings as a percentage of Total Expenditure by Scenario ($000)**

| Scenario A           | 0.0%    | 0.0%    | -2.2%   | -1.3%   | 3.5%    | 3.5%    | 3.5%    | 3.6%    | 3.0%    | 3.5%    | 2.8%        |
| Scenario B           | 0.0%    | 0.0%    | -1.8%   | -0.9%   | 2.8%    | 2.8%    | 2.8%    | 2.9%    | 2.4%    | 2.8%    | 2.2%        |
| Scenario C           | 0.0%    | 0.0%    | -1.9%   | -0.6%   | 1.0%    | 1.0%    | 1.0%    | 1.0%    | 0.9%    | 1.0%    | 0.7%        |
3.3 Assessment of Potential Costs and Savings of Local Government Reform

As we have seen, the cost estimates contained in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* rest on a multitude of assumptions of varying degrees of plausibility. If some or all of these assumptions do not accurately reflect real-world structural change in local government, then this necessarily implies that its cost estimates will be inaccurate and thus cannot form the basis for sound public policy making.

A vivid illustration of how misleading financial modelling using assumptions can be (rather than using real-world experience) has been uncovered by Drew and Dollery (2013) in their analysis of the financial consequences of the forced amalgamation and then subsequent de-amalgamation of Noosa Shire Council, Caloundra City Council and Maroochy Shire Councils as part of the broader 2008 Queensland local government amalgamation program. In 2008 Noosa Shire Council, Caloundra City Council and Maroochy Shire Council were compulsorily merged into a new Sunshine Coast Regional Council (SCRC). Five years on, unyielding public opposition and a new Queensland Government secured the de-amalgamation of Noosa Shire from the Sunshine Coast Regional Council. As part of their financial analysis, Drew and Dollery (2013) examined the 2007 financial statements of the three former constituent councils and then the consequences of amalgamation on the predicted and actual financial outcomes for the councils involved.

In particular, they examined operating results before and after amalgamation. The combined operating results of the three councils prior to amalgamation were: surplus of $152.8m in 2007, $159.05m surplus in 2006 and $160.78m surplus in 2005. Operating results for SCRC in subsequent years were $126m surplus (2010 financial year), $372m deficit (2011 financial
year) and $80m surplus (2012 financial year), excluding asset revaluations. This contrasts starkly with the Queensland Treasury Corporation (QBC 2009; p.2012) financial modelling which forecast significant savings from amalgamation largely from scale economies!

The underlying assumptions of the *Potential Costs and Savings of Local Government Reform in Hawkes Bay* financial modelling can also be criticised on the grounds that the assumptions may have been selected to present the program in its ‘best light’. In other words, it is possible that certain assumptions may have been chosen in order to make the program ‘look more appealing’. While this is not a criticism of the method *per se*, the authors should have conducted a sensitivity analysis of Scenario A, Scenario B, and Scenario C.

In essence, a sensitive analysis – which is based on making plausible changes to the financial model’s underlying assumptions – is used to estimate ‘worst case’ and ‘best case’ scenarios. It is surprising that the authors did not present ‘worst case’ and ‘best case’ estimates for Scenarios A, B, and C, especially given that it is standard practice to do so when undertaking a cost-benefit analysis of competing policy options. In the absence of a sensitivity analysis it is difficult to gauge the robustness of the proposed cost savings (and how sensitive these proposed savings may be to either large or small changes in the underlying assumptions).

The financial modelling presented in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* also ignores equity issues. It is unclear who bears the incidence of the costs and benefits accrued under Scenarios A, B and C? In other words, are the associated cost and benefits of the proposed amalgamation borne equally among residents? Who are the
‘winners’ and ‘losers’? If the benefits and costs are borne unequally, should the ‘winners’ compensate the ‘losers’? Unfortunately, these important policy questions have not been canvassed in *Potential Costs and Savings of Local Government Reform in Hawkes Bay*.

Finally, it is important to note that the financial analysis presented in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* is compared with an alternative scenario based on an estimate of what would have happened in the absence of council amalgamations (i.e., the base case). While the base case (i.e., retaining the existing structure and number of councils) represents the current situation, it is highly likely that some changes would have occurred during this period. Thus, the evaluation of costs savings in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* is based on a comparison of two uncertain forecast scenarios!

**3.4 Assessment of Estimated Transition Costs in Potential Costs and Savings**

*Potential Costs and Savings of Local Government Reform in Hawkes Bay* (McGredy Winder & Co., 2013b, pp.14/15) has a section devoted to the estimation of the costs of transition for the three structural change scenarios. In short, its authors project the following transition costs:

- **Scenario A**: $10.4m plus $1.25m p.a. of costs associated with ‘harmonising’ staff
- **Scenario B**: $8.1m and $1m p.a. of costs associated with ‘harmonising’ staff
- **Scenario C**: $7.5m and $1m p.a. of costs associated with ‘harmonising’ staff
Potential Costs and Savings of Local Government Reform in Hawkes Bay (McGredy Winder & Co., 2013b, pp.14/15) sets out the numerous assumptions which underpin these estimates. For example, it is presumed that ‘the new transition provisions of the Local Government Act 2002 would apply’ and the process ‘would involve doing as much as possible in the year before the establishment of any new council to make the transition as smooth as possible’. It is further assumed that ‘an interim Chief Executive is appointed for each new council very early in the process, contributes to and/or develops the change management plan for approval of the Transition Board and then leads the implementation of the plan’.

As we have seen, the following elements comprise the transition costs in Potential Costs and Savings of Local Government Reform in Hawkes Bay (McGredy Winder & Co., 2013b, p.14/15):

xii. The establishment of a Transition Board to supervise the transition process.

xiii. Appointment of interim Chief Executive on annual salary.

xiv. Development of a change management plan to guide transition process;

xv. Creating a human resources team to help design new entity, select and appoint staff, etc.

xvi. Select and migrate to one to a current council finance system.

xvii. Select and migrate to other necessary business systems.

xviii. Integrate records of merging councils.

xix. Appointment of ‘second-tier’ managers for merged entity.

xx. Recruitment of staff and payment of legal costs, branding, etc., for new entity.
xxi. 2% of the annual cost of staff as a one off and on-going change in remuneration ‘to harmonise staff salaries and conditions’.

xxii. No allowance has been made for the costs of housing the Transition Board and its operation.

It is important to reflect on what potentially expensive costs are not included in this list. In the first place, in terms of direct costs, ‘no allowance has been made for the costs of housing the Transition Board and its operation’ which could be housed within one of the existing council buildings. Similarly, no consideration is given to the establishment of a ‘capital’ centre from which the council will be run and the multitudinous costs associated with moving people and property to this new centre, as well as the costs of leases and other contracts on buildings and machines which will no longer be required.

Secondly, no indirect costs are considered, such as the inevitable loss of skilled workers as a consequence of employment uncertainties, the fall in staff morale and associated productivity losses, and so forth. The authors of Potential Costs and Savings of Local Government Reform in Hawkes Bay (McGredy Winder & Co., 2013b, p.15) candidly admit that ‘it is very difficult to estimate transition costs without fully understanding the nature of the existing staff, business systems and business processes within each council’ and as a result ‘the estimates that have been made here are probably best regarded as indicative of the sort of costs that will be incurred and their order of magnitude.

Some idea of the wildly arbitrary nature of projected transition costs for council mergers can be gleaned from hard-won experience in the Queensland amalgamation program in 2008. For instance, in its review of the 2008 Queensland experience with amalgamations, the
Queensland Treasury Corporation gathered estimates from merged councils on the costs of their amalgamation at that stage. These are set out in Table 3.3.

Table 3.3: Amalgamation Queensland Council Estimates of Costs of Mergers

<table>
<thead>
<tr>
<th>Council</th>
<th>Estimated Costs by Council (AUD$)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bundaberg</td>
<td>14,705,273</td>
</tr>
<tr>
<td>Cairns Regional</td>
<td>N/A</td>
</tr>
<tr>
<td>Central Highlands</td>
<td>21,533,762</td>
</tr>
<tr>
<td>Charters Towers</td>
<td>1,268,268</td>
</tr>
<tr>
<td>Gladstone</td>
<td>15,316,400</td>
</tr>
<tr>
<td>Goondiwindi</td>
<td>7,117,277</td>
</tr>
<tr>
<td>Gympie</td>
<td>2,282,366</td>
</tr>
<tr>
<td>Isaac</td>
<td>12,112,850</td>
</tr>
<tr>
<td>Lockyear Valley</td>
<td>3,647,603</td>
</tr>
<tr>
<td>Logan City</td>
<td>4,884,647</td>
</tr>
<tr>
<td>Mackay</td>
<td>7,575,854</td>
</tr>
<tr>
<td>Maranoa</td>
<td>2,682,547</td>
</tr>
<tr>
<td>North Burnett</td>
<td>7,341,912</td>
</tr>
<tr>
<td>Rockhampton</td>
<td>6,520,353</td>
</tr>
<tr>
<td>Scenic Rim</td>
<td>12,634,356</td>
</tr>
<tr>
<td>Somerset</td>
<td>2,523,929</td>
</tr>
<tr>
<td>South Burnett</td>
<td>5,286,920</td>
</tr>
<tr>
<td>Southern Downs</td>
<td>5,104,919</td>
</tr>
<tr>
<td>Sunshine Coast</td>
<td>13,720,844</td>
</tr>
<tr>
<td>Tablelands</td>
<td>10,751,120</td>
</tr>
<tr>
<td>Toowoomba</td>
<td>10,152,954</td>
</tr>
<tr>
<td>Townsville</td>
<td>3,980,997</td>
</tr>
<tr>
<td>Western Downs</td>
<td>8,113,510</td>
</tr>
<tr>
<td>Whitsunday</td>
<td>7,235,105</td>
</tr>
<tr>
<td>TOTAL</td>
<td>186,493,766</td>
</tr>
<tr>
<td>Mean</td>
<td>8,108,425</td>
</tr>
<tr>
<td>Median</td>
<td>7,235,105</td>
</tr>
</tbody>
</table>


As we can see from Table 3.3, transition costs had amounted to a mean of AUD 8,108,425 (and $184.71 million in total) by 2009! Moreover, at this early stage many costs were still recurring. Given the prohibitively high costs of amalgamation, exponents of forced amalgamation for the Hawkes Bay Region should make clear who will pay for the proposed amalgamation program: New Zealand taxpayers or Hawkes Bay Region ratepayers?
3.5 Concluding Remarks

As we have seen in Chapter 3, the cost savings estimates provided in Potential Costs and Savings of Local Government Reform in Hawkes Bay are far from convincing. It would thus be most unwise for the New Zealand Local Government Commission and other local government policy makers to base policy recommendations on these estimates.

Perhaps the most striking problem with the cost savings estimates in Potential Costs and Savings of Local Government Reform in Hawkes Bay is the fact that they entirely ignore the claims made in Future Prosperity of the Hawkes Bay Region which centred on the primacy of effective regional leadership as the main driver of regional development in the Hawkes Bay Region. As we saw in Chapter 2, Future Prosperity of the Hawkes Bay Region (McGredy Winder & Co., 2013a, p.48) claimed that ‘leadership’ as by far the most ingredient for a prosperous future for the Hawkes Bay Region. Given the pivotal importance attached to leadership, it is thus most surprising that Potential Costs and Savings of Local Government Reform in Hawkes Bay made no attempt to provide empirical validation for this far-reaching claim.

A second fundamental problem with Potential Costs and Savings of Local Government Reform in Hawkes Bay is that it nowhere seeks external validation for the accuracy of its projected cost savings. The best method of doing this would have been for its authors to examine previous amalgamation episodes in Australian and New Zealand local government and then compare projected costs savings pre-amalgamation with actual realised cost savings post-amalgamation. As we have seen in section 3.3, Drew and Dollery (2013) conducted an exercise of this kind for the SCRC in Queensland which found stark differences between
projected and realised cost savings. In addition, as we shall see in Chapter 4, had the authors of *Potential Costs and Savings of Local Government Reform in Hawkes Bay* bothered to consult the findings of numerous public inquiries into the effects of amalgamation in the different Australian state local government systems, they would have found that claims of cost savings and other pecuniary gains from amalgamation were almost never realised in practice.

Third, it is very difficult to assess the robustness of the purported cost saving presented in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* because the authors failed to conduct a sensitivity analysis of their alternative cost savings scenarios. In essence, this means that policy makers have no estimate of either a ‘worst case’ or ‘best case’ scenario. The omission of a sensitivity analysis is somewhat surprising given the inherent uncertainty surrounding the costs and benefits associated with local government consolidation.

Finally, it is important to stress the cost saving presented in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* is based on an estimate of what would have happened in the absence of council amalgamations (i.e., the base case). Although the base case represents the ‘status quo’ it needs to be borne in mind the some changes (including cost savings) may have happened during this period. Therefore, one needs to be cognisant of the fact that the reported cost savings are based on a comparison of two uncertain forecast scenarios!
CHAPTER 4: CONCEPTUAL AND EMPIRICAL EVIDENCE ON AMALGAMATION

4.1 Introduction

In Chapter 2 of this Report, we saw that the authors of *Future Prosperity of the Hawkes Bay Region* examined 13 policy options for reform in the Hawkes Bay Region, which included improving the performance of local government. Six options were considered as specific methods of enhancing the operation of local government: ‘Shared Services; More Effective Collaboration and a Hawkes Bay Plan; Key investments; Increased Regional Role – Transfer of Responsibilities; Rural Amalgamation; and Regional Amalgamation’.

After evaluating these six options, *Future Prosperity of the Hawkes Bay Region* recommended the amalgamation of the Central Hawkes Bay District Council, Hastings District Council, Napier City Council, Wairoa District Council and the Hawkes Bay Regional Council. However, as we saw in Chapter 2, the analysis in the *Future Prosperity of the Hawkes Bay Region* was severely flawed in several respects, not least because it entirely ignored available empirical evidence on council amalgamation, scale economies in local government and shared services in local government.

In its municipal amalgamation recommendations, *Future Prosperity of the Hawkes Bay Region* followed a depressingly well-trodden path. Historically both Australian and New Zealand governments have repeatedly employed structural reform programs of different degrees of intensity which have almost invariably involved compulsory council consolidation. Thus in New Zealand the post-war period can be divided into three main phases of local government structural reform (Reid, 2013). Over the period 1946 to 1989,
phase 1 saw structural change in local government centred chiefly on removal of single purpose local bodies and the formation of councils as multi-functional bodies with adequate capacity to employ suitably qualified staff and maintain satisfactory local infrastructure. Phase 2 from 1989 to 2012 witnessed important changes made to the Local Government Commission rules, including enhancing the capacity of local communities to reject amalgamation proposals. It witnessed only the Nelson Marlborough Regional Council disbanded, with Nelson City Council, Marlborough District Council and Tasman District Council joining Gisborne District Council as unitary authorities. However, in 2009, the Commissioners recommended the creation of a unitary authority – the Auckland Council – to assume all local government responsibilities previously held by the (then) eight councils in the Auckland metropolitan area. It had a two-tier representation model: an elected Auckland Council and six elected local councils. Phase 3 saw the enactment of Local Government Act 2002 Amendment Act 2012 which introduced a new era for structural reform in New Zealand. If amalgamation proceeds in the Hawkes Bay Region, then it will form part of structural reform ushered in under the new legislation.

Australia has seen even more draconian forced amalgamation. Over the past twenty years, New South Wales, Victoria, Queensland, South Australia, Tasmania and the Northern Territory have all witnessed extensive municipal restructuring. To date, Western Australia is the only local government jurisdiction to have escaped forced amalgamation. However, it is presently implementing its *Metropolitan Local Government Review Final Report* recommendations which proposed *inter alia* a radical reduction in the number of local authorities in the Greater Perth metropolitan region to a mere 12 local entities.
The Australian and New Zealand local government systems share a great deal in common, especially their comparatively narrow focus on ‘services to property’, and can be readily distinguished in terms of their functional operations from their counterparts in other developed countries. It thus seems clear that the ongoing concentration on amalgamation as the primary policy instrument for local government reform in Australia and New Zealand underlines the traditional view of Antipodean local government policy makers that ‘bigger is better’ in local government (Dollery and Crase, 2006).

However, despite the ubiquitous use of mergers in Australian and New Zealand local government, amalgamation remains contentious (see, for instance, Dollery, Grant and Kortt, 2012). Advocates of amalgamation 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 consolidation typically underline the divisive nature of amalgamations, the absence of supportive empirical evidence, the equivocal outcomes observed in case studies, and the diminution of local democracy.

In addition, 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). Against this background, Chapter 4 considers conceptual and empirical evidence on the controversial question of amalgamation in local government as a means of assessing the viability of the council amalgamation program proposed in *Future Prosperity of the Hawkes Bay Region*. 
Chapter 4 is divided into four main parts. Section 4.2 describes the historical scale of municipal mergers in New Zealand and Australia and compares the current size of Antipodean councils with their counterparts in other advanced countries. Section 4.3 provides a synoptic account of the international and Antipodean scholarly research on local government consolidation. Section 4.4 considers the effects of 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. Chapter 4 ends with some brief concluding remarks in section 4.5.

4.2 Local Government Amalgamation in New Zealand and Australia

4.2.1 New Zealand

As we have seen, Reid (2013) has argued that structural reform in New Zealand the post-war period involves three main phases. Phase 1 constitutes the period between the creation of the Local Government Commission in 1946 and the wide-ranging restructuring of the local government sector which occurred in 1989. Phase 2 comprises the period between 1989 and the close of 2012 in which amalgamation provisions in the legislation were amended. Phase 3 arises with the new amalgamation provisions adopted with the Local Government Act 2002 Amendment Act 2012.
**Table 4.1: Number of local councils in New Zealand, 1946 to 2012**

<table>
<thead>
<tr>
<th>Phase</th>
<th>Type</th>
<th>Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>Phase I: Pre-1989</td>
<td>Territorial authorities*</td>
<td>217</td>
</tr>
<tr>
<td></td>
<td>Regional authorities</td>
<td>22</td>
</tr>
<tr>
<td></td>
<td>Special purpose</td>
<td>453</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>692</td>
</tr>
<tr>
<td>Phase 2: 1989-2012</td>
<td>Territorial authorities*</td>
<td>74</td>
</tr>
<tr>
<td></td>
<td>Regional councils</td>
<td>13</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>87</td>
</tr>
</tbody>
</table>

Source: Adapted from Reid (2013, Table 4).

* Includes unitary councils, which are territorial authorities with regional council functions.

Table 4.1 illustrates the drastic reduction in the number of councils in New Zealand in the post-1946 era. However, despite this decrease, and the concomitant rise in the average population of New Zealand councils, calls for further structural change continued unabated, including in the Hawkes Bay Region.

**4.2.1 Australia**

Structural reform – or more specifically forced amalgamation – has been the most common method of reform applied to Australian local government since Federation in 1901 (Dolley, Grant and Kortt, 2012). Table 4.2 summarises the effects of compulsory consolidation on local council numbers over time.

**Table 4.2: Number of local councils in Australia, 1910 to 2012**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>NSW</td>
<td>324</td>
<td>224</td>
<td>175</td>
<td>176</td>
<td>177</td>
<td>152</td>
<td>152</td>
</tr>
<tr>
<td>VIC</td>
<td>206</td>
<td>210</td>
<td>211</td>
<td>210</td>
<td>184</td>
<td>79</td>
<td>79</td>
</tr>
<tr>
<td>QLD</td>
<td>164</td>
<td>131</td>
<td>134</td>
<td>134</td>
<td>125</td>
<td>73</td>
<td>73</td>
</tr>
<tr>
<td>SA</td>
<td>175</td>
<td>142</td>
<td>127</td>
<td>n/a</td>
<td>119</td>
<td>68</td>
<td>68</td>
</tr>
<tr>
<td>WA</td>
<td>147</td>
<td>144</td>
<td>138</td>
<td>138</td>
<td>144</td>
<td>142</td>
<td>139</td>
</tr>
<tr>
<td>TAS</td>
<td>51</td>
<td>49</td>
<td>49</td>
<td>46</td>
<td>29</td>
<td>29</td>
<td>29</td>
</tr>
<tr>
<td>NT</td>
<td>0</td>
<td>1</td>
<td>6</td>
<td>22</td>
<td>63</td>
<td>16</td>
<td>16</td>
</tr>
<tr>
<td>TOTAL</td>
<td>1,067</td>
<td>901</td>
<td>840</td>
<td>726</td>
<td>841</td>
<td>559</td>
<td>556</td>
</tr>
</tbody>
</table>

A striking feature of Table 4.2 resides in the fact that the aggregate number of councils in Australia has decreased from 1,067 to 556 (a 48% decline) between 1910 and 2012. 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 persons per council – has increased markedly. For example, the average size of councils nationally has grown from 4,147 persons per council to 40,118 persons per council between 1910 and 2012 (Dolley, Grant and Kortt, 2013).

In the amalgamation debate, it is important to consider New Zealand and Australian local government from an international perspective. How does the population average size of New Zealand and Australian councils compare with other advanced countries? Table 4.3 sheds light on this question by providing an international comparison of average council size in 2007. Of the 18 countries listed in Table 4.3, the UK 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, New Zealand has the third largest councils and Australia has the fourth largest councils. Put differently, New Zealand and Australian councils are already large by the standards of other advanced countries.
### Table 4.3: An international comparison of average council size, 2007

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

Source: Adapted from Callanan, Murphy and Quinlivan (2012)

*Number of persons per council

### 4.3 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 (2004; 2006), 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 Mieleczarek (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 Ceunineck et al. (2010) concluded that council mergers had not met expectations.
The bulk of Antipodean evidence on the outcomes of amalgamation programs in state and territory local government systems derives largely from Australian public inquiries into local government. As we shall see in section 4.4, a host of recent Australian national and state inquiries into municipal financial sustainability has established that numerous councils in all Australian local government jurisdictions still face daunting financial problems, despite amalgamation. In the light of these findings, Dollery, Byrnes and Crase (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 statewide data. For example, Drew, Kortt and Dollery (2013a) 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 (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 mergers evaporates.

Similarly, Drew, Kortt and Dollery (2013b) 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 the evidence in favour of scale economies disappears.

4.4 Assessment of Australian Amalgamation Programs


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

While the overwhelming emphasis in most of these public inquiries fell squarely on financial sustainability *per se* in local government, many of the 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.

### 4.4.1 Hawker Inquiry (2003)

A striking feature of the Hawker Report (2003) *Rates and Taxes: A Fair Share for Responsible Local Government* (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’.

### 4.4.2. 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’ (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 South Australian 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.

4.4.3 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’ (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’.

4.4.4 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.
4.4.5 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’.


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’. 

87
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.

4.4.7 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.

4.4.8 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* (Dolley, 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.

4.5 Conclusion

Chapter 4 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 New Zealand and Australian stress on council mergers has been 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 Australian 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.

However, 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.
CHAPTER 5: ECONOMETRIC ANALYSIS OF PROPOSED AMALGAMATIONS

5.1 Introduction

In Chapter 5 an econometric analysis is conducted to determine whether there is a statistically significant association between population size and local government expenditure for Central Hawkes Bay District Council (CBDC), Hastings District Council, Napier City Council and Wairoa District Council. If economies of scale are not present, then the case for amalgamation is seriously weakened. Moreover, from a policy perspective, there would be no reason to believe that the proposed cost-savings – as advanced in Potential Costs and Savings of Local Government Reform in Hawkes Bay – would be realised.

Against this background, we forensically examine the relationship between population size and per capita expenditure for the councils of Central Hawkes Bay, Hastings, Napier, and Wairoa using a 10 year panel data set covering the period 2003 to 2012. In conducting our econometric analysis, we explicitly assessed the proposed merger option of creating a single territorial authority by amalgamating Central Hawkes Bay, Hastings, Napier, and Wairoa councils. In sum, our econometric analysis reveals that there is no statistically significant relationship between population size and per capita expenditure. Thus, from a policy perspective, there is no empirical reason to believe that the proposed mergers as canvassed in Potential Costs and Savings of Local Government Reform in Hawkes Bay will result in any significant cost-savings.
Chapter 5 is comprised of four main parts. Section 5.2 will provide a synoptic review of the concept and measurement of economies of scale. Section 5.3 will describe the data source, econometric model, and the empirical strategy employed. The results along with the discussion are presented in section 5.4. Chapter 5 concludes with some brief remarks in section 5.5.

5.2 Economies of Scale in Local Government

Economies of scale play a central role in the debate on structural reform in local government. Expressed differently, structural reform is predicated on the notion that larger councils are more efficient than smaller councils (Faulk and Hicks, 2011). Claims of ‘bigger is cheaper’ and ‘bigger means better services’ rest squarely on the assumption that the delivery of local government services is characterised by substantial scale economies (Dollery, Crase and Johnson, 2006).

Advocates of council amalgamations typically argue that larger councils servicing a larger population will benefit from, among other things, lower administrative costs and improved use of equipment (Andrews and Boyne, 2009; Dollery, Byrnes and Crase, 2008). On the other hand, opponents of council amalgamations argue that smaller councils are less bureaucratic, compete enthusiastically with each other and, as a result, usually display a lower cost profile (Boyne, 1995).

In general, it would appear that labour-intensive services, such as health inspection, would generate few economies of scale because an increased volume of services will require a larger number of health inspectors. On the other hand, capital-intensive services, such water and
sewerage networks, may yield substantial economies of scale since the fixed costs can be spread across a greater number of households (Dollery, Crase and Johnson, 2006).

Nevertheless, it is important to note that the current body of research on economies of scale in the context of local government is mixed and ultimately inconclusive (Byrnes and Dollery 2002; Dollery, Grant, and Kortt, 2012). Although the evidence is inconclusive it does suggest that while amalgamations may enhance the administrative and technical capacity of municipalities, it is not only costly but has other adverse consequences, such as the loss of ‘local identity’, ‘local voice’, and ‘local choice’ (Andrews and Boyne, 2009; Dollery, Crase and Johnson, 2006).

To determine whether economies of scale exist, the empirical literature typically estimates the association between local government output (typically measured in terms of population size) and the cost of local government service provision (typically measured in terms of per capita expenditure). However, population size has been criticised as being a poor proxy for output because local government areas with similar sized populations may exhibit quite distinct economic and social characteristics. Although population size may be a crude proxy for output, finding precise measures of local government outputs is fraught with considerable difficulty (Andrews and Boyne, 2009). Even in the event that separate output measures were readily available, it is far from clear whether these measures could be combined to produce a meaningful local government output index. Nevertheless, population size is often used in empirical studies because:

- It provides a simple and transparent proxy for total output; and
- It is typically the focus in policy debates about local government amalgamation.
Thus, in the current context, *economies of scale* refer to the impact of population size on per capita expenditure. Therefore, if a larger population size is associated with lower per capita expenditure, then scale economies are said to exist. On the other hand, if a larger population is associated with high per capita expenditure, then diseconomies of scale are said to exist.

### 5.3 Data and Empirical Strategy

The dataset employed in Chapter 5 contains an extensive range of information on the following New Zealand councils, including details on expenditure, income, rates, employee costs, population size, and population density:

- Central Hawkes Bay District Council
- Hastings District Council
- Napier City Council
- Wairoa District Council
- Hawkes Bay Regional Council.

The data was used to create a panel dataset consisting of the councils of Central Hawkes Bay, Hastings, Napier, and Wairoa ($n = 4$) covering the 10 year period from 2003 to 2013 ($T = 10$). Thus, our analytical sample consists of 40 observations (i.e., $nT = 40$). This dataset was used to assess the proposed merger of Central Hawkes Bay, Hastings, Napier, and Wairoa councils. While our principal focus is to examine the association between population size and council expenditure, we also investigated the relationship between population size and income, rates and employee costs in an effort to determine whether there may be any other potential benefits associated with council consolidation.
It is also important to note that our econometric analysis excludes the Hawkes Bay Regional Council because: (i) the population size this ‘regional council’ is the sum of Central Hawkes Bay, Hastings, Napier, and Wairoa councils; and (ii) any potential economies of scale would be reaped by amalgamating the populations of Central Hawkes Bay, Hastings, Napier, and Wairoa councils.

5.3.1 Dependent Variables

Against this background, the following dependent variables were used in our econometric analysis:

- The log of per capita operating expenditure;
- The log of per capita income;
- The log of per capita rates; and
- The log of per capita employee costs.

All dependent variables were converted into 2012 dollars using the New Zealand Consumer Price Index to remove the effects of inflation.

5.3.2 Independent Variables

The independent variables used in our econometric analysis were:

- Population size;
- Population density;
- Councils; and
- Time.
Population size was measured as the number of people residing in each local government area, while population density was measured as the number of people per square kilometre. Dummy variables were used to classify councils into relevant groups (with Napier City Council selected as the excluded reference group). Finally, time was divided into 10 categories (1 = 2003; 2 = 2004; 3 = 2005; 4 = 2006; 5 = 2007; 6 = 2008; 7 = 2009; 8 = 2010; 9 = 2011; 10 = 2012), with the year 2003 selected as the excluded reference group.

Inclusion of the council and time dummy variables is particularly important in the current context because the:

- Council dummy variables capture the effects of omitted variables like ‘cultural norms’ that are constant over time but vary across local government areas; and
- Time dummy variables capture the effects of omitted variables, such as ‘central government regulations’, which are constant across councils but vary over time.

In other words, these ‘council fixed effects’ and ‘time fixed effects’ allow us to reduce the bias arising from both unobserved variables that are constant over time and across local government areas.

5.3.3 Empirical Strategy

To estimate the relationship between local government finances and population size, we adopted a conventional multiple linear regression framework:

\[ Y_{it} = \beta_1 P_{it} + \beta_2 C_{it} + \beta_3 T_{it} + \mu_{it} \]  

(1)
In Equation (1), $Y_{it}$ is either: (i) the log of per capita operating expenditure; (ii) the log of per capita income; (iii) the log of per capita rates; or (iv) the log of per capita employee costs. The subscripts $i$ and $t$ are for council and year, respectively. $P_{it}$ is a vector of population variables (i.e., population size and population density), $C_{it}$ are council dummy variables, $T_{it}$ are time dummy variables, and $\mu_{it}$ is the error term.

With respect to the dummy variables, it is important to note that they measure the influence on the dependent variable of a subject being in one category rather than being in the excluded reference category. All results were estimated using ordinary least squares (OLS). Given that we observed the same councils over multiple waves, our standard errors are clustered at the council-level so as to account for within-council serial correlation.

### 5.4. Discussion of Results

#### 5.4.1 Summary Statistics

In Table 5.1 we report the summary statistics – mean, median, standard deviation (SD), minimum, and maximum – for per capita expenditure, per capita income, per capita rates, per capita employee costs, population size and population density for the four councils covering the period 2003 to 2012. Looking across Table 5.1, the following points are worth noting. To begin with, Wairoa has the highest expenditure per capita (mean = $2,061.71; SD = $381.37) while Hastings has the lowest expenditure per capita (mean = $1,015.45; SD = $158.84). With respect to income, Wairoa receives the highest per capita income (mean = $2,043.75; SD = $412.93) while Hastings receives the lowest per capita income (mean = $1,039.41; SD = $104.77). A similar pattern emerges with respect to rates. Wairoa has the highest rates per
capita (mean = $928.38; SD = $169.64) while Hastings has the lowest rates per capita (mean = $260.35; SD = $85.06). However, in terms of employee costs, Napier has the highest costs per capita (mean = $342.54; SD = $87.75) while CHBC has the lowest cost per capita (mean = $181.81; SD = $37.73).

Table 5.1: Summary Statistics for select New Zealand councils, 2003 to 2012

<table>
<thead>
<tr>
<th>Council</th>
<th>Mean</th>
<th>Median</th>
<th>SD</th>
<th>Min.</th>
<th>Max.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Napier: Expenditure p/c</td>
<td>$1,120.48</td>
<td>$1,191.35</td>
<td>$176.49</td>
<td>$832.06</td>
<td>$1,315.88</td>
</tr>
<tr>
<td>Income p/c</td>
<td>$1,273.01</td>
<td>$1,325.39</td>
<td>$182.43</td>
<td>$924.26</td>
<td>$1,475.86</td>
</tr>
<tr>
<td>Rates p/c</td>
<td>$675.72</td>
<td>$685.16</td>
<td>$78.23</td>
<td>$551.41</td>
<td>$775.78</td>
</tr>
<tr>
<td>Employee cost p/c</td>
<td>$342.54</td>
<td>$373.53</td>
<td>$87.75</td>
<td>$216.18</td>
<td>$436.78</td>
</tr>
<tr>
<td>Population Size</td>
<td>56,970</td>
<td>56,950</td>
<td>651.58</td>
<td>55,900</td>
<td>57,800</td>
</tr>
<tr>
<td>Population Density</td>
<td>537.45</td>
<td>537.26</td>
<td>6.15</td>
<td>527.36</td>
<td>545.28</td>
</tr>
<tr>
<td>Wairoa: Expenditure p/c</td>
<td>$2,061.71</td>
<td>$1,977.23</td>
<td>$381.37</td>
<td>$1,614.33</td>
<td>$2,774.94</td>
</tr>
<tr>
<td>Income p/c</td>
<td>$2,043.75</td>
<td>$2,020.48</td>
<td>$412.93</td>
<td>$1,569.44</td>
<td>$2,909.46</td>
</tr>
<tr>
<td>Rates p/c</td>
<td>$928.38</td>
<td>$928.97</td>
<td>$169.64</td>
<td>$726.90</td>
<td>$1,199.88</td>
</tr>
<tr>
<td>Employee cost p/c</td>
<td>$287.21</td>
<td>$295.92</td>
<td>$88.14</td>
<td>$166.56</td>
<td>$489.07</td>
</tr>
<tr>
<td>Population Size</td>
<td>8,692</td>
<td>8,530</td>
<td>457.04</td>
<td>8,140</td>
<td>9,720</td>
</tr>
<tr>
<td>Population Density</td>
<td>2.12</td>
<td>2.08</td>
<td>0.11</td>
<td>1.98</td>
<td>2.37</td>
</tr>
<tr>
<td>Hastings: Expenditure p/c</td>
<td>$1,015.45</td>
<td>$1,017.42</td>
<td>$158.84</td>
<td>$759.66</td>
<td>$1,211.47</td>
</tr>
<tr>
<td>Income p/c</td>
<td>$1,039.41</td>
<td>$1,095.81</td>
<td>$104.77</td>
<td>$849.07</td>
<td>$1,143.90</td>
</tr>
<tr>
<td>Rates p/c</td>
<td>$676.53</td>
<td>$682.97</td>
<td>$85.06</td>
<td>$558.75</td>
<td>$793.88</td>
</tr>
<tr>
<td>Employee cost p/c</td>
<td>$260.35</td>
<td>$270.95</td>
<td>$64.44</td>
<td>$155.02</td>
<td>$336.82</td>
</tr>
<tr>
<td>Population Size</td>
<td>73,650</td>
<td>73,750</td>
<td>1,518.95</td>
<td>71,100</td>
<td>75,500</td>
</tr>
<tr>
<td>Population Density</td>
<td>2.12</td>
<td>2.08</td>
<td>0.11</td>
<td>1.98</td>
<td>2.37</td>
</tr>
<tr>
<td>CHBD: Expenditure p/c</td>
<td>$1,569.67</td>
<td>$1,482.82</td>
<td>$352.01</td>
<td>$1,071.97</td>
<td>$2,180.90</td>
</tr>
<tr>
<td>Income p/c</td>
<td>$1,598.04</td>
<td>$1,543.08</td>
<td>$363.45</td>
<td>$1,056.29</td>
<td>$2,200.00</td>
</tr>
<tr>
<td>Rates p/c</td>
<td>$919.60</td>
<td>$929.94</td>
<td>$192.85</td>
<td>$642.05</td>
<td>$1,186.44</td>
</tr>
<tr>
<td>Employee cost p/c</td>
<td>$181.81</td>
<td>$184.94</td>
<td>$37.73</td>
<td>$128.33</td>
<td>$234.89</td>
</tr>
<tr>
<td>Population Size</td>
<td>13,310</td>
<td>13,275</td>
<td>114.99</td>
<td>13,200</td>
<td>13,500</td>
</tr>
<tr>
<td>Population Density</td>
<td>4.00</td>
<td>3.99</td>
<td>0.03</td>
<td>3.97</td>
<td>4.06</td>
</tr>
</tbody>
</table>

In terms of population size, Napier City Council has the largest population (mean = 56,970) while Wairoa has the smallest population (mean = 8,692). With regard to population density – the number of residents per square kilometre – Napier City Council has the highest population density (mean = 537.45 or approximately 537 people per square kilometre) while
Wairoa has the lowest population density (mean = 2.12 or approximately 2 people per square kilometre). In essence, the summary statistics reported in Table 5.1 highlight that significant differences exist between these four councils.

To gain further insight into associations, we plotted the relationship between expenditure, income, rates, and employee costs and population size for Wairoa, CHBD, Napier and Hastings councils (Figure 5.1).

**Figure 5.1: Summary Charts**

In the top left hand corner of Figure 5.1, we plot the relationship between per capita expenditure and population size for Wairoa, CHBD, Napier and Hastings councils between 2003 and 2012. In reviewing this relationship, it is worth noting that there appears to be a
negative association between per capita expenditure and population size. However, it is important to stress that this relationship does not take into account omitted variable bias arising from ‘council fixed effects’ and ‘time fixed effects’ (i.e., bias arising from both unobserved variables that are constant over time and across local government areas).

In the top right hand corner of Figure 5.1, we plot the relationship between per capita income and population size for Wairoa, CHBD, Napier and Hastings councils between 2003 and 2012. In examining this relationship, there appears to be negative relationship between per capita income and population size. However, as previously noted, this relationship does not take into account omitted variable bias arising from ‘council fixed effects’ and ‘time fixed effects’.

In the bottom left hand corner of Figure 5.1 we plot the relationship between rates per capita and population size for Wairoa, CHBD, Napier and Hastings councils between 2003 and 2012. In reviewing this relationship it appears that there is no association between rates per capita and population size. However, it needs to be borne in mind that this relationship does not take into account omitted variable bias arising from ‘council fixed effects’ and ‘time fixed effects’.

In the bottom right hand corner of Figure 5.1 we plot the relationship between per capita employee costs and population size for Wairoa, CHBD, Napier and Hastings councils between 2003 and 2012. In considering this relationship there appear an inverted ‘u-shaped’ relationship between per capita employee costs and population size. However, as previously noted, this relationship does not take into account omitted variable bias arising from ‘council fixed effects’ and ‘time fixed effects’.

102
To further investigate the relationships plotted in Figure 5.1, we now turn to our econometric analysis.

### 5.4.2 The relationship between per capita expenditure and population size

To gain further insight into the relationship between per capita expenditure and population size, we report our regression results in Table 5.2. To aid the interpretation of our results, we divided population by 10,000 so that the estimated coefficients represent the marginal effect of a 10,000 person increase in population size.

<table>
<thead>
<tr>
<th>Independent variables</th>
<th>Model (1)</th>
<th>Model (2)</th>
<th>Model (3)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population Size</td>
<td>-0.0947* (0.0180)</td>
<td>-0.0916* (0.0160)</td>
<td>-0.1751 (0.1337)</td>
</tr>
<tr>
<td>Population Density</td>
<td>-0.0001 (0.0001)</td>
<td>-0.0031 (0.0029)</td>
<td></td>
</tr>
<tr>
<td>Council fixed effects</td>
<td>No</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Time fixed effects</td>
<td>No</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Constant</td>
<td>7.6960** (0.1152)</td>
<td>7.6970** (0.1173)</td>
<td>9.6251* (2.2303)</td>
</tr>
<tr>
<td>N</td>
<td>40</td>
<td>40</td>
<td>40</td>
</tr>
<tr>
<td>$R^2$</td>
<td>0.79</td>
<td>0.79</td>
<td>0.97</td>
</tr>
</tbody>
</table>

Table 5.2: Effect of population size on council expenditure, 2003 to 2012

Model 1 in Table 5.2 reports the OLS results of population size on the log of per capita expenditure **without** controlling for population density, ‘council fixed effects’ and ‘time fixed effects’. According to this estimate ($\beta = -0.0947; p < 0.05$), which is statistically significant at the 5% level, a 10,000 increase in the population is associated with a 9% decline in per capita expenditure.

To account for different population densities among these four councils, we extended Model 1 in Table 5.2 to include our population density variable (Model 2). However, the
inclusion of our population density variable is statistically insignificant and does not change our principal finding.

However, Model 3 in Table 5.2, which now includes the council and time dummy variables, suggests that the association in Model 1 and Model 2 is affected by omitted variable bias. More importantly, our estimated population size coefficient ($\beta = -0.1751$) is now statistically insignificant. In other words:

- **There is no statistically significant relationship between population size and the log of per capita expenditure for the councils of Central Hawkes Bay, Hastings, Napier, and Wairoa.**

Clearly, our ‘council fixed effects’ and ‘time fixed effects’ account for a relatively large amount of the variation in the data as indicated in the substantial increase in the $R^2$ value from 0.79 to 0.97.

While our initial analysis fails to find a statistically significant relationship between population size and per capita expenditure, it is important to examine whether there may be any other potential financial benefits associated with amalgamating Central Hawkes Bay, Hastings, Napier, and Wairoa councils. Against this background, we investigate the relationship between income, rates, and employee costs and population size.
5.4.3 The relationship between per capita income and population size

Model 1 in Table 5.3 below reports the OLS results of population size on the log of per capita income without controlling for population density, ‘council fixed effects’ and ‘time fixed effects’. According to this estimate (β = -0.0840; p < 0.05), which is statistically significant at the 5% level, a 10,000 increase in the population is associated with an 8.4% decline in per capita income.

Table 5.3: Effect of population size on council income, 2003 to 2012

<table>
<thead>
<tr>
<th>Independent variables</th>
<th>Model (1)</th>
<th>Model (2)</th>
<th>Model (3)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population Size</td>
<td>-0.0840** (0.0159)</td>
<td>-0.0878** (0.0142)</td>
<td>-0.4893 (0.2307)</td>
</tr>
<tr>
<td>Population Density</td>
<td>0.0001 (0.0000)</td>
<td>-0.0004 (0.0051)</td>
<td></td>
</tr>
<tr>
<td>Council fixed effects</td>
<td>No</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Time fixed effects</td>
<td>No</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Constant</td>
<td>7.6966** (0.1032)</td>
<td>7.6954** (0.1044)</td>
<td>10.1476 (3.8007)</td>
</tr>
</tbody>
</table>

N: 40 40 40
R²: 0.75 0.76 0.91

To account for the differences in population density, we extend Model 1 in Table 5.3 to include our population density variable (Model 2). However, the inclusion of our population density variable is statistically insignificant.

However, Model 3 in Table 5.3, which now controls for ‘council fixed effects’ and ‘time fixed effects’ suggests that the reported associations in Model 1 and Model 2 is affected by omitted variable bias. Most importantly, our estimated population size coefficient (β = -0.4893) is now **statistically insignificant**. In other words:
• There is no statistically significant relationship between population size and the log of per capita income for the councils of Central Hawkes Bay, Hastings, Napier, and Wairoa.

Clearly, our ‘council fixed effects’ and ‘time fixed effects’ account for a relatively large amount of the variation in the data as indicated in the substantial increase in the $R^2$ value from 0.76 to 0.91.

5.4.4 The relationship between per capita rates and population size

Model 1 in Table 5.4 below reports the OLS results of population size on the log of per capita rates without controlling for population density, ‘council fixed effects’ and ‘time fixed effects’. According to this estimate ($\beta = -0.0527; p < 0.01$), which is statistically significant at the 1% level, a 10,000 increase in the population is associated with a 5.3% decline in per capita rates.

Table 5.4: Effect of population size on rates, 2003 to 2012

<table>
<thead>
<tr>
<th>Independent variables</th>
<th>Model (1)</th>
<th>Model (2)</th>
<th>Model (3)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population Size</td>
<td>-0.0527**(0.0064)</td>
<td>-0.0475** (0.0003)</td>
<td>-0.3851 (0.1345)</td>
</tr>
<tr>
<td>Population Density</td>
<td>-0.0002** (0.0000)</td>
<td>-0.0074 (0.0028)</td>
<td></td>
</tr>
<tr>
<td>Council fixed effects</td>
<td>No</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Time fixed effects</td>
<td>No</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Constant</td>
<td>6.9776** (0.0122)</td>
<td>6.9792** (0.0031)</td>
<td>12.6485** (2.1572)</td>
</tr>
<tr>
<td>$N$</td>
<td>40</td>
<td>40</td>
<td>40</td>
</tr>
<tr>
<td>$R^2$</td>
<td>0.72</td>
<td>0.75</td>
<td>0.98</td>
</tr>
</tbody>
</table>

Standard errors in parentheses. * $p<0.05$, ** $p<0.01$
To account for the differences in population density, we extend Model 1 in Table 5.4 to include our population density variable (Model 2). The inclusion of our population density, which is statistically significant ($\beta = -0.0002; p < 0.01$), attenuates the impact of our population size variable ($\beta = 0.0475; p < 0.01$). Thus, a 10,000 increase in the population is now associated with a 4.8% decline in per capita rates holding population density fixed.

However, Model 3 in Table 5.4, which now controls for ‘council fixed effects’ and ‘time fixed effects’ suggests that the reported association in Model 1 and Model 2 is affected by omitted variable bias. Most importantly, our estimated population size coefficient ($\beta = -0.3851$) is now statistically insignificant. In other words:

- There is no statistically significant relationship between population size and the log of per capita rates for the councils of Central Hawkes Bay, Hastings, Napier, and Wairoa.

Our ‘council fixed effects’ and ‘time fixed effects’ account for a relatively large amount of the variation in the data as indicated in the increase in the $R^2$ value from 0.75 to 0.98.

5.4.5 The relationship between per capita employee costs and population size

Model 1 in Table 5.5 below reports the OLS results of population size on the log of per capita employee costs without controlling for population density, ‘council fixed effects’ and ‘time fixed effects’. Model 1 suggests that there is no relationship between population size and per capita employee costs.
To account for population density, we extend Model 1 in Table 5.5 to include our population density variable. Inclusion of population density variable, which is statistically significant at the 1% level, suggests that there is a relationship between population density and employee costs.

However, Model 3 in Table 5.5, which now controls for ‘council fixed effects’ and ‘time fixed effects’ suggests that the reported association in Model 1 and Model 2 is affected by omitted variable bias. More importantly, our estimated population size coefficient ($\beta = -0.1227$) is now statistically insignificant. In other words:

- **There is no statistically significant relationship between population size and the log of per capita employee costs for the councils of Central Hawkes Bay, Hastings, Napier, and Wairoa.**
5.4.6 Robustness Checks

To investigate the robustness of our analytical approach we:

- Re-ran our full econometric specification (i.e., Model 3) reported in Tables 5.2, 5.3, 5.4, and 5.5 with the inclusion of a quadratic population term (i.e., we included population squared term in our model to account for any possible non-linearity); and
- Re-ran our full econometric specification (i.e., Model 3) reported in Tables 5.2, 5.3, 5.4, and 5.5 using per capita expenditure in dollar terms and a quadratic in population.

The results from our robustness checks are reported in our Statistical Appendix (section 5.6). The ‘bottom line’ is that our alternative econometric specifications do not change our overall result (although we do find evidence to support a ‘u-shaped’ relationship between employee costs and population size). More specifically, Models 1 in Table 5.5 and Table 5.6 of our Statistical Appendix show that there is no statistically significant association between population size and council expenditure once ‘council fixed effects’ and ‘time fixed effects’ are taken into account. In other words, our principal empirical findings are not sensitive to alternate econometric specifications.

5.5 Conclusion

In Chapter 5, we examined the relationship between local government expenditure and population size for Central Hawkes Bay, Hastings, Napier, and Wairoa using a 10 year panel dataset covering the period 2003 to 2012. Based on our econometric analysis of available data, there is no evidence of a statistical relationship between population size and expenditure...
for the councils. Since scale economies are not present, this seriously undermines the arguments in favour of council amalgamations.

In other words, there is no evidence for the presence of scale economies within the current context. Thus, from a local government policy perspective, there is no reason to believe that a proposed merger of Central Hawkes Bay, Hastings, Napier, and Wairoa councils – as advocated in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* – will result in any cost-savings.
### 5.6 Statistical Appendix

#### Table 5.6: Robustness Check 1 – Inclusion of population squared term

<table>
<thead>
<tr>
<th></th>
<th>Model (1) Expenditure</th>
<th>Model (2) Income</th>
<th>Model (3) Rates</th>
<th>Model (4) Employee costs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population</td>
<td>0.0474</td>
<td>0.0266</td>
<td>-0.1129</td>
<td>-3.0260*</td>
</tr>
<tr>
<td></td>
<td>(0.6634)</td>
<td>(1.1524)</td>
<td>(0.5504)</td>
<td>(0.6542)</td>
</tr>
<tr>
<td>Population²</td>
<td>-0.0173</td>
<td>-0.0401</td>
<td>-0.0212</td>
<td>0.2446*</td>
</tr>
<tr>
<td></td>
<td>(0.0582)</td>
<td>(0.1002)</td>
<td>(0.0498)</td>
<td>(0.0525)</td>
</tr>
<tr>
<td>Population Density</td>
<td>-0.0039</td>
<td>-0.0022</td>
<td>-0.0084</td>
<td>0.0102</td>
</tr>
<tr>
<td></td>
<td>(0.0051)</td>
<td>(0.0087)</td>
<td>(0.0045)</td>
<td>(0.0043)</td>
</tr>
<tr>
<td><strong>Council fixed effects</strong></td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td><strong>Time fixed effects</strong></td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Constant</td>
<td>9.3266**</td>
<td>9.4556*</td>
<td>12.2833**</td>
<td>9.5844*</td>
</tr>
<tr>
<td></td>
<td>(1.1055)</td>
<td>(1.6459)</td>
<td>(1.0395)</td>
<td>(2.1092)</td>
</tr>
<tr>
<td><strong>N</strong></td>
<td>40</td>
<td>40</td>
<td>40</td>
<td>40</td>
</tr>
<tr>
<td><strong>R²</strong></td>
<td>0.97</td>
<td>0.91</td>
<td>0.98</td>
<td>0.89</td>
</tr>
</tbody>
</table>

Standard errors in parentheses. * $p<0.05$, ** $p<0.01$

#### Table 5.6: Robustness Check 2 -- Per capita expenditure in dollar terms and a quadratic in population

<table>
<thead>
<tr>
<th></th>
<th>Model (1) Expenditure</th>
<th>Model (2) Income</th>
<th>Model (3) Rates</th>
<th>Model (4) Employee costs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population</td>
<td>-850.34)</td>
<td>-727.74</td>
<td>-123.62</td>
<td>-964.65*</td>
</tr>
<tr>
<td></td>
<td>(1035.60)</td>
<td>(1994.07)</td>
<td>(544.84)</td>
<td>(230.93)</td>
</tr>
<tr>
<td>Population²</td>
<td>6.80</td>
<td>-22.26</td>
<td>-25.30</td>
<td>75.58*</td>
</tr>
<tr>
<td></td>
<td>(90.19)</td>
<td>(173.52)</td>
<td>(48.66)</td>
<td>(16.83)</td>
</tr>
<tr>
<td>Population Density</td>
<td>-10.01</td>
<td>-6.25</td>
<td>-9.28</td>
<td>5.37**</td>
</tr>
<tr>
<td></td>
<td>(7.83)</td>
<td>(15.06)</td>
<td>(4.32)</td>
<td>(0.76)</td>
</tr>
<tr>
<td><strong>Council fixed effects</strong></td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td><strong>Time fixed effects</strong></td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Constant</td>
<td>10918.07**</td>
<td>9460.16*</td>
<td>7100.45**</td>
<td>505.92</td>
</tr>
<tr>
<td></td>
<td>(1641.82)</td>
<td>(2808.74)</td>
<td>(944.60)</td>
<td>(409.67)</td>
</tr>
<tr>
<td><strong>N</strong></td>
<td>40</td>
<td>40</td>
<td>40</td>
<td>40</td>
</tr>
<tr>
<td><strong>R²</strong></td>
<td>0.97</td>
<td>0.89</td>
<td>0.97</td>
<td>0.88</td>
</tr>
</tbody>
</table>

Standard errors in parentheses. * $p<0.05$, ** $p<0.01$
CHAPTER 6: GOVERNANCE AND ADMINISTRATION COSTS AND EFFICACY

6.1 Introduction

As we have seen in Chapter 2, the *Future Prosperity of the Hawkes Bay Region* proposed 13 policy initiatives to enhance regional growth and development in the Hawkes Bay Region, one of which centred on local government amalgamation. In terms of structural mergers, three alternative amalgamation scenarios were considered. Several claims of varying degrees of plausibility were made in *Future Prosperity of the Hawkes Bay Region* with respect to cost savings and other purported advantages which could flow from such forced mergers.

Subsequently *Potential Costs and Savings of Local Government Reform in Hawkes Bay* sought to determine in more detail the benefits and costs associated with Scenario A, Scenario B and Scenario C. Chapter 3 critically examined the cost calculations in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* and found numerous problems with the cost estimates. Chapter 6 tackles the proposed governance arrangements for the Scenario A, Scenario B and Scenario C and demonstrates that *Potential Costs and Savings of Local Government Reform in Hawkes Bay* has taken far too a benign view of the costs and efficacy of these arrangements, especially with respect to community boards.

Chapter 6 is divided into four main parts. Section 6.2 briefly sets out the assessment of governance arrangements undertaken in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* (2013b), particularly in regard to community boards. Section 6.3 critically evaluates the performance of community boards as sub-council representative structures in New Zealand local government. Section 6.4 assesses the cost estimates of the
operation of community boards in *Potential Costs and Savings of Local Government Reform in Hawkes Bay*. Chapter 6 ends with some brief concluding comments in section 6.5.

### 6.2 Proposed Governance Arrangements for Three Amalgamation Scenarios

*Potential Costs and Savings of Local Government Reform in Hawkes Bay* reiterates the three structural reform models under consideration and outlines the governance arrangements attached to Scenario A, Scenario B and Scenario C as follows:

**Scenario A: A Single Unitary Authority as proposed by A Better Hawkes Bay**

Scenario A consists of a single unitary authority possessing the powers of both regional councils and territorial local authorities. It would be governed by elected representatives and community boards as prescribed by the ABHB interest group which originally proposed model A.

**Scenario B: A single territorial authority and the existing regional council**

Scenario B would combine ‘Wairoa, Central Hawkes Bay and Hastings District Councils with Napier City Council to form a single territorial authority for Hawkes Bay’.

**Scenario C: Two territorial authorities and the existing regional council**

Scenario C would see the existing regional council remain unchanged, but the establishment of two territorial authorities: (a) a ‘northern council including Napier City, Wairoa District and the part of Hastings District north of the Tutaekuri River’ and (b) ‘a southern council comprising the balance of Hastings District and Central Hawkes Bay District’. It would include the three councils and four community boards (with two in each territorial authority).
The estimated governance and management cost of the three alternative structural scenarios are examined in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* (McGredy Winder & Co., 2013b, p.15/16). The authors contend that governance and management costs represent ‘one of the easily identified areas of change with each of the reform scenarios is that of governance and management’. *Potential Costs and Savings of Local Government Reform in Hawkes Bay* (McGredy Winder & Co., 2013b, Table 4, p.17) sets out the estimated cost of governance and management. This Table is reproduced below.

<table>
<thead>
<tr>
<th></th>
<th>Current ($000)</th>
<th>Scenario A Number ($000)</th>
<th>Scenario B Number ($000)</th>
<th>Scenario C Number ($000)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mayors/Chair/Councillors</td>
<td>2215</td>
<td>17</td>
<td>1270</td>
<td>24</td>
</tr>
<tr>
<td>Community Boards</td>
<td>20</td>
<td>25</td>
<td>725</td>
<td>25</td>
</tr>
<tr>
<td>Maori Board</td>
<td>5</td>
<td>145</td>
<td>See note</td>
<td>See note</td>
</tr>
<tr>
<td>Key Personnel</td>
<td>5472</td>
<td>8</td>
<td>1800</td>
<td>17</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>7707</strong></td>
<td><strong>3940</strong></td>
<td><strong>5394</strong></td>
<td><strong>6879</strong></td>
</tr>
<tr>
<td>Potential Annual Savings</td>
<td><strong>3767</strong></td>
<td>2313</td>
<td>828</td>
<td></td>
</tr>
</tbody>
</table>

Note: It has been assumed in Scenario B and C that the Regional Council's Joint Planning Committee would continue instead of establishing a new Maori Board as proposed by ABHB. The costs of the Joint Committee are already reflected in the regional council's costs and are therefore not separated out here.

*Potential Costs and Savings of Local Government Reform in Hawkes Bay* (McGredy Winder & Co., 2013b, p.15) distinguishes between methods of estimating governance and management costs: Method 1 ‘would be to assume that the governance role within the region does not change under any of the scenarios and to therefore leave the current pool of funds allocated by the Remuneration Authority unchanged’. Method 2 assumes ‘levels of remuneration for the governance roles that reflect the sort of payments that the Remuneration Authority makes to members in similar roles in similar sized councils. The authors followed the second method.
Potential Costs and Savings of Local Government Reform in Hawkes Bay (McGredy Winder & Co., 2013b, p.15) notes that ‘the Remuneration Authority does not apply a linear scale to the remuneration of elected representatives’ since ‘remuneration in larger councils is higher than in smaller ones, but is determined using a range of factors and the recognition that the underlying responsibilities of governance roles are the same in all councils’.

Potential Costs and Savings of Local Government Reform in Hawkes Bay (McGredy Winder & Co., 2013b, p.16) observe that ‘the major projected change from the current situation shown in Table 4 relates not to elected representatives, but to senior management’. However, its authors could also have drawn readers’ attention to the fact that all three options have community boards, with 25 members in each of A and B at $725,000 in remuneration alone, and 20 members on C at $580,000 per annum in remuneration alone. As we shall see, not only does this underestimate the real costs of community boards, but it also ignores empirical evidence on their steadily decreasing performance across New Zealand local government as a whole.

6.3 Operation of Local/Community Boards in New Zealand

Despite extravagant claims in Future Prosperity of the Hawkes Bay Region concerning the primacy of leadership in fostering regional development in the Hawkes Bay Region, Potential Costs and Savings of Local Government Reform in Hawkes Bay has nothing to say about the efficacy of leadership in scenarios A, B and C. This is more than a little surprising since an empirical literature exists on the operation of community/local boards in New Zealand. It is thus well worth considering community/local boards in the light of this critical literature.
Community boards were established as part of broader local government reform in New Zealand in 1989. In 2012, 116 community boards existed in New Zealand. New Zealand community/local boards have two main functions: (a) representation and advocacy on behalf of their local communities and (b) consideration of any matter referred to them by their local councils.

In addition, community/local boards can also tackle the following matters:

- Make annual submissions to local councils on expenditure questions.
- Review the local services provided by the local council to the local community.
- Engage with local community organisations and other local interest groups in the community.
- Undertake any other responsibilities delegated to them by their local council.

Under New Zealand Local Electoral Act 2001 Section 19(f), community boards must comprise at least four members, but not more than twelve members. In addition, at least four persons must be elected. Finally, the number of appointed members must be less than half the total membership.

Community Level Governance (2013, pp.12/14) – commissioned by the Independent Local Government Panel in New South Wales – raised various problems with the operation of community/local boards in New Zealand. For instance, Community Level Governance acknowledged that ‘over recent years, the number of community boards has been in decline, substantially because of proposals by councils in representation reviews to disestablish
community boards’. This has been a consequence of the fact that it reflects ‘a combination of what is seen as the relative insignificance of a community board, and a parent council not placing any particular value on continuing a community board already in existence (especially given the remuneration situation)’. Furthermore, *Community Level Governance* admitted that ‘an important destabilising factor in the relationship between some councils and their community boards has been the way in which New Zealand’s Remuneration Authority has set the remuneration for elected members’. This has had the unintended result that ‘unsurprisingly councillors tended to see themselves as meeting half of community board members’ allowances out of their own pockets’.

In his *Roles and Functions of Community Boards: Report for the Community Board’s Executive Committee*, Richardson (2008) provided a thorough appraisal of the effectiveness of New Zealand community boards. Richardson (2008) considered the functions carried out by community boards, community board ‘satisfaction’ with relationships between local councils and community boards, and how the functions of community boards have changed over time.

Richardson (2008, pp.6/9) summarised his findings as follows:

- Wide variation existed ‘in the number of decision-making and advisory powers delegated’ in different local authorities, with 45% of community boards enjoying advisory roles, 7% decision-making roles, and 46% council functions.
- Respondents specified that the advisory roles of community board vacillated between formal and *ad hoc* roles, usually at the discretion of council officers, council committees or council meetings.
- Some local authorities had established other engagement mechanisms apart from community boards for pursuing community advice, including advisory structures and designated ward committees.
- Variation existed in the ‘delegation of decision-making and advisory roles across functions’, with community boards typically exercising ‘advisory roles in policy and planning’, but with ‘decision-making roles in planning and policy were rarely delegated to community boards’.
- Resource management roles were ‘largely performed by councils only’ and community boards mostly exercised advisory roles in service delivery functions.
- Community boards were most likely to have delegated decision-making in areas ‘concerning community centres and halls, community grants, sports and recreation activities, and parks, reserves and gardens’.
- The community board role had metamorphosed through time. Richardson (2008) observed that ‘it appears that councils were less likely to delegate decision-making or advisory roles to community boards in 2007 than in 1995’. Moreover, ‘there was a significant reduction in the number of community boards that had a decision-making
role from 1995 to 2007’. Lastly, ‘in most functional areas community boards also had fewer advisory roles in 2007 than in 1995’.

*Roles and Functions of Community Boards* drew several broad conclusions. In particular, it found that while ‘the majority of respondents (65%) were satisfied with the overall relationship between the board and the council, a sizeable minority of respondents (35%) indicated that they were dissatisfied’.

Against this background, it is immediately apparent that community/local boards are far from an effective form of sub-council governance. Perhaps the most telling observation resides in the fact that while the New Zealand *Local Government Act 2002* empowered community boards to carry out various functions, Richardson (2008, p.9) found that ‘community boards appear to have fewer delegations in 2007 than in 1995’!

### 6.4 Evaluation of Cost Estimates for Community Boards

As we have seen, for the purposes of financial modelling, *Potential Costs and Savings of Local Government Reform in Hawkes Bay* (McGredy Winder & Co., 2013, p.15) employed Method 2 to calculate costs of community council members by assuming ‘levels of remuneration for the governance roles that reflect the sort of payments that the Remuneration Authority makes to members in similar roles in similar sized councils’. It also assumed that community boards in amalgamated Hawkes Bay councils would broadly follow the approach taken by their counterparts in the Auckland Council community councils.
While this approach is plausible for remuneration costs, it is noteworthy for what it neglects to mention. The monetary costs associated with the establishment and maintenance local boards comprise two main elements: (a) the costs of the establishment of local boards and (b) the ongoing running costs of local boards. It is thus worth considering the Auckland experience to gain an appreciation of the magnitude of these costs, especially since _Potential Costs and Savings of Local Government Reform in Hawkes Bay_ draws explicit parallels with Auckland community boards.

_Community Level Governance_ (2013, p.17) observed that for Auckland ‘local boards are still very much “work in progress”’. However, _Community Level Governance_ (2013, p.17) noted that each Auckland local board seemed to have ‘apparent authority for a budget in the order of $20 million’, and the specific case study examined in _Community Level Governance_ (2013, p.17) had ‘a budget with operating expenditure of $41 million and capital expenditure of $6.8 million for the 2012/2013 year’. Nonetheless _Community Level Governance_ speculated that ‘in practice it seems the amount over which the board is able to exercise real discretion is significantly less than $1 million’.

With respect to the costs associated with local boards in the recently merged Auckland Council, _Community Level Governance_ (2013, p.18) noted that while ‘local board areas have a population on average of approximately 70,000, the staffing resource is only some three or four persons for each board to provide advice, and manage the board’s administrative processes’ and these persons are ‘employed directly by Auckland Council and not the local board’.
In order to garner an informed estimate of the costs of local boards in any Hawkes Bay Region amalgamated council, it is useful to follow the Auckland Council example. In its *Auckland Remuneration Decision 2013/2014*, the Remuneration Board handed down the following remuneration decision for Auckland: in Howick (the highest paid Auckland local board) the local board chair will be paid $88,222 in 2013 and a board member will be paid $40,344, compared with Great Barrier (the lowest paid Auckland local board) where the local board chair will be paid $45,211 and a board member will be paid $21,713. The resultant direct annual costs for board members can be gathered from the fact that Howick has a chair and eight members and Great Barrier has a chair and four members. It is thus evident that Auckland with 21 local boards which have a total of 148 members, as well as an Auckland Council, has considerable costs associated with local boards (as its second tier of local government). In addition, in Auckland, each local board has a three/four person secretariat.

How would these costs translate to forcible amalgamated Hawkes Bay councils? Aside from member remuneration, with the magnitudes shown in Table 6.1, we must also take into account of an Auckland-style secretariat of three/four persons. If we err on the conservative side, and assume each amalgamated Hawkes Bay community board will have only three (and not four) staff members. If each staff member is paid only $60,000, then we get remuneration costs of $180,000. If we add 30% on-costs, then this becomes $234,000. Accordingly, the direct remuneration costs of offers attached to each amalgamated community board could be around $234,000 per board, without considering the remuneration costs of members! Furthermore, this also excludes the costs of office accommodation and running expenses.
6.5 Conclusions

Chapter 6 has considered the cost estimates for governance and administration for scenarios A, B and C in Potential Costs and Savings of Local Government Reform in Hawkes Bay. We can draw two main conclusions for the analysis in Chapter 3.

- Despite extravagant claims on the pivotal role of leadership in the growth and development of Hawkes Bay Region in Future Prosperity of the Hawkes Bay Region and Potential Costs and Savings of Local Government Reform in Hawkes Bay, their authors have not bothered to consult the relevant literature, especially on the operation of community boards. As we have seen, the operation of community/local boards has been far from satisfactory. Indeed, as Richardson (2008) has shown, community/local boards are used much less frequently and make fewer decisions than when they were first established in 1989.

- The estimated costs of community boards in Potential Costs and Savings of Local Government Reform in Hawkes Bay understate the real costs of establishing local boards in the proposed amalgamated scenarios A, B and C. In particular, despite advocating Auckland-style community boards, no consideration is given to the costs of administrative personnel, office accommodation and the like.
CHAPTER 7: LOCAL GOVERNMENT COMMISSION REORGANISATION

APPROACH

7.1 Background

Reid (2013) has identified three distinct stages in local government restructuring in New Zealand in the post-war period. Phase 1 subsumes the period between the establishment of the Local Government Commission (LGC) in 1946 and the radical restructuring of local government sector in 1989. Phase 2 covers the period between 1989 and December 2012, whereupon the amalgamation provisions in LGA 2002 Amendment Act 2012 were revised. Phase 3 thus ushers in a new era based on the new LGC local government restructuring process.

Chapter 7 provides a critical evaluation of the new Commission process. In particular, we examine the Draft Proposal for Reorganisation of Local Government in Northland (LGC, 2013b) prepared by the Commission as a salient and worrying example of how the revised process is interpreted to work by the Commission. The Draft Proposal for Reorganisation of Local Government in Northland is important for local government reorganisation in the Hawke’s Bay Region because of its remarkable resemblance to the drastic recommendations in Future Prosperity of the Hawkes Bay Region. Both reports propose a single unitary authority for their respective regions in place of existing functioning and financially viable district councils and regional councils.
Chapter 7 is divided into three main parts. Section 7.2 presents a synoptic account of the new LGC process for determining local government reorganisation. Section 7.3 critically examines the LGC Draft Proposal for Reorganisation of Local Government in Northland (LGC, 2013b) as the most recent example of how the Commission is approaching local government amalgamation, concentrating on: (a) the almost complete absence of any empirical or other justification for extravagant claims centred on increased efficiency and cost savings from the proposed forced merger; and (b) its recommendation for extended powers for community boards, including a worrying degree of authority in the sphere of local infrastructure maintenance and investment. Chapter 7 ends with some brief concluding remarks in Section 7.4.

7.2 Local Government Board Amalgamation Process

Under the LGA 2002 Amendment Act 2012 the Commission is responsible for dealing with local government restructuring applications. Upon receipt of an application, and after due consideration and public consultation, the Commission may decide to prepare a reorganisation proposal which could be placed before affected voters in a poll. If a proposal is approved, council restructuring can then proceed. Under Section 34 of the LGA 2002 Amendment Act 2012 the LGC enjoys the authority of a Commission of Inquiry with powers to summon witnesses, request information and to obtain evidence.

In terms of the LGA 2002 Amendment Act 2012 local government restructuring involves modification of the area, functions or structure of a local government entity, such as a city, district council, or a regional council. Reorganisation encompasses boundary alterations, statutory obligation transfers, and the establishment of unitary authorities. Section 24 of the
LGA 2002 Amendment Act 2012 stipulates that restructuring applications can be made for the following types of change:

- The union of districts or regions
- The constitution of new districts or regions
- The abolition of districts or regions
- The alteration of boundaries of a district or region
- The transfer of a statutory obligation from one local authority to another
- The establishment of a territorial authority as a unitary authority.

The aims of municipal reorganisation are twofold under Section 24AA of the Act, which hold that restructuring should seek to ‘improve the effectiveness and efficiency of local government’ through:

- Giving local communities ‘the opportunity to initiate, and participate in considering, alternative local government arrangements for their area’; and
- Charging the LGC ‘in consultation with communities’ to ‘identify, develop and implement in a timely manner the option that best promotes good local government’.

The procedure for lodging reorganisation applications is set out under clause 3 of Schedule 3. An application can be made by ‘any person, body or group including (but not limited to) one or more affected local authorities, or the Minister of Local Government’.
In determining whether to prepare a draft reorganisation proposal after receiving a reorganisation application, the LGC must follow clause 12 of Schedule 3 of the Act and ask whether the application would best promote ‘good local government’ in the area in question. Thus sound applications must promote ‘good local government’ as set out in section 10 of the Act, which states that local government has two chief roles:

(a) ‘To enable democratic local decision-making and action by, and on behalf of, communities’; and
(b) ‘To meet the current and future needs of communities for good-quality local infrastructure, local public services and performance of regulatory functions in a way that is most cost-effective for households and businesses’.

According to Subsection 10(2), ‘good quality’ is defined as follows:

‘In this Act, in relation to local infrastructure, local public services, and performance of regulatory functions, means infrastructure, services, and performance that are:

(a) efficient and
(b) effective and
(c) appropriate to present and anticipated future circumstances’.

The nature of performance improvements is set out in Clause 12(b) of Schedule 3 to include the following:
(a) ‘Efficiencies and cost savings and
(b) Productivity improvements, both within the local authorities and for businesses and households that interact with those local authorities and
(c) Simplified planning processes within and across the affected area through, for example, the integration of statutory plans or a reduction in the number of plans to be prepared or approved by a local authority’.

In its *Local Government Reorganisation Guidelines*, the LGC (2013a, p.5) notes that Clause 12(b) ‘may be seen to be about changes that will lead to doing more with the same resources, or doing the same with less resources while also (where relevant) simplifying local government processes. Local authority service delivery should be appropriate to the area, the communities and their circumstances both in the present and for the future’. It observes further that ‘the ultimate beneficiaries of good local government, i.e. improved local decision-making and economic performance, are not the local authorities, but rather the residents and ratepayers, whether businesses or households, serviced by those local authorities’.

Upon receipt of an application, the LGC must decide whether the application is prohibited by the restrictions in clause 4 of Schedule 3 of the Act, which are as follows:

(a) ‘The application relates to a local authority that has been the subject of local government reorganisation’ and
(b) ‘The application is made in a period specified in a previous local government reorganisation scheme as to when further changes are prohibited’.
If an application is determined as valid, then the LGC must decide whether or not to assess the application. According to *Local Government Reorganisation Guidelines*, the LGC (2013a, p.7/8) grounds for declining to assess an application are prescribed in clause 7 of Schedule 3 of the Act as follows:

(a) ‘The application is frivolous’.
(b) ‘The application does not contain the information required by clause 5(1) on the required contents of an application’.

Once the LGC has decided to assess an application, then under clause 6 of the LGA 2002 Amendment Act 2012, it must determine whether community support exists for the application in a quadrilateral stage process:

- The LGC must ensure that an application enjoys community support ‘in the district of each affected territorial authority’.
- Prior to assessing an application, the LGC must establish that ‘there is demonstrable community support in the district of each affected territorial authority for local government reorganisation in the affected area’.
- Where alternative reorganisation applications have been lodged sought and a preferred application must be determined, the LGC must take into account the ‘degree of community support for relevant applications that has been demonstrated to the Commission’.
- The LGC must determine if the final proposal will have ‘demonstrable community support in the district of each affected territorial authority’.
The LGC must also determine ‘affected area’ in terms of applications. The phrase is defined in Section 5 of the Act as follows:

(a) ‘An area that would be included in the district or region of a new or different local authority if local government in the area were to be reorganised in accordance with the reorganisation application, draft proposal, or final proposal’.

(b) ‘An area that remains in the district or region of a local authority, but the local authority’s responsibilities would be changed if local government in the area were to be reorganised in accordance with the reorganisation application, draft proposal, or final proposal’.

(c) ‘An area of the district or region of a local authority, if the Commission has declared it to be an affected area because the operational scale, scope, or capability of the local authority would be materially affected if local government in relation to the area were to be reorganised’.

Finally, the LGC must consider ‘responsibilities’. It has determined that these refer only to ‘the duties, functions and powers of a local authority’ (LGC, 2013a, p.10). In practice, these embrace instances where ‘a territorial authority becomes a unitary authority and takes on the responsibilities of a regional council’ or where ‘a local authority transfers a statutory obligation to another local authority’.
7.3 Assessment of the Local Government Board Northland Draft Proposal

7.3.1 Genesis of Draft Proposal

Local government reorganisation in Northland commenced on 18th December 2012 with the receipt by the LGC of an application from Far North District Council to transform itself into a unitary authority, combining the powers of a territorial authority and a regional council. The LGC found the application met all legal requirements and called for alternative applications as required under the legislation. 41 responses in total were received, of which seven alternative proposals met the prescribed guidelines.

The Commission considered all these alternative proposals in terms of ‘reasonably practicable’ options for reorganisation in Northland. Taking into account these options, the Commission formulated its ‘preferred option’ which consisted of the establishment of a single unitary authority for Northland Region combined with local community boards. This makes the Draft Proposal for Reorganisation of Local Government in Northland (LGC, 2013b) important for local government reorganisation in the Hawke’s Bay Region given the striking resemblance between its recommendations and those in Future Prosperity of the Hawkes Bay Region. Both propose a single unitary authority for their respective regions in place of existing satisfactory and financial viable district councils and regional councils.

7.3.2 Nature of Draft Proposal

In essence, the Draft Proposal for Reorganisation of Local Government in Northland (LGC, 2013b) recommends a single unitary authority for the Northland region, combining the functions of a district council and a regional council, to be named the Northland Council to
replace the Far North District Council (FNDC), Whangarei District Council (WDC), Kaipara District Council (KDC) and the Northland Regional Council (NRC). The proposed Northland Council would represent a single elected body with nine councillors elected from seven wards and a mayor elected directly by all Northland voters. In addition, a Northland Council would have seven community boards with 42 elected members, which would share common boundaries with the seven council wards. This would give the new entity a total of 52 elected representatives. While its administrative headquarters would be in the Whangarei District, Kaitaia, Rawene, Kaeo, Kerikeri, Kaikohe, Kawakawa, Ruakaka, Mangawhai and Dargaville would all have local service centres.

Existing council debt and other financial arrangements would be ‘ring-fenced’ for ‘at least six years’ and remain the responsibility of those local communities which incurred these obligations or derived advantage from them. By contrast, ‘current regional assets’ would be transferred to Northland Council.

The Commission argued that its recommendation embodied a ‘whole of Northland’ approach designed to combine all Northland local communities to ‘create a stronger strategic vision for the region’, which would ‘provide more effective advocacy to deal with central government, public sector agencies and commercial interests’, as well as ‘create simplified and streamlined processes for residents and ratepayers’. Furthermore, the additional second tier of community boards would not only adequately reflect ‘the diverse local communities of the region’, but also be ‘empowered to make decisions on matters that directly affect those local communities’. 
The Commission (2013b, p.47) asserted that its preferred option possessed numerous strengths. In the first place, it claimed that the proposal recognises ‘Northland’s regional community of interest’ despite the fact that the Northland Region contained an amorphous mix of diverse urban and rural communities. It further claimed that the new local government would provide ‘a single voice to advocate to central government and to other parties on behalf of all of Northland in relation to economic, social, cultural and environmental issues, and to negotiate partnerships, contracts and joint ventures’, without considering alternative cheaper and less divisive methods of achieving the same representative outcome through an alliance model or a Regional Organisation Council (ROC) arrangement (see, for example, Dollery, Grant and Kortt (2012) for an exhaustive discussion of these models of regional leadership).

In terms of the efficiency and financial viability of its recommended council structure, the Commission contends that its proposal ‘recognises the inefficiencies and duplications inherent in the existing local government structures comprising four local authorities’. However, it provides no evidence in support of this claim nor does it even bother to innumerate its veracity. In a similar vein, the Commission asserts that a single unitary authority for the Northland region would ‘facilitate improved economic performance both within the new council and for the benefit of Northland businesses and households’ which would somehow ‘arise from cost savings and efficiencies resulting from consolidation of council activities and elimination of duplication’, ‘productivity improvements for those seeking council approvals and consents from a new “one stop shop”’ as well as ‘simplified planning processes arising from integration of regional and district planning and a reduction in the number of plans’. These latter changes would serve to ‘eliminate confusion caused by
the varying policies, standards and approaches of the existing four local authorities’. Once again, the ‘evidence-free’ approach of the Commission is striking since no evidence of any kind is offered in support of these purported advantages of the proposed new local government structure.

The Commission makes further unsubstantiated claims regarding the strengths of the proposed new governance arrangements. For instance, it contends the new structure would ‘better distinguish between strategic decision-making for Northland as a whole and local decision-making on matters of importance to local communities’ and it would ‘provide for empowered local decision-making under new region-wide community board arrangements’. In addition, it is claimed that the new structure would ‘achieve enhanced strategic capacity for Northland local government as a result of increased scale and specialisation’ and it would ‘enhance operational capacity for core service delivery areas of councils such as roading and the ‘three waters’, although not a shred of evidence is adduced in favour of these assertions.

Finally, the Commission makes broad sweeping claims regarding the efficacy of its recommended Northland unitary authority, observing that ‘the proposal best provides for future proofing Northland communities of interest against projected adverse demographic change and the consequences of economic deprivation in particular parts of the region’. It adds that the establishment of a single new authority would provide ‘certainty and eliminate the need for ongoing discussion between the current councils about possible better arrangements and whether voluntary shared service arrangements could achieve desired outcomes’, as if the quest for improved collaborative regional service provision is something to be avoided rather than stimulated! The Commission concludes by stressing that ‘of the
available options, the proposal for a single unitary authority best meets the criteria in the Local Government Act for “good local government”.

The stilted and unbalanced advocatory character of Draft Proposal for Reorganisation of Local Government in Northland (LGC, 2013) is underlined in its dismissive assessment of the disadvantages inherent its proposal. Firstly, with respect to representation under the new structure, the Commission notes that while ‘the proposal would result in reduced numbers of councillors and mayors to represent Northland’, this would be counterbalanced ‘by significantly enhanced local representation and decision-making by community boards’, a point to which we return to later. Similarly, it is claimed that whereas ‘there may be a perceived risk of the new local authority being dominated by Whangarei’, this has been addressed ‘by a ward system of representation and a structure of empowered community boards able to make decisions on local matters’, as if this will somehow prevent the preponderant concentration of council administration, council staff and council expenditure in Whangarei. It is further conceded that although ‘there may be a perceived risk of loss of local identity with the establishment of one council’, this fear is unwarranted since (a) forced council mergers elsewhere have not led to a loss of local identity; (b) the ‘ongoing viability of local communities is more significantly impacted by economic decline than by local government arrangements’; and (c) the new community boards would address ‘some concerns raised about local matters not being dealt with locally’. No evidence is presented in support of propositions (a), (b) or (c).

Had the Commission bothered to consult the voluminous literature on the consequences of the forced amalgamation of rural and regional local authorities in geographic areas dominated demographically by a single large population centre, such as Whangarei in Northland, it
would have discovered that fears of a loss of identity, together with the effective ‘takeover’ of local government by numerically dominant population centres, are not only far from fanciful, but indeed typical of experience with compulsory consolidation everywhere. This literature has been exhaustively summarised in *Councils in Cooperation* (Dollery, Grant and Kortt, 2012). Moreover, for a recent ‘lived experience’ the Commission could easily have contacted Queensland councils comprised of large and small country towns forcibly merged in 2008 where it would have learned of widespread unhappiness and subsequent de-amalgamations.

The Commission is equally blasé over well-based concerns about the economic effects of compulsory council consolidation. For instance, while it concedes that ‘there will be uncertainty for staff as the result of the union of existing authorities and in the period immediately after the establishment of the new council’, the Commission blithely contends that this can be addressed ‘by an effective transition processes including good communication’. With respect to the inevitable disruption in service provision attendant upon forced amalgamation, the Commission accepts that whereas ‘there is a risk to continued delivery of services to the public during the transition period and for a time after establishment of the new council’, and it notes that ‘these problems will somehow need to be addressed through the transition process’, as if reassurance is equivalent to solution! The Commission admits that there will be ‘one-off costs arising from transition, such as staff redundancies, development of new plans and policies, and new integrated support systems including information technology systems’. However, it claims without any empirical or other justification that ‘apart from staff redundancies, most one-off costs will occur over several years and be carefully planned, funded and managed over an appropriate period’. Similarly, the Commission concedes that ‘there is potential for loss of employment in local areas because of council redundancies and a possible shift towards fewer council contract’
but maintains these worries will have to be met by new Northland Council through ‘strategies
to help address these concerns’. Furthermore, the Commission acknowledges that ‘there may
be concerns about excessive centralisation of council functions in the largest centre(s)’, but
observes that these concerns ‘can be partly addressed through the transition process and
decisions by the new council’, including ‘creative use of technology and the spread of service
centres across the region’. In addition, the Commission accepts that fears exist ‘about the
spread of existing localised debt across the region’, but claims that these fears are groundless
given the ‘ring-fencing of debt for a period of at least six years’, whereupon it will simply ‘be
up to the new council, reflecting the views of Northland residents and ratepayers, to decide
whether there should be any changes to these arrangements’.

As we saw in Chapter 4 of this Report, economic and fiscal concerns are entirely warranted
in the light of both the academic literature as well as the observed experience of all of the
Australian state local government systems which is fully documented in the various
Australian national and state inquiries. In particular, the sanguine attitude of the Commission
to the costs of amalgamation has no basis in reality, as we saw exemplified in Chapter 4 of
this Report with the exorbitant costs of the Queensland compulsory council consolidation
program after only one year!

7.3.3 Efficiency Gains and Cost Savings

As we have seen, the *Draft Proposal for Reorganisation of Local Government in Northland*
(LGC, 2013b) makes a number of unsubstantiated claims regarding the efficiency
consequences of the introduction of a unitary Northland Council. The Commission is obliged
under the *LGA 2002 Amendment Act 2012 Schedule 3 clause 12* to prepare a *Draft Proposal*
which must demonstrate that its preferred option meets the following economic criteria:
‘(b) will facilitate, in the affected area, improved economic performance, which may (without limitation) include—

(i) efficiencies and cost savings; and

(ii) productivity improvements, both within the local authorities and for the businesses and households that interact with those local authorities; and

(iii) simplified planning processes within and across the affected area through, for example, the integration of statutory plans or a reduction in the number of plans to be prepared or approved by a local authority.

This ‘economic performance’ requirement is explicitly expressed in Draft Proposal for Reorganisation of Local Government in Northland (LGC, 2013b, p.19) which acknowledges that ‘the LGC’s preferred option must also help achieve improved economic performance in the area’, where ‘improved economic performance includes such things as efficiencies and cost savings, productivity improvements and simplified planning processes’.

The Draft Proposal for Reorganisation of Local Government in Northland (LGC, 2013b, p.23/25) expended a mere two pages on attempting to demonstrate that its preferred option satisfied the ‘economic performance’ requirement. The Commission pointed out that in establishing whether ‘improved economic performance’ would follow the creation of a unitary Northland Council, it would have to employ ‘measures of improved economic performance’ such as ‘efficiencies and savings’, ‘productivity improvements for local authorities, businesses and households’ as well as ‘simplified planning processes’. 
With respect to enhanced efficiency and cost savings, the Commission asserts that it identified ‘a number of efficiencies and savings that could be achieved by reorganisation of councils in Northland’, adding the immediate caveat that the new unitary authority was ‘most likely to result in more efficient and effective processes for delivering services to the community rather than reductions in rates’.

Listed sources of municipal savings and efficiency encompassed were threefold:

- The first group of savings pinpointed ‘elected member remuneration (depending on the final number of elected members in a new structure), chief executive remuneration (for example having only one chief executive under the single unitary authority option as opposed to four chief executives under current council arrangements), and audit fees (say one set of fees compared to four)’. However, no pecuniary estimates were provided for this source of claimed savings and no indirect evidence was adduced. Furthermore, the Draft Proposal for Reorganisation of Local Government in Northland (LGC, 2013b, p.23/25) provided no indication of what proportion of the annual budget would be affected, doubtless because it was aware that the percentage savings involved would be trivial compared to transition costs.

- The second constellation of purported savings comprised reductions ‘in current corporate support costs of the four councils if one unitary authority for Northland were to be established’. The Commission asserts that this amounted to ‘potential annual savings in the order of $5 million’ which would derive from ‘savings are in personnel as a result of combining activities such as financial services, rating, human resources, information technology, records and professional services such as lawyers’.
Once again, the Commission provides no monetary estimates for the claimed savings, it offers no indirect evidence, and it gives no indication of how the calculations were made.

- The third group of purported savings flows from scale and scope economies the Commission assumes exist. It asserts that ‘further efficiencies and savings are likely in the delivery of services by combining teams working in particular areas, rationalising contracts for the purchase of goods or the delivery of services, and rationalising office accommodation and vehicles’. The Commission provides no pecuniary estimates for these claimed savings, no indirect evidence, and no indication of how its estimates were made.

Two major qualifications were appended to these efficiency and cost savings claims. In the first place, the Commission conceded that ‘while efficiencies and savings would be achieved on an ongoing basis, these would initially be offset against one-off transition costs’, which would embrace ‘the costs of the body appointed to make detailed decisions about the structure of the new council organisation and how it would operate, and any staff redundancy costs’. It is worth stressing that these costs do not include the vast bulk of expenses typically associated with council amalgamation, such as the costs of establishing a new central council headquarters, installing new single IT systems, harmonising remuneration between employees from constituent councils, redundancy payments, synchronising council records and financial systems, and the like.

The second caveat effectively undermines the Commission’s efficiency and cost saving claims by shifting the main objectives of the Northland local council reorganisation recommendation away from savings towards other objectives which cannot be objectively
measured. The Commission argued that whereas ‘efficiencies and savings would be achieved, enhanced organisational capacity, consistency of approach and the removal of duplication in processes were more important in promoting economic development and well-being in Northland’!

It is thus clear that apart from vague and completely unsubstantiated claims regarding efficiency gains and cost savings, the Draft Proposal for Reorganisation of Local Government in Northland (LGC, 2013b) has not demonstrated that efficiencies and savings would flow from the establishment of a Northland Council. Nor has it even attempted to provide defensible pecuniary estimates for the magnitude of the savings purportedly involved, the costs of the proposed amalgamation, and then the net costs or net savings. In other words, it has failed to meet the ‘efficiencies and cost savings’ requirement of the LGA 2002 Amendment Act 2012 Schedule 3 clause 12.

This raises the question of what kinds of empirical evidence could the Commission have provided had it thoroughly considered the ‘efficiencies and cost savings’ criterion. In principle, at least three kinds of evidence could have been presented:

- The Commission could have undertaken a comprehensive econometric modelling exercise which examined the relationship between council population size and council per capita expenditure for the recommended Northland Council, along the lines of the modelling set out in Chapter 5 in this Report. This is common practice in sound public policy making in local government restructuring through forced amalgamation.
- The Commission could have undertaken specific econometric modelling which investigated relationships between particular council functions and per capita
expenditure for the recommended Northland Council. The academic literature is replete with examples of this kind of empirical work.

- The Commission could have examined existing empirical evidence on the costs and savings experienced by groups of amalgamated councils comparable to the Northland councils, in an analogous fashion to Chapter 4 in this Report. Had it done so, it would have realised how seldom optimistic claims of significant efficiency gains and cost savings attendant upon forced amalgamation ever eventuate in practice!

7.3.4 Community Boards

As we have seen in Section 7.2, the *Draft Proposal for Reorganisation of Local Government in Northland* (LGC, 2013b) proposed a single unitary Northland Council with its administrative headquarters in Whangarei, but with ‘council service centres’ in the other nine Northland settlements of Kaitaia, Rawene, Kaeo, Kerikeri, Kaikohe, Kawakawa, Ruakaka, Mangawhai and Dargaville. In terms of functions, the Commission recommended that the Northland Council be ‘responsible for ‘the big picture’ across Northland’, developing budgets, policies and strategies, as well as striking rates and imposing bylaws for the Northland as a whole. Furthermore, the Northland Council would liaise with central government, commercial entities and civil service agencies.

In addition to its first-tier governance structure with a directly elected mayor and nine councillors elected from seven wards, the Northland Council would possess a second-tier comprised of seven community boards with six members each. The seven council wards and seven community boards would share common boundaries. This would yield a total number of 52 Northland representatives from the Northland Council and its community boards.
According to the *Draft Proposal for Reorganisation of Local Government in Northland* (LGC, 2013b), under its North Council proposal community boards would enjoy ‘significant levels of authority and empowerment’. In terms of functions, community boards would oversee the operations of ‘day-to-day services and facilities used by households, businesses and local group’. Moreover, community boards would determine service levels for numerous local facilities, including libraries, halls, museums, parks and sporting amenities. In addition, boards would administer local services in their own ward areas, such as car parks, cycle ways, footpaths, and traffic control. Furthermore, community boards would be empowered to advise on matters like drinking water quality, garbage collection and disposal, recycling, and water, wastewater and stormwater infrastructure. However, community boards would not be authorised to borrow money, employ staff, levy rates, make bylaws, or sell assets.

However, in its *Draft Proposal for Reorganisation of Local Government in Northland* (LGC, 2013b), the Commission goes to pains to stress that it regards Auckland-style local boards – as distinct from community boards – as better suited to meet the needs of the highly diverse Northlands community. For instance, *Draft Proposal* (2013b, p.8) has observed that:

The LGC notes that an amendment to the Local Government Act 2002 (LGA) to allow for local boards, as distinct from community boards, to be established in areas like Northland under a unitary authority model has been introduced to Parliament. While this is not a legal option at this time for Northland, the LGC is seeking views on a possible modification of its draft proposal to provide for local boards in Northland.
The Commission (2013b, p. 25) goes on to further stress this point:

During its consideration of its preferred option, the LGC was aware of the Minister of Local Government’s announcement that a Bill to amend the Local Government Act 2002 to allow for local boards (as established in Auckland) was to be introduced to Parliament before the end of the year. When enacted, this would allow for the establishment of local boards in Northland, for example, if one or more unitary authorities were to be established in the region.

In order to impress the point even more, the Commission (2013b, p. 26) reiterated its attraction to the introduction of local boards into the proposed Northland Council rather than community boards by noting that same ‘if the Bill comes into law before the LGC has finished its considerations on Northland, the LGC could modify its draft proposal to provide for local boards in place of the proposed community boards’.

The Commission (2013b, p. 25/26) spells out in some detail salient differences between the duties, powers and responsibilities of local boards and community boards. In the first place, whereas ‘local boards are established as part of a reorganisation scheme in a particular area’ and can only be extinguished through further local government restructuring, community boards have a much ‘less certain’ future tenure since they can be as they can be removed by means of a given council’s representation review. Secondly, the Commission underlines the fact that while local boards as a rule ‘share decision-making with the governing body of the council (the mayor and councillors) on non-regulatory matters, community boards enjoy only limited delegation powers from their councils, which can be readily withdrawn. Finally, in
stark contrast to community boards, ‘local boards have a more certain level of funding as there is provision for a formal process for boards to develop local plans and to agree funding for these with the governing body’.

These reflections by the Commission on the comparative advantages of local boards over community boards represent a significant cause for concern not only in the context of its Northland Council proposal, but also more generally for other local government reorganisation processes, such as the Hawke’s Bay reorganisation process.

In order to appreciate the nature of the dangers posed by the Commission’s support for local boards over community boards, it is worth stressing the powers already ceded to community boards in the recommended Northland Council. Schedule C of the Draft Proposal for Reorganisation of Local Government in Northland (LGC, 2013b) sets out the ‘Powers and Responsibilities of Community Boards’ in terms of (a) the statutory role of community boards; (b) the powers of community boards in respect of ‘planning powers’, ‘decision-making powers’ and ‘recommendation and submission powers’. For example, planning powers include the preparation of a community plan ‘to reflect that community’s priorities and preferences in relation to the level and nature of activities and services, and proposed developments to be provided or approved by the council in that community’. Similarly, where the desired service levels sought by a community board ‘are higher than the existing or proposed district-wide levels of service, the community board will recommend to the council the funding mechanisms to address this variation’. This includes maintenance and investment in significant and costly local infrastructure such as ‘local roads, bridges, footpaths, cycle ways, car parks and street lighting in the community’, ‘water supply in the community’, ‘wastewater collection and treatment in the community’, ‘stormwater and river management
in the community’, ‘solid waste management in the community’, coastal structures such as
wharves and walls in the community’, ‘local aerodromes and airfields in the community’,
‘the mitigation of natural hazards in the community’, ‘libraries and other community facilities
such as halls in the community’, ‘cemeteries in the community’, and ‘camping grounds, parks
and reserves in the community’.

It is thus planned that community boards can already exercise a significant degree of control
over planning, regulation, maintenance and investment in their own areas in terms of local
government service provision and local infrastructure. While this is a matter for concern with
respect to private investment, public investment and local government infrastructure which
affects the Northland region since community boards typically lack the requisite expertise to
evaluate substantial investment projects, as well as understandably exhibiting a local area
bias, the problem would be made much more acute if local boards were substituted for
community boards – which the Commission repeatedly emphasises would be desirable –
because of their more powerful and entrenched role. It would be more advisable from a
regional perspective for local/community boards to enjoy only advisory powers. From the
viewpoint of the proposed Northland Council, advice on community attitudes to substantial
investment projects, as well as local knowledge and local information concerning investment
projects would represent a beneficial role for local/community boards.

Finally, despite its explicitly positive view of Auckland-style local boards in the context of
non-metropolitan local government management, in its Draft Proposal for Reorganisation of
Local Government in Northland (LGC, 2013b) the Commission makes no mention of the
considerable costs associated with local boards. As we saw in Chapter 6 of this Report, these
costs would be substantial in single unitary councils, such as the proposed Northland Council and the proposed Hawke’s Bay Council.

7.4 Conclusion
Chapter 7 has sought to provide a critical assessment of the process adopted by the Commission under the new local government reorganisation provisions of the LGA 2002 Amendment Act 2012. By way of a recent and salient example of how the revised process works, we critically examined the Draft Proposal for Reorganisation of Local Government in Northland (LGC, 2013b) which recommended a single unitary Northland Council for the Northland Region. The Draft Proposal for Reorganisation of Local Government in Northland has particular relevance for local government reorganisation in the Hawke’s Bay Region because of its arresting resemblance to the recommendation in Future Prosperity of the Hawkes Bay Region. Both documents recommend a single unitary authority to replace the existing network of well-functioning and financial viable district councils and regional councils in their respective regions.

Our appraisal of the Draft Proposal for Reorganisation of Local Government in Northland (LGC, 2013b) as a recent example of how the Commission approaches local government amalgamation revealed an almost entirely ‘evidence-free’ methodology on the part of the Commission. Given the pivotal importance of local government reorganisation and the dire need to prevent expensive and divisive errors – such as those which bedevilled the 2008 Queensland amalgamation program – it is vital that proposed reorganisation proposals are based on extensive econometric modelling and the best available empirical evidence. This is unfortunately not the case with the Draft Proposal for Reorganisation of Local Government in Northland (LGC, 2013b).
This failing was especially concerning in two respects: (a) the almost complete absence of any empirical or other justification for extravagant claims centred on increased efficiency and cost savings from the proposed forced merger of Northland councils and (b) the Commission’s recommendation for extended powers for community boards and its strong preference local boards, despite the threats this poses for regional infrastructure maintenance and investment.
CHAPTER 8: CONCLUSIONS

8.1 Introduction

This Report has provided a critical evaluation of: (i) *Future Prosperity of the Hawkes Bay Region*, (ii) *Potential Costs and Savings of Local Government Reform in Hawkes Bay*, and (iii) *Draft Proposal for Reorganisation of Local Government in Northland*. In this Report, we have shown that the analysis conducted in *Future Prosperity of the Hawkes Bay Region*, *Potential Costs and Savings of Local Government Reform in Hawkes Bay* and the *Draft Proposal for Reorganisation of Local Government in Northland* is seriously deficient and the conclusions regarding the purported benefits of local government amalgamation are thus rendered unreliable.

Against this background, we found that (i) *Future Prosperity of the Hawkes Bay Region*, (ii) *Potential Costs and Savings of Local Government Reform in Hawkes Bay*, and (ii) *Draft Proposal for Reorganisation of Local Government in Northland* to be flawed in a number of respects.

8.2 Specific Limitations with *Future Prosperity of the Hawkes Bay Region*

*Future Prosperity of the Hawkes Bay Region* was seriously deficient in two main respects:

i. It has ignored the extensive literature on structural reform in local government, which includes a substantial corpus of thought on Australasian local government reform, including structure reform through council consolidation. This neglect is most unfortunate since a wealth of material exists, which clearly documents that forced
council amalgamation rarely improves performance of local authorities, especially in regional areas; and

ii. Shared services offers a promising alternative to forced amalgamation, particularly in the regional context and this should have been considered in detail in *Future Prosperity of the Hawkes Bay Region*.

The authors of *Future Prosperity of the Hawkes Bay Region* should have been aware that effective regional leadership is best fostered through the establishment of regional development bodies rather than through conflict-ridden battles over forced consolidation which typically results in the domination of rural areas by regional centres.

### 8.3 Specific Limitations with Potential Costs and Savings of Local Government Reform in Hawkes Bay

*Potential Costs and Savings of Local Government Reform in Hawkes Bay* was seriously wanting in a number of respects:

i. The Report entirely ignored the claims advanced in *Future Prosperity of the Hawkes Bay Region* on the primacy of effective regional leadership as the main driver of regional development in the Hawkes Bay Region and made no attempt to provide empirical validation for this far-reaching claim;

ii. The Report nowhere sought to validate the accuracy of it projected cost savings by examining previous amalgamation episodes in Australian and New Zealand. Had this been done, the Report would have found that claims of cost savings and other financial gains from council consolidation were almost never realized in practice.
iii. The robustness of the purported cost savings in the Report cannot be assessed because its authors did not conduct a sensitivity analysis of alternative cost saving scenarios. Thus, policy makers do not have estimates of either ‘worse case’ or ‘best case’ scenarios for options A, B or C. This is a serious omission given the inherent uncertainty surrounding the purported costs and benefits associated with local government amalgamation.

iv. The cost-savings presented in *Future Prosperity of the Hawkes Bay Region* are based entirely on what would have happened in the absence of council consolidations (i.e., the base case) which effectively ignores any cost savings that may have occurred without council mergers. Thus, the reported savings are based on a comparison of two uncertain forecasting settings.

### 8.4 Other Limitations

More generally, *Future Prosperity of the Hawkes Bay Region* and *Potential Costs and Savings of Local Government Reform in Hawkes Bay* had entirely ignored the findings from the bulk of the scholarly literature, which has found that council consolidation has not met its intended aims. Furthermore, the weight of opinion in a host of recent Australian national and state inquiries into the impact of amalgamation public inquiries agreed that the stress on council mergers has been misplaced. In particular, *Future Prosperity of the Hawkes Bay Region* and *Potential Costs and Savings of Local Government Reform in Hawkes Bay* had been remiss in neglecting the potential contribution of shared services to improving the performance of local government.
To ascertain whether there were would be any potential savings in merging Central Hawkes Bay, Hastings, Napier, and Wairoa councils, we conducted econometric modelling to determine whether there is any statistically significant relationship between council population size and local government expenditure. The econometric analysis reveals that there is no statistically significant relationship between council population size and per capita expenditure. There is thus little, if any, reason to assume that the cost savings proclaimed in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* would be realised.

Finally, we assessed the proposed governance arrangements for the Scenario A, Scenario B and Scenario C forced amalgamation models and demonstrated that *Potential Costs and Savings of Local Government Reform in Hawkes Bay* had taken far too a benign view of the costs and efficacy of these arrangements, especially with respect to community boards. In particular, our analysis found that:

- Despite extravagant claims in *Future Prosperity of the Hawkes Bay Region* on crucial role of leadership in the development, its authors had not consulted the relevant literature, especially on the operation of community boards. This was most unfortunate since the operation of community/local boards has not lived up to expectations. Indeed, Richardson (2008) had demonstrated that community/local boards were used less than when first established in 1989.
- The anticipated costs of community boards in *Potential Costs and Savings of Local Government Reform in Hawkes Bay* had underestimated the real costs of establishing local boards in proposed amalgamated scenarios A, B and C. In particular, despite
advocating Auckland-style community boards, no consideration was given to the costs of administrative personnel, office accommodation and the like.

8.5 Specific Limitations with the Draft Proposal for Reorganisation of Local Government in Northland

The Draft Proposal for Reorganisation of Local Government in Northland was seriously deficient in a number of respects:

i. Our appraisal of the Draft Proposal for Reorganisation of Local Government in Northland as a recent example of how the Commission approaches local government amalgamation revealed an almost entirely ‘evidence-free’ approach on the part of the LGC. Given the pivotal importance of local government reorganisation and the need to prevent expensive and divisive errors, it is vital that proposed reorganisation proposals are based on extensive econometric modelling and the best available empirical evidence.

ii. This failing was especially concerning in the almost complete absence of any empirical or other justification for the extravagant claims in Draft Proposal for Reorganisation of Local Government in Northland centred on increased efficiency and cost savings from the proposed forced merger of Northland councils.

iii. The Commission’s recommendation for extended powers for community boards and its strong preference local boards, despite the threats this poses for regional infrastructure maintenance and investment, represent a worrying aspect in the Commission’s thinking.
8.6 Conclusions

Thus, taking into account the weight theoretical and empirical evidence it is concluded that:

1. The proposed amalgamations scenarios advocated in: (i) *Future Prosperity of the Hawkes Bay Region*, (ii) *Potential Costs and Savings of Local Government Reform in Hawkes Bay* and (iii) *Draft Proposal for Reorganisation of Local Government in Northland* are not supported by available empirical evidence and past experience of compulsory council mergers; and

2. Shared service arrangements should be considered as an alternative option to forced council amalgamations.
REFERENCES


