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Analysis of local government reform options in the Northern Sydney area

FINAL REPORT

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Shire Council

22 May 2014

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Key findings

- Local governments in New South Wales (NSW) perform crucial functions and are key platforms for local democracy and representation, however, their structure and functions have largely remained static despite structural changes in the economy.
- Financial sustainability is a key consideration for local government in NSW, with 46 per cent of councils estimated to have a financial sustainability rating of ‘weak’ or lower within three years.
- To support more sustainable local governments over the long term, there are a number of potential reform options, including – for example – amalgamations, boundary reform, and shared services. The recent report by the Independent Local Government Review Panel, *Revitalising Local Government*, provided a comprehensive analysis of these options in the NSW context.
- Although there are broader impacts associated with reform, a key consideration is the potential financial benefits. Evidence suggests that economies of scale can be achieved in Australia, as demonstrated by seven out of nine studies of domestic reform experience.
- Previous experience suggests that the quality of service delivery, financial sustainability, and the effectiveness of local representation are consistently applied to develop and analyse the impacts of local government reform.
- Reform options were developed based on the common underlying principles of previous reform experience and consultations with Hornsby Shire Council management. Reform options included both amalgamations and shared services arrangements.
- An amalgamation of Hornsby and The Hills Councils is estimated to result in a net operating result of about \$26.9 million in 2017-18 (for the Hornsby Shire entity), representing about a 17 per cent improvement to the current forecast net operating result.
- An amalgamation of Hornsby Shire and Ku-ring-gai Councils is estimated to result in a net operating result of around \$26.2 million in 2017-18 (for the Hornsby Shire entity), representing about a 14 per cent improvement to the current forecast net operating result.
- An amalgamation of Hornsby, The Hills, and Ku-ring-gai Councils is estimated to result in a net operating result of about \$29.0 million for the Hornsby Shire entity in 2017-18. This represents about a 26 per cent improvement to the current forecast net operating result.
- A shared services model¹ between the Hornsby and The Hills Councils is estimated to result in a net operating result of around \$24.0 million in 2017-18 (for the Hornsby Shire entity), representing about a 4 per cent improvement to the current forecast net operating result.

¹ In a shared services model, it was assumed that councils would retain more control over their services. In particular, the option assumes that only the Infrastructure and Recreation divisions would be shared across councils.

- A shared services model including the Hornsby Shire and Ku-ring-gai Councils is estimated to result in a net operating result of around \$23.9 million in 2017-18 (for the Hornsby Shire entity), representing about a 3 per cent improvement to the current forecast net operating result.
- A shared services model, encompassing Hornsby, The Hills, and Ku-ring-gai Councils is estimated to result in a net operating result of around \$24.2 million in 2017-18 (for the Hornsby Shire entity), representing about a 5 per cent improvement to the current forecast net operating result.
- In addition to financial impacts, there are broader factors that should be considered to as part of the due diligence process, including asset utilisation and renewal, impacts to service delivery, governance structures, and transition measures.
- Further, more detailed due diligence is required to fully understand the potential impacts of reform options considered, and this should be supported by extensive engagement with neighbouring councils. As part of future due diligence, broader non-financial impacts should be considered, for example through the use of multi-criteria analysis.
- Following the completion of thorough due diligence, there must be an effective implementation strategy that should be underpinned by the due diligence itself in addition to a communications and change management strategy and planning for process and systems integration.

Executive summary

Background and purpose

Local government forms one of Australia's three levels of government. It performs crucial functions and is a key platform for local democracy and representation. Despite a series of structural changes in the Australian economy over time, the structure and functions of local government have largely remained static.

In response to this context, the NSW Independent Local Government Review Panel (ILGRP) was appointed to develop options to improve the strength and effectiveness of local government in NSW. In its Final Report, *Revitalising Local Government*, released in January 2014, noted that there is no one-size-fits-all model for structural reform of local government. There is, however, agreement that a strategic framework needs to be established in order for reform to be successful, and that this must be flexible to meet the demands of local communities.

In this context, Hornsby Shire Council engaged KPMG to undertake financial and strategic analysis of local government reform options in the Northern Sydney area including Hornsby, The Hills, and Ku-ring-gai Councils. The purpose of this analysis is to:

- enable effective and informed participation in, and contribution to, the local government reform agenda in NSW by Hornsby Shire Council;
- identify feasible local government reform options with reference to a predetermined set of local government reform principles; and
- identify and consider broader implications of local government reform alongside detailed financial analysis, in particular around effective implementation and communication.

Summary of approach and key findings

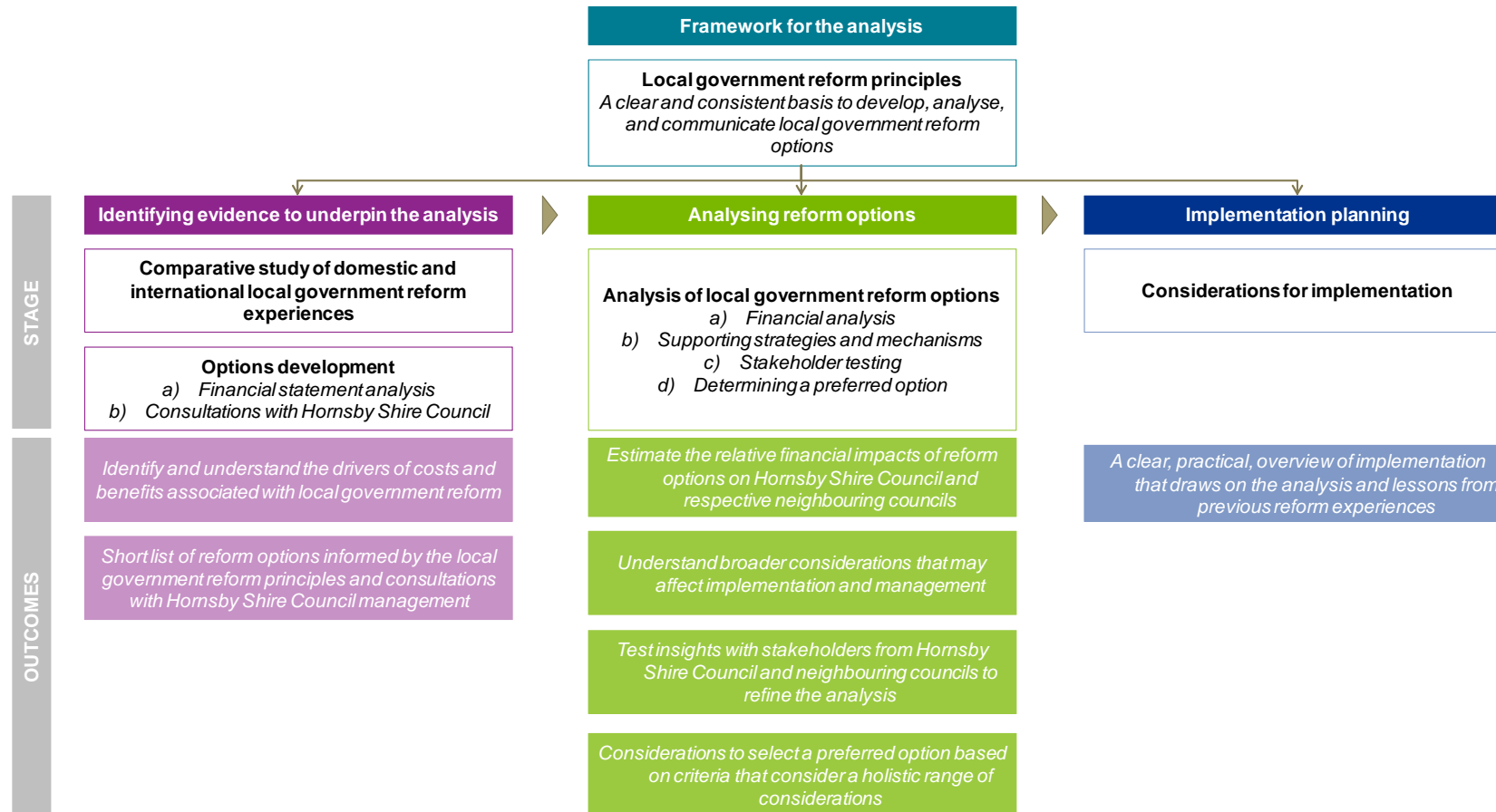
It is noted that the analysis within this report has been informed by the *Revitalising Local Government* Final Report released by the Independent Local Government Review Panel (ILGRP) in January 2014 (dated October 2013).

The approach for the analysis in this report has considered and addressed limitations in previous analyses of local government reform to contribute to a more holistic evidence base. An overview of the key stages and outcomes within the approach is provided in Figure ES.1.

Local government reform principles

Prior to undertaking the analysis, a set of local government reform principles were developed to guide the development, analysis, and communication of local government reform options.

Figure ES.1: Approach and key outcomes



Source: KPMG.

A review of domestic and international reform experiences in Queensland, Tasmania and New Zealand identified a number of underlying principles or themes.^{2 3 4} Additionally, a critique of the principles underpinning the local government reform process in Queensland by Dollery, Ho and Alin was also reviewed.⁵ Across these examples, three principles were consistently identified, namely:

- **local government capacity**, or the ability of local government to maintain or enhance levels of service delivery;
- **financial sustainability**, as this impacts the ability of councils to sustainably fund adequate and effective services; and
- **local representation**, or the effectiveness with which local government can represent ratepayers in the broader public debate.

Options

Table ES.2 summarises the reform options that were developed with reference to the local government reform principles and in consultation with Hornsby Shire Council management.

Table ES.2: Options summary

Option	Description
Option 1 <i>Base case</i>	Option 1 is the base case – or ‘do nothing’ option – in which the current structure of local government areas considered within the analysis were assumed to remain constant.
Option 2 <i>Hornsby and The Hills Councils</i>	Option 2 is an amalgamation option that would involve combining Hornsby and The Hills Councils , with minor adjustments to each council’s southern boundaries.
Option 3 <i>Hornsby and Ku-ring-gai Councils</i>	Option 3 is an amalgamation option that would involve combining Hornsby and Ku-ring-gai Councils , with a minor adjustment to the southern boundary of Hornsby Shire Council. It is noted that the specification of Option 3 is consistent with the recommendation made in the ILGRP Final Report.
Option 4 <i>Hornsby, The Hills, and Ku-ring-gai Councils</i>	Option 4 is an amalgamation option that would involve combining Hornsby, The Hills, and Ku-ring-gai Councils , with an adjustment to the southern boundary of Hornsby and The Hills Councils.

² Local Government Board (2010), ‘Report on Principles for Voluntary Mergers’, Hobart.

³ Local Government Reform Commission (2007), ‘Report of the Local Government Reform Commission: Volume 1’, Brisbane.

⁴ Thames Coromandel District Council 2013, Local Government Reorganisation & Unitary Authority Project, Thames, <http://www.tcdc.govt.nz/amalgamations>.

⁵ Dollery, B., Ho, C. and Alin, J. (2008), ‘No lessons learned: a critique of the Queensland Local Government Reform Commission final report’, Agenda: A Journal of Policy Analysis and Reform, vol. 15, no. 1, pp. 67-84.

Option	Description
Option 5 <i>Shared Infrastructure and Recreation between Hornsby and The Hills Councils</i>	Option 5 is a shared services model between Hornsby and The Hills Councils , where an Infrastructure and Recreation division would be shared across councils.
Option 6 <i>Shared Infrastructure and Recreation between Hornsby and Ku-ring-gai Councils</i>	Option 6 is a shared services model between Hornsby and Ku-ring-gai Councils , where an Infrastructure and Recreation division would be shared across councils.
Option 7 <i>Shared Infrastructure and Recreation between Hornsby, The Hills, and Ku-ring-gai Councils</i>	Option 7 is a shared services model between Hornsby, The Hills, and Ku-ring-gai Councils , where an Infrastructure and Recreation division would be shared across councils.

Source: KPMG.

Analysis

Analysis was undertaken from the perspective of each council affected by the respective option. Results of the financial analysis were considered:

- separately for each council, and compared to the projected net operating results published in respective long term financial projections; and
- in aggregate, and compared to the aggregate projected aggregate net operating results of affected councils.

Where data permitted, costs and benefits were quantified in monetary terms. Where data was insufficient to quantify costs or benefits, these were qualitatively analysed.

Given the nature of available data, more detailed analysis was undertaken for Hornsby Shire Council, with simplifying assumptions used to undertake higher level analysis for other councils. It is noted that estimates for other councils are illustrative only, given the nature of available data and the underlying assumptions. To assist in considering these results in this context, the approach also included:

- a formal approach to neighbouring councils for participation through the analysis, including the provision of more detailed financial and operational data;
- a consultation process with neighbouring councils to test insights and assumptions; and
- development of the modelling framework with the flexibility to update the analysis over time.

Given this approach, there is scope to refine and extend the analysis over time, should further, more detailed data become available.

It is noted that all assumptions underpinning the financial analysis were determined in consultation with, and reviewed and approved by, relevant Hornsby Shire Council management personnel.

Table ES.3 to Table ES.8 summarise the financial analysis results for each reform option, including from the perspective of:

- Hornsby Shire Council only, measured relative to Hornsby Shire Council’s current long term financial projections (base case); and
- new local government entities created within each option, measured relative to the sum of respective councils’ current long term financial projections (base case).

Option 2

Option 2 projects substantial gains in percentage terms relative to the base case, with the key drivers expected to be staffing efficiencies and efficiencies in *Materials and contracts* and *Other expenses*.

ES.3: Summary of net operating results and projected savings – Option 2

	2013-14	2014-15	2015-16	2016-17	2017-18	Cumulative 2013-14 to 2017-18	Cumulative 2013-14 to 2022-23
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Option 1 (Base case) <i>consisting of</i>	79.6	39.8	46.9	61.8	77.7	305.9	709.8
<u>Hornsby</u>	16.1	13.5	12.1	19.7	23.0	84.5	209.0
<u>The Hills</u>	63.5	26.3	34.9	42.1	54.6	221.4	500.7
Option 2	76.8	47.0	54.5	69.7	85.9	333.8	783.7
Saving	-2.8	7.2	7.5	7.8	8.2	27.9	74.0

Note: Cumulative impacts are not discounted.

Source: KPMG calculations.

Option 3

The projections show that the gains relative to the base case are substantial, however, less than expected for Option 2, reflective of the difference in operational scale between The Hills Shire Council and Ku-ring-gai Council. For example, The Hills Shire Council had 580 FTEs at the end of June 2013 compared to 430 FTEs at Ku-ring-gai Council. Further, projected expenditure for 2013-14 at The Hills Shire Council is about \$130 million, compared to \$105 million at Ku-ring-gai Council.

Table ES.4: Summary of net operating results and projected savings – Option 3

	2013-14	2014-15	2015-16	2016-17	2017-18	Cumulative 2013-14 to 2017- 18	Cumulative 2013-14 to 2022- 23
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Option 1 (Base case) <i>consisting of</i>	30.9	44.2	48.7	77.1	66.1	267.1	558.7
<u>Hornsby</u>	16.1	13.5	12.1	19.7	23.0	84.5	209.0
<u>Ku-ring-gai</u>	14.8	30.7	36.6	57.4	43.1	182.6	349.7
Option 3	27.3	49.3	54.0	82.6	71.9	285.0	609.1
Saving	-3.6	5.1	5.3	5.5	5.8	18.0	50.4

Note: Cumulative impacts are not discounted.

Source: KPMG calculations.

Option 4

Option 4 is projected to deliver the largest percentage gains to both Hornsby Shire Council and the aggregate entity relative to the base case. This reflects the increased opportunity for staffing and other expenditure efficiencies attributable to the increased scale of three councils relative to two in Options 2 and 3.

Table ES.5: Summary of net operating results and projected savings – Option 4

	2013-14	2014-15	2015-16	2016-17	2017-18	Cumulative 2013-14 to 2017- 18	Cumulative 2013-14 to 2022- 23
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Option 1 (Base case) <i>consisting of</i>	94.4	70.5	83.6	119.2	120.8	488.5	1,059.4
<u>Hornsby</u>	16.1	13.5	12.1	19.7	23.0	84.5	209.0
<u>The Hills</u>	63.5	26.3	34.9	42.1	54.6	221.4	500.7
<u>Ku-ring-gai</u>	14.8	30.7	36.6	57.4	43.1	182.6	349.7
Option 4	94.3	85.9	99.6	135.8	138.2	553.8	1,222.6
Saving	-0.1	15.4	16.0	16.6	17.5	65.3	163.1

Note: Cumulative impacts are not discounted.

Source: KPMG calculations.

Option 5, 6 and 7

For the shared service options the projections show that gains are marginal relative to the respective amalgamation options, reflective of:

- the reduced potential for efficiencies of scale, given only one division (Infrastructure and Recreation) is assumed to be shared; and
- the likely non-linear nature of costs to implement a shared services arrangement (i.e. the marginal cost to share additional divisions would decrease for each additional division).

Table ES.6: Summary of net operating results and projected savings – Option 5

	2013-14	2014-15	2015-16	2016-17	2017-18	Cumulative 2013-14 to 2017-18	Cumulative 2013-14 to 2022-23
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Option 1 (Base case) consisting of	79.6	39.8	46.9	61.8	77.7	305.9	709.8
<u>Hornsby</u>	16.1	13.5	12.1	19.7	23.0	84.5	209.0
<u>The Hills</u>	63.5	26.3	34.9	42.1	54.6	221.4	500.7
Option 5	77.6	41.5	48.7	63.6	79.5	311.0	725.1
Saving	-2.1	1.7	1.8	1.8	1.9	5.1	15.3

Note: Cumulative impacts are not discounted.

Source: KPMG calculations.

Table ES.7: Summary of net operating results and projected savings – Option 6

	2013-14	2014-15	2015-16	2016-17	2017-18	Cumulative 2013-14 to 2017-18	Cumulative 2013-14 to 2022-23
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Option 1 (Base case) <i>consisting of</i>	30.9	44.2	48.7	77.1	66.1	267.1	558.7
<u>Hornsby</u>	16.1	13.5	12.1	19.7	23.0	84.5	209.0
<u>Ku-ring-gai</u>	14.8	30.7	36.6	57.4	43.1	182.6	349.7
Option 6	28.8	45.4	50.0	78.4	67.5	270.0	569.2
Saving	-2.2	1.2	1.3	1.3	1.3	3.0	10.5

Note: Cumulative impacts are not discounted.

Source: KPMG calculations.

Table ES.8: Summary of net operating results and projected savings – Option 7

	2013-14	2014-15	2015-16	2016-17	2017-18	Cumulative 2013-14 to 2017-18	Cumulative 2013-14 to 2022-23
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Option 1 (Base case) <i>consisting of</i>	94.4	70.5	83.6	119.2	120.8	488.5	1,059.4
<u>Hornsby</u>	16.1	13.5	12.1	19.7	23.0	84.5	209.0
<u>The Hills</u>	63.5	26.3	34.9	42.1	54.6	221.4	500.7
<u>Ku-ring-gai</u>	14.8	30.7	36.6	57.4	43.1	182.6	349.7
Option 7	91.8	73.4	86.6	122.3	124.0	498.0	1,086.6
Saving	-2.6	2.9	3.0	3.1	3.2	9.5	27.2

Note: Cumulative impacts are not discounted.

Source: KPMG calculations.

Supporting strategies and mechanisms

Implementing local government reform, whether through boundary reform or shared services, requires consideration of a variety of supporting factors in addition to the expected financial impacts. This supporting strategies and mechanisms include:

- asset utilisation, renewal and financial sustainability, including
 - valuation and stock take of assets; and
 - maintenance of infrastructure.
- service delivery pathways to promote quality provision of council services, including consideration of:
 - service levels between councils;
 - human resource management across councils; and
 - corporate support functions.
- governance structures of new council entities, including consideration of how governance may impact the effectiveness of local representation; and
- transition measures to underpin the implementation of reforms.

Determining the preferred option

The preferred option should be identified using multi-criteria analysis to recognise that broader supporting strategies need to be considered in conjunction with the projected financial impacts for different reform options. The framework for conducting a multi-criteria analysis should therefore consider a range of appropriate financial and non-financial criteria, for example:

- the expected financial impacts of options;
- risks to financial sustainability over the longer term;
- strategic risks;
- risks to service quality and effectiveness;
- risks to the effectiveness of local representation; and
- risk to effective implementation and management over time.

The framework for Hornsby Shire Council to undertake the multi-criteria analysis has been provided within this report, however, further consultations and analysis is required to determine:

- the scoring for each criteria, particularly non-financial criteria; and
- appropriate weightings for each criterion, to be determined by stakeholders.

Next steps

There are a number of precursors to the finalisation and implementation of a preferred option by Hornsby Shire Council. These include, for example:

- continued engagement in the broader local government reform debate in NSW, particularly when the NSW Government formalises its position to the *Revitalising Local Government* report recently released by the ILGRP; and
- further, more detailed due diligence of reform options, particularly from the perspective of other councils in the reform process.

The recommended approach for Hornsby Shire Council is to actively engage all relevant councils and the NSW Government concurrently to undertaking a more comprehensive evaluation of the costs and benefits of all options. The approach to developing the analysis within this report has the flexibility to be extended and refined over time, should further, more detailed data become available.

Following the completion of detailed due diligence, stakeholder engagement, and agreement of a preferred option, there should be detailed implementation planning to ensure successful delivery of reform over time. A structured and effectively communicated approach to implementation and management of the reform process is critical for its overall success, including the realisation of potential benefits.

A high level implementation plan for an amalgamation or shared services reform model is presented within this report, however, a more complete implementation plan will be required following the completion of all required due diligence that provides:

- greater detail that is targeted to the specific option being considered;
- target completion dates for actions; and
- accountabilities for those actions within agreed timeframes.

1 Introduction

Local government forms one of Australia's three levels of government, with the others being the Federal Government and the respective State and Territory governments. Although local government arguably has the lowest public profile of the three levels of government, it performs crucial functions and is a key platform for local democracy and representation.

Most local governments in Australia are statutory bodies that are empowered by the respective State/Territory legislature to undertake and enforce certain responsibilities within their local jurisdiction. They provide local governance and are responsible for the delivery of a range of services to their local communities. In particular, the main roles of local governments include:

- local governance and advocacy across different levels of government (e.g. State/Territory and Federal);
- oversight of planning and community development;
- certain regulatory requirements, for example planning and development approvals;
- the provision and maintenance of trunk infrastructure, for example roads, bridges, and water and waste water management; and
- service delivery, for example household waste collection and disposal and some health services.

To fund their obligations, local governments raise revenue from:

- taxation, typically referred to as 'rates', that are determined with respect to the value of constituents' property;
- user charges for infrastructure and services; and
- grants from Federal and State/Territory governments.

1.1 Purpose

This report provides a strategic and financial analysis of local government reform options in the Northern Sydney area. It is noted that the analysis within this report has been informed by the *Revitalising Local Government* Final Report released by the Independent Local Government Review Panel (ILGRP), entitled *Revitalising Local Government*, released in January 2014 (dated October 2013).

The purpose of this report is to:

- enable effective and informed participation in, and contribution to, the local government reform agenda in New South Wales (NSW) by Hornsby Shire Council;
- identify feasible local government reform options with reference to a predetermined set of local government reform principles; and
- identify and consider broader implications of local government reform alongside detailed financial analysis, in particular around effective implementation and communication.

This report considers and extends upon analysis previously commissioned by Hornsby Shire Council, including:

- research undertaken by The Crosby|Textor Group to assess community perceptions and preferences with respect to local government representation and reform; and
- analysis undertaken by PricewaterhouseCoopers (PwC) of amalgamation options that included Hornsby Shire Council and neighbouring councils.

1.2 Scope

The scope of the engagement was to:

- develop seven local government reform options (including a base case) with reference to a predetermined set of local government reform principles;
- conduct a financial and strategic analysis of options, including:
 - detailed financial statement analysis of Hornsby Shire Council data;
 - high level financial statement analysis of publicly available Council data for neighbouring councils;
 - financial modelling and sensitivity testing of options;
 - internal stakeholder consultations and testing with up to three internal stakeholders at Hornsby Shire Council;
 - analysis of broader supporting strategies and mechanisms, including service delivery pathways, asset utilisation and renewal, socio-economic and cultural considerations, and governance structures; and
 - multi-criteria analysis with up to five financial and non-financial criteria to determine the preferred option for Hornsby Shire Council.
- seek input to the analysis from neighbouring councils that may be impacted by local government reform options considered in this report.

1.3 Report structure

This summary report is structured as follows:

- Chapter 2 provides background information to Hornsby Shire Council and the public policy context for local government reform in NSW;
- Chapter 3 discusses the approach to undertake the financial and strategic analysis of local government reform options;
- Chapter 4 presents the local government reform principles that underpin the development, analysis, and communication of local government reform options;
- Chapter 5 provides the key insights from a comparative study of domestic and international local government reform experience with respect to the local government reform principles;
- Chapter 6 presents reform options that were developed with respect to the local government reform principles and consultations with Hornsby Shire Council management;
- Chapter 7 presents the financial and strategic analysis of short listed local government reform options;

- Chapter 8 provides a high level implementation plan, drawing on the outcomes of the financial and strategic analysis, the comparative study, and the Independent Local Government Review Panel report, *Revitalising Local Government*; and
- a series of appendices provides detailed supporting information.

2 Background

This chapter provides background information to the role of local government in Australia, an overview of Hornsby Shire Council, the public policy context associated with local government reform in NSW, and key drivers of the local government reform debate.

2.1 Local government in Australia

Local government forms one of Australia's three levels of government, with the others being the Federal Government and the respective State and Territory governments. Although local government arguably has the lowest public profile of the three levels of government, it performs crucial functions and is a key platform for local democracy and representation.

Most local governments in Australia are statutory bodies that are empowered by the respective State/Territory legislature to undertake and enforce certain responsibilities within their local jurisdiction. They provide local governance and are responsible for the delivery of a range of services to their local communities. In particular, the main roles of local governments include:

- local governance and advocacy across different levels of government (e.g. State/Territory and Federal);
- oversight of planning and community development;
- certain regulatory requirements, for example planning and development approvals;
- the provision and maintenance of trunk infrastructure, for example roads, bridges, and water and waste water management; and
- service delivery, for example household waste collection and disposal and some health services.

To fund their obligations, local governments raise revenue from:

- taxation, typically referred to as 'rates', that are determined with respect to the value of constituents' property;
- user charges for infrastructure and services; and
- grants from Federal and State/Territory governments.

In 2008, there were 559 local councils in Australia, as shown in Table 2.1. The number of local councils today reflects the century-long process of change, where population growth, improvements in technology, and other factors of change have reshaped the role and scale of local government in Australia, for example by:

- increasing opportunities for, and costs associated with, economic and social interaction;
- influencing people's notion of identity, role, and connection with local communities; and
- increasing population densities, particularly in major metropolitan areas, thereby improving the benefits of fewer, larger council areas.

The number of local councils in NSW has varied substantially over the last 150 years. In 1858, there were 10 local governments in NSW, and this increased to 324 by 1910. Similar to the

aggregate, there were a number of local government amalgamations over the century from 1910, and today there are 152 councils.

Table 2.1: Number of local councils in Australia, selected years, 1910 to 2008

	1910	1967	1982	1990	2000	2008
New South Wales	324	224	175	176	174	152
Victoria	206	210	211	210	78	79
Queensland	164	131	134	134	157	73
South Australia	175	142	127	122	68	68
Western Australia	147	144	138	138	142	142
Tasmania	51	49	49	46	29	29
Northern Territory	-	1	6	22	69	16
Total	1,067	901	840	848	771	559

Source: Aulich et al. (2011).

Table 2.2 provides a comparison of the number of local government areas in capital cities in Australia relative to population and land mass. Relative to other major capital cities in Australia (i.e. Melbourne and Brisbane), Sydney has a relatively high number of local government areas relative to land mass and population.

Table 2.2: Comparison of local government across capital cities in Australia, 2011

Jurisdiction	Local government areas	Area	Population (2011)	Comparator statistics (rank) ⁶		
				population density per km ²	land area per council (km ²)	average number residents per council
	no.	km ²	no.			
Sydney	43	12,138	4,575,532	377 (4)	282 (6)	106,408 (5)
Melbourne	31	7,692	4,077,036	530 (5)	248 (4)	131,517 (6)
Brisbane	6	5,950	2,043,185	343 (3)	992 (7)	340,531 (7)
Perth ^a	30	5,386	1,696,062	315 (2)	180 (3)	56,535 (3)
Adelaide	18	1,827	1,203,873	659 (6)	102 (2)	66,882 (4)
Hobart	5	1,357	214,705	158 (1)	271 (5)	42,941 (2)
Darwin	3	112	127,500	1,138 (7)	37 (1)	42,500 (1)

^a Following the Final Report of the Metropolitan Local Government Review Panel, the Western Australian Government has indicated that the number of local councils in Perth will be reduced from 30 to 15.⁷

Source: Metropolitan Local Government Review Panel (2012).

⁶ Ranks are from lowest to highest.

⁷ Spagnolo, J. (2013), 'Perth councils to be halved from 30 to 15 under new WA Govt proposal', PerthNow, November 12, <http://www.perthnow.com.au/news/western-australia/perth-councils-to-be-halved-from-30-to-15-under-new-wa-govt-proposal/story-fnhocxo3-1226758223632> (accessed 10 December 2013).

2.2 Hornsby Shire Council

Hornsby Shire Council, located in the north of Sydney, is a diverse locality that covers 510 square kilometres from the suburban centres of Epping to Wiseman’s Ferry in the north and Danger Island in the east.⁸ Hornsby Shire was first incorporated in 1906 and has grown from a population of around 4,700 in 1906 to around 157,000 in 2011.⁹ In 2012, Hornsby Shire Council had a Gross Regional Product (GRP) of \$6.0 billion, or about 1.4 per cent of the Gross State Product of NSW.¹⁰

Chart 2.1: Map of Hornsby Shire Council and the Sydney Metropolitan Region



Source: Atlas.id (2013).

Within Hornsby Shire Council:

⁸ Hornsby Shire Council (2013), ‘Wards and Boundaries’, <http://www.hornsby.nsw.gov.au/council/about-our-shire/wards-and-boundaries> (accessed 10 December 2013).

⁹ Hornsby Shire Council (2013), ‘History’, <http://www.hornsby.nsw.gov.au/council/about-our-shire/history>, (accessed 10 December 2013); ABS 2011, ‘Hornsby Local Government Area, QuickStats: People’, http://www.censusdata.abs.gov.au/census_services/getproduct/census/2011/quickstat/LGA14000?opendocument&navpos=220, accessed 10 December 2013.

¹⁰ Economy.id 2013, ‘Hornsby Shire Economic Profile’, Economic profile-lite, <http://economy.id.com.au/hornsby>, accessed 10 December 2013; ABS 2013, ‘Australian National Accounts: National Income, Expenditure and Product, Sep 2013’, Cat. No. 5206.0, Canberra.

- around 23 per cent engage in volunteer work, higher than the NSW average of 17 per cent;¹¹
- nearly 39 per cent of residents were born overseas, higher than the NSW average;
- 56 per cent of households are classified as ‘couples with children’, around 10 percentage points higher than the NSW average; and
- residents tend to have higher than average earnings, with 23 per cent of households earning greater than \$3,000 per week compared to 12 per cent for NSW.

2.3 Public policy context for local government reform

Despite a series of structural changes in the Australian economy over time, the structure and functions of local government have largely remained static.

Today, many councils in NSW have been determined to be financially unsustainable, including through analysis by the NSW Treasury Corporation (TCorp) and the ILGRP. Further to these structural considerations at the council level, there are external challenges associated with population and economic growth that will continue to increase pressure on limited resources.

Over time, local government reform in NSW can increase the potential for local government to deliver better, more sustainable services to their local communities, including through:

- more financially sustainable operating structures;
- improved capacity for representation across levels of government; and
- strategic planning, information exchange, cooperative policy development and resource sharing.

The following sub sections discuss key milestones in the public policy debate in NSW.

2.3.1 *Destination 2036*

In August 2011, representatives from each council in NSW gathered in a process known as *Destination 2036*, with a key purpose being to discuss strategies to enhance the financial viability and service delivery capability of local governments.¹²

The motivations for *Destination 2036* were:

- discrepancies between the local government landscape in NSW relative to other Australian jurisdictions, as highlighted in Section 2.1; and
- recognition of structural population, technological, and economic changes in NSW and Australia more broadly, and the potential impacts of these trends over the medium and long term.

Participants at *Destination 2036* discussed a broad range of issues, including challenges and opportunities for local councils in the future. The top three challenges for local councils were:

- infrastructure and asset issues (27 per cent);

¹¹ ABS 2011, *op. cit.*

¹² Elton Consulting 2011, ‘Destination 2036: A Path Together’, Outcomes Report, Prepared for the Division of Local Government, Sydney.

- financial sustainability (26 per cent); and
- population and demographic changes (19 per cent).

The workshop resulted in the development of proposed priority actions in the following areas:

- **governance** – a review of the *Local Government Act*;
- **structure** – review of the current model and involvement of Regional Organisation of Councils in the development of major strategies and infrastructure issues;
- **functions** – service review to identify the needs and wants of the community and decide what bodies should be responsible for providing these services;
- **finance** – establish a working group to review local government finances and develop a new financing formula; and
- **capacity** – simplify and determine corporate governance arrangements between, and in partnership with, the three levels of governance.

2.3.2 Independent Local Government Review Panel

A key outcome of *Destination 2036* was the establishment of the NSW ILGRP, which was appointed to develop options to improve the strength and effectiveness of local government in NSW. Within its terms of reference, the ILGRP was tasked with investigating and identifying options for governance models, structural arrangements, and boundary changes. To date, this work has been informed by research reports, survey data, and community consultations.

The final ILGRP report, *Revitalising Local Government*, was released in early January 2014.¹³ The report highlights the case that there is a need for reform of local government in NSW, arguing that the current number of councils is unsustainable and that consolidation is required. The case for change is driven by the following factors:

- financial sustainability;
- infrastructure management and backlog; and
- projected increases in the population of NSW.

Financial sustainability of councils

A key issue identified by the ILGRP was poor financial viability of local governments in NSW. As part of the review process, NSW TCorp was appointed to assess the financial sustainability of councils in NSW. TCorp used a number of metrics, termed financial sustainability ratios (FSRs), to compare the financial performance of councils across NSW.^{14,15} In particular, the TCorp analysis found that:

- the majority of councils reported operating deficits over the review period from 2009-12, with only one-third reporting an operating surplus;

¹³ NSW Independent Local Government Review Panel 2013, *Revitalising Local Government*, Final Report, Sydney, October.

¹⁴ It is noted that there are a number of potential limitations associated with the use of FSRs, and these are outlined in further detail in Appendix C.

¹⁵ Treasury Corporation 2013, 'Financial Sustainability of the New South Wales Local Government Sector: Findings, Recommendations and Analysis', Prepared for the Independent Local Government Review Panel, April, Sydney.

- the sustainability of many councils is expected to deteriorate over the short term, based on current long term financial plans, with 46 per cent of councils estimated to be rated as ‘weak’ or lower within three years, compared to the 26 per cent that were rated in the same category when the analysis was conducted; and
- there was a \$7.2 billion infrastructure backlog in 2012, an average annual increase of 7.5 per cent from 2009-12, with around 61 per cent of this backlog in public roads (e.g. footpaths and car parks).

Significantly, the ILGRP made a strong case for the amalgamation of councils. The Panel pointed to a previous report, in which Graham Sansom (Chair of the ILGRP) was a co-author, which indicated that:

“...amalgamations offer the surest way to achieve efficiency and economies of scale, service improvements and strategic capacity. Stronger regional collaboration and shared services organisation may do so, but the outcomes across the board are less certain.”¹⁶

The TCorp analysis rated the financial sustainability of Hornsby Shire Council as ‘moderate’ and gave an outlook of ‘neutral’. These outcomes indicate that Hornsby Shire Council is expected to have:

- adequate capacity to meet its financial commitments in the short to medium term; and
- acceptable capacity to meet its financial commitments in the long term.

Attributes of local government reform

A key point highlighted by the ILGRP is that there is no one size fits all model with regards to structural reform. There is agreement that a strategic framework needs to be established in order for reform to be successful. Structural reform must be flexible in order to meet the demands of local communities. To that end, the report outlines a spectrum of potential reforms, including:

- amalgamation of councils;
- establishing Community Boards that are elected or appointed sub-council organisations that carry out a wide range of representational, planning and service delivery functions delegated by the council to assist in maintaining community identity and representation in areas where amalgamation is necessary;
- establishing statutory groupings of local councils known as Regional Joint Organisations to undertake high level functions; and
- introducing rural councils that are somewhat different to local councils and operate as part of a Joint Organisation in rural areas, as an alternative to amalgamations in addressing the needs of remote and rural communities.

The report suggests that amalgamations are the most effect form of local government consolidation (see Table 2.3). On the four attributes that it considers important in assessing local government reform – efficiencies, strategic capacity, service improvement, and local democracy –

¹⁶ *Ibid.*, pp. 72.



amalgamations are suggested as the strongest, compared to boundary changes, shared services, and regional collaboration.

Table 2.3: Summary attributes of different forms of consolidation

	Amalgamation	Boundary change^a	Shared services^b	Regional collaboration
Efficiency and economies of scale	Strong link	Potentially strong link, subject to size/disposition of re-shaped councils	Strong link	Weak link
Strategic capacity	Strong link	As above – benefits will flow to larger ‘new’ council/s	Potential medium-strong link subject to organisation structure and governance	Weak link
Service improvement and innovation	Strong link	As above	Strong link (but limited to services that are effectively shared)	Potential link subject to nature and scope of collaboration
Potential diminution of local democracy	Distinct risk, but can be managed	Some risk depending on nature of ‘new’ councils – can be managed	Risk where extensive decision making is ceded to joint authority – may be difficult to manage	Little or no risk

^a To create a larger, higher capacity council.

^b Assume more robust, statutory regional organisations.

Source: ILGRP (2013); Australian Centre of Excellence for Local Government (2011).

Community opinion

As part of the review process, the ILGRP commissioned research to investigate community views on the quality of service delivery, financial sustainability, local representation, and boundary reforms.¹⁷ The research found that local councils are generally able to provide the following core services effectively:

- waste management;
- parks and recreation facilities;
- library services;
- community services; and
- environmental management.

However, they appear less able to provide the following services and infrastructure effectively:

- road maintenance;
- footpath maintenance; and
- development assessment and planning.

Where financial management has been demonstrated by councils and where additional requirements are small, the research also found that communities may be willing to make greater contributions to local government to:

- maintain levels of services; and
- maintain or improve facilities that are locally important.

The research found that local representation was highly valued, particularly in rural and regional areas. It also identified that communities, particularly in metropolitan Sydney, may be willing to consider boundary changes.

Recommendations and implementation

The ILGRP made 65 recommendations for reforming local government in NSW. In particular, those specific to structural and boundary reform include:

- introduce additional options for local government structures, including regional joint Organisations, 'Rural Councils' and Community Boards, to facilitate a better response to the needs and circumstances of different regions;
- legislate a revised process for considering potential amalgamations and boundary changes through a re-constituted and more independent Boundaries Commission;
- encourage voluntary mergers of councils through measures to lower barriers and provide professional and financial support;

¹⁷ Elton Consulting (2012), 'Review of community surveys/polling on local government', Prepared for the Independent Local Government Review Panel, December, Sydney. Also see IRIS Research (2013), 'Local Government in NSW: Future Directions Opinion Poll', Prepared for the Independent Local Government Review Panel, August, Wollongong.

- strengthen arrangements within State government for coordinated metropolitan planning and governance, and to ensure more effective collaboration with local government; and
- seek evidence-based responses from metropolitan councils to the Panel's proposals for mergers and major boundary changes, and refer both the proposals and responses to the proposed Ministerial Advisory Group for review, with the possibility of subsequent referrals to the Boundaries Commission.

See Appendix A for the list of all recommendations and an indication of the potential impacts on Hornsby Shire Council.

The ILGRP also noted considerations with respect to the implementation of structural reforms to local government, as outlined in Box 2.1.

Box 2.1: Implementation of structural reforms

For amalgamations to be successful, NSW must be equipped with the appropriate processes to enable successful implementation of mergers on a case-by-case basis. In particular, these processes should include:

- decision making about the need for change and present a suitable proposal;
- detailed planning for implementation and ongoing management;
- implementing measures to lower the barriers to voluntary mergers and provide incentives to councils that indicate a willingness to pursue this type of reform;
- further developing proposals for required legislative changes;
- effectively managing the implementation in accordance with an agreed plan; and
- continuous monitoring and evaluation of these processes.

2.4 Previous analysis of local government reform options

There have been a number of previous analyses of local government reform options, including studies commissioned by Hornsby Shire Council and other councils. The approaches, analysis, and key findings of these studies were reviewed through the preparation of this report. The following sections discuss these studies and their role in informing the approach to developing this report for Hornsby Shire Council.

2.4.1 Analysis commissioned by Hornsby Shire Council

To contribute to a sustainable system of local governments in NSW, Hornsby Shire Council has engaged proactively with respect to the local government reform agenda. Hornsby Shire Council's contributions include a response to the ILGRP's consultation paper, which supported or supported in-principle 24 of the recommendations and noted points of clarification with respect to the remaining two.¹⁸

Further to its response the ILGRP consultation paper, Hornsby Shire Council has separately commissioned:

¹⁸ Phillips, S. (2013), 'Independent Local Government Review Panel Consultation Paper – Future Directions for NSW Local Government – Twenty Essential Steps', Letter from Hornsby Shire Council to the ILGRP, June 27, Sydney.

- research from The Crosby|Textor Group to assess its constituents’ views about local government reform options;¹⁹ and
- analysis by PricewaterhouseCoopers (PwC) of amalgamation options that included Hornsby Shire Council and neighbouring councils.²⁰

Crosby|Textor research

The Crosby|Textor research found that local government reform is not a primary concern for residents, with awareness of the ongoing reform process at around 53 per cent. This was reflected in the relatively high level of ‘soft’ support or opposition to reform. The research found a shared services model received a higher level of support compared to amalgamations, with a shared services model receiving the support of 73 per cent of residents. This was driven by a perception that this model would reduce costs and improve service delivery.

Key reasons for support and opposition of local government reform identified through the Crosby|Textor research are outlined in Table 2.4.

Table 2.4: Key reasons for support and opposition of local government reform.

	Reasons for support	Reasons for opposition
Local representation	Greater power of local councils to advocate for local needs.	Potential loss of local identity. Reduced levels of representation at the local level.
Financial sustainability	The ability for larger, merged councils to prioritise capital projects. Administrative cost reductions.	Cost efficiencies being unlikely to lead to reductions in local rates and charges.
Local government capacity	Residents may have access to a wider range of community service centres.	Competing priorities and interests for resources that may result in reductions in non-core or localised community projects.

Source: Crosby|Textor (2013).

PwC report

The PwC report examined the advantages and disadvantages associated with Hornsby Council merging with either:

- The Hills Shire;
- Hawkesbury Council; and

¹⁹ Crosby Textor (2013), ‘Crosby Textor Qualitative Research’, Sydney.

²⁰ PwC (2013), ‘The Hills Shire Council and Hornsby Shire Council: Preliminary analysis of a Hills/Hornsby Council merger’, April 11, Sydney.

- Ku-ring-gai Council.

The report found that each council was in a different financial position, with Hornsby and Hawkesbury being in worse financial positions due to net operating deficit positions in 2011-12. Consequently, there may be perceived ‘winners’ and ‘losers’ in any merged council scenario. The Hills Shire and Hornsby Shire Councils have aligned strategic directions, and this can provide a framework for potentially greater synergies in a merged council. Cost efficiencies are most likely to be found in corporate support functions, and the benefits of merged councils was likely to mainly increase the financial sustainability of the merged entity, but also increase its lobbying power.

It is noted that the PwC analysis provides some context to the development of reform options. For the purposes of supporting decision making, however, it is illustrative only, and therefore preliminary in nature, given that:

- it does not consider a broader range of reform options (e.g. shared services);
- financial impacts associated options considered are not quantified; and
- while focus on financial impacts is important, there needs to be consideration of broader impacts and how best to manage these during implementation and over time.

2.4.2 Analysis commissioned by other parties

SGS Economics & Planning was engaged by Warringah Council in 2013 to undertake a high level strategic and financial analysis of options for local government structural change. In particular, the report analysed four reform options under three different scenarios.

Options analysed included:

- a base case, where current local government boundaries were assumed to remain unchanged;
- an amalgamation of Manly, Pittwater, and Warringah Councils;
- an amalgamation of Manly, Mosman, Pittwater, and Warringah Councils; and
- an amalgamation of Manly, Pittwater, Warringah, Ku-ring-gai, and Hornsby Councils (with a minor boundary adjustment south of the M2 Motorway).

Each option was analysed under three different scenarios, namely:

- councils adopting the cost structure of Warringah Council across five major service areas;
- reductions in per capita costs of service, estimated using econometric techniques with data from selected councils in NSW; and
- per capita costs set at the upper limit (with a 75 per cent confidence interval) based on the results of the econometric model in the second scenario.

In net present value (NPV) terms, the cost savings estimated by SGS Economics & Planning were:

- between \$12.1 million and \$376.6 million over 10 years for Option 2;
- between \$96.2 million and \$503.1 million over 10 years for Option 3; and

- between -\$45.3 million and \$732.8 million over 10 years for Option 4.

The analysis provided in the SGS Economics & Planning report should be considered high level, given a number of limitations with the approach. For example:

- the report does not detail the framework within which reform options were established, citing only discussions with Warringah Council;
- the report does not consider either the upfront or ongoing costs associated with implementation and management of reform options, meaning that the net impact of options for affected councils cannot be determined; and
- it may be unreasonable to assume that a council could adopt another council's cost structure without substantial cost, given potential differences in – for example – organisational structure, the location and profile of assets, and responsibilities in service provision.

2.4.3 Underpinning more informed contributions to the local government reform debate

Previous analyses commissioned by Hornsby Shire Council and other councils have been useful in establishing some of the context for consideration of local government reform options. Effective and informed decision making by Hornsby Shire Council will, however, require more substantive analysis and insights. In particular, analysis needs to more holistically consider:

- a broader range of reform options, and practical considerations with pursuing these options;
- financial analysis underpinned by more evidence-based assumptions to deliver more meaningful analysis to inform decision making;
- broader impacts of reform options in addition to financial impacts, for example the relationship between reform options and the capacity for improvements in service delivery and local representation; and
- strategies to support effective implementation and communication and drive better practice, that draw on learnings from domestic and international reform experiences and consider these in the context of the reform environment in NSW.

The development of the approach for the analysis in this report has considered and addressed these limitations by extending the approaches to previous analyses. The purpose is to contribute to a more holistic evidence base to underpin decision making by Hornsby Shire Council. Further detail on the approach is provided in Chapter 1.

2.5 Summary of the need for local government reform

Historically, boundary reforms have been used to improve the efficiency and effectiveness of local government, both in Australia and internationally. Often, the success or failure of these reforms has been dependent on their design and implementation. Prior experience suggests that the successful design and implementation of local government reform is dependent on several factors, including:

- the involved councils conducting appropriate due diligence;
- community engagement;
- close liaison with the Division of Local Government;

- detailed transition planning, including a dedicated project team with staff from all the involved councils;
- a capacity to explain the benefits and costs to stakeholders; and
- open minds, adaptability and flexibility of councillors and staff.²¹

Given the current policy and operational context in NSW, a financial and strategic analysis of local government reform options will help to develop an evidence base to inform and support the reform journey, including through:

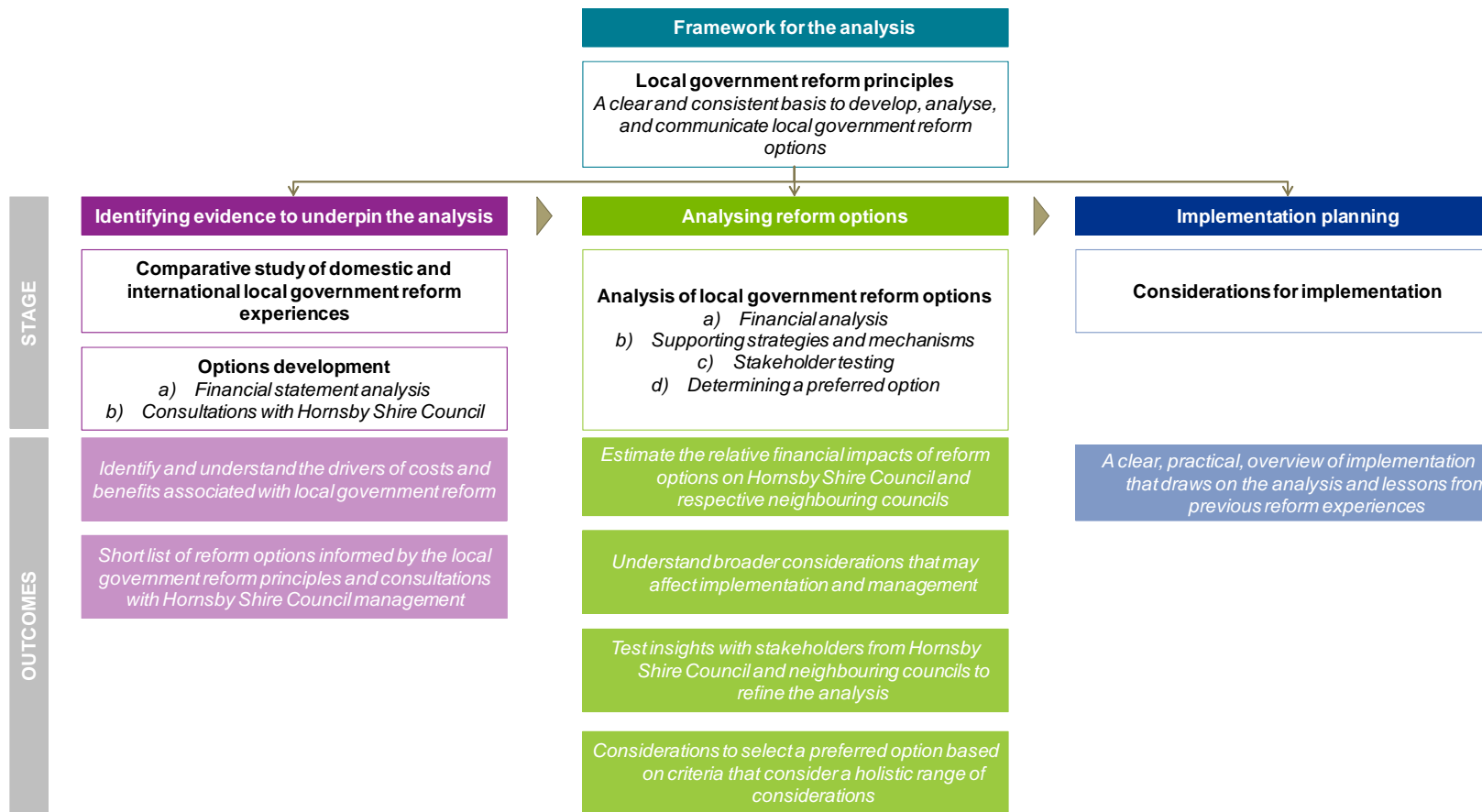
- demonstrating an objective, evidence-based approach to developing and assessing reform options to stakeholders;
- enabling councils to communicate the benefits and costs of reform options to stakeholders;
- as a component of the required due diligence that underpins the implementation of reform; and
- informing transition planning, community and stakeholder engagement, and governance.

²¹ Davis, B. (2013), 'Council amalgamations: some insights from the experiences of City of Greater Geraldton, amalgam of City of Geraldton, Shire of Greenough & Shire of Mullewa', Presentation to Local Government Finance Professionals, Melville, August 16.

3 Approach

This chapter provides an overview of the approach to undertaking the financial and strategic analysis of local government reform options for Hornsby Shire Council.

Figure 3.1: Approach and key outcomes



Source: KPMG.

3.1 Local government reform principles

Prior to undertaking the financial and strategic analysis, a set of local government reform principles was developed. The purpose of the principles was to provide the lens through which to develop, analyse, and communicate reform options with community, government, and other stakeholders.

The approach to developing the local government reform principles involved:

- high level desktop research of domestic and international experience, including in Tasmania, Queensland, Canada, and New Zealand, to identify, where applicable, the:
 - principles or concepts that guided the development of reform options;
 - measures by which the success of reforms were measured following implementation of the reforms; and
 - similarities and differences in the structures and functions of local government across jurisdictions to better understand how the researched examples may be relevant in the context of Hornsby and the Northern Sydney area.
- a consultation and testing process with the Hornsby Shire Council Executive Committee (EXCO), to ensure that the scope of the principles was sufficient to:
 - capture key issues identified through the desktop research and from the experience of EXCO members; and
 - provide flexibility to ensure that options could be developed and analysed in the context of the Northern Sydney area.
- a secondary testing process with Hornsby Shire Councillors.

3.2 Comparative study of domestic and international boundary reform experiences

Having developed the local government reform principles, the next stage involved a detailed comparative study of domestic and international boundary reform experiences. The objective of the comparative study was to:

- better understand the costs and benefits associated with local government reform in other jurisdictions;
- support the options development; and
- inform the analysis of those options.

The comparative study consisted of a literature scan to identify post-reform evaluations of instances of boundary reform in the New Zealand, the United Kingdom, Canada, and the United States. The jurisdictions in the literature scan were chosen given the similarity of their political cultures and systems of government to Australia.

Examples of local government reform were then assessed against the local government reform principles, namely the impacts and considerations for implementation with respect to:

- financial sustainability;
- the capacity for, and quality of, service delivery; and
- effectiveness of representation and governance.

3.3 Options development

The financial and strategic analysis involved the analysis of seven local government reform options, including a base case – or ‘do nothing’ – option.

The objective of the options development was to identify a full range of reform options, including amalgamations, boundary reform, and shared services, through:

- drawing on the insights from the comparative study of reform experience across domestic and international jurisdictions;
- a consultation process with Hornsby Shire Council management to test and tailor insights from the comparative study to the context of Hornsby Shire Council and the Northern Sydney area more broadly; and
- comparing – at a high level – the financial performance of key councils in the Northern Sydney area (Hornsby Shire, The Hills Shire, Ku-ring-gai and Parramatta).

3.3.1 Financial statement analysis

The financial performance of councils in the Northern Sydney area was assessed using selected FSRs used by TCorp in its analysis for the ILGRP.²² These include:

- the operating performance ratio, which measures the sufficiency of operating revenue to cover operating expenditure;
- the own source operating revenue ratio, which measures the reliance on revenue from revenue sources other than fees, utilities, and charges (e.g. grants);
- the unrestricted current ratio, which measures the ability to access cash to meet operating and borrowing costs;
- the debt service cover ratio, which measures the use of operating cash to cover any debt from interest, principal, and lease payments;
- the capital expenditure ratio measures the extent to which capital expenditure replaces or expands the existing asset base;
- the cash expense cover ratio, which measures the capacity to pay immediate expenses without the need for additional cash; and
- the interest cover ratio, which measures the capacity to meet borrowing costs.

Detailed financial and staffing establishment data were received from Hornsby Shire Council, whereas data for the other councils was limited to higher level, publicly available data. Given the scope of available data, the financial statement analysis was:

²² It is noted that there were some FSRs that were not included in the analysis given data limitations, namely those related to asset renewals (e.g. the infrastructure backlog ratio, asset maintenance ratio, and building and infrastructure renewals ratio).

- more detailed for Hornsby Shire Council; and
- informed from publicly available data for other councils in the Northern Sydney area.

The FSRs were compared to benchmarks that were developed through work undertaken by the Queensland Treasury Corporation and the NSW Independent Pricing and Regulatory Tribunal (IPART).

The results of the financial statement analysis are provided at Appendix C.

3.3.2 Consultations with Hornsby Shire Council

Consultations were undertaken with Hornsby Shire Council management to:

- better understand the structure, functions, and operation of different divisions;
- test insights from the comparative study at a high level against the experience of divisional managers; and
- inform the development of assumptions to underpin the financial and strategic analysis of short listed reform options.

Further consultations were undertaken with managers from four divisions, namely:

- Corporate Support;
- Environment and Human Services;
- Infrastructure and Recreation; and
- Planning.

The outcomes of the consultations are provided at Appendix D.

3.4 Financial and strategic analysis of options

Having developed and short listed local government reform options in the Northern Sydney area, the next stage of the analysis was to undertake a financial and strategic analysis of short listed options. The analysis involved:

- estimation, where data permitted, of major financial costs and benefits that would be expected to accrue to Hornsby Shire Council;
- consideration of strategies and mechanisms to support effective implementation, as identified in the local government reform principles;
- testing of key insights with stakeholders from Hornsby Shire Council and neighbouring councils in the Northern Sydney area that may be affected by reform options considered in this report; and
- a multi-criteria analysis of reform options to determine the preferred option.

3.4.1 Financial analysis

Short listed options were subject to financial analysis to quantify the impact of major costs and benefits on the net operating results (i.e. income and expenditure items) of Hornsby Shire Council and respective councils considered within options.

Incremental financial inflows and outflows relative to Option 1 (base case) were identified through the detailed desktop research and estimated on a nominal basis using:

- detailed data provided by Hornsby Shire Council, including:
 - detailed long term financial statement projections over the period from 2013-14 to 2022-23;
 - current staffing data (budget and actual full time equivalent (FTE) employees, annual salary, accrued annual leave and long service leave) by division, branch, section, and team; and
 - community and cultural facility data for 2012-13, including income, expenditure, utilisation, and number of facility hires.
- publicly available financial statement data from The Hills Shire Council and Ku-ring-gai Council; and
- assumptions determined with respect to:
 - insights from the comparative study of domestic and international local government reform experience;
 - insights from consultations with divisional managers at Hornsby Shire Council; and
 - the scope and scale of available data.

Analysis was undertaken from the perspective of each council affected by the respective option. Results of the financial analysis were considered:

- separately for each council, and compared to the projected net operating results published in respective long term financial projections; and
- in aggregate, and compared to the aggregate projected aggregate net operating results of affected councils.

Where data permitted, costs and benefits were quantified in monetary terms. Where data was insufficient to quantify costs or benefits, these were qualitative analysed.

Given the nature of available data, more detailed analysis was undertaken for Hornsby Shire Council, with simplifying assumptions used to undertake higher level analysis for other councils. It is noted that estimates for other councils are illustrative only, given the nature of available data and the underlying assumptions. To assist in considering these results in this context, the approach also included:

- a formal approach to neighbouring councils for participation through the analysis, including the provision of more detailed financial and operational data;
- a consultation process with neighbouring councils to test insights and assumptions; and
- development of the modelling framework with the flexibility to update the analysis over time, should:
 - further, more detailed financial or operational data become available; and/or
 - assumptions be refined.

Given this approach, there is scope to refine and extend the analysis over time, should further, more detailed data become available.

It is noted that all assumptions underpinning the financial analysis were determined in consultation with, and reviewed and approved by, relevant Hornsby Shire Council management personnel.

A detailed description of the approaches and supporting assumptions underpinning the financial analysis is provided at Appendix B.

3.4.2 Analysis of supporting strategies and mechanisms

Having estimated the costs and benefits associated with reform options, the analysis considered a range of strategies and mechanisms to support effective implementation and management over time. The concepts within the analysis are aligned to the local government reform principles, and include:

- the impacts of reform options on the capacity for financially sustainable asset utilisation and renewal;
- effective and efficient service delivery pathways to support the capacity for quality service delivery;
- governance structures and strategies to ensure transparent and effective representation; and
- considerations for implementation, drawing on the desktop research and analysis.

3.4.3 Stakeholder testing

Following the completion of the analysis of financial impacts and supporting strategies and mechanisms, a stakeholder testing process was undertaken with key stakeholders from neighbouring councils considered within the analysis to:

- test and refine the assumptions and results of the financial analysis;
- develop a more detailed understanding of strategic and operational factors that may inform the broader analysis; and
- inform the development of the high level implementation plan.

Given the options analysed within the report, the management of The Hills Shire and Ku-ring-gai Councils were approached by Hornsby Shire Council management to participate in the testing process. Both The Hills and Ku-ring-gai Councils' management declined the invitation to participate.

3.4.4 Determining a preferred option

The final stage of the analysis involved identifying considerations for Hornsby Shire Council to select a preferred reform option, including:

- engagement with internal and external stakeholders to identify relevant financial and non-financial criteria to underpin the analysis;
- determining appropriate weightings for criteria that best reflect the values and priorities of stakeholders;

- ranking options with respect to each criteria, based on the outcomes of further, more detailed due diligence; and
- determining a preferred option, based on the weighted scores of each option with respect to the established criteria.

3.5 Considerations for implementation

Effective design of local government reform is important, however, insufficient to ensure success. Success is highly dependent on the quality of implementation of reforms. Given this importance, implementation considerations were identified and discussed at a high level by drawing on:

- guides to local government reform – including amalgamations – that have been issued by governments in Australia, Ireland and Canada;
- the comparative study of domestic and international local government reform experiences;
- consultations with members of Hornsby Shire Council;
- implementation plans for public sector organisational redesigns, on which KPMG has acted as an advisor; and
- a review of additional research material, including the ILGRP's Final Report.

It is noted that the implementation considerations are outlined at a high level only, and that a more detailed implementation plan would be required to support a final decision on reform options.

4 Local government reform principles

This chapter discusses the development of a set of local government reform principles that were used to underpin the development, analysis, and communication of local government reform options in the Northern Sydney area for Hornsby Shire Council.

4.1 Discussion of research findings

A review of domestic and international reform experiences identified a number of underlying principles or themes. These were identified through an examination of government documents related to local government reform efforts in Queensland, Tasmania, and New Zealand.^{23 24 25} Additionally, a critique of the principles underpinning the local government reform process in Queensland by Dollery, Ho and Alin was also reviewed.²⁶

The review identified three factors that were common considerations within the reform journey across the jurisdictions considered, namely:

- financial sustainability;
- service delivery; and
- quality of local representation.

Another key theme arising from the review was ‘communities of interest’. ‘Communities of interest’ is a common concept in discussions of local government reform, and can be considered with respect to three dimensions:

- **perceptual** – a sense of belonging to an area or locality that can be clearly defined;
- **functional** – the ability to meet with reasonable economy the community's requirements for comprehensive physical and human services; and
- **political** – the ability of the elected body to represent the interest and reconcile the conflicts of all its members.²⁷

The first dimension – perceptual – is inherently hard to measure. This shortcoming is amplified by the reality that people's sense of belonging can shift over time. This quality does not lend that dimension to being used to help develop fixed council boundaries.

The second dimension – functional – is related to the common understanding of the concept of ‘communities of interest’. The Victorian Commission in Local Government noted in 1986 that:

²³ Local Government Board (2010), ‘Report on Principles for Voluntary Mergers’, Hobart.

²⁴ Local Government Reform Commission (2007), ‘Report of the Local Government Reform Commission: Volume 1’, Brisbane.

²⁵ Thames Coromandel District Council 2013, Local Government Reorganisation & Unitary Authority Project, Thames, <http://www.tcdc.govt.nz/amalgamations>.

²⁶ Dollery, B., Ho, C. and Alin, J. (2008), ‘No lessons learned: a critique of the Queensland Local Government Reform Commission final report’, *Agenda: A Journal of Policy Analysis and Reform*, vol. 15, no. 1, pp. 67-84.

²⁷ Fulcher, H. (1989), ‘The concept of community of interest’, Discussion paper prepared for the S.A. Department of Local Government, accessed 28 November 2013, <http://www.dlg.nsw.gov.au/DLG/DLGHome/documents/CommissionsTribunals/bconcept.pdf>.

“Units of local government will be more effective if they cover the same area as that in which people live, work and play. This is because the most responsive municipality is one which is securely rooted in a well established community.”²⁸

It is noted that this dimension is not as practicable in today’s metropolitan areas unless there are much larger local government areas. This dimension may be more appropriate in localities that are more geographically enclosed (e.g. rural or remote areas).

The final dimension is potentially the most applicable in the context of this analysis, and aligns with an earlier identified principle, ‘quality of local representation’.

Given the above clarifications, the concept of ‘communities of interest’ has not been included as an explicit local government reform principle.

There were a number of other minor concepts identified within the review (e.g. the importance of ‘clean’ boundaries) that have been incorporated within each of the three main principles as appropriate.

4.2 Local government reform principles

The local government reform principles, along with indicators of those principles and key considerations, are outlined in Table 4.1.

²⁸ Victorian Local Government Commission (1986), ‘The Structure of Local Government in Victoria: Principles and Programs’, Melbourne, p. 52.

Table 4.1: Local government reform principles

Principle	Indicators	Key considerations
Local Government capacity <i>The ability of Local Government to maintain or enhance service delivery</i>	<ul style="list-style-type: none"> Quality of service delivery Quality of planning and infrastructure delivery Capacity to attract specialist skills 	<p>With effective coordination and management, larger Councils tend to have greater capacity than smaller Councils to leverage financial and operational scale to:</p> <ul style="list-style-type: none"> better manage planning and infrastructure delivery; and concurrently maintain or improve the quality and efficiency of services to residents.
Financial sustainability <i>The ability of the Council to sustainably fund adequate and effective services</i>	<ul style="list-style-type: none"> The capacity to secure economies of scale and scope Scope and scale of the resource base 	<p>Continued or improved financial sustainability is crucial in maintaining the capacity to deliver services, and it is often a key motivation of pursuing boundary reforms.</p> <p>Ensuring that any boundary reforms increase the financial sustainability of Council is vital, and this will be assessed through the financial statement analysis and cost benefit analysis.</p>
Local representation <i>The ability of the Local Government authority to effectively represent ratepayers</i>	<ul style="list-style-type: none"> Quality of local representation Communities of interest Quality of stakeholder management 	<p>Boundary reform options should be evaluated with respect to their impact on the effectiveness of local representation.</p> <p>The effectiveness of representation affects the quality of governance. Representation that is more reflective of the community is more likely to lead to outcomes aligned with the needs of the governed. Effective representation also helps manage the diverse (and sometimes competing) communities of interest that form a Council locality.</p>

Source: KPMG.

5 Comparative study of domestic and international local government reform experience

This chapter discusses the findings of the comparative study of domestic and international local government reform experience in the context of the local government reform principles:

- local government capacity;
- financial sustainability; and
- local representation.

Insights from relevant domestic and international reform case studies were used to inform the approach and assumptions for the financial analysis and considerations associated with supporting strategies and mechanisms to assist implementation and management.

Table 5.1 shows the relevance of the key sources from the comparative study to indicators within each local government reform principle.

Table 5.1: Relevance of key sources to local government reform principles

	Service delivery			Financial sustainability		Effectiveness of local representation		
	Quality of service delivery	Quality of planning and infrastructure	Capacity to attract specialist skills	Capacity to secure economies of scale and scope	Scope and scale of resource base	Quality of local representation	Communities of interest	Quality of stakeholder management
Reform case studies								
Auckland (2010)	✓	✓		✓	✓	✓	✓	✓
Queensland (2008)	✓	✓	✓	✓	✓	✓	✓	
Toronto (1998)	✓			✓	✓	✓	✓	✓
Victoria (1993)	✓		✓	✓	✓	✓		
Key domestic sources								
Aulich et. al. (2011)	✓	✓	✓	✓	✓	✓	✓	✓
Byrnes, J. & Dollery, B. (2002)				✓	✓			
Davis, B. (2013)		✓		✓	✓	✓		✓
Dollery, B., Ho, C. and Alin, J. (2008)	✓	✓	✓	✓	✓		✓	
Dollery, B. And Crase, J. (2004)	✓	✓	✓	✓	✓	✓	✓	✓

	Service delivery			Financial sustainability		Effectiveness of local representation		
	Quality of service delivery	Quality of planning and infrastructure	Capacity to attract specialist skills	Capacity to secure economies of scale and scope	Scope and scale of resource base	Quality of local representation	Communities of interest	Quality of stakeholder management
Financial Sustainability Review Board (2005)				✓	✓			
Local Government Reform Commission (2007)	✓	✓	✓	✓	✓	✓	✓	✓
Martin, J. (1999)	✓	✓	✓	✓	✓	✓	✓	
Key international sources								
Office of the Auditor-General (2012)	✓	✓	✓	✓	✓	✓	✓	✓
Office of the Chief Administrative Officer (1999)	✓	✓	✓	✓	✓	✓	✓	✓

Source: KPMG.

5.1 Key insights from domestic and international case studies

Insights from the comparative study of boundary reforms are relevant to both the development and analysis of potential boundary reform options for Hornsby Shire Council. Detailed case studies that underpin these key findings are provided at Appendix E.

5.1.1 Insights for the development of reform options

The key learning that should guide the development of boundary reform options is that boundary reforms are more likely to be straightforward when the councils being merged or entering into a shared services arrangement are of a similar size and type. Similarities between councils can include, but may not be limited to:

- density of development;
- demographic profile of residents;
- alignment of existing service provision and council operations; and
- economic profile of the region.

A partnership between relatively similar councils can help provide greater leverage to maintain or increase local government service delivery capacity. A council with a less heterogeneous population does not need to provide a more diffuse range of services; they can focus on core services for the demographic profile in the area. This ability to focus on core services can reduce the financial burden on the council, and hence improve their financial sustainability.

The effectiveness of local representation also improves in a council where representatives have a less heterogeneous population. As the number of communities of interest in an area increase, the time devoted by councillors to representing each community's interest must decline. This may negatively impact the quality of local representation.

5.1.2 Insights for the analysis of reform options

The comparative study identified a number of insights with respect to the potential impacts of reforms on financial sustainability, service delivery, and governance and representation.

Financial sustainability

Boundary reforms have both cost saving and expenditure implications for affected councils.

Benefits accrue in the form of cost savings, typically achieved through:

- staffing efficiencies; and
- property, plant, and equipment rationalisation.

The staffing efficiencies that have been achieved vary significantly, and are often dependent on the context of the reforms, though tend to have been between four per cent and seven per cent of the full time equivalent (FTE) staffing establishment. It is important to consider that these efficiencies will vary according to the function of the division or branch, and tend to be disproportionately achieved from reductions in administrative support functions and managerial positions.

Efficiencies can also be achieved through the rationalisation of buildings and equipment, however, there was little detail on either the magnitude or timing of these efficiencies in the comparisons. Given the permanency of property, plant, and equipment, it is reasonable to infer that:

- the scale of rationalisation would likely be dependent on:
 - the degree to which services reliant on infrastructure are aligned between councils; and
 - the age and location of existing infrastructure of the merging councils.
- efficiencies would materialise over a longer timeframe than staffing efficiencies.

A more detailed comparison of economies of scale achieved through local government reform in domestic and international jurisdictions was undertaken, and this is discussed in Section 5.2.

It is also critical to consider the upfront and recurrent costs associated with implementation of boundary reforms. Only the experience of Toronto provided explicit estimates of the costs of amalgamations. Upfront costs were estimated at 4.7 per cent of total expenditure, while ongoing costs were less than one per cent of ongoing expenditure.

Service delivery

The impact of boundary reforms on service delivery was only explicitly evaluated in the international case studies. In both cases, the boundary reforms largely resulted in maintaining or enhancing the quality of service delivery. In Toronto, despite initial widespread opposition to the boundary reforms, several years after the implementation, surveys showed that the public believed services had improved and boundary reform had been the right option.

In the domestic case studies, the impact was more variable, with the impact on service delivery often being a function of the quality of implementation rather than the structure of the reform. The quality of implementation of boundary reform relates to:

- the involved councils conducting appropriate due diligence;
- the extent and nature of community engagement;
- close liaison with the Division of Local Government;
- detailed transition planning, including a dedicated project team with staff from all the involved councils;
- a capacity to explain the benefits and costs to stakeholders; and
- the ability of leadership to foster open minds, adaptability, and flexibility of councillors and staff.²⁹

Governance and representation

In the case studies identified in the comparative study, the ratio of elected representatives to resident declined, however, this was balanced by the formation of larger councils that could:

- more effectively advocate for constituents; and

²⁹ Davis, B. (2013), *op. cit.*

- partner with other levels of government.

Further, boundary reforms that resulted in councils covering large geographies (e.g. Auckland and Toronto) used local community boards to maintain community engagement at the local level.

5.2 Evidence associated with economies of scale

The purpose, scale, and role of local government varies across jurisdictions, however, in most jurisdictions (including Australia), there is the mismatch between:

- the responsibilities of local government; and
- the legal authority of local government to raise revenue in order to fund the services necessary to meet responsibilities.

Boundary reform

One response to this misalignment has been local government amalgamations, and these have typically been driven by a belief that larger councils can provide service more efficiently than smaller councils – hence, increase their financial sustainability. This belief has tended to be supported by rapid social, economic, and technological changes that have reduced the impacts associated with low population density that often necessitated geographically smaller councils. A key focus of the comparative study was therefore to identify evidence, if any, associated with economies of scale that can be obtained through local government reform.

Within the international literature, there was mixed evidence associated with economies of scale. In summary:

- 29 per cent of research papers found evidence of a U-shaped cost curve, where diseconomies of scale can exist when the population is either too large or small;
- eight per cent found evidence of economies of scale; and
- 39 per cent found no statistical relationship between per-capita expenditure and population size;
- 24 per cent found diseconomies of scale.³⁰

The mixed evidence within the international literature is largely attributable to different services provided by local government in various countries. Consequently, most results from local governments across jurisdictions are too dissimilar for meaningful comparison. For example, in much of the research that focuses on the United Kingdom, the dependent variable that is measured against population size is housing expenditure. This reflects the historic role that local councils in Britain have fulfilled in the provision of public housing. Similarly, social services and education expenditure is also used frequently as a dependent variable in research on local councils in Canada and the United States. In Australia, local government has an extremely limited to negligible role in the provision of these services, as they are largely the responsibility of State/Territory and Federal governments.

³⁰ Byrnes, J. & Dollery, B. (2002), 'Do Economies of Scale Exist in Australia Local Government? A Review of the Research Evidence', *Urban Policy and Research*, vol. 20, iss. 4, pp 391-414

International examples are less useful in providing insight into the extent of the overall economies of scale that can be generated from boundary reform in the Australian context. However, specific international case studies can be useful in understanding the economies of scale that can be obtained through boundary reform in particular areas of local councils' operations.

Within the Australian literature, there were nine papers that had conducted regressions of local government expenditure against population to determine if economies of scale existed in the operation of local government. Of these:

- seven found evidence for economies of scale;
- one found evidence of economies of scale; and
- one found no evidence of economies of scale.

Importantly, none of the Australian research findings found evidence for diseconomies of scale. This is significant, given that the research from the Australian context is more applicable than the international evidence when considering boundary reform options in the Northern Sydney area.

All else equal, the evidence suggests that increases in the ratepayer base and geographic area of councils in Australia could reasonably be expected to deliver economies of scale. It is important, however, to consider that the extent of potential deliver economies of scale is dependent on broader factors, in particular the effectiveness of implementation and ongoing management.

Shared services

The economies of scale achieved from shared services models may be smaller compared to a council amalgamation since only a subset of the councils' activities would be brought together. Creating shared services is, however, associated with less structural change than boundary reforms, and has the potential to achieve both economies of scale, while minimised the potential impact on the effectiveness of local representation.

A number of benefits have been identified from shared services, as outlined in Table 5.2.

Table 5.2: Potential benefits associated with shared services

Benefit	Mechanism
Access to skills and expertise	Shared resourcing
Exchange of best practise and standardisation, consistency and continuous improvement of processes	Knowledge transfer
Economies of scale leading to procurement savings and lower staff costs	Shared resourcing
Improved community outcomes and achievement of customer service focus	Governance
Coordinated services	Governance
Improved compliance with standards and regulations	Governance

Benefit	Mechanism
Greater concentration on strategic outcomes	Governance

Source: de Souza, V. and Dollery, B. (2011), 'Shared Services in Australian Local Government: The Brighton Common Service Model', *Journal of Economic and Social Policy*: Vol. 14: Iss. 2. Article 4.

The degree of success varies considerably among shared services models. Key considerations that may influence the success of the models include spatial distance, conflicting objectives of the parties, uncertainty about potential benefits. The services which are suitable for shared delivery are those which enable the councils to achieve the most benefits while overcoming the challenges of implementing the shared services model.

A more detailed overview of the relevant domestic and international literature on economies of scale is provided at Appendix E.

5.3 Limitations of the comparative study

Insights from the comparative study have some inherent limitations, and these should be considered when applying the learning's to the analysis of local government reform options in the Northern Sydney area.

- There are substantial differences in the nature and type of services provided by local government in other countries. To enable reasonable comparisons, changes in the scope and scale of local government attributable to boundary reform means that the magnitude and impact of efficiencies in Australian jurisdictions should be considered in this context.
- The types of boundary reforms examined did not include councils that form a sub-section of a greater metropolitan area. For example, Toronto and Auckland councils are responsible for entire cities. Unlike these examples, local governments in Australia typically only have responsibility for sub-sections of larger geographies.
- Case studies of boundary reforms within the analysis were initiated by the relevant State Governments and largely met with opposition from affected councils and their constituents. This is significant, as it would have affected the approach of the councils to implementation of the reforms. For example, it may have limited their engagement during the development of the options and impacted the structures to support effective implementation. In contrast, there is a more constructive and proactive approach to assessing potential boundary reform options in the Northern Sydney area. This means that there may be greater scope to develop more detailed analysis and identify more effective strategies and mechanisms to both support implementation and derive greater benefits for the affected councils and the broader community.

6 Options development

This chapter discusses the development of reform options to be considered within the financial and strategic analysis. Seven options – including a base case – were identified to be subject to further analysis.

6.1 Options development framework

The framework used to develop options was developed based on insights from the comparative study of domestic and international boundary reform experience (see Chapter 5) and consultations with Hornsby Shire Council.

The comparative study showed that previous boundary reform options tended to be developed with respect to:

- geographical similarities across council areas under consideration;
- socio-economic characteristics of council areas; and
- similarities in financial sustainability and opportunities for scale efficiencies.

Each of these characteristics is directly related to one or more indicators within the local government reform principles developed in Chapter 4, as outlined in Table 6.1.

Given the nature of shared services relative to boundary reform, the indicators listed above were not directly relevant to the options development.

ILGRP Final Report

In January 2014, the ILGRP released its Final Report, *Revitalising Local Government*. In the report, the ILGRP recommended the formation of Joint Organisations (JO) for councils in NSW. The recommendation for JOs derived from a proposal in the Panel's earlier report, *Future Directions*, to establish stronger regional entities by amending the County Council provisions of the *Local Government Act*. The Panel's Final Report incorporated feedback on the County Council model to recommend the establishment of JOs. The proposed core functions of JOs include:

- strategic regional and sub-regional planning;
- inter-government relations and regional advocacy;
- regional alliances of local government utilities; and
- other joint activities, such as major infrastructure projects, regional waste and environmental management, regional economic development, regional library services and 'high level' corporate services of 'back office' functions.

JOs are intended to replace County Councils in regional NSW and Regional Organisation of Councils in metropolitan Sydney.

In metropolitan Sydney, five JOs are proposed. Importantly, the boundary between the North and the West JO is proposed to mirror the existing boundary between Hornsby and The Hills

Shire Councils. However, the ILGRP noted that JOs would not be needed in metropolitan Sydney unless a reduction in the number of councils did not take place.

In the context of this report, the financial impacts associated with shared services options can be seen as an approximation of the financial impacts of a JO. It is noted, however, that the operation of any shared service model (or JO) would be dependent on the nature of additional factors, including the governance arrangements and the scope of the model.

Table 6.1: Indicators for reform option development

	Service delivery			Financial sustainability		Effectiveness of local representation		
	Quality of service delivery	Quality of planning and infrastructure	Capacity to attract specialist skills	Capacity to secure economies of scale and scope	Scope and scale of resource base	Quality of local representation	Communities of interest	Quality of stakeholder management
Geography								
Proximity and similarity of urban and rural areas	✓	✓		✓	✓			
Minor boundary changes	✓	✓		✓	✓			
Socio-demographic characteristics								
Population growth and density	✓	✓				✓	✓	
Demographic characteristics of residents	✓	✓				✓	✓	
Property prices					✓			✓
Financial scale sustainability								
Comparison of annual operating expenditure and staffing establishment	✓		✓	✓	✓			✓
Financial sustainability outlook	✓	✓	✓	✓	✓			✓

Source: KPMG.

6.2 Option 1 – Base case

Option 1 is the base case – or ‘do nothing’ option – in which the current local government structure in the northern Sydney area was assumed to remain constant.

6.3 Option 2 – Hornsby and The Hills Shire Councils

Option 2 is an amalgamation option that would involve combining Hornsby Shire Council and The Hills Shire Council, with minor adjustments to each council’s southern boundaries.

6.3.1 Geography

In Option 2, the southern boundary of the new local government area would become the Hills Motorway (M2), meaning that the suburbs of Carlingford, Beecroft (south of the Hills Motorway), Epping, Oatlands, North Parramatta, North Rocks (south of the Hills Motorway), Carlingford, and Northmead would not be part of the new local area. There were two key reasons for the inclusion of these minor adjustments in Option 2, namely:

- the creation of a neater southern boundary (i.e. the Hills Motorway); and
- the suburbs included within the minor adjustments tend to be physically closer to either Parramatta or Ryde than the current administrative centres of The Hills Shire and Hornsby Shire Councils (i.e. Castle Hill and Hornsby).³¹ This can reduce the time needed to travel for residents to administrative centres and thus increase service delivery capacity, albeit at the margin – the provision of most council services are not based on if residents are local residents or from neighbouring councils.

The boundary reform within Option 2 represents a natural geographic fit, with both having similar geographies, including:

- semi-rural areas in the north; and
- suburban centres in the south.

The similar geographies of the councils means that there will be a greater functional alignment – for instance, both have large bushlands and section of council that are semi-rural – in any merger, which could produce operating efficiencies, as a result of greater scale. A merger between these councils would potentially allow a more efficient use of assets to manage infrastructure in the common semi-rural part in the north of the councils.

6.3.2 Financial scale and sustainability

The Hills Shire Council has greater operational scale than Hornsby Shire Council, with:

- operating expenditure of \$152.4 million in 2012-13, relative to \$118.4 million for Hornsby Shire Council; and
- a total FTE establishment of 580 employees, relative to 509 at Hornsby Shire Council at the end of 2012-13.

³¹ It is noted that the impacts of minor boundary adjustments were not able to be quantified in the financial analysis, however, are analysed qualitatively against relevant indicators.

The Hills Shire Council was assessed as having ‘sound’ financial sustainability by TCorp in its analysis for the ILGRP, with an outlook of ‘positive’. There are potential financial sustainability risks for Hornsby Shire Council, with TCorp assigning ratings of ‘moderate’ and ‘neutral’ respectively. It is noted that, since the TCorp analysis, Hornsby Shire Council has identified a number of structural changes within its financial statement projections that may impact its financial sustainability over time.

6.4 Option 3 – Hornsby and Ku-ring-gai Councils

Option 3 is an amalgamation option that would involve combining Hornsby Shire and Ku-ring-gai Councils, with a minor adjustment to the southern boundary of Hornsby Shire Council. It is noted that the specification of Option 3 is consistent with the recommendation made in the ILGRP Final Report.

6.4.1 Geography

In Option 3, areas of Hornsby Shire Council north of the Hills Motorway would combine with existing areas of Ku-ring-gai Council. Similar to Option 2, the purpose of the minor adjustment at the southern boundary would be to ensure a neater boundary. In particular, this would mean that Carlingford and Beecroft (south of the Hills Motorway), and Epping would not be part of the new area.

Ku-ring-gai Council is geographically smaller than Hornsby Shire Council, however, both councils have a significant proportion of bushland, with 175 km² of designated national park located in the area. However, unlike in option 2, both councils do not both have large semi-rural areas – Ku-ring-gai is an urban council. For instance, the suburb with the lowest population density in Ku-ring-gai Council is North Turramurra (3.4 residents/hectare). More than three-quarters of Hornsby Shire’s area has a population density lower than that rate, with half the area having a population density of 0.16 residents per hectare. This may limit the scale that could be generated in service provision to the semi-rural area.

Hornsby and Ku-ring-gai are currently grouped together in the same sub-regional planning zone, the North subregion. The Subregional Strategy translates the objectives of the NSW Government’s Metropolitan Strategy and State Plan to the local level. A merged council entity would have greater leverage in being able to coordinate and deliver the Strategy, thus enhancing the service delivery capacity of the entity. As a result of the councils being grouped together, the respective Planning Divisions will already have a better working relationship.

6.4.2 Financial scale and sustainability

Although relatively similar in size and scale, Hornsby Shire Council is slightly larger than Ku-ring-gai Council, with:

- operating expenditure of \$118.4 million in 2012-13, relative to \$95.7 million for Ku-ring-gai; and
- a total FTE establishment of 509 employees, relative to 430 at Ku-ring-gai at the end of 2012-13.

Analysis suggests there are potential financial sustainability risks for both councils. Ku-ring-gai Council was assessed as having ‘sound’ financial sustainability by TCorp in its analysis for the ILGRP, with an outlook of ‘neutral’. Hornsby Shire Council was assigned ratings of ‘moderate’

and ‘neutral’. As outlined above, Hornsby Shire Council has identified a number of structural changes within its financial statement projections that may impact its financial sustainability over time.

6.5 Option 4 – Hornsby, The Hills, and Ku-ring-gai Councils

Option 4 is an amalgamation option that would involve combining Hornsby Shire, The Hills Shire and the Ku-ring-gai Councils, with an adjustment to the southern boundary lines, as outlined previously in Option 2 and Option 3.

6.5.1 Geography

In Option 4, the adjustment to the boundary would occur on the southern lines of the Councils with the new boundary line becoming the Hills Motorway (M2). The new boundary line means that the suburbs of Carlingford, Beecroft (south of the Hills Motorway), Epping, Oatlands, North Parramatta, North Rocks (south of the Hills Motorway), would not be part of the new local area. Similar to Options 2 and 3, the boundary adjustment would help to ensure a neater boundary.

The amalgamation would create a substantially greater council area, thereby helping to improve the capacity of the council to achieve efficiencies in service delivery. Further, the mergers will help to strengthen the collective bargaining power of the councils through greater coordination of operational and strategic objectives.

6.5.2 Financial scale and sustainability

The Hills Shire Council has a greater operational scale than both Hornsby Shire Council and Ku-ring-gai Council, with:

- operating expenditure of \$152.4 million in 2012-13, relative to \$118.4 million for Hornsby and \$95.7 million for Ku-ring-gai; and
- a total FTE establishment of 580 employees in comparison to 509 and 430 FTE establishment for Hornsby and Ku-ring-gai, respectively, at the end of 2012-13.

Under the remit of the ILGRP, the financial sustainability of the all three councils was assessed by TCorp. The analysis suggested the both Ku-ring-gai and Hornsby face potential financial sustainability risks, with Ku-ring-gai assessed as having ‘sound’ financial sustainability and an outlook of ‘moderate’. Hornsby Shire Council was assigned ratings of ‘moderate’ and ‘neutral’, respectively, while The Hills Shire Council was assessed as having ‘sound’ financial sustainability with an outlook of ‘positive’. As outlined above, Hornsby Shire Council has identified a number of structural changes within its financial statement projections that may impact its financial sustainability over time.

Shared services models

Further to the amalgamation options, the analysis considers three shared services options, namely:

- **Option 5:** An Infrastructure and Recreation division would be shared between Hornsby and The Hills Councils;
- **Option 6:** An Infrastructure and Recreation division would be shared between Hornsby and Ku-ring-gai Councils; and

- **Option 7:** An Infrastructure and Recreation division would be shared between Hornsby, The Hills, and Ku-ring-gai Councils.

Under this shared services model councils retain more control over their services. The model recognises the political sensitivities that surround some functions of council, such as Planning, and responsibilities for which may be more readily located with each local council. The manner of local representation in this model most closely approximates the status quo.

In this model, the functions that would be shared would be limited to those residing within the Infrastructure and Recreation division of Hornsby Shire Council. All other divisions would continue to operate independently of the other councils. This likely will limit the potential efficiencies that could be gained – and impact the financial sustainability of council in a smaller manner. The Infrastructure and Recreation division at Hornsby Shire Council includes the following branches:

- asset management and maintenance;
- design and construction;
- parks and recreation;
- traffic and road safety;
- waste management; and
- works executive.

The Infrastructure and Recreation division accounts for around 36 per cent of total wages and salaries at the council. However, it is responsible for a disproportionate share of plant and equipment. Consequently, the efficiencies gained from cooperating with other councils and sharing resources, would only accrue to that fraction of the council overall expenditure.

The Crosby|Textor research commissioned by Hornsby Shire Council found that support for the shared services model was very strong among residents in all councils surveyed, with 73 per cent supporting the option and 19 per cent opposing. It is noted that, notwithstanding the shared services model considered within this report, there is a high degree of scalability in shared services options.³² In the literature, an amalgamation is an extreme form of a shared service model. Shared services can be viewed on a continuous spectrum – moving from highly centralised to very decentralised. As outlined above, Options 5, 6, and 7 consider a relatively more decentralised shared services model.

7 Analysis of local government reform options

This chapter presents and discusses the results of the financial and strategic analysis of local government reform options, including:

- results of the financial analysis, including:
 - quantification of major cost and benefit streams, where data permits;
 - qualitative analysis of cost and benefit streams where data was limited;
 - sensitivity analysis of key assumptions and inputs; and
 - limitations of the financial analysis.
- analysis of supporting strategies and mechanisms to underpin effective implementation and management over time;
- insights from the stakeholder testing process with Hornsby Shire Council and neighbouring councils in the Northern Sydney area; and
- a multi-criteria analysis of reform options to determine the preferred option for Hornsby Shire Council.

7.1 Results summary

The following boxes summarise the financial analysis results for each reform option, including from the perspective of:

- Hornsby Shire Council only, measured relative to Hornsby Shire Council's long term financial projections (Base case); and
- new local government entities created within each option, measured relative to the sum of respective councils' long term financial projections (Base case).

The boxes also identify key considerations with respect to strategies and mechanisms that will support effective implementation and management over time.

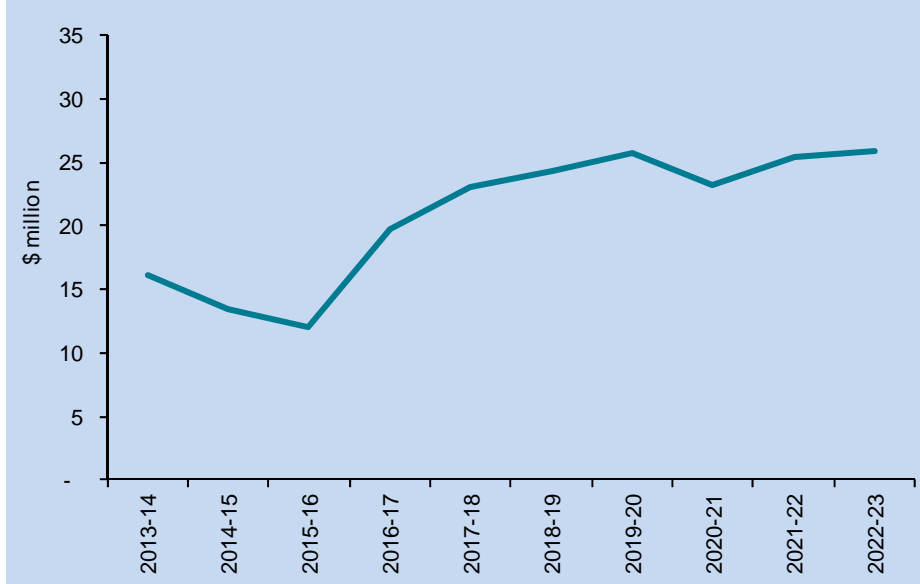
Option 1 – Base case

In Option 1, Hornsby Shire Council is assumed not to pursue any local government reform, meaning that the financial and strategic outcomes of this option are the basis with which to compare the impacts of reform options.

Financial analysis

The expected financial outcomes for Hornsby Shire Council and neighbouring councils in Option 1 will be consistent with projections in each council’s respective long term financial plans. The projected net operating results for Hornsby Shire Council only are shown in Chart 7.1. There is expected to be an 11 per cent improvement in the net operating result in 2021-22 relative to 2013-14, and this reflects a range of planned structural and operational adjustments by Hornsby Shire Council.

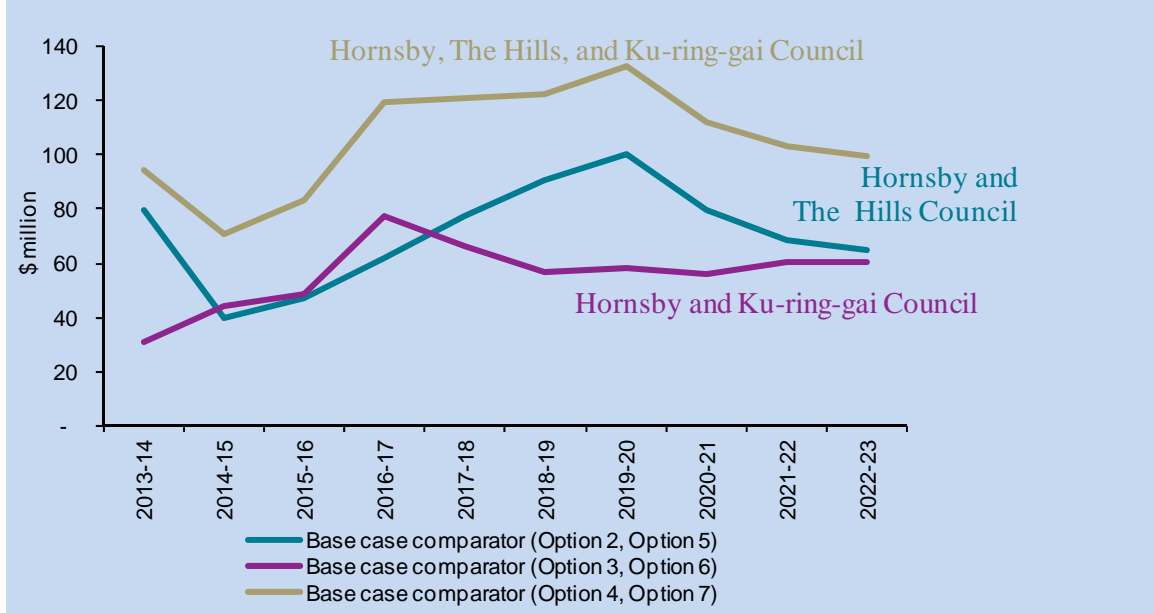
Chart 7.1: Projected net operating result (base case)



Source: Hornsby Shire Council.

The net operating result comparators (i.e. the base case comparators) for each reform option are shown in Chart 7.2. It is noted that – unlike the analysis for Hornsby Shire Council only – the base case comparators are different across options. This reflects that different options consider different combinations of affected councils. To enable a consistent basis for comparison, incremental impacts for reform options were considered against the sum of projected net operating positions for the respective combination of councils.

Chart 7.2: Projected net operating result (base case) by reform option



Note: Aggregate net operating results in the Base case are the sum of net operating results contained in respective councils' long term financial projections.

Source: Hornsby Shire Council; The Hills Shire Council (2013), *Resourcing Plan*; Ku-ring-gai Council (2013), *Long Term Financial Plan 2013-2023*.

Supporting strategies and mechanisms

In the absence of reform, there are a number of broader considerations for Hornsby Shire Council, given its longer term financial sustainability outlook of 'neutral' from TCorp.

Table 7.1: Summary of supporting strategies considerations for Option 1

Consideration	Relevance
<u>Asset utilisation and renewal</u>	
Valuation and stock take of assets	✓
Maintenance of infrastructure	✓
<u>Service delivery</u>	
Service levels between councils	✗
Human resource management	✗
Corporate support functions	✗
<u>Governance structures</u>	
Amalgamation	✗
Shared services	✗
<u>Transition measures</u>	
Transition measures	✗

Source: KPMG.

Option 2 – Hornsby Shire Council and The Hills Shire Council

Option 2 is an amalgamation option that would involve combining Hornsby Shire Council and The Hills Shire Council, with minor adjustments to each council’s southern boundaries.

Financial analysis

The projected impacts of the net operating results and projected savings are provided in Table 7.2 and Chart 7.3 below.

Over the period 2013-14 to 2022-23 the projected improvement in the bottom line is estimated to be \$35.0 million (17 per cent). Over the same period the projected improvement for the aggregates entity is \$74.0 million (10 per cent).

The key drivers of the impacts are expected to be employee cost savings and efficiencies in *Materials and contracts* and *Other expenses*.

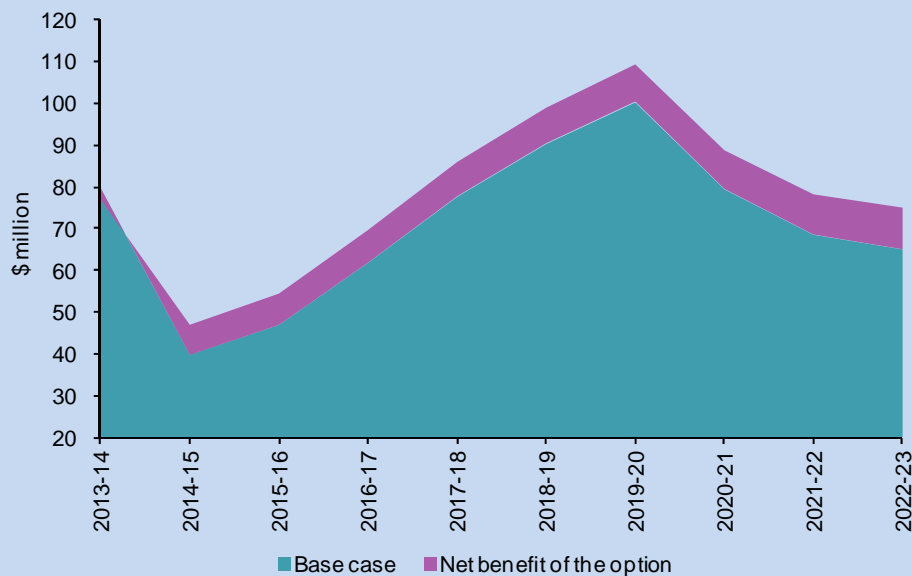
Table 7.2: Summary of net operating results and projected savings – Option 2

	2013-14	2014-15	2015-16	2016-17	2017-18	Cumulative 2013-14 to 2017- 18	Cumulative 2013-14 to 2022- 23
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Option 1 (Base case) <i>consisting of</i>	79.6	39.8	46.9	61.8	77.7	305.9	709.8
<u>Hornsby</u>	16.1	13.5	12.1	19.7	23.0	84.5	209.0
<u>The Hills</u>	63.5	26.3	34.9	42.1	54.6	221.4	500.7
Option 2	76.8	47.0	54.5	69.7	85.9	333.8	783.7
Saving	-2.8	7.2	7.5	7.8	8.2	27.9	74.0

Note: Cumulative impacts are not discounted.

Source: KPMG calculations.

Chart 7.3: Base case and projected net benefits, 2013-14 to 2022-23



Source: KPMG calculations.

Supporting strategies and mechanisms

There are a number of broader considerations to support effective implementation and management of Option 2 over time, as outlined below and discussed further in Section 7.3.

Table 7.3: Summary of supporting strategies considerations for Option 2

Consideration	Relevance
<u>Asset utilisation and renewal</u>	
Valuation and stock take of assets	✓
Maintenance of infrastructure	✓
<u>Service delivery</u>	
Service levels between councils	✓
Human resource management	✓
Corporate support functions	✓
<u>Governance structures</u>	
Amalgamation	✓
Shared services	✗
<u>Transition measures</u>	
Transition measures	✓

Source: KPMG.

Option 3 – Hornsby Shire Council and Ku-ring-gai Council

Option 3 is an amalgamation option that would involve combining Hornsby Shire and Ku-ring-gai Councils, with a minor adjustment to the southern boundary of Hornsby Shire Council.

Financial analysis

The projected impacts of the net operating results and projected net benefits, for both Hornsby Shire Council and for the amalgamated councils, are provided in Table 7.4 and Chart 7.4 below.

Between 2013-14 and 2022-23 the projected improvement in the Hornsby Shire Council bottom line is estimated to be \$27.7 million (13 per cent). Over the same period the projected improvement for the aggregates entity is \$50.4 million (9 per cent). The projections show that the gains relative to the base case are substantial, however, less than expected for Option 2, reflective of the difference in operational scale between The Hills Shire Council and Ku-ring-gai Council. For example, The Hills Shire Council had 580 FTEs at the end of June 2013 compared to 430 FTEs at Ku-ring-gai Council. Further, projected expenditure for 2013-14 at The Hills Shire Council is about \$130 million, compared to \$105 million at Ku-ring-gai Council.

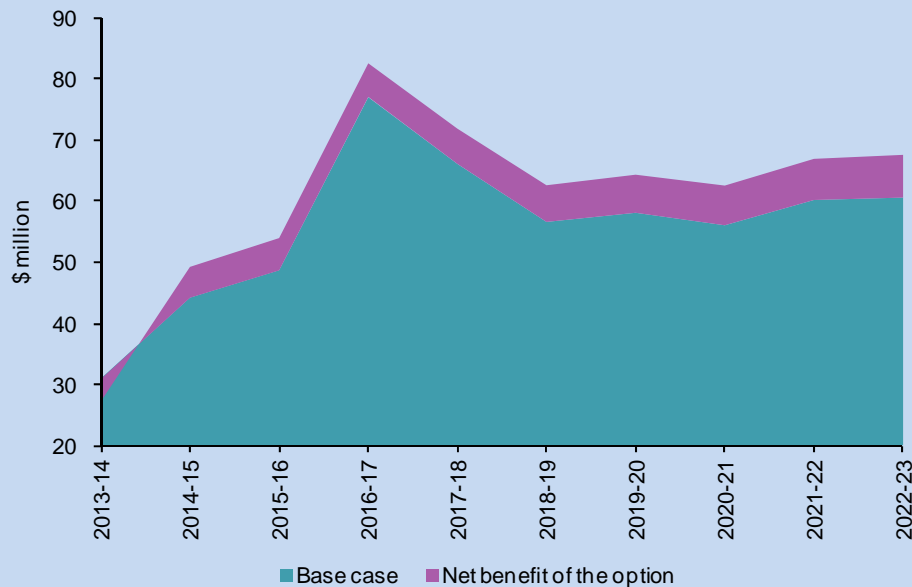
Table 7.4: Summary of net operating results and projected savings – Option 3

	2013-14	2014-15	2015-16	2016-17	2017-18	Cumulative 2013-14 to 2017- 18	Cumulative 2013-14 to 2022- 23
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Option 1 (Base case) <i>consisting of</i>	30.9	44.2	48.7	77.1	66.1	267.1	558.7
<u>Hornsby</u>	16.1	13.5	12.1	19.7	23.0	84.5	209.0
<u>Ku-ring-gai</u>	14.8	30.7	36.6	57.4	43.1	182.6	349.7
Option 3	27.3	49.3	54.0	82.6	71.9	285.0	609.1
Saving	-3.6	5.1	5.3	5.5	5.8	18.0	50.4

Note: Cumulative impacts are not discounted.

Source: KPMG calculations.

Chart 7.4: Base case and projected net benefits, 2013-14 to 2022-23 – Option 3



Source: KPMG calculations.

Supporting strategies and mechanisms

There are a number of broader considerations to support effective implementation and management of Option 3 over time, as outlined below and discussed further in Section 7.3.

Table 7.5: Summary of supporting strategies considerations for Option 3

Consideration	Relevance
<u>Asset utilisation and renewal</u>	
Valuation and stock take of assets	✓
Maintenance of infrastructure	✓
<u>Service delivery</u>	
Service levels between councils	✓
Human resource management	✓
Corporate support functions	✓
<u>Governance structures</u>	
Amalgamation	✓
Shared services	✗
<u>Transition measures</u>	
Transition measures	✓

Source: KPMG.

Option 4 – Hornsby, The Hills, and Ku-ring-gai Council

Option 4 is an amalgamation option that would involve merging Hornsby, The Hills, and Ku-ring-gai Councils into a single entity.

Financial analysis

The projected impacts of the net operating results and projected net benefits, for both Hornsby Shire Council and for the amalgamation of all councils, are provided in Table 7.6, and Chart 7.5 below.

Over the period 2013-14 to 2022-23 the projected improvement in the bottom line is estimated to be \$55.7 million (27 per cent) for Hornsby Shire Council. Over the same period the projected improvement for the aggregates entity is \$163.1 million (15 per cent).

The projections show that the gains relative to the base case are highest under the amalgamation of all three councils. This result is reflective of a larger operational scale and further increased efficiencies between the three merged councils.

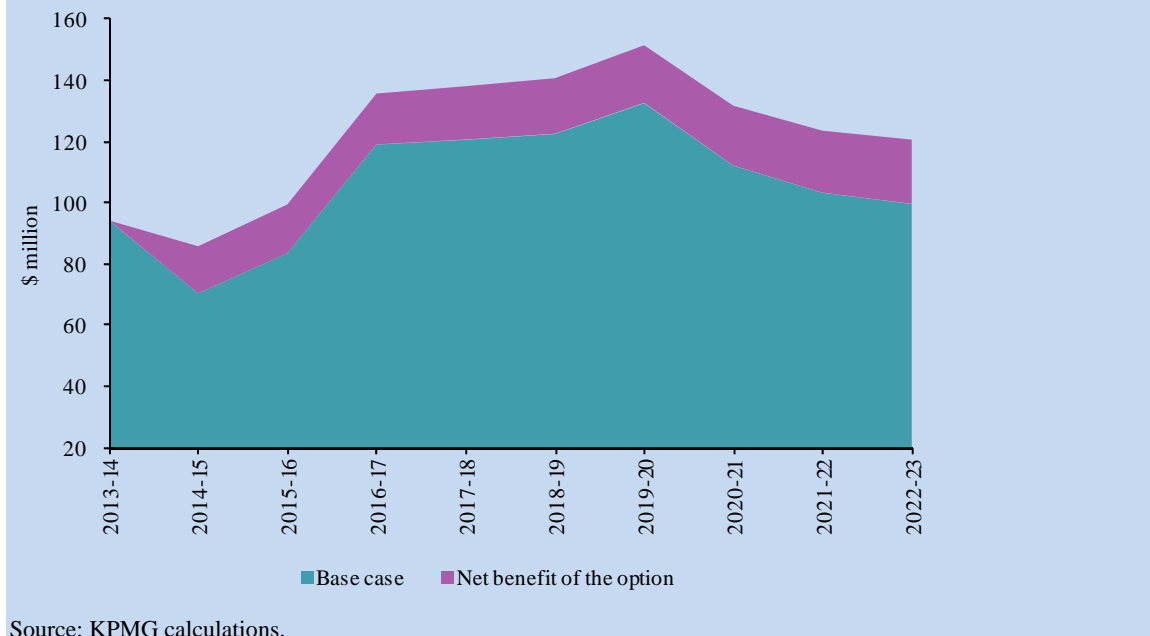
Table 7.6 Summary of net operating results and projected savings – Option 4

	2013-14	2014-15	2015-16	2016-17	2017-18	Cumulative 2013-14 to 2017- 18	Cumulative 2013-14 to 2022- 23
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Option 1 (Base case) <i>consisting of</i>	94.4	70.5	83.6	119.2	120.8	488.5	1,059.4
<u>Hornsby</u>	16.1	13.5	12.1	19.7	23.0	84.5	209.0
<u>The Hills</u>	63.5	26.3	34.9	42.1	54.6	221.4	500.7
<u>Ku-ring-gai</u>	14.8	30.7	36.6	57.4	43.1	182.6	349.7
Option 4	94.3	85.9	99.6	135.8	138.2	553.8	1,222.6
Saving	-0.1	15.4	16.0	16.6	17.5	65.3	163.1

Note: Cumulative impacts are not discounted.

Source: KPMG calculations.

Chart 7.5: Base case and projected net benefits, 2013-14 to 2022-23 – Option 4



Source: KPMG calculations.

Option 5 - Shared services with Hornsby and The Hills Shire Councils

Option 5 is a shared services model between Hornsby and The Hills Shire Councils, with an Infrastructure and Recreation division being shared between the two councils.

Financial analysis

The projected impacts to the net operating results of Hornsby Shire Council and the aggregate entity are presented in Table 7.7 and Chart 7.6 below.

Over the period 2013-14 to 2022-23 the projected improvement in the bottom line is estimated to be \$7.4 million (4 per cent). Over the same period the projected improvement for the aggregates entity is \$15.3 million (2 per cent).

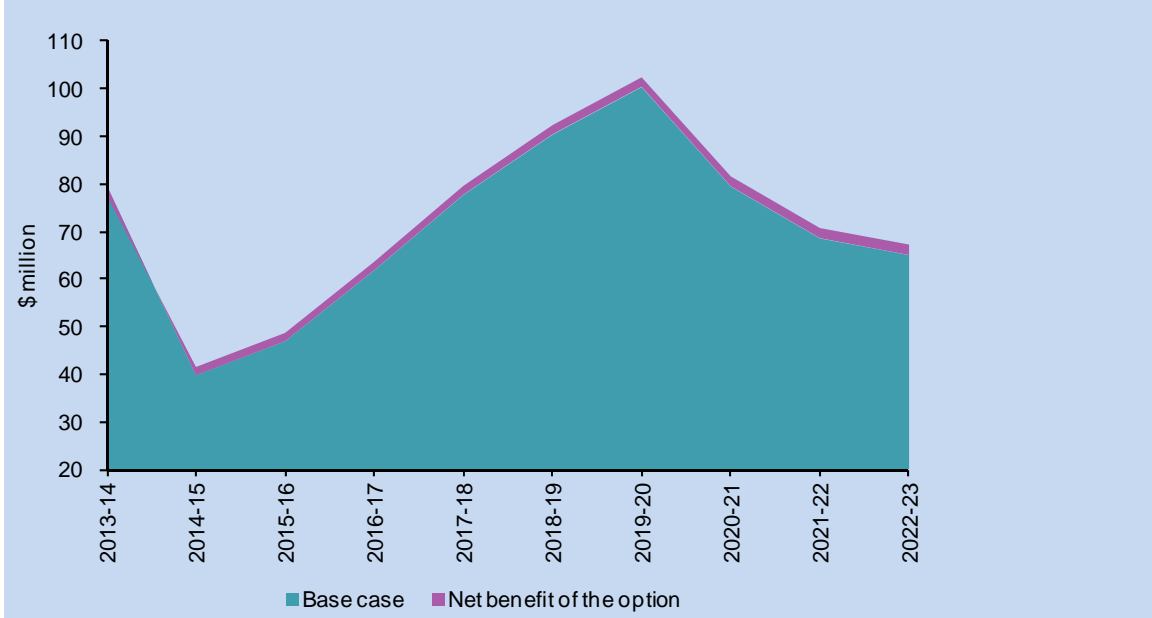
Table 7.7 Summary of net operating results and projected savings – Option 5

	2013-14	2014-15	2015-16	2016-17	2017-18	Cumulative 2013-14 to 2017-18	Cumulative 2013-14 to 2022-23
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Option 1 (Base case) consisting of	79.6	39.8	46.9	61.8	77.7	305.9	709.8
<u>Hornsby</u>	16.1	13.5	12.1	19.7	23.0	84.5	209.0
<u>The Hills</u>	63.5	26.3	34.9	42.1	54.6	221.4	500.7
Option 5	77.6	41.5	48.7	63.6	79.5	311.0	725.1
Saving	-2.1	1.7	1.8	1.8	1.9	5.1	15.3

Note: Cumulative impacts are not discounted.

Source: KPMG calculations.

Chart 7.6: Base case and projected net benefits, 2013-14 to 2022-23 – Option 5



Source: KPMG calculations.

Table 7.8: Summary of supporting strategies considerations for Option 5

Consideration	Relevance
<u>Asset utilisation and renewal</u>	
Valuation and stock take of assets	✓
Maintenance of infrastructure	✓
<u>Service delivery</u>	
Service levels between councils	✓
Human resource management	✓
Corporate support functions	✓
<u>Governance structures</u>	
Amalgamation	✗
Shared services	✓
<u>Transition measures</u>	
Transition measures	✓

Source: KPMG.

Option 6 - Shared services with Hornsby Shire Council and Ku-ring-gai Council

Option 6 is a shared services model between Hornsby and Ku-ring-gai Councils, with a shared Infrastructure and Recreation division being shared between the two councils.

Financial analysis

The projected impacts to the net operating result and net benefits are presented in Table 7.9 and Chart 7.7 below.

Between 2013-14 and 2022-23, the projected improvement in the bottom line for the Hornsby Shire Council is estimated to be \$6.5 million (3 per cent). Over the same period the projected improvement for the shared services aggregates is \$10.5 million (2 per cent).

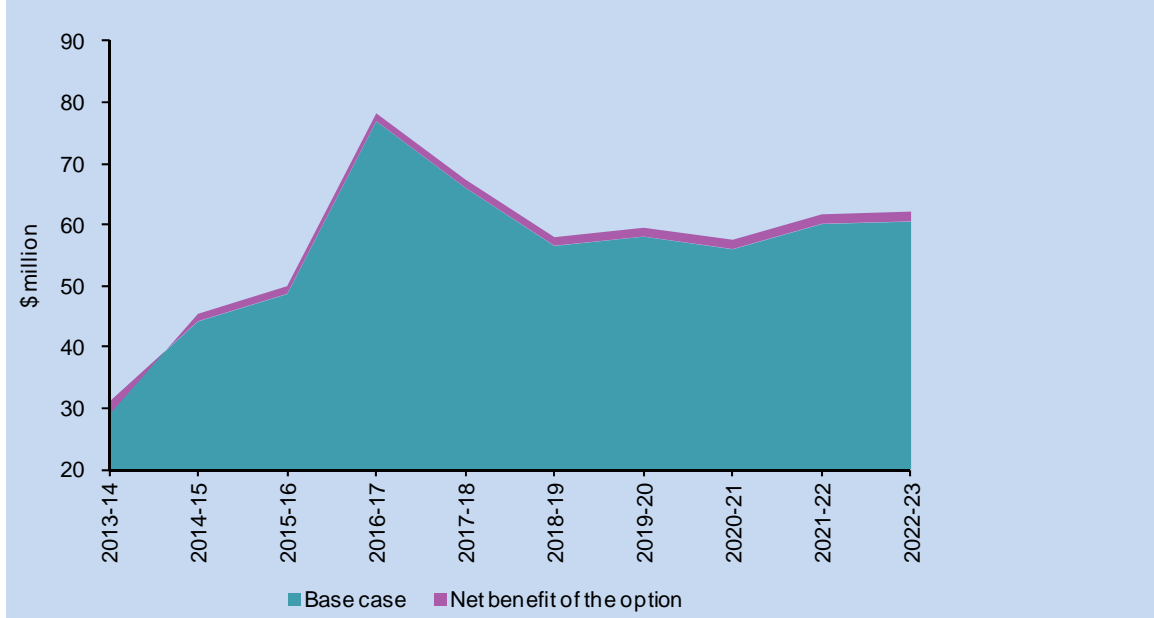
Table 7.9 Summary of net operating results and projected savings – Option 6

	2013-14	2014-15	2015-16	2016-17	2017-18	Cumulative 2013-14 to 2017-18	Cumulative 2013-14 to 2022-23
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Option 1 (Base case) consisting of	30.9	44.2	48.7	77.1	66.1	267.1	558.7
<u>Hornsby</u>	16.1	13.5	12.1	19.7	23.0	84.5	209.0
<u>Ku-ring-gai</u>	14.8	30.7	36.6	57.4	43.1	182.6	349.7
Option 6	28.8	45.4	50.0	78.4	67.5	270.0	569.2
Saving	-2.2	1.2	1.3	1.3	1.3	3.0	10.5

Note: Cumulative impacts are not discounted.

Source: KPMG calculations.

Chart 7.7 : Base case and projected net benefits, 2013-14 to 2022-23 – Option 6



Source: KPMG.

Table 7.10: Summary of supporting strategies considerations for Option 6

Consideration	Relevance
<u>Asset utilisation and renewal</u>	
Valuation and stock take of assets	✓
Maintenance of infrastructure	✓
<u>Service delivery</u>	
Service levels between councils	✓
Human resource management	✓
Corporate support functions	✓
<u>Governance structures</u>	
Amalgamation	✗
Shared services	✓
<u>Transition measures</u>	
Transition measures	✓

Source: KPMG.

Option 7 - Shared services with Hornsby, The Hills, and Ku-ring-gai Councils

Option 7 is a shared services model between Hornsby, The Hills, and Ku-ring-gai Councils. In this option, councils it is assumed that an Infrastructure and Recreation division would be shared across councils.

Financial analysis

The projected impacts to the net operating result and projected benefits in comparison to the base cases, for Hornsby Shire Council and in aggregate, are presented in Table 7.11 and Chart 7.8 below.

Over the period 2013-14 to 2022-23 the projected improvement in the Hornsby Shire Council bottom line is estimated to be \$9.9 million (5 per cent). Over the same period the projected improvement for the aggregates entity is \$27.2 million (3 per cent).

For Option 7, the projections show that gains are marginal, reflective of:

- the reduced potential for efficiencies of scale, given only one division (Infrastructure and Recreation) is assumed to be shared; and
- the non-linear nature of costs to implement a shared services arrangement (i.e. the marginal cost to share additional divisions would decrease for each additional division).

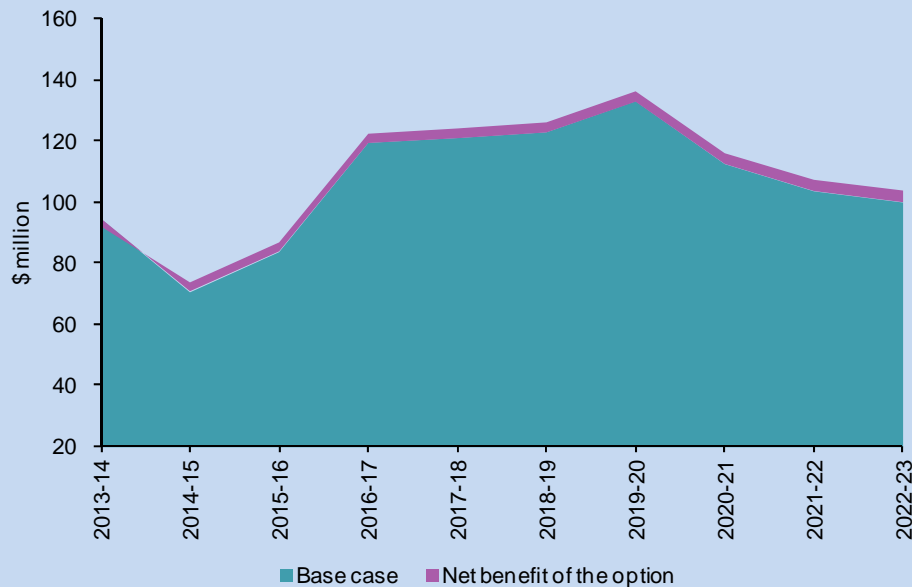
Table 7.11 Summary of net operating results and projected savings – Option 7

	2013-14	2014-15	2015-16	2016-17	2017-18	Cumulative 2013-14 to 2017-18	Cumulative 2013-14 to 2022-23
	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Option 1 (Base case) consisting of	94.4	70.5	83.6	119.2	120.8	488.5	1,059.4
<u>Hornsby</u>	16.1	13.5	12.1	19.7	23.0	84.5	209.0
<u>The Hills</u>	63.5	26.3	34.9	42.1	54.6	221.4	500.7
<u>Ku-ring-gai</u>	14.8	30.7	36.6	57.4	43.1	182.6	349.7
Option 7	91.8	73.4	86.6	122.3	124.0	498.0	1,086.6
Saving	-2.6	2.9	3.0	3.1	3.2	9.5	27.2

Note: Cumulative impacts are not discounted.

Source: KPMG calculations.

Chart 7.8 : Base case and projected net benefits, 2013-14 to 2022-23 – Option 7



Source: KPMG calculations.

Supporting strategies and mechanisms

There are a number of broader considerations to support effective implementation and management of Option 7 over time, as outlined below and discussed further in Section 7.3.

Table 7.12: Summary of supporting strategies considerations for Option 7

Consideration	Relevance
<u>Asset utilisation and renewal</u>	
Valuation and stock take of assets	✓
Maintenance of infrastructure	✓
<u>Service delivery</u>	
Service levels between councils	✓
Human resource management	✓
Corporate support functions	✓
<u>Governance structures</u>	
Amalgamation	x
Shared services	✓
<u>Transition measures</u>	
Transition measures	✓

Source: KPMG.

7.2 Detailed financial analysis results

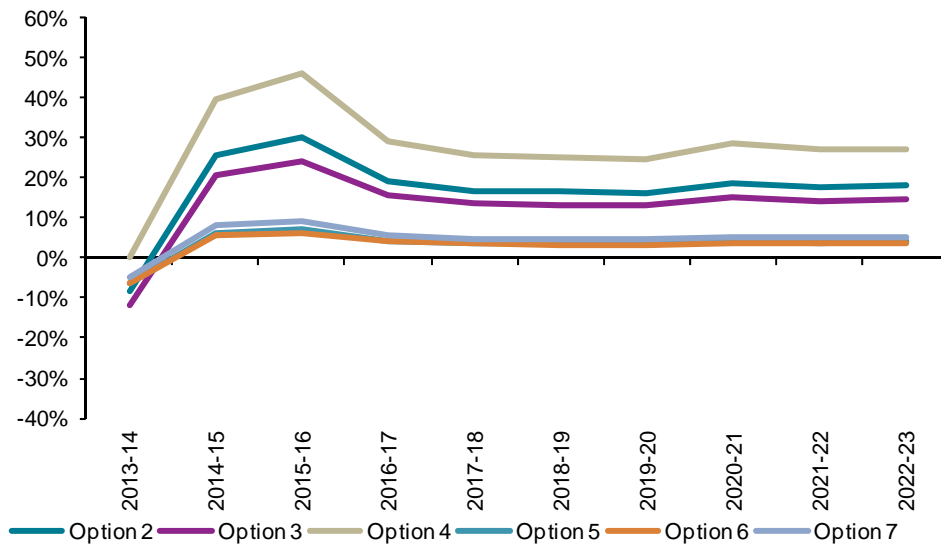
This section provides detailed financial analysis results and sensitivity testing to supplement the summary results provided in Section 7.1.

7.2.1 Comparison of percentage point improvements

As outlined previously, the financial analysis considered results from the perspective of both Hornsby Shire Council and the aggregate operating entities under respective reform options. Estimated percentage point improvements to net operating results for both Hornsby Shire Council and aggregate entities are shown in Chart 7.9 and Chart 7.10 respectively. The charts show that:

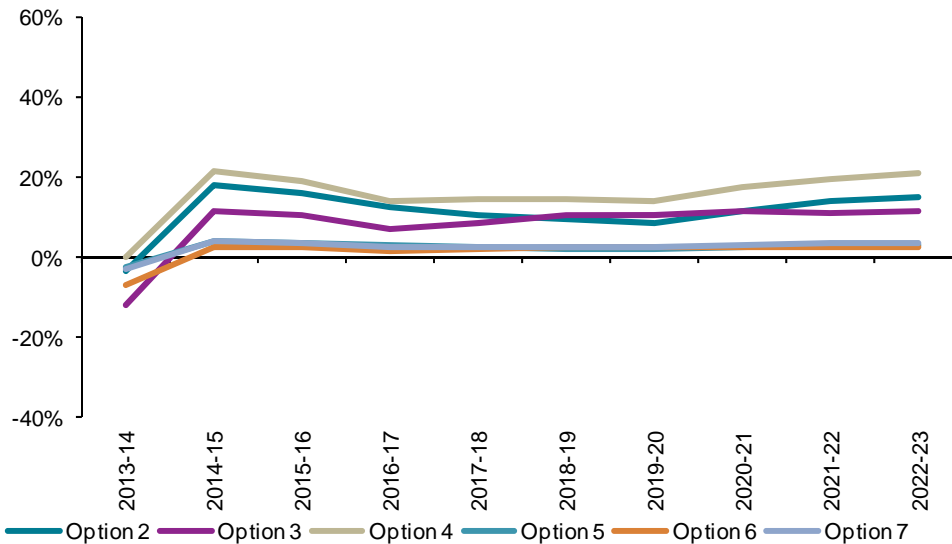
- the relative order of preference for reform options with respect to financial impacts only is expected to be consistent for both Hornsby Shire Council and aggregate entities;
- percentage point improvements in aggregated entities are expected to be less than for Hornsby Shire Council only, reflective of the different bases from which these deviations are calculated.

Chart 7.9: Percentage point impacts to the net operating result (Hornsby Shire Council only)



Source: KPMG calculations.

Chart 7.10: Percentage point impacts to the net operating result (aggregate results)



Source: KPMG calculations.

7.2.2 Income statement projections

This sub section provides income statement projections, including:

- detailed projections for Hornsby Shire Council of major line items within income and expenditure from continuing operations; and
- high level projections for neighbouring councils of total income and expenditure from continuing operations.

Income statement projections were prepared by allocating estimated incremental impacts to relevant line items within respective long term financial projections. It is noted that line items impacted by allocation of the incremental impacts are underlined where applicable.

The level of detail within the income statement projections reflects the relative level of detail within the financial modelling approach for different councils. As discussed, the level of detail was determined by the scope and scale of available data. There is also scope to refine these results over time, should further, more detailed data become available.

Table 7.13: Income statement projections for Hornsby Shire Council, \$'000 (Option 2)

	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
Income from continuing operations										
Rates and annual charges	91,289	93,389	92,833	95,618	98,487	101,441	104,485	107,619	110,848	114,173
<u>User charges and fees</u>	15,246	15,793	16,468	17,198	17,628	18,069	18,521	18,984	19,458	19,945
<u>Interest and investment revenue</u>	2,202	1,960	2,440	3,208	4,064	4,994	6,022	6,923	7,883	8,404
Other revenues	12,087	6,239	6,395	6,555	6,719	6,887	7,059	7,236	7,416	7,602
Grants and contributions provided for operating purposes	12,735	13,053	13,380	13,714	14,057	14,408	14,769	15,138	15,516	15,904
Grants and contributions provided for capital purposes	4,915	6,965	7,139	14,132	14,485	14,847	15,218	12,678	12,995	13,320
Net gains from the disposal of assets	-	-	-	-	-	-	-	-	-	-
Joint ventures and associated entities	-	-	-	-	-	-	-	-	-	-
<i>Total income from continuing operations</i>	<i>138,473</i>	<i>137,399</i>	<i>138,655</i>	<i>150,425</i>	<i>155,440</i>	<i>160,647</i>	<i>166,073</i>	<i>168,577</i>	<i>174,116</i>	<i>179,348</i>
Expenses from continuing operations										
<u>Employee benefits and on-costs</u>	43,015	44,347	45,834	47,371	47,960	49,572	51,239	52,936	54,688	56,498
<u>Borrowing costs</u>	1,772	1,484	1,189	1,100	1,016	940	884	847	827	812
<u>Materials and contracts</u>	38,657	39,875	41,503	42,511	43,705	45,273	46,859	48,485	50,151	52,065
Depreciation and amortisation	22,312	21,337	20,748	21,108	21,429	21,750	22,059	22,369	22,678	23,094
Impairment	-	-	-	-	-	-	-	-	-	-
<u>Other expenses</u>	17,956	13,360	13,694	14,868	14,408	14,769	15,138	16,348	15,925	16,323
Interest and investment losses	-	-	-	-	-	-	-	-	-	-
Net losses from the disposal of assets	-	-	-	-	-	-	-	-	-	-
Joint ventures and associated entities	-	-	-	-	-	-	-	-	-	-
<i>Total expenses from continuing operations</i>	<i>123,712</i>	<i>120,403</i>	<i>122,968</i>	<i>126,958</i>	<i>128,517</i>	<i>132,303</i>	<i>136,179</i>	<i>140,984</i>	<i>144,269</i>	<i>148,791</i>
Net operating result for the year	14,761	16,996	15,687	23,468	26,923	28,343	29,895	27,593	29,847	30,557

Source: Hornsby Shire Council; KPMG calculations.

Table 7.14: Income statement projections for Hornsby Shire Council, \$'000 (Option 3)

	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
Income from continuing operations										
Rates and annual charges	91,289	93,389	92,833	95,618	98,487	101,441	104,485	107,619	110,848	114,173
User charges and fees	15,247	15,795	16,470	17,200	17,630	18,071	18,522	18,986	19,460	19,947
<u>Interest and investment revenue</u>	2,202	1,960	2,440	3,208	4,064	4,994	6,022	6,923	7,883	8,404
Other revenues	12,087	6,239	6,395	6,555	6,719	6,887	7,059	7,236	7,416	7,602
Grants and contributions provided for operating purposes	12,735	13,053	13,380	13,714	14,057	14,408	14,769	15,138	15,516	15,904
Grants and contributions provided for capital purposes	4,915	6,965	7,139	14,132	14,485	14,847	15,218	12,678	12,995	13,320
Net gains from the disposal of assets	-	-	-	-	-	-	-	-	-	-
Joint ventures and associated entities	-	-	-	-	-	-	-	-	-	-
<i>Total income from continuing operations</i>	<i>138,475</i>	<i>137,401</i>	<i>138,656</i>	<i>150,427</i>	<i>155,442</i>	<i>160,648</i>	<i>166,075</i>	<i>168,579</i>	<i>174,118</i>	<i>179,350</i>
Expenses from continuing operations										
<u>Employee benefits and on-costs</u>	43,705	45,057	46,565	48,124	48,736	50,371	52,062	53,784	55,561	57,397
<u>Borrowing costs</u>	1,717	1,429	1,134	1,045	961	885	829	792	772	757
<u>Materials and contracts</u>	38,664	39,882	41,510	42,518	43,712	45,281	46,867	48,493	50,160	52,073
Depreciation and amortisation	22,312	21,337	20,748	21,108	21,429	21,750	22,059	22,369	22,678	23,094
Impairment	-	-	-	-	-	-	-	-	-	-
<u>Other expenses</u>	17,818	13,360	13,694	14,868	14,408	14,769	15,138	16,348	15,925	16,323
Interest and investment losses	-	-	-	-	-	-	-	-	-	-
Net losses from the disposal of assets	-	-	-	-	-	-	-	-	-	-
Joint ventures and associated entities	-	-	-	-	-	-	-	-	-	-
<i>Total expenses from continuing operations</i>	<i>124,216</i>	<i>121,065</i>	<i>123,652</i>	<i>127,664</i>	<i>129,246</i>	<i>133,056</i>	<i>136,956</i>	<i>141,786</i>	<i>145,096</i>	<i>149,645</i>
Net operating result for the year	14,259	16,335	15,004	22,763	26,195	27,593	29,120	26,794	29,022	29,705

Source: Hornsby Shire Council; KPMG calculations.

Table 7.15: Income statement projections for Hornsby Shire Council, \$'000 (Option 4)

	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
Income from continuing operations										
Rates and annual charges	91,289	93,389	92,833	95,618	98,487	101,441	104,485	107,619	110,848	114,173
User charges and fees	15,246	15,793	16,468	17,198	17,628	18,069	18,521	18,984	19,458	19,945
<u>Interest and investment revenue</u>	2,202	1,960	2,440	3,208	4,064	4,994	6,022	6,923	7,883	8,404
Other revenues	12,087	6,239	6,395	6,555	6,719	6,887	7,059	7,236	7,416	7,602
Grants and contributions provided for operating purposes	12,735	13,053	13,380	13,714	14,057	14,408	14,769	15,138	15,516	15,904
Grants and contributions provided for capital purposes	4,915	6,965	7,139	14,132	14,485	14,847	15,218	12,678	12,995	13,320
Net gains from the disposal of assets	-	-	-	-	-	-	-	-	-	-
Joint ventures and associated entities	-	-	-	-	-	-	-	-	-	-
<i>Total income from continuing operations</i>	<i>138,473</i>	<i>137,399</i>	<i>138,655</i>	<i>150,425</i>	<i>155,440</i>	<i>160,647</i>	<i>166,073</i>	<i>168,577</i>	<i>174,116</i>	<i>179,348</i>
Expenses from continuing operations										
<u>Employee benefits and on-costs</u>	41,039	42,311	43,737	45,211	45,736	47,281	48,879	50,505	52,185	53,919
<u>Borrowing costs</u>	1,928	1,640	1,345	1,256	1,172	1,096	1,040	1,003	983	968
<u>Materials and contracts</u>	38,657	39,875	41,503	42,511	43,705	45,273	46,859	48,485	50,151	52,065
Depreciation and amortisation	22,312	21,337	20,748	21,108	21,429	21,750	22,059	22,369	22,678	23,094
Impairment	-	-	-	-	-	-	-	-	-	-
<u>Other expenses</u>	18,351	13,360	13,694	14,868	14,408	14,769	15,138	16,348	15,925	16,323
Interest and investment losses	-	-	-	-	-	-	-	-	-	-
Net losses from the disposal of assets	-	-	-	-	-	-	-	-	-	-
Joint ventures and associated entities	-	-	-	-	-	-	-	-	-	-
<i>Total expenses from continuing operations</i>	<i>122,288</i>	<i>118,523</i>	<i>121,028</i>	<i>124,954</i>	<i>126,449</i>	<i>130,168</i>	<i>133,975</i>	<i>138,710</i>	<i>141,922</i>	<i>146,369</i>
Net operating result for the year	16,186	18,875	17,627	25,471	28,991	30,478	32,098	29,868	32,194	32,979

Source: Hornsby Shire Council; KPMG calculations.

Table 7.16: Income statement projections for Hornsby Shire Council, \$'000 (Option 5)

	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
Income from continuing operations										
Rates and annual charges	91,289	93,389	92,833	95,618	98,487	101,441	104,485	107,619	110,848	114,173
User charges and fees	15,247	15,795	16,470	17,200	17,630	18,071	18,522	18,986	19,460	19,947
<u>Interest and investment revenue</u>	2,139	1,895	2,354	3,106	3,957	4,882	5,905	6,800	7,754	8,269
Other revenues	12,087	6,239	6,395	6,555	6,719	6,887	7,059	7,236	7,416	7,602
Grants and contributions provided for operating purposes	12,735	13,053	13,380	13,714	14,057	14,408	14,769	15,138	15,516	15,904
Grants and contributions provided for capital purposes	4,915	6,965	7,139	14,132	14,485	14,847	15,218	12,678	12,995	13,320
Net gains from the disposal of assets	-	-	-	-	-	-	-	-	-	-
Joint ventures and associated entities	-	-	-	-	-	-	-	-	-	-
<i>Total income from continuing operations</i>	<i>138,412</i>	<i>137,336</i>	<i>138,571</i>	<i>150,325</i>	<i>155,335</i>	<i>160,536</i>	<i>165,958</i>	<i>168,456</i>	<i>173,990</i>	<i>179,215</i>
Expenses from continuing operations										
<u>Employee benefits and on-costs</u>	45,373	46,775	48,334	49,947	50,613	52,305	54,054	55,835	57,674	59,573
<u>Borrowing costs</u>	969	681	386	297	213	137	81	44	24	9
<u>Materials and contracts</u>	39,395	40,637	42,295	43,322	44,539	46,137	47,754	49,410	51,108	53,058
Depreciation and amortisation	22,312	21,337	20,748	21,108	21,429	21,750	22,059	22,369	22,678	23,094
Impairment	-	-	-	-	-	-	-	-	-	-
<u>Other expenses</u>	15,214	13,541	13,880	15,069	14,603	14,968	15,343	16,569	16,140	16,544
Interest and investment losses	-	-	-	-	-	-	-	-	-	-
Net losses from the disposal of assets	-	-	-	-	-	-	-	-	-	-
Joint ventures and associated entities	-	-	-	-	-	-	-	-	-	-
<i>Total expenses from continuing operations</i>	<i>123,263</i>	<i>122,970</i>	<i>125,644</i>	<i>129,744</i>	<i>131,397</i>	<i>135,297</i>	<i>139,290</i>	<i>144,227</i>	<i>147,625</i>	<i>152,278</i>
Net operating result for the year	15,149	14,366	12,927	20,581	23,938	25,239	26,668	24,229	26,365	26,937

Source: Hornsby Shire Council; KPMG calculations.

Table 7.17: Income statement projections for Hornsby Shire Council, \$'000 (Option 6)

	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
Income from continuing operations										
Rates and annual charges	91,289	93,389	92,833	95,618	98,487	101,441	104,485	107,619	110,848	114,173
User charges and fees	15,247	15,795	16,470	17,200	17,630	18,071	18,522	18,986	19,460	19,947
<u>Interest and investment revenue</u>	2,140	1,896	2,356	3,109	3,960	4,885	5,908	6,803	7,757	8,273
Other revenues	12,087	6,239	6,395	6,555	6,719	6,887	7,059	7,236	7,416	7,602
Grants and contributions provided for operating purposes	12,735	13,053	13,380	13,714	14,057	14,408	14,769	15,138	15,516	15,904
Grants and contributions provided for capital purposes	4,915	6,965	7,139	14,132	14,485	14,847	15,218	12,678	12,995	13,320
Net gains from the disposal of assets	-	-	-	-	-	-	-	-	-	-
Joint ventures and associated entities	-	-	-	-	-	-	-	-	-	-
<i>Total income from continuing operations</i>	<i>138,414</i>	<i>137,337</i>	<i>138,573</i>	<i>150,328</i>	<i>155,337</i>	<i>160,539</i>	<i>165,961</i>	<i>168,459</i>	<i>173,993</i>	<i>179,219</i>
Expenses from continuing operations										
<u>Employee benefits and on-costs</u>	45,452	46,857	48,419	50,034	50,703	52,397	54,149	55,933	57,775	59,677
<u>Borrowing costs</u>	969	681	386	297	213	137	81	44	24	9
<u>Materials and contracts</u>	39,395	40,637	42,295	43,322	44,539	46,137	47,754	49,410	51,108	53,058
Depreciation and amortisation	22,312	21,337	20,748	21,108	21,429	21,750	22,059	22,369	22,678	23,094
Impairment	-	-	-	-	-	-	-	-	-	-
<u>Other expenses</u>	15,198	13,541	13,880	15,069	14,603	14,968	15,343	16,569	16,140	16,544
Interest and investment losses	-	-	-	-	-	-	-	-	-	-
Net losses from the disposal of assets	-	-	-	-	-	-	-	-	-	-
Joint ventures and associated entities	-	-	-	-	-	-	-	-	-	-
<i>Total expenses from continuing operations</i>	<i>123,327</i>	<i>123,052</i>	<i>125,728</i>	<i>129,831</i>	<i>131,487</i>	<i>135,390</i>	<i>139,385</i>	<i>144,325</i>	<i>147,726</i>	<i>152,382</i>
Net operating result for the year	15,086	14,285	12,845	20,497	23,851	25,150	26,576	24,134	26,267	26,836

Source: Hornsby Shire Council; KPMG calculations.

Table 7.18: Income statement projections for Hornsby Shire Council, \$'000 (Option 7)

	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
Income from continuing operations										
Rates and annual charges	91,289	93,389	92,833	95,618	98,487	101,441	104,485	107,619	110,848	114,173
User charges and fees	15,247	15,795	16,470	17,200	17,630	18,071	18,522	18,986	19,460	19,947
<u>Interest and investment revenue</u>	2,134	1,890	2,348	3,099	3,949	4,874	5,896	6,791	7,744	8,260
Other revenues	12,087	6,239	6,395	6,555	6,719	6,887	7,059	7,236	7,416	7,602
Grants and contributions provided for operating purposes	12,735	13,053	13,380	13,714	14,057	14,408	14,769	15,138	15,516	15,904
Grants and contributions provided for capital purposes	4,915	6,965	7,139	14,132	14,485	14,847	15,218	12,678	12,995	13,320
Net gains from the disposal of assets	-	-	-	-	-	-	-	-	-	-
Joint ventures and associated entities	-	-	-	-	-	-	-	-	-	-
<i>Total income from continuing operations</i>	<i>138,407</i>	<i>137,331</i>	<i>138,565</i>	<i>150,318</i>	<i>155,327</i>	<i>160,528</i>	<i>165,949</i>	<i>168,447</i>	<i>173,980</i>	<i>179,206</i>
Expenses from continuing operations										
<u>Employee benefits and on-costs</u>	45,144	46,539	48,092	49,697	50,355	52,040	53,781	55,554	57,384	59,275
<u>Borrowing costs</u>	969	681	386	297	213	137	81	44	24	9
<u>Materials and contracts</u>	39,395	40,637	42,295	43,322	44,539	46,137	47,754	49,410	51,108	53,058
Depreciation and amortisation	22,312	21,337	20,748	21,108	21,429	21,750	22,059	22,369	22,678	23,094
Impairment	-	-	-	-	-	-	-	-	-	-
<u>Other expenses</u>	15,260	13,541	13,880	15,069	14,603	14,968	15,343	16,569	16,140	16,544
Interest and investment losses	-	-	-	-	-	-	-	-	-	-
Net losses from the disposal of assets	-	-	-	-	-	-	-	-	-	-
Joint ventures and associated entities	-	-	-	-	-	-	-	-	-	-
<i>Total expenses from continuing operations</i>	<i>123,081</i>	<i>122,735</i>	<i>125,401</i>	<i>129,494</i>	<i>131,140</i>	<i>135,032</i>	<i>139,017</i>	<i>143,946</i>	<i>147,335</i>	<i>151,980</i>
Net operating result for the year	15,327	14,596	13,164	20,824	24,187	25,496	26,932	24,502	26,645	27,225

Source: Hornsby Shire Council; KPMG calculations.



Table 7.19: Income statement projections for The Hills Shire Council, \$'000

	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
Option 2										
Total income from continuing operations	192,749	160,693	174,013	185,790	203,554	219,660	234,309	222,100	214,891	216,510
Total expenses from continuing operations	130,696	130,673	135,243	139,605	144,604	149,144	154,992	160,999	166,591	172,061
Net operating result for the year	62,053	30,020	38,769	46,185	58,949	70,516	79,316	61,101	48,300	44,449
Option 4										
Total income from continuing operations	192,749	160,693	174,013	185,790	203,554	219,660	234,309	222,100	214,891	216,510
Total expenses from continuing operations	129,105	128,598	133,105	137,396	142,255	146,717	152,465	158,388	163,870	169,250
Net operating result for the year	63,644	32,095	40,907	48,393	61,299	72,943	81,844	63,712	51,021	47,260
Option 5										
Total income from continuing operations	192,683	160,624	173,923	185,682	203,441	219,541	234,184	221,970	214,755	216,367
Total expenses from continuing operations	130,259	133,454	138,141	142,624	147,831	152,500	158,514	164,675	170,438	176,061
Net operating result for the year	62,424	27,170	35,782	43,058	55,610	67,042	75,670	57,295	44,317	40,306
Option 7										
Total income from continuing operations	192,678	160,619	173,916	185,674	203,432	219,533	234,175	221,961	214,745	216,357
Total expenses from continuing operations	130,056	133,195	137,875	142,349	147,540	152,200	158,203	164,353	170,104	175,717
Net operating result for the year	62,622	27,424	36,042	43,325	55,892	67,333	75,973	57,607	44,641	40,640

Source: The Hills Shire Council (2013b); KPMG calculations.



Table 7.20: Income statement projections for Ku-ring-gai Council, \$'000

	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
Option 3										
Total income from continuing operations	119,416	137,731	145,975	170,054	159,168	153,116	157,828	163,342	168,864	173,640
Total expenses from continuing operations	106,392	104,791	106,991	110,243	113,474	118,078	122,583	127,566	130,948	135,754
Net operating result for the year	13,024	32,940	38,984	59,811	45,694	35,038	35,245	35,776	37,916	37,886
Option 4										
Total income from continuing operations	119,416	137,731	145,975	170,054	159,168	153,116	157,828	163,342	168,864	173,640
Total expenses from continuing operations	104,921	102,818	104,947	108,119	111,212	115,714	120,156	125,071	128,386	133,123
Net operating result for the year	14,495	34,913	41,028	61,935	47,956	37,402	37,672	38,271	40,478	40,517
Option 6										
Total income from continuing operations	119,416	137,731	145,975	170,054	159,168	153,116	157,828	163,342	168,864	173,640
Total expenses from continuing operations	105,724	106,576	108,853	112,189	115,543	120,247	124,828	129,893	133,357	138,248
Net operating result for the year	13,692	31,155	37,122	57,865	43,625	32,869	33,000	33,449	35,507	35,392
Option 7										
Total income from continuing operations	119,416	137,731	145,975	170,054	159,168	153,116	157,828	163,342	168,864	173,640
Total expenses from continuing operations	105,556	106,349	108,618	111,945	115,283	119,975	124,549	129,606	133,062	137,945
Net operating result for the year	13,860	31,382	37,357	58,109	43,885	33,141	33,279	33,736	35,802	35,695

Source: Ku-ring-gai Council (2013b); KPMG calculations.

7.2.3 Sensitivity analysis

Sensitivity analysis was undertaken to illustrate the potential impacts of changes to key assumptions on the results of the financial analysis. Sensitivity analysis was undertaken with four illustrative specifications, as outlined in Table 7.21.

Table 7.21: Specification of sensitivity analysis

	Direct staffing efficiencies³³	Materials and contracts and Other expenses efficiencies	Upfront and ongoing costs³⁴
Specification 1	No benefits in the year of implementation		
Specification 2	+10 per cent	+10 per cent	+10 per cent
Specification 3	-10 per cent	-10 per cent	-10 per cent
Specification 4	+10 per cent	No change	-10 per cent
Specification 5	No change	+10 per cent	-10 per cent
Specification 6	-10 per cent	No change	+10 per cent
Specification 7	No change	-10 per cent	+10 per cent

Source: KPMG.

The results of the sensitivity analysis for Hornsby Shire Council only and in aggregate are presented in Table 7.22. The results show that:

- the order of preference for options remains consistent across the specifications, provided benefits realisation is sufficient in the implementation year; and
- the financial viability risks associated with Options 5, 6, and 7 should be considered in detail, given the magnitude of the projected benefits relative to the costs associated with implementation and management over time.

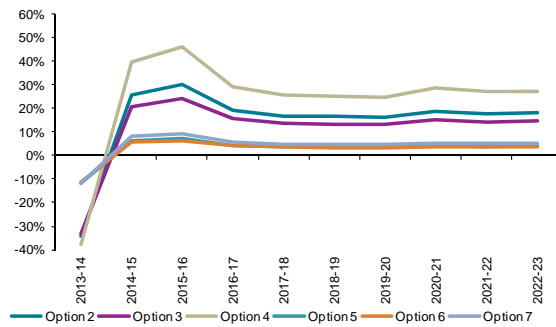
³³ It is noted that changes in staffing efficiencies affect both changes in avoided salaries (benefit) and changes in redundancy payments (cost).

³⁴ Redundancy payments are not included in the cost stream sensitivity parameters as they are directly determined with respect to the level of staffing efficiency.

Table 7.22: Sensitivity analysis results

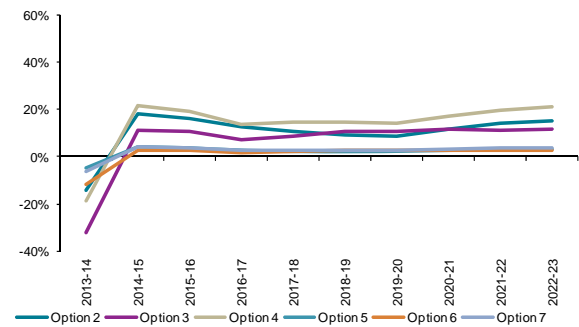
Hornsby Shire Council only	Aggregate results
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Chart 7.11: Estimated percentage point improvements to net operating results (Specification 1)



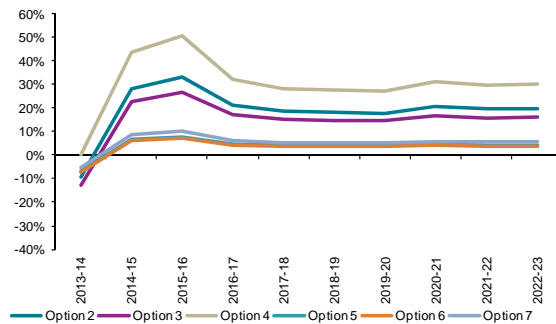
Source: KPMG calculations.

Chart 7.12: Estimated percentage point improvements to net operating results (Specification 1)



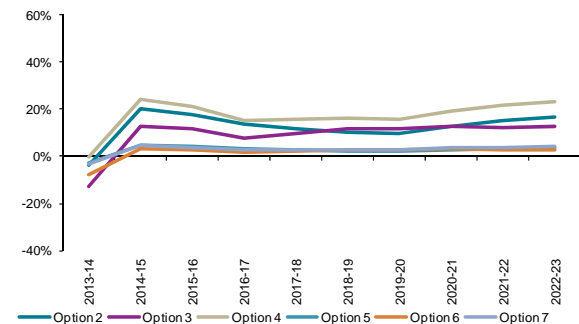
Source: KPMG calculations.

Chart 7.13: Estimated percentage point improvements to net operating results (Specification 2)



Source: KPMG calculations.

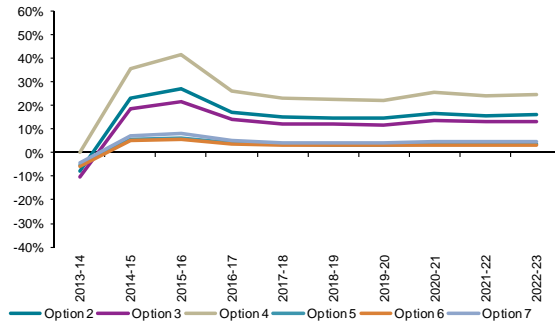
Chart 7.14: Estimated percentage point improvements to net operating results (Specification 2)



Source: KPMG calculations.

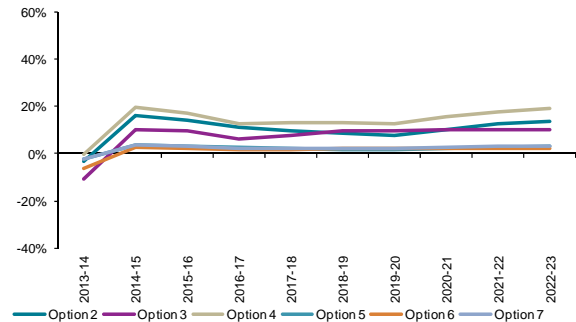
Hornsby Shire Council only
Aggregate results

Chart 7.15: Estimated percentage point improvements to net operating results (Specification 3)



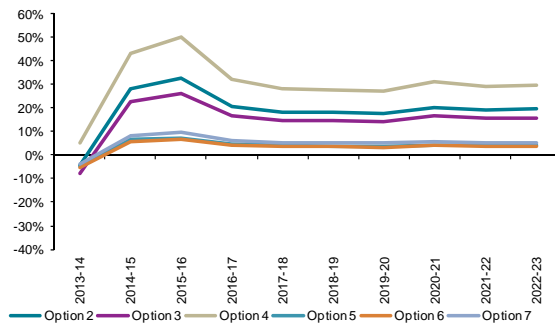
Source: KPMG calculations.

Chart 7.16: Estimated percentage point improvements to net operating results (Specification 3)



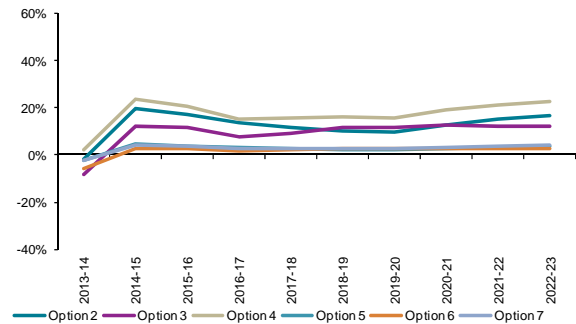
Source: KPMG calculations.

Chart 7.17: Estimated percentage point improvements to net operating results (Specification 4)



Source: KPMG calculations.

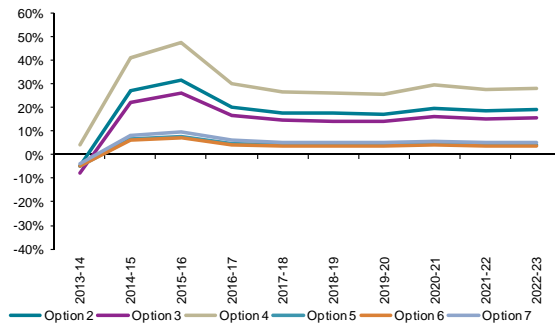
Chart 7.18: Estimated percentage point improvements to net operating results (Specification 4)



Source: KPMG calculations.

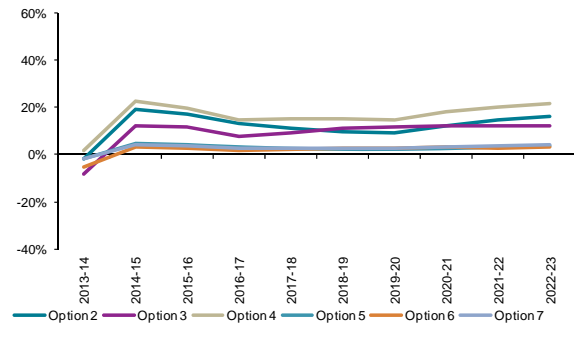
Hornsby Shire Council only **Aggregate results**

Chart 7.19: Estimated percentage point improvements to net operating results (Specification 5)



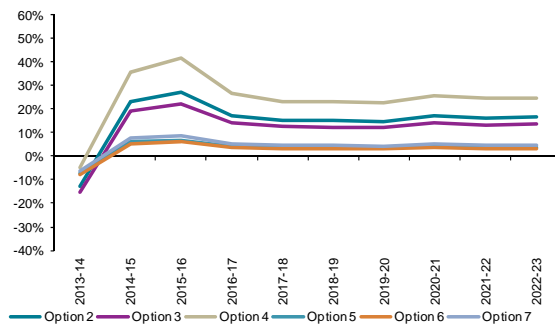
Source: KPMG calculations.

Chart 7.20: Estimated percentage point improvements to net operating results (Specification 5)



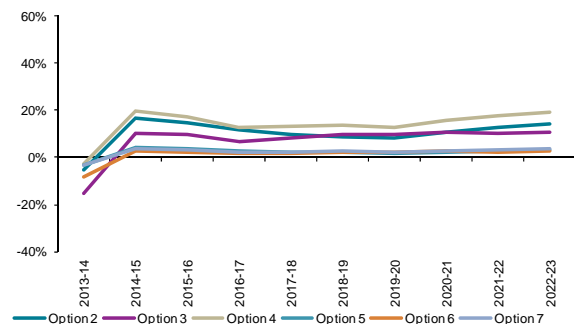
Source: KPMG calculations.

Chart 7.21: Estimated percentage point improvements to net operating results (Specification 6)



Source: KPMG calculations.

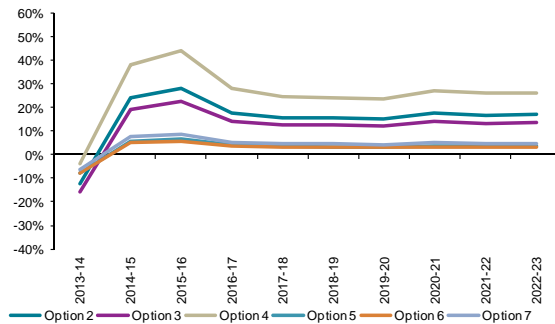
Chart 7.22: Estimated percentage point improvements to net operating results (Specification 6)



Source: KPMG calculations.

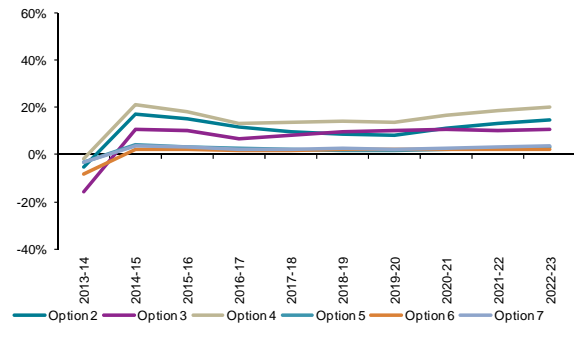
Hornsby Shire Council only **Aggregate results**

Chart 7.23: Estimated percentage point improvements to net operating results (Specification 7)



Source: KPMG calculations.

Chart 7.24: Estimated percentage point improvements to net operating results (Specification 7)



Source: KPMG calculations.

7.2.4 Limitations

It is important to consider the results of the analysis in the context of the both the supporting assumptions and their limitations. There are a number of limitations associated with the available data and the assumptions necessary to undertake the analysis.

- The financial analysis only considered major cost and benefit streams, and it is acknowledged that there may be other impacts that may materialise upfront or over time, although it is expected that these would be relatively minor.
- The financial analysis only considered whole-of-council level impacts. It is noted that there may be some distributional impacts as part of reform options, in particular in relation to rate revenue. For example, the aggregate rate revenue would be expected to be unchanged by reform options, however, potential differentials in property values may mean that individual rate liabilities are impacted by reform. These impacts are not accounted for in the financial analysis, and are separately discussed in the analysis of supporting strategies and mechanisms (see Section 7.3).
- The financial analysis of impacts for neighbouring councils across reform options was limited by the scope and scale of available data. Given these limitations, the estimates are illustrative only and high level and the results should therefore be considered in this context. Further, more detailed analysis will be required to extend this preliminary analysis and support a formal decision on a preferred option from councils.
- The specification of the financial analysis inherently assumes that there are appropriate supporting mechanisms to ensure effective implementation and management over time. For example, there may be fewer benefits or increased costs (i.e. reduced net benefits) if there are improper implementation and management of the reform process by Hornsby Shire Council or other impacted councils. These considerations cannot be accounted for within the financial analysis, and are considered qualitatively in the discussion of supporting strategies and mechanisms (see Section 7.3) and in the high level implementation plan (see Chapter 8).

There were a number of components within the approach to address limitations to the greatest extent within the scope of work and with available data, namely:

- sensitivity analysis was undertaken to illustrate the potential impacts of changes in key assumptions and inputs on the results; and
- the multi-criteria analysis considered a broader range of factors than the results of the financial analysis, in particular qualitative analysis of factors in the context of Hornsby Shire Council.

7.3 Supporting strategies and mechanisms

Implementing local government reform, whether through boundary reform or shared services, requires consideration of a variety of supporting factors in addition to the expected financial impacts. This section identifies and discusses these factors to assist in enhancing the efficiency and effectiveness of reform options. Supporting strategies and mechanisms include:

- asset utilisation, renewal and financial sustainability;
- service delivery pathways to promote quality provision of council services;
- governance structures of new council entities, including ensuring effective representation of residents; and
- transition measures.

Drawing on previous experiences, both nationally and internationally, a number of strategies and mechanisms are discussed to inform the reform process for councils and local communities.

7.3.1 Asset utilisation, renewal and financial sustainability

The financial sustainability of the council is strongly linked to the utilisation of assets and their renewal. To smooth the process of any reform, councils should consider:

- valuation and stock take of assets; and
- maintenance of infrastructure.

Valuation and stock take of assets

To ensure that all parties to a reform arrangement enter it with accurate information, councils should undertake a comprehensive stock take of their assets. As part of this, councils should ensure that their valuation and depreciation of assets follow appropriate standards, and are undertaken on a consistent basis with other parties to the reform arrangement. This will help to ensure that:

- asset management ratios are as meaningful and representative as possible, thereby enabling more effective judgement, both through the reform process and over time;
- reduce the risk of misunderstandings or possible recriminations, should there be inaccurate valuations; and
- provide a consistent basis to understand the success of reforms following implementation.

As part of the stock take of council assets, councils should use the reform process as an opportunity to review the commerciality of current asset utilisation. This should involve an analysis of the utilisation of all council assets, for example community centres, depots, and libraries. Where assets do not meet utilisation benchmarks or are unviable (i.e. if revenues are not sufficient to cover expenditure), they should be considered for rationalisation on a case-by-case basis.

Maintenance of infrastructure

The provision of local infrastructure and amenities for community use is a key function of local councils. The quality of infrastructure has a direct relationship with economic development and property values within areas. Therefore, the failure to maintain and renew infrastructure can impede economic development.

The calculation of the infrastructure backlog in councils is an important part of providing infrastructure to the community. It helps councils understand the extent of the challenge and therefore can guide planning and deployment of strategies to alleviate the backlog over time.

The reported infrastructure backlog in Hornsby Shire Council is substantially smaller than in neighbouring councils, including after adjustment for the relative size of councils. Understanding the sources of these discrepancies, for example differences in accounting methodologies, reality, or a combination of both, will be crucial to comprehend the extent of the liabilities being taken on.

7.3.2 Service delivery

The provision of effective and efficient services is a key focus of councils. Both boundary reform and shared services options present specific challenges to the effective delivery of services. These challenges must be considered and planned for to minimise impacts on successful implementation and service quality over time. These challenges include the need to align and consolidate:

- service levels between councils;
- human resource management across councils; and
- corporate support functions, which enable service delivery.

Service levels between councils

The implication of different levels of service offered by different councils, and how this is consolidated through the reform process, needs to be considered. Differences in service levels between councils can arise as a result of the varying demographic profile of the councils that may necessitate different types or levels of service provision. For example, Parramatta Council is largely urban, with a mix of high, medium, and low density commercial and residential buildings. Conversely, Hornsby Shire Council, Ku-ring-gai Council and The Hills Shire Council have large bushland areas.

A key part of an amalgamation or a shared services model is that residents receive the same level of service regardless of their location within the council. Key considerations over the medium term for service level harmonisation include:

- alignment of fees and charges levied by council for some services;
- alignment of business processes when handling issues such as development applications and customer contact points; and
- budgetary impacts of changes to ensure that, as far as reasonably practicable, impacts are budget-neutral.

Human resource management

The provision of services by council is dependent on having effective workforce capacity, and an important goal of local government reform is to increase financial sustainability. It is acknowledged that one of the most significant sources of these efficiencies will be more effective use of larger staffing establishments.

The change management component of the reform process will require a considered approach that recognises that some areas of council operations will need staffing levels maintained, while other areas will present opportunities to realise efficiencies. By their nature, staffing efficiencies will tend to disproportionately impact management.

To be best placed for change management, councils should undertake a thorough analysis of the operations of the councils involved in the reform to:

- understand the structure and function of councils at the operational level;
- analyse the current distribution and utilisation of human resources across functions and divisions within the council, including:
 - by major division; and
 - by function, for example customer-facing roles relative to strategic roles.

Appropriate management of this process will be critical to ensure:

- the functional capacity and service delivery standards of the council are maintained; and
- cohesion and morale of staff are not adversely impacted.

Corporate support functions

Boundary reform or shared services models will require consolidation and alignment of corporate support functions to enable the potential efficiencies of scale to be realised over time

Components of the alignment of corporate support functions will include:

- consolidation of information technology (IT) facilities and systems that support council operations, for example through integration and harmonisation of software used by councils.
- procurement practices; and
- human resources and finance functions.

Notwithstanding substantial upfront costs the consolidation of corporate support, effective implementation is required to unlock potential gains over time. For example, with respect to IT integration and harmonisation, opportunities for cost savings through scale can arise through:

- improved cost effectiveness of software licensing and maintenance;
- improved streamlining of IT integration with service delivery; and
- capacity to support workforce productivity improvements.

7.3.3 Governance structures

The implementation of new governance structures is crucial in facilitating any reform option. There are different governance considerations for boundary reform and shared service options.

Amalgamation

The pursuit of local government reform through an amalgamation will present potential governance issues that include:

- the location where the new council should be situated;
- redrawing council and ward boundary lines; and
- the effective representation of residents.

Given the consolidation of two councils into one central governing body, there must be consideration of the location of any newly formed council. It may be possible – and cost effective – to utilise one of the former council offices, however, there may be resistance within the community driven by concerns over local representation and identity. While such a decision would have relatively minor practical impacts on service delivery, this issue has potentially significant symbolic importance and should be managed with stakeholder engagement.

Amalgamation of councils will likely result in the redrawing of ward boundaries and, potentially, council boundaries. The redrawing of ward boundaries is likely to be accompanied by a reduction in the total number of councillors representing the merged area, and there is potential for:

- resistance in local communities driven by concerns of the capacity or quality of representation of community needs; and
- political considerations to influence the process or outcome.

To best manage these risks, a considered approach should be undertaken that is underpinned by strong stakeholder engagement with the interests of residents at its core.

In other cases of local government reform, such as the creation of Auckland Council, concerns among residents about adequate local representation have been addressed by creating community councils or boards. Community councils are responsible for engaging with local communities and addressing relatively minor issues (e.g. removal of vegetation on council-owned nature strips). Further, community councils and boards can provide a forum for local to communicate their needs, interests, and preferences on strategies, plans, policies in local communities.

The key risk with implementation of community councils or boards is the unnecessary addition of bureaucracy on residents, and this should be carefully considered and managed within the overarching governance framework.

Shared services

The implementation of a shared services model can avoid many of the governance challenges associated with amalgamation options, for example the potential to redraw ward boundaries. Research undertaken by Crosby|Textor for Hornsby Shire Council also found that a shared services model was the most popular local government reform option amongst residents. Notwithstanding this preference, shared services models raise different governance considerations, of which the nature and extent can depend on the type of model adopted.

The shared services models considered above place the authority and responsibility for each function or branch with one council. This arrangement would need to be governed by a detailed Memorandum of understanding (MoU) that would provide a clear framework for:

- day-to-day functions and responsibilities; and
- clear dispute resolution pathways and a mutually agreed independent arbitrator, should an unresolved dispute be escalated beyond the participating councils.

This MoU would also organise processes to be followed when residents in one council receive services from another council, and are seeking redress for an issue.

7.3.4 Transition measures

The implementation of local government reform is a significant undertaking that will impact various stakeholders, including council staff, residents, suppliers, contractors, and local businesses. While the implementation of a shared services model is distinct, the amalgamation of Hornsby Shire Council with a similar sized council would be equivalent to a mid-sized corporate merger, namely a merging of entities with combined assets of nearly \$3.0 billion. The transition period will be critical in creating the right conditions for realisation of the potential benefits of reform over time.

Councils will have to implement a comprehensive change management program to assist the successful delivery of reform, including:

- undertaking internal and cross-council engagement to understand whether a dedicated project management office is required to, and, if so, establishing it;
- identify and assign program-level and overall accountability for the agreed change management program across each area of the council;
- undertake consistent internal and external stakeholder engagement about the reform process, including:
 - the rationale, approach, and management strategy;
 - timeframes for implementation; and
 - the expected impacts of the reform process, targeted to stakeholders.
- establishing processes to ensure the longevity of reforms, for example through performance management, and periodic program and service delivery reviews.

The ILGRP suggested maintaining the existing ward boundaries and number of councillors for two electoral terms to assuage any concerns about the adequacy of local representation.

Following this transitory period, new ward boundaries would come into effect, which would result in the reduction of the number of representatives.

The ILGRP's Final Report recommended that the State Government provide incentives – in the form of technical assistance – to early adopters of local government reform, for example:

- professional change management support for assessing business cases and then negotiating, planning and implementing mergers;
- consultants to assist councils with the integration of rating and IT systems; and
- transitional funding through a mix of grants and low or no interest loans, consistent with an agreed implementation plan.

Notwithstanding the ILGRP's qualification that financial support should be directed towards councils with limited revenue potential or those with higher liabilities, Hornsby Shire Council should proactively engage with the NSW Government to:

- explore potential forms of assistance to support different reform options; and
- inform the preparation of a business case for assistance that may be available.

7.4 Stakeholder testing with neighbouring councils

Given the options analysed within the report, Hornsby Shire Council management approached the management of The Hills Shire and Ku-ring-gai Councils to review and provide feedback on the Draft Report. The purpose of the testing process was to:

- test and refine the assumptions and results of the financial analysis;
- develop a more detailed understanding of strategic and operational factors that may inform the broader analysis; and
- inform the development of the high level implementation plan.

Both The Hills and Ku-ring-gai Councils' management declined the opportunity to review and provide feedback on the Draft Report.

7.5 Determining a preferred option

Further due diligence, particularly from the perspective of other councils in the reform process, is required to support a final decision as to the best way forward. The recommended approach for Hornsby Shire Council is to actively engage all relevant councils and undertake a more comprehensive evaluation of the costs and benefits of all options. The approach to developing the analysis within this report has the flexibility to be extended and refined over time, should further, more detailed data become available.

As part of further due diligence, the preferred option should be identified using multi-criteria analysis to recognise that there may be broader impacts associated with reform options. Illustrative financial and non-financial criteria to support the decision making process are outlined in Table 7.23, and were identified in the context of the local government reform principles outlined earlier in this report.

Table 7.23: Illustrative financial and non-financial decision making criteria

	Measure
Financial criteria	
The net financial benefits of options	Ranking of percentage point impacts relative to the base case net operating results
Risks to financial sustainability over the medium to long term	Informed by the financial analysis and financial statement analysis of Hornsby Shire Council and neighbouring councils in the Northern Sydney area.
Non-financial criteria	
Strategic risks	Determined with respect to the analysis of supporting strategies and mechanisms and high level implementation considerations.
Risks to service quality and effectiveness over time	
Risks to the quality and effectiveness of local representation	
Risks to effective implementation and management over time	

Source: KPMG.

To complete a multi-criteria analysis of reform options, it is recommended that Hornsby Shire Council:

- engage with internal and external stakeholders to refine the financial and non-financial criteria to underpin the analysis;
- determine appropriate weightings for criteria that best reflect the values and priorities of stakeholders;
- rank options with respect to each criteria, based on the outcomes of further, more detailed due diligence; and
- determine a preferred option, based on the weighted scores of each option with respect to the established criteria.

8 Considerations for implementation

There are a number of precursors to the finalisation and implementation of a preferred option by Hornsby Shire Council. These include, for example:

- continued engagement in the broader local government reform debate in NSW, particularly when the NSW Government formalises its position to the *Revitalising Local Government* report recently released by the ILGRP; and
- further, more detailed due diligence of reform options, particularly from the perspective of other councils in the reform process.

The recommended approach for Hornsby Shire Council is to actively engage all relevant councils and the NSW Government concurrently to undertaking a more comprehensive evaluation of the costs and benefits of all options. The approach to developing the analysis within this report has the flexibility to be extended and refined over time, should further, more detailed data become available.

This section provides a suggested high level implementation plan for an amalgamation or shared services reform model. Through the remainder of the due diligence process, a more complete implementation plan will be required that provides:

- greater detail that is targeted to the specific option being considered;
- target completion dates for actions; and
- accountabilities for those actions within agreed timeframes.

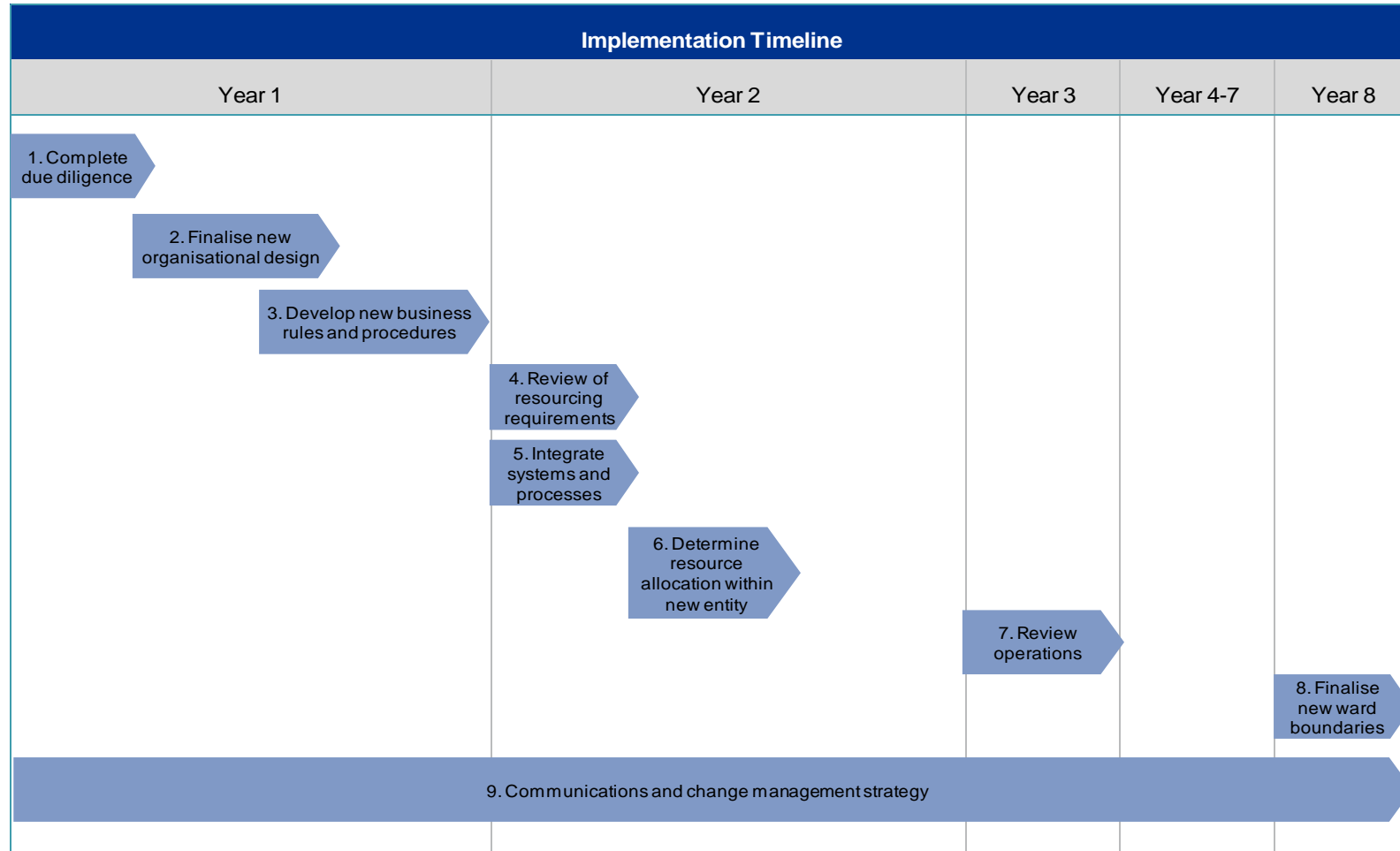
A prerequisite for any implementation plan is thorough planning and effective communication with stakeholders. An illustrative implementation plan is presented in Figure 8.1 for an eight year period, recognising the recommendation from the ILGRP that existing ward boundaries and councillor numbers must remain for two electoral terms.³⁵

Notwithstanding the length of the implementation plan, major elements would be expected to conclude in the medium term (i.e. within 18 months), including:

- **planning** in the first 12 months (see Section 8.1 to Section 8.2); and
- **execution** over a 12 to 18 month period (see Section 8.4 to Section 8.9).

³⁵ The last Local Government elections were held in 2012, and electoral terms run for four years.

Figure 8.1: Illustrative implementation timeline



Source: KPMG.

8.1 Complete due diligence

Prior to formally committing to an amalgamation or shared services model, it is recommended that Hornsby Shire Council undertakes appropriate due diligence in good faith with other parties. The purpose of the due diligence process will be to ensure effective and informed decision making that is underpinned by a thorough consideration of factors that may impact the decision, either during implementation or over time.

The scope of the due diligence should include the following:

- financial stability, including:
 - financial viability and management;
 - policies, procedures and systems; and
 - strength of audit.
- operations;
 - past performance;
 - staff capacity and capability; and
 - program management.
- governance and internal control;
 - governance;
 - risk management;
 - relationship with partners (e.g. suppliers, contractors); and
 - fraud, bribery and corruption.

8.2 Finalise new organisational design

To realise the benefits of an amalgamation between two or more organisations, a new organisational design is particularly important, especially where the councils do not share similar organisational structures. Depending on the type of shared services model implemented, an organisational redesign may also be required at the new council, for example if some functions are handled solely by one council.

This phase of implementation should include the following steps:

- agreement of a Target Operating Model that will guide development of the organisational design itself. This will include agreeing design principles that will influence how the organisation will operate (for example the balance of delivery versus commissioning), understanding the value chain of operations, and how governance will work;
- agreement and acceptance of a high-level organisational design for the new entity, including functional descriptions, accountabilities; and allocations of FTE resources;

- agreement and acceptance of a detailed organisational design, including role descriptions for all positions within the new organisation;
- development of a change management strategy and plan, including cultural change assessment, communication of the new structure, including its implementation, to staff;
- preparing a stock take of current and future reforms, initiatives, strategies and work plans, and preparing appropriate areas within the new structure to account for these;
- aligning the new structure and associated accountabilities to individual, team, branch and divisional performance management metrics; and
- designing and documenting activities, services, and functions of teams and branches within the new structure to understand the interdependencies, capacity, and functional effectiveness across the organisation.

8.3 Develop new business rules and procedures

The extent of the need for new business rules and procedures would be dependent on the type of reform that is implemented, and may include:

- aligning the strategic focus through publication of revised strategic documents (e.g. Community Strategic Plan);
- alignment of business rules, procedures, and protocols for interaction across the entity, including in:
 - corporate support functions (e.g. finance, procurements, human resources, IT, and legal); and
 - service provision (e.g. library services, childcare, waste management, parks, and recreation).
- planned consolidation of physical properties and location of staff within new structure.

8.4 Review of resourcing requirements

A review of resource requirements and allocation should be undertaken based on the type of reform that is implemented and the scale of efficiencies that are expected to be achieved. Should resource reallocation be required within the new council entity, it should include the following steps:

- development of a resource allocation plan for the new organisational structure;
- consistent and clear communications with staff, and – where appropriate – unions; and
- consider hiring freezes to allow for natural attrition of positions within the organisations.

8.5 Integrate systems and processes

This phase of the implementation should focus on the execution of system and process integration or alignment that was planned in Section 8.2. System integration and alignment for

an entity with multi-billion dollar assets must occur without interruption in service provision to residents.

8.6 Ongoing monitoring of resource allocation

Following the development of the resource allocation model for the new entity, there should be ongoing monitoring of resource allocation and efficiency against that model. In particular, this should include:

- monitoring of existing staff skills, knowledge, and capability;
- incorporation of monitoring results in a merit-based selection process to manage excess positions, as they relate to the new structure, including identification of potential ‘swaps’ and transfers; and
- refinement, where necessary, of the resource allocation model.

8.7 Review operations of reformed entity

This phase of the implementation plan provides an opportunity to examine the impact of reform on the operations of the council. The review should be conducted with reference to the intended outcomes of the organisational redesign and its associated functions and accountabilities (see Section 8.2).

An effective basis for the review could include the local government reform principles used to develop and analyse reform options upfront, namely:

- local government capacity – the ability of local government to maintain and enhance service quality;
- financial sustainability – the ability for councils to sustainably fund adequate and effective services and operations over time; and
- local representation – the ability of local government to effectively represent ratepayers (see Section 4.2).

8.8 Finalise new ward boundaries

The finalisation of new ward boundaries is temporally separated from earlier stages of the implementation plan. This is due to a recommendation by the ILGRP that existing ward boundaries remain in amalgamated councils for two electoral terms to ensure that the number of elected representatives does not decrease. Following this period, the number of councillors in an amalgamated council should be reduced and new ward boundaries drawn to reflect this. Consideration should be given to the ideal number of councillors that would facilitate the operations of the council and ensure levels of representation are preserved.

The timing of ward boundary adjustments is unlikely to be eight years, as suggested in Figure 8.1, given that local government elections occur every four years. Given the last elections were held in 2012, new ward boundaries could be drawn for elections in either 2020 or 2024.

Ward boundaries should ideally be re-drawn by an independent, non-partisan entity.

8.9 Communications and change management strategy

The communications and change management strategy is a crucial component of the implementation plan, and it should be sufficiently planned and executed through the implementation process to best enable buy-in of key stakeholders. This phase of the plan should include:

- developing an overarching change strategy to guide how the implementation will be managed, including phasing of approaches;
- analysing the change impact, including an assessment of organisational culture(s) and any mitigating action required;
- developing and managing a communication plan to advise external stakeholders of organisational change, and communicating change to stakeholders, including:
 - residents;
 - businesses;
 - staff, contractors, and suppliers;
 - neighbouring councils; and
 - other government agencies.
- developing a change management program, including:
 - developing and maintaining an inventory of tasks;
 - determining and assigning accountabilities and timeframes;
 - risk management considerations; and
 - identifying measures to monitor and the success of implementation over time; and
- agreeing arrangements to close and review program and implementation success.

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A Summary of ILGRP Revitalising Local Government recommendations and their impact on Hornsby Shire Council

The ILGRP's Final Report contained 65 recommendations. Table A.1 contains a list of the ILGRP's Principal Recommendations and provides a high level indication of the potential impact on Hornsby Shire Council. It is noted that Hornsby Shire Council should consider these recommendations in detail to understand the likely impacts, whether positive or negative.

Table A.1: Impact of ILGRP's principle recommendations on Hornsby Shire Council

	Principal Recommendations	Impacts Hornsby?	Positive or Negative?
Fiscal responsibility	Establish an integrated Fiscal Responsibility Program, coordinated by DLG and also involving TCorp, IPART and LGNSW... (5.1 and 5.3)	✓	●
	Introduce more rigorous guidelines for Delivery Programs... (5.2)	✓	●
	Place local government audits under the aegis of the Auditor General (5.4)	✓	●
Strengthening the Revenue Base	Commission IPART to undertake a further review of the rating system focused on: options to reduce or remove excessive exemptions and concessions... (6.2); more equitable rating of apartments and other multi-unit dwellings... (6.3)	✓	●
	Either replace rate-pegging with a new system of 'rate benchmarking' or streamline current arrangements to remove unwarranted complexity, costs, and constraints to sound financial management (6.5)	✓	●
	Subject to any legal constraints, seek to redistribute federal Financial Assistance Grants and some State grants in order to channel additional support to councils and communities with the greatest needs (6.6)	✓	●
	Establish a State-wide borrowing facility to enable local government to make increased use of debt where appropriate... (6.7)	✓	●
Meeting Infrastructure Needs	Maintain the Local Infrastructure Renewal Scheme (LIRS) for at least 5 years, with a focus on councils facing the most severe infrastructure problems (7.2)	✓	●
	Pool a proportion of funds from the roads component of federal Financial Assistance Grants and, if possible, the Roads to Recovery program in order to establish a Strategic Projects Fund for roads and bridges... (7.2)	✓	●

	Principal Recommendations	Impacts Hornsby?	Positive or Negative?
	Adopt a similar model to Queensland's of Regional Roads and Transport Groups... (7.4)		●
Improvement, Productivity and Accountability	Commission IPART to undertake a whole-of-government review of the regulatory, compliance and reporting burden on councils (8.2)	✓	●
	Amend IPR Guidelines to require councils to incorporate regular service reviews in their Delivery Programs (8.4)	✓	●
	Strengthen requirements for internal and performance auditing as proposed in Box 17 (8.5)	✓	●
Political Leadership and Good Governance	Require councils to undertake regular Representation Reviews ... (9.1)	✓	●
	Amend the legislated role of councillors and mayors... and introduce mandatory professional development programs (9.2 and 9.3)	✓	●
	Amend the legislated role and standard contract provisions of General Managers... (9.5)	✓	●
	Develop a Good Governance Guide ... (9.7)	✓	●
Advance Structural Reform	Introduce additional options for local government structures, including regional Joint Organisations, 'Rural Councils' and Community Boards, to facilitate a better response to the needs and circumstances of different regions (10.1)	✓	●
	Legislate a revised process for considering potential amalgamations and boundary changes through a re-constituted and more independent Boundaries Commission (10.3)	✓	●
	Encourage voluntary mergers of councils through measures to lower barriers and provide professional and financial support (10.4)	✓	●
Regional Joint Organisations	Establish new Joint Organisations (JOs) for each of the regions shown on Map 2 ... under new provisions of the Local Government Act that replace those for County Councils(11.5)	✗	N/A
	Establish Regional Water Alliances in each JO along the lines proposed in the 2009 Armstrong-Gellatly report (11.3)	✗	N/A
'Rural Councils' and Community Boards	Establish a working party... to further develop the concept of 'Rural Councils' (12.1)	✗	N/A
	Include provisions for <i>optional</i> Community Boards ... (12.2)	✓	●

	Principal Recommendations	Impacts Hornsby?	Positive or Negative?
Metropolitan Sydney, Hunter and Central Coast	Seek evidence-based responses from councils to the Panel's proposals for mergers and major boundary changes... (13.3, 14.1, 14.2)	✓	●
	Maximise utilisation of the local government revenue base in the eastern half of the Sydney region in order to free-up State resources...(13.6)	✓	●
Non-Metropolitan Regions	Progressively refer (non-metropolitan) councils ... to the reconstituted Boundaries Commission in accordance with Table 11 and the proposed timeline (15.1)	✗	N/A
The Far West	Agree in principle to the establishment of a Far West Regional Authority (16.3)	✗	N/A
	Adopt the preferred new arrangements for local government set out in Box 40...(16.4)	✗	N/A
State-Local Government Relations	Introduce new arrangements for collaborative, whole-of-government strategic planning at a regional level (17.3)	✓	●
	Amend the State Constitution to strengthen recognition of elected local government (17.4)	✓	●

Note: ● = expected positive impact; ● = insufficient information to determine / expected neutral impact; ● = expected negative impact.

Source: ILGRP (2013); KPMG.

B Detailed approach and supporting assumptions

This appendix provides detailed information on the approach and supporting assumptions used to undertake the financial analysis of reform options. For each major income and expenditure stream associated with reform options, this appendix provides:

- the approaches used to estimate impacts, developed with respect to the scope and scale of available data; and
- supporting assumptions required to undertake the analysis with available data, developed with respect to insights from the comparative study and consultations with Hornsby Shire Council.

Given the nature of available data for neighbouring councils, impacts for these councils were developed using higher level approaches that necessarily required additional supporting assumptions to the approach for Hornsby Shire Council. The approaches and assumptions to estimate impacts for Hornsby Shire Council and neighbouring councils are therefore separately discussed.

For the purposes of modelling shared services options, there was insufficient data to estimate the impacts of individual benefit and cost streams, as was undertaken for boundary reform options. Therefore, assumptions were made with respect to the aggregate benefits and costs based on the outcomes of the desktop research, comparative study, and consultations with Hornsby Shire Council.

B.1 Hornsby Shire Council only

Major financial cost and benefit streams, along with the approach to estimating these for Hornsby Shire Council, are outlined in Table B.1. Supporting assumptions specific to different options are also outlined in Table B.2.

Table B.1: Approach to quantify major cost and benefit streams for Hornsby Shire Council

Approach	Data source(s)
1. Benefit streams	
<i>Direct staffing efficiencies(all options)</i>	
<p>Avoided salaries and wages expenditure</p>	<p>Detailed staffing establishment data by branch were analysed by using a standard process model that identifies the functional type of a particular role. Efficiencies were estimated as percentage reductions to the current FTE establishment by functional type. Estimated efficiencies were disproportionately allocated to strategic and support functions, where there are naturally higher economies of scale compared to customer-facing operations. Division level efficiencies were cross-checked against evidence from the comparative study in respect to aggregate staffing efficiencies achieved through boundary reform.</p>
	<p>Hornsby Shire Council staffing establishment data.</p> <p>FTE establishment of The Hills Shire and Ku-ring-gai Councils.</p> <p>Annual salaries and wages expenditure (including on-costs) for The Hills Shire and Ku-ring-gai Councils.</p> <p>ABS 2012, Cat. No. 6348.0, <i>Labour Costs, Australia, 2010-11.</i></p>
<i>Other operational efficiencies(all options)</i>	
<p>Efficiency savings in 'Materials and contracts' expenses</p>	<p>Detailed cost items within 'Materials and contracts' from Hornsby Shire Council financial statements were reviewed to determine the scope of applicability of efficiency savings. The assumed value of efficiency savings, estimated as a proportion of eligible 'Materials and contracts' expenses, was applied to projected 'Materials and contracts' expenses from Hornsby Shire Council long term financial projections.</p>
	<p>Hornsby Shire Council 2012-13 financial statements.</p> <p>Hornsby Shire Council long term financial projections.</p>
<p>Efficiency savings in 'Other expenses'</p>	<p>Detailed cost items within 'Other expenses' from Hornsby Shire Council financial statements were reviewed to determine the scope of applicability of efficiency savings. The assumed value of efficiency savings, estimated as a proportion of eligible 'Other expenses', was applied to projected 'Other expenses' from Hornsby Shire Council long term financial projections.</p>
	<p>Hornsby Shire Council 2012-13 financial statements.</p> <p>Hornsby Shire Council long term financial projections.</p>
<i>Asset utilisation and renewal (Option 2, Option 3, Option 4 only)</i>	

	Approach	Data source(s)
Avoided annual facilities expenditure Forgone annual user charges revenue from facilities	<p>Operational data for community facilities, including annual revenue, expenditure, and utilisation, were used as the basis to identify opportunities for asset rationalisation.</p> <p>Opportunities for asset rationalisation were determined with respect to both:</p> <ul style="list-style-type: none"> the profitability of the facility's operation (i.e. whether operational revenue exceeded operational costs); and the geographical proximity of the asset to boundaries of amalgamating councils. <p>The purpose of considering the geographical proximity to boundaries of amalgamating councils was necessary given that it would be incorrect to attribute the impacts of asset rationalisation to boundary reform if it is not directly attributable to the reform process.</p>	Hornsby Shire Council community and cultural facility data for 2012-13.
Improved capacity to fund infrastructure backlogs	<p>Improved financial sustainability from staffing efficiencies and infrastructure rationalisation will improve the capacity of councils to fund infrastructure backlogs, either:</p> <ul style="list-style-type: none"> directly, through financing of new infrastructure or capital refurbishment; or indirectly, through improved capacity to manage debt. <p>There was insufficient data to estimate the monetary benefits associated with improved capacity to fund infrastructure backlogs. This benefit stream was therefore qualitatively analysed.</p>	N/A
2. Cost streams		
<i>Upfront costs (all options)</i>		
Redundancy costs	<p>Redundancy costs were estimated based on:</p> <ul style="list-style-type: none"> the estimated staffing efficiencies by division (see above); average salaries and accruals (annual leave and long service leave) by division from Hornsby Shire Council; and <p>an assumption about the average tenure of employees to determine the redundancy liability as a function of annual salaries.</p>	Hornsby Shire Council staffing establishment data. Hornsby Shire Council (2013), <i>Workforce planning 2013-17</i> .
Facility consolidation IT consolidation	<p>Data were not available to directly estimate these costs, however, evidence from the comparative study was available that related to:</p> <ul style="list-style-type: none"> aggregate upfront costs of boundary reform as a 	Hornsby Shire Council long term financial projections.

	Approach	Data source(s)
Staff retraining costs	function of total annual expenditure; and	
Other costs	<ul style="list-style-type: none"> the distribution of the total upfront cost by cost type. 	
<i>Recurrent costs (all options)</i>		
Service level harmonisation	Evidence on the costs associated with service level harmonisation were available from international examples in the comparative study, however, there was insufficient information on the comparability of the cost of service to the Australian context. Therefore, it was determined that there was insufficient information to quantitatively estimate these costs.	N/A
Cost of debt financing for upfront costs	The cost of debt associated with financing the upfront cost of reform was determined by considering the reasonableness of Hornsby Shire Council funding the costs from its free cash flow. This determination was made with respect to detailed financial data provided by Hornsby Shire Council and tested with Hornsby Shire Council.	Hornsby Shire Council long term financial projections. RBA 2013, <i>Indicator Lending Rates</i> .
Forgone interest on cash or cash equivalents	Where the upfront cost of reform was determined to be financed from Hornsby Shire Council's cash and cash equivalents, the value of forgone interest on those cash and cash equivalents was estimated.	Hornsby Shire Council long term financial projections.

Source: KPMG.

Table B.2: Assumptions to quantify major cost and benefit streams for Hornsby Shire Council

Assumptions	Option 2	Option 3	Option 4	Option 5	Option 6	Option 7						
Avoided salaries and wages expenditure	Aggregate efficiency Overall staffing efficiencies were estimated at between four per cent and seven per cent of the establishment, based on insights from the comparative study. These were allocated across divisions based on the approach in Section 3.4.						✓	✓	✓	✗	✗	✗
	Nominal salaries and wages growth rate 3 per cent per annum, consistent with Hornsby Shire Council long term financial projections.						✓	✓	✓	✓	✓	✓
	Labour costs The labour on-cost multiplier for the Public Administration and Safety industry was calculated from <i>Labour Costs, Australia, 2010-11</i> (ABS).						✓	✓	✓	✓	✓	✓
	Assumptions specific to shared services options 60 per cent of the average efficiencies from the corresponding amalgamations for the Infrastructure and Recreation division only.						✗	✗	✗	✓	✓	✓
Efficiency savings in 'Materials and contracts' expenses	Scope of applicability All cost items associated with materials and contracts were assumed to be subject to efficiency savings.						✓	✓	✓	✓	✓	✓
	Value of efficiency It was conservatively assumed that there would be an efficiency saving of three per cent of applicable expenses, based on the Auckland experience from the comparative study.						✓	✓	✓	✓	✓	✓

	Assumptions	Option 2	Option 3	Option 4	Option 5	Option 6	Option 7
Efficiency savings in 'Other expenses'	Scope of applicability All cost items within 'Other expenses' were assumed to be subject to efficiency savings except: <ul style="list-style-type: none"> • bad and doubtful debts; • bank charges and cash collection expenses; • contributions/levies to other levels of government; • councillor expenses (mayoral and councillors' fees and other expenses); and • donations, contributions and assistance. 	✓	✓	✓	✓	✓	✓
	Value of efficiency It was conservatively assumed that there would be an efficiency saving of three per cent of applicable expenses, based on the Auckland experience from the comparative study.	✓	✓	✓	✓	✓	✓
Avoided annual facilities expenditure Forgone annual user charges revenue from	Basis for rationalisation Facilities were assumed to be rationalised as a result of boundary reform if: <ul style="list-style-type: none"> • current utilisation meant that it was economic to do so (i.e. if revenue was not sufficient to exceed expenditure in 2012-13); and • it was located within reasonable geographic proximity to the boundary of respective councils to be included in the boundary reform. One asset was identified for rationalisation within Option 2 and Option 4. On the basis of the criteria above, no other assets were identified for rationalisation in Option 2, Option 3, or Option 4.	✓	✓	✓	x	x	x

Assumptions		Option 2	Option 3	Option 4	Option 5	Option 6	Option 7
facilities	Gain/loss on disposal of assets Due to limited data availability, any gains or losses associated with the disposal of assets were not estimated.	✓	✓	✓	x	x	x
	Inflation rate 2.5 per cent per annum, consistent with Hornsby Shire Council long term financial projections and the midpoint of the RBA target range for inflation.	✓	✓	✓	x	x	x
Redundancy costs	Redundancy payment Staff tenure was estimated with respect to the 2012 employee turnover rate at Hornsby Shire Council (9.4 per cent) and the current staffing establishment. The estimated tenure was assumed to be consistent across all divisions.	✓	✓	✓	✓	✓	✓
	Payment of annual leave accrual Average annual leave accruals per FTE were applied to the estimated efficiency.	✓	✓	✓	✓	✓	✓
	Payment of long service leave accrual Average long service leave accruals per FTE were applied to the estimated efficiency.	✓	✓	✓	✓	✓	✓
Facility consolidation IT consolidation	Cost distribution Total upfront costs were estimated at 4.7 per cent of total annual expenditure and apportioned across cost types based on the Toronto experience discussed in the comparative study.	✓	✓	✓	x	x	x

	Assumptions	Option 2	Option 3	Option 4	Option 5	Option 6	Option 7
Staff retraining costs	Assumptions specific to shared services options Only the Infrastructure and Recreation division was assumed to be shared in Options 5, 6, and 7, and this accounts for 39 per cent of the FTE establishment at Hornsby Shire Council.	x	x	x	✓	✓	✓
Cost of debt financing for upfront costs	Basis to seek debt financing The upfront cost to implement options was compared against projected cash and cash equivalents in the long term financial projections provided by Hornsby Shire Council. Where requirements were less than 10 per cent of cash and cash equivalents, it was assumed that Hornsby Shire Council would finance the implementation out of its cash and cash equivalents.	✓	✓	✓	✓	✓	✓
	Cost of debt The cost of debt was assumed to be the current weighted average small business lending rate, published by the Reserve Bank of Australia (RBA) (6.8 per cent per annum).	✓	✓	✓	✓	✓	✓
Forgone interest on cash or cash equivalents	Investment returns The return on cash and cash equivalents was assumed to be consistent with assumptions in Hornsby Shire Council's long term financial projections.	✓	✓	✓	✓	✓	✓

Source: KPMG.

B.2 Neighbouring councils

In the absence of detailed data, financial analysis for other councils was limited to higher level analysis based on publicly available financial and operational data. To ensure consistency in assumptions and the basis of the analysis, financial impacts for other councils were estimated with reference to ratios calculated in the more detailed analysis for Hornsby Shire Council. The use of this approach represented the most reasonable way to account for the relative scale of councils given the available data.

The approaches for each major impact are outlined in further detail in Table B.3.

Table B.3: Approach to estimating boundary reform impacts for neighbouring councils

	Approach
1. Benefit streams	
<i>Direct staffing efficiencies</i>	
Avoided salaries and wages expenditure	Estimated reductions in salaries and wages (including on-costs) for Hornsby Shire Council were calculated as a proportion of projected total salaries and wages expenditure (including on-costs). This ratio was applied to total projected salaries and wages expenditure (including on-costs) for other councils. Use of the ratio of the monetary value of staffing efficiencies compared to the ratio of FTE reductions recognised that the distribution of staffing efficiencies was disproportionately allocated to functional divisions and management roles, for which salaries tend to be greater than average.
<i>Other operational efficiencies</i>	
Efficiency savings in 'Materials and contracts' expenses	Same approach as for Hornsby Shire Council, however, the composition of 'Materials and contracts' expenses and 'Other expenses' was assumed to be consistent with Hornsby Shire Council.
Efficiency savings in 'Other expenses'	
<i>Asset utilisation and renewal</i>	
Avoided annual expenditure (e.g. staffing, maintenance)	There was insufficient data to estimate impacts associated with asset utilisation and renewal. Given the approach to estimating impacts for Hornsby Shire Council was undertaken on an asset-by-asset basis, there were no reasonable simplifying assumptions that could be applied.
Forgone annual revenue	
Improved capacity to fund infrastructure backlogs	
2. Cost streams	
<i>Upfront costs</i>	

	Approach
Redundancy costs	Estimated redundancy costs (including redundancy payments, annual leave accruals, and long service leave accruals) for Hornsby Shire Council were calculated as a proportion of the total upfront cost of boundary reform. This ratio was applied to the total estimated upfront cost of boundary reform for other councils.
Facility consolidation	Same approach as for Hornsby Shire Council.
IT consolidation	
Staff retraining costs	
Other costs	
<i><u>Recurrent costs</u></i>	
Service level harmonisation	Similar to the approach for Hornsby Shire Council, there was insufficient data to estimate the impacts associated with service level harmonisation.
Cost of debt financing for upfront costs	Same approach as for Hornsby Shire Council.
Forgone interest on cash or cash equivalents	Same approach as for Hornsby Shire Council.

Source: KPMG.

C Financial statement analysis

This appendix discusses financial statement analysis that was undertaken using the FSRs previously used by TCorp in its analysis for the ILGRP. The analysis was undertaken:

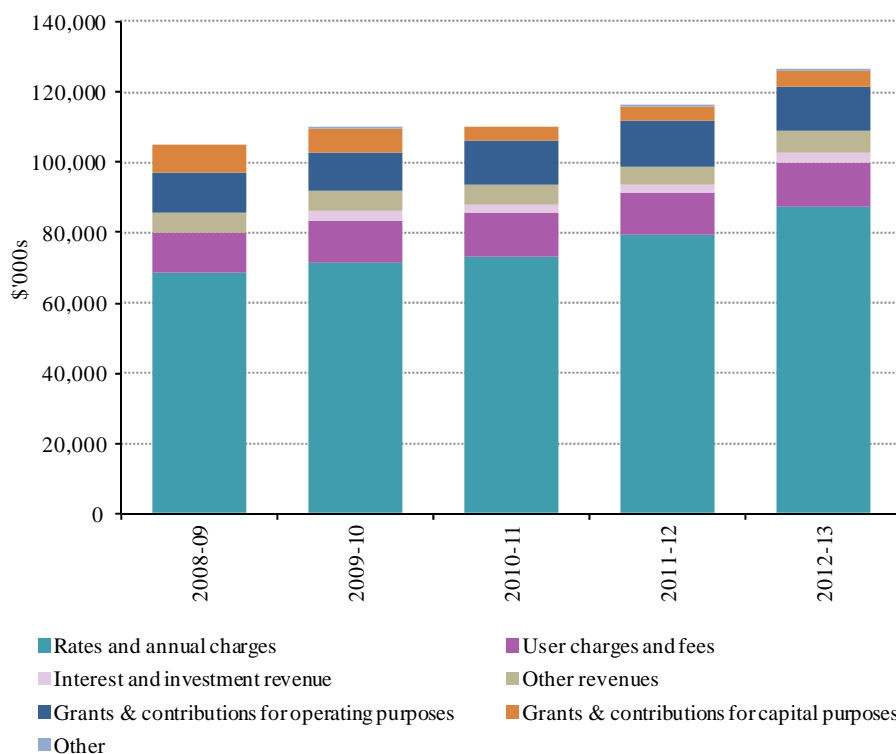
- using detailed financial data for Hornsby Shire Council; and
- higher level, publicly available data for The Hills Shire, Parramatta, and Ku-ring-gai Councils.

The purpose of the financial statement analysis was to provide a high level comparison of financial performance across councils. It is noted that there are a number of potential limitations associated with the financial statement analysis, and these are outlined in Section C.3.

C.1 Detailed financial statement analysis for Hornsby Shire Council

The financial statement analysis for the Hornsby Shire Council analyses the council's income and expenditure between 2008-09 and 2012-13. Chart C.1 below details the operating revenue for the Hornsby Shire Council.

Chart C.1: Operating revenue for the Hornsby Shire Council, 2008-09 to 2012-13



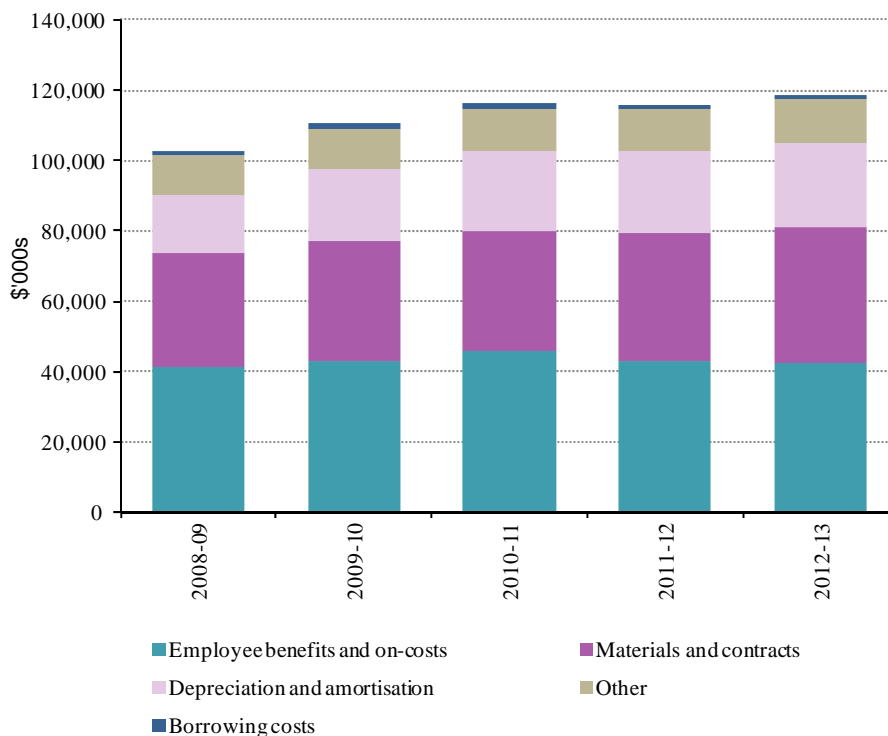
Source: Hornsby Shire Council.

Over the period total revenue increased by 20% (\$21.1m). The main driver of the increase in revenue has been the gradual increase in revenues from rates and charges increasing by over 26% (\$19m) over the period. Revenue from user charges and fees fluctuated between over \$10

million at the beginning of the period to a little over \$12 million in 2012-13. Revenue from grants and contributions to maintain operations also varies over the period reaching a peak of over \$13 million in 2011-12.

Chart C.2 below highlights the operating costs for the council between 2008-09 and 2012-13. Over the period total operating costs increased by 14.6 per cent (\$15.1 million). The principal drivers on the increases in operating costs are increases in materials and contracts expenses and increases in depreciation costs due to asset revaluation. Materials and contracts increased by 19 per cent (\$63 million) and depreciation expenses increased by 45 per cent (\$74.7m). Borrowing costs were reduced over the period by 29 per cent (\$0.4 million). Other expenditure increased over the period by eight per cent (\$0.9 million).

Chart C.2: Operating expenditure for the Hornsby Shire Council, 2008-09 to 2012-13



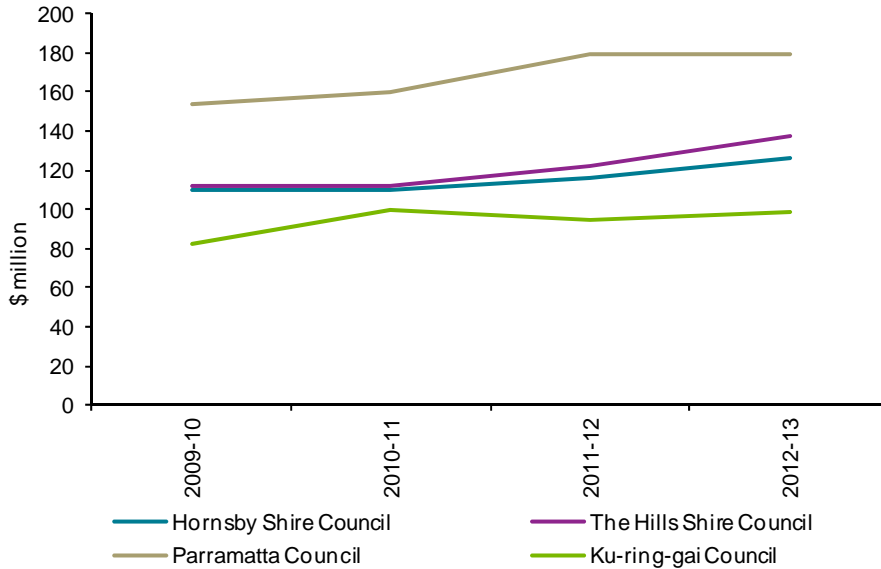
Source: Hornsby Shire Council.

C.2 Comparative financial statement analysis of councils in the northern Sydney area

C.2.1 Operating revenue and expenditure

Chart C.3 below show the operating revenues for each of the Councils between 2009/10 to 2012/13. Over the period each Council has experienced an increase in revenue, between 4% and 5.2% per cent on a compound average annual growth basis. The increases in operating revenue have been driven by increases in revenue from Council rates and annual charges.

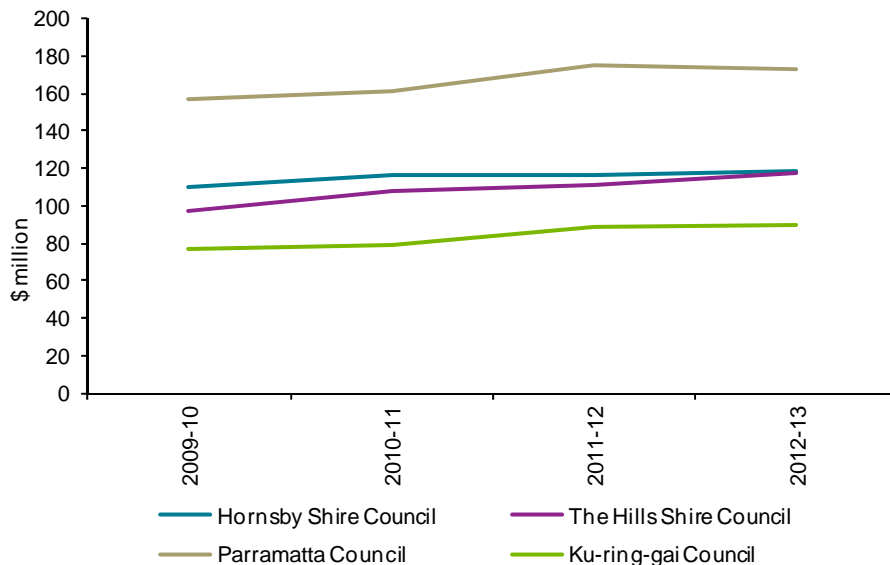
Chart C.3: Operating revenue, 2009-10 to 2012-13 ('000)



Source: Publicly available financial statements and long term financial projections (various councils).

On the expenditure side the Chart C.4 below show the operating expenditures for each of the Councils between 2009-10 and 2012-13. Over the period each Council has experienced an increase in expenditures, Hornsby by seven per cent, Hills by 20 per cent, Parramatta by 10 per cent and Ku-ring-gai by 17 per cent.

Chart C.4 Operating expenditure, 2009-10 to 2012-13



Source: Publicly available financial statements and long term financial projections (various councils).

C.2.2 Financial sustainability ratios

The Division of Local Government commissioned TCorp to develop a number of financial benchmark indicators (i.e. the FSRs) to assess the financial sustainability of NSW councils. Financial statements for Hornsby Shire Council, The Hills Shire Council, Parramatta Council, and Ku-ring-gai Council were used to calculate a number of FSRs, namely:

- operating performance ratio;
- unrestricted current ratio;
- debt service cover ratio;
- cash expense service ratio; and
- own source operating ratio.

Data limitations meant that some FSRs, in particular those requiring estimates of the value of infrastructure renewals, were not able to be calculated.

The FSRs for each council are presented and discussed below. The TCorp ratios were calculated on based on the publically available council financial statements.³⁶ Where available, the analysis also considered the change in the FSRs implied by long term financial projections for respective councils.

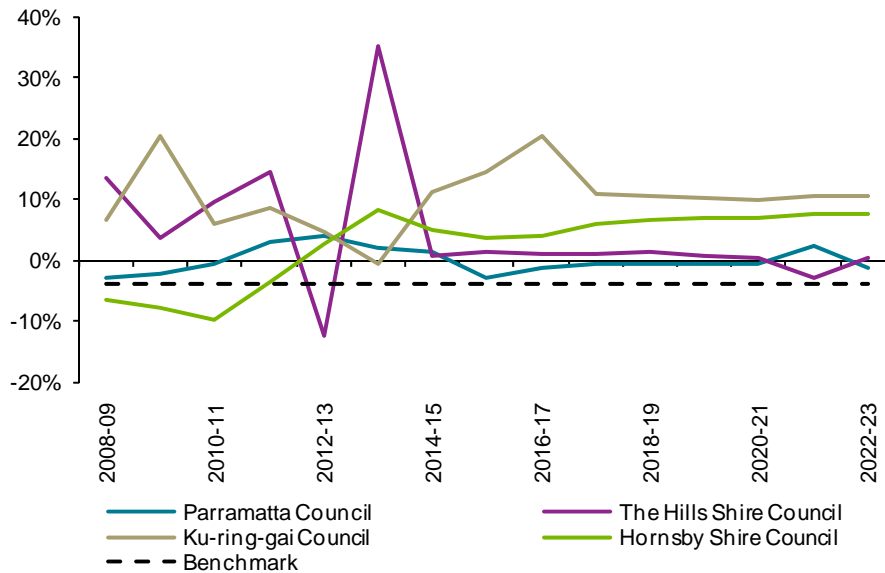
Operating performance ratio

The operating performance ratio is a measure of a council's ability of containing operating expenditure within operating revenue. An important consideration is that the ratio is assessing a council's operating performance, therefore capital grants and contributions are excluded. The benchmark for the operating performance ratio is set at greater than -4 per cent (i.e. the benchmark represents an operating loss). It is noted that better practice for councils should be to set internal benchmarks greater than a 'break even' operating position (i.e. a ratio of zero per cent) in the long run to prevent deterioration of their financial positions.

Chart C.5 presents the operating performance ratio between 2009-10 and 2022-23.

³⁶ It is noted that there are discrepancies between the amounts related to interest and investment revenue in the TCorp analysis and publicly available financial statements. For the purposes of this report, relevant publicly available financial statements published by relevant councils were assumed as the definitive source.

Chart C.5: Operating performance ratio, 2009-10 to 2022-13



Source: Publicly available financial statements and long term financial projections (various councils).

The chart shows that Ku-ring-gai and Hornsby Shire Council are expected to show the strongest performance relative to the benchmark over the period to 2022-23, given:

- the high value of the ratio for Ku-ring-gai Council relative to other councils over most of the projection horizon;
- the high value of the ratio relative to the standard benchmark (-4 per cent) and the better practice benchmark (zero per cent), unlike The Hills Shire and Parramatta Council, which are not expected to significantly exceed the better practice benchmark; and
- the magnitude of the expected improvement for Hornsby Shire Council, reflective of assumed structural adjustments that have been incorporated into its long term financial projections.

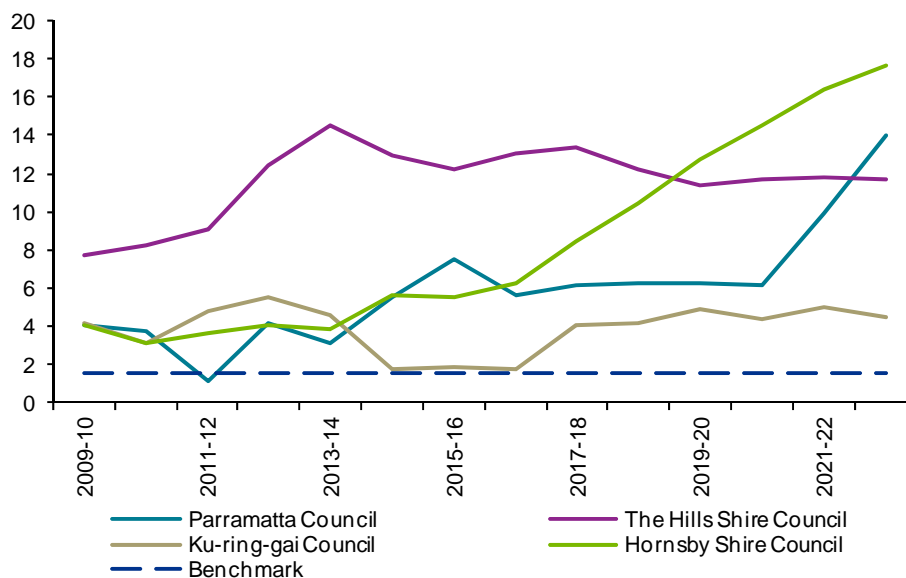
It is noted that the strong performance by The Hills Shire Council in 2013-14 is due to net gains from the disposal of an asset.

Unrestricted current ratio

The unrestricted current ratio is designed to assess a council’s ability to access cash to meet operating and borrowing costs.³⁷ Traditional current ratios tend to include restricted funding that is set aside for specific purposes (e.g. funds held for water and sewage works) and cannot be accessed to meet the operating and borrowing costs of the council. Excluding restricted funding sources means that the ratio can better represent the true ability to meet short term financial payments when they are due. The performance benchmark for this ratio set by TCorp is that the ratio should be greater than 1.5.

Chart C.6 shows the unrestricted current ratios for Hornsby Shire Council, Parramatta Council, The Hills Shire, and Ku-ring-gai Council from 2009-10 to 2022-23.

Chart C.6: Unrestricted current ratio, 2009-10 to 2022-23



Source: Publicly available financial statements and long term financial projections (various councils).

Historically, The Hills Shire Council has shown the strongest liquidity, ranging from about 6.6 in 2009-10 to 9.1 in 2012-13. The performance of The Hills Council is attributable to low levels of borrowing costs, as outlined in its historical financial statements.

Over the same period, Hornsby Shire Council and Ku-ring-gai Council have consistently achieved results above the benchmark, although substantially lower than The Hills Shire Council. This indicates that they can comfortably meet short term payments when due.

Hornsby Shire Council’s long term financial projections indicate that borrowing costs are expected to decline, explaining the strength in the unrestricted ratio, particularly from 2016-17.

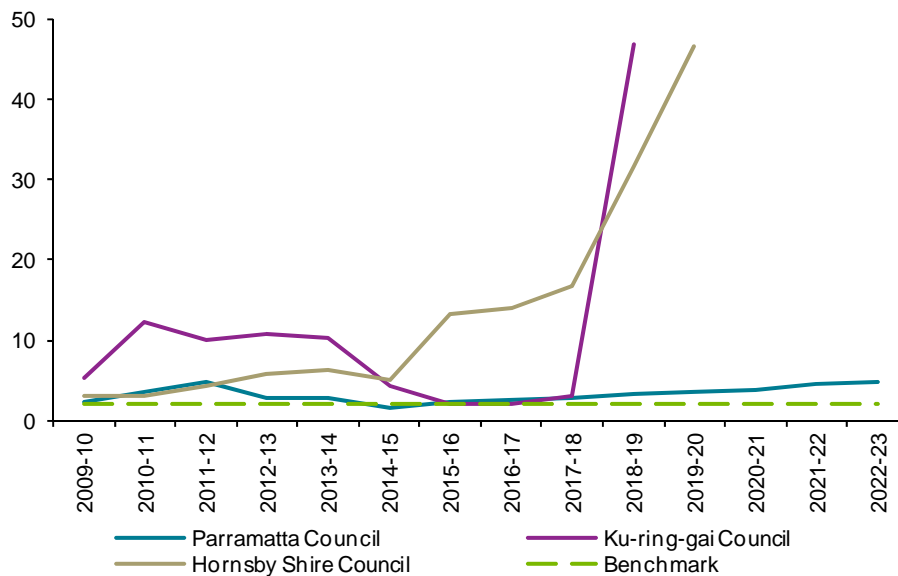
³⁷ These ratios are based on the data available in the publically financial statements.

Debt service cover ratio

The debt service ratio is a measure of each Council’s ability to use its operating cash to cover any interest, principal, and lease payments. The benchmark established by TCorp is for the ratio to be greater than two.

Chart C.7 shows the debt service cover ratio for Hornsby Shire Council, Parramatta Council, and Ku-ring-gai Council from 2009-10. The chart shows that councils have maintained, and are largely expected to maintain, above-benchmark ratios over time.

Chart C.7: Debt service cover ratio, 2009-10 to 2016-17



Note: The debt service cover ratios for Hornsby Shire Council and Ku-ring-gai Council are not included for the whole period to 2022-23 given that low expected levels of debt mean that the ratios increase significantly (i.e. there is a lower base) and therefore become meaningless.

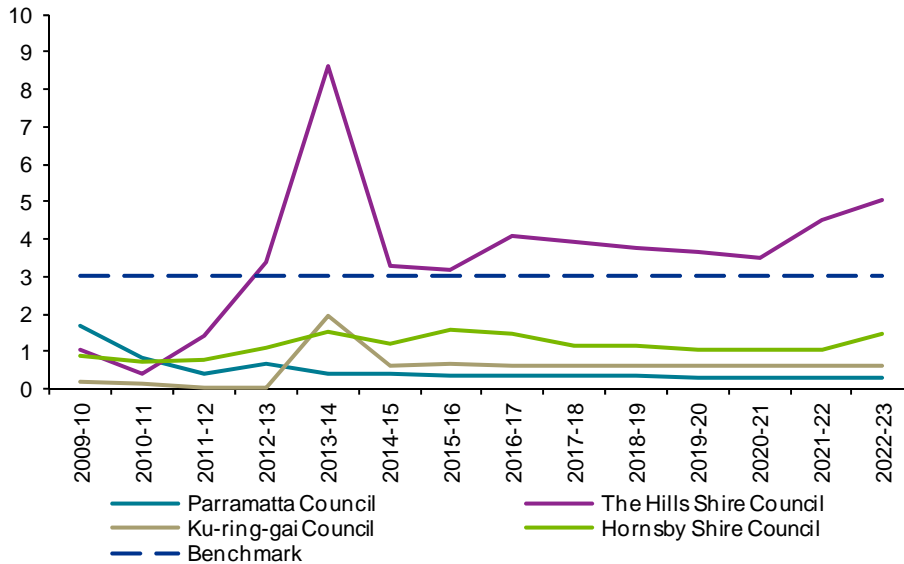
Source: Publicly available financial statements and long term financial projections (various councils).

Cash expense cover ratio

The cash expense cover ratio is also known as the liquidity ratio and indicates the number of months that a council can continue paying immediate expenses without the need for additional cash. The benchmark for the ratio is set at greater than three months.

Chart C.8 shows the cash expense ratio for each of the councils from 2009-10 to 2022-23.

Chart C.8: Cash expense cover ratio, 2009-10 to 2022-23



Source: Publicly available financial statements and long term financial projections (various councils).

The results suggest that, apart from The Hills Shire Council, councils are expected to have insufficient cash to meet immediate expenses for three months. Conversely, The Hills Shire Council is expected to exceed the benchmark over the long term financial projection horizon.³⁸

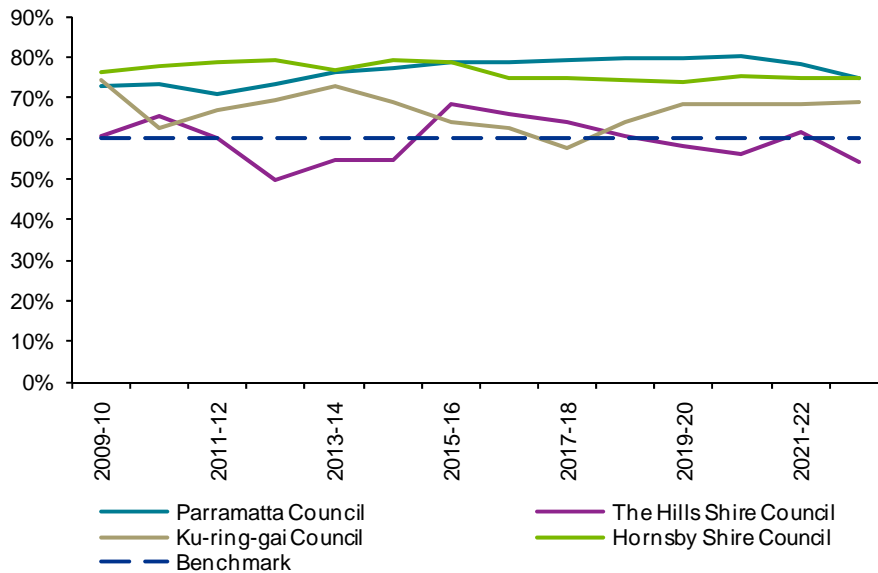
Ku-ring-gai Council holds the majority of its funds in current investments, which potentially explains its low cash expense cover ratio. Hornsby Shire Council also invests in long term deposits, and these are excluded from the ratio. Should these councils be able to liquidate these investments in the short term, the ratio may underestimate the capacity to cover short term expenses.

Own source operating revenue ratio

The own source operating revenue ratio is a measure of a council’s fiscal flexibility, and it highlights the extent to which councils are reliant on external funding sources (e.g. operating grants and contributions). The benchmark for the own source operating revenue ratio is set at greater than 60 per cent.

³⁸ Note that cash and cash equivalents are taken from the balance sheet from actual and future financial statements available publically.

Chart C.10: Own source operating revenue ratio, 2009-10 to 2022-23



Source: Publicly available financial statements and long term financial projections (various councils).

The chart shows that Hornsby Shire Council and Parramatta Council have historically had, and are expected to continue having, relatively stable own source operating ratios well above the established benchmark. The expected stability of the ratio for these councils suggests a greater level of certainty over future revenue sources, thereby underpinning greater flexibility. Over the period, The Hills Shire Council’s own source operating revenue ratio is expected to vary substantially and be below the benchmark in most years.

C.3 Limitations of the financial statement analysis

The purpose of the financial statement analysis is to provide a high level comparative financial analysis of Hornsby Shire Council, The Hills Shire Council, Parramatta Council, and Ku-ring-gai Council. It should be noted that the purpose of the financial analysis is not to provide a direct or definitive indication of the each council’s financial sustainability, rather, is intended to provide context to underpin the development of local government reform options.

It is noted that there have been some concerns about the use of the FSRs in the literature. In particular, these relate to the exclusion of ratios including budget overrun, per capita long term debt, variations in the market value of property, and community satisfaction data.

With respect to the benchmarks, it is noted that these were calculated based on previous financial statements from Queensland. In some cases (e.g. the operating performance ratio), the established benchmarks may not be representative of better practice, therefore, councils should undertake their own internal decision making with respect to targets that reflect:

- better practice, for example resetting the benchmark for the operating performance ratio to zero per cent or greater, implying at least a ‘break even’ position; and
- strategic and operational priorities and changes within councils.



It is also noted that there are some strong correlations between some FSRs given their similarity, and this can limit insights. For example, the interest and debt service ratios both measure a council's ability to meet borrowing costs, therefore can be highly correlated.

D Consultations with Hornsby Shire Council

A number of consultations were undertaken with divisional managers at Hornsby Shire Council to better understand the organisational structure and functions within each division, namely:

- Corporate Support;
- Environment and Human Services;
- Infrastructure and Recreation; and
- Planning.

The purpose of the consultations was to inform the development of assumptions to underpin the financial and strategic analysis, in particular through:

- testing insights from the comparative study of domestic and international experience at a high level against the experience of divisional managers; and
- expressing assumptions in the context of Hornsby Shire Council’s organisational structure and functions.

Table D.1 below outlines the key insights from each consultation.

Table D.1: Consultations with Hornsby Shire Council

Division	Key items
Corporate Support	<ul style="list-style-type: none"> • Hornsby undertook a formal process to review operation efficiencies in 2011-12, which resulted in \$1.4 million in savings (reduction in 30 to 35 FTE) • It is believed service quality was not negatively affected • Cross subsidisation occurs among residents, with semi-rural residents being subsidised by metropolitan residents • NSROC has been good for lobbying, but there has been insignificant monetary benefits because of the relative scale of Hornsby and smaller councils.

Division	Key items
Environment and Human Services	<ul style="list-style-type: none"> • Provided a detailed description of the different services within the division • Responsible for the management of community centres • Some centres are run on a voluntary basis on behalf of the council • Thought has already gone into rationalisation of assets • Highlighted the issue of maintaining ageing stock particularly if buildings are being under utilised • A high proportion of casual staff are employed in child care centres that generate revenue for the council • In remote and rural areas where councils border there is some scope to share community centres
Infrastructure and Recreation	<ul style="list-style-type: none"> • Responsible for the project management for maintenance and building of main infrastructure and buildings for the entire council • Undertook an extensive re valuation of current stock • Highlighted that other councils have made different assumptions with regards to asset valuation • Hornsby is responsible as the funder and provider of the development of parks and recreation projects • Continue to make staffing improvements and efficiencies • Waste management is out sourced • The council has on depot for service delivery • Rationalisation of assets is already takes place

Division	Key items
Planning	<ul style="list-style-type: none">• Highlighted that the statutory responsibilities are set by the State government• There are different levels of expectations within communities with regards to boundary reform• Detailed description of the organisational structure and the divisions processes• There are strategic sub regional issues for residents such as employment and housing provision

Source: KPMG.

E Detailed literature summary and comparative study

This section provides supplementary detail to the comparative study of domestic and international local government reform experience, namely:

- literature associated with evidence of economies of scale in the provision of local government services; and
- reform experiences in selected domestic and international jurisdictions with respect to the local government reform principles.

E.1 Evidence of economies of scale

Table E.1: International literature

Author	Jurisdiction	Dependent variable	Measure of output	Economies of Scale?
Ahlbrant (1973)	Seattle, United States	Fire-fighting expenditure	Population	No evidence
Alt (1971)	United Kingdom	Education, social services, housing, police, fire-fighting expenditure	Population	No evidence in education, housing; Both in social services, police and fire-fighting;
Ashford et. al. (1976)	United Kingdom	Total expenditure	Population	Diseconomies of scale
Boaden (1971)	Britain	Social services, police, fire-fighting expenditure	Population	Both
Chicoine et. al. (1989)	Illinois	Rural road expenditure	Gravel road equivalent mileage	Both
Danzinger (1978)	United Kingdom	Social services, police, fire-fighting expenditure	Population	No evidence in social services; Diseconomies in police and fire-fighting
Davies et. al. (1971)		Total expenditure	Population	Diseconomies of scale
Davies et. al. (1972)		Total expenditure	Population	No evidence of scale

Author	Jurisdiction	Dependent variable	Measure of output	Economies of Scale?
Foster et. al. (1980)	United Kingdom	Total expenditure; education expenditure	Population; number of school children	No evidence in total expenditure; diseconomies in education
Gupta and Hutton (1968)	United Kingdom	Social services, housing, rural road expenditure	Social services expenditure; population; number of social service recipients	Both
Hirsch (1959)	Missouri	Education, police, fire- fighting, refuse collection expenditure	Number of school children, night time population	No evidence in education, police and refuse collection; both in fire- fighting
Hirsch (1965)	Missouri	Refuse collection	Number of collection trucks	No evidence
Jackman and Papadachi (1981)	United Kingdom	Education expenditure	Number of school children	No evidence
Kleinman et. al. (1990)	England	Housing expenditure	Population	No evidence
Lamont (1982)	Scotland	Housing expenditure	Population in public housing	No evidence
McDavid (2001)	Canada	Residential solid-waste collection	Household served per truck	Economies of scale
Nicholson and Topham (1975)	United Kingdom	Housing expenditure	Population	Economies of scale
Ostrom and Parks (1973)	United States	Police expenditure	Population	Diseconomies of scale
Pinch (1978)	United Kingdom	Housing expenditure	Population	Diseconomies of scale

Author	Jurisdiction	Dependent variable	Measure of output	Economies of Scale?
Schofield (1978)		Social services, police expenditure	Population	No evidence in social services; both in police expenditure
Smet and Nonneman (1998)	Belgium	Education expenditure	Number of students	Economies of scale

Source: Byrnes and Dollery (2002).

Table E.2: Domestic literature

Author	Jurisdiction	Dependent variable	Explanatory variable	Economies of scale?
Abelson (1981)	Sydney	Total expenditure per household affiliation; number of households; household density	Median household income; dependents as a proportion of LGA population	No evidence
Institute of Public Affairs (1993)	Victoria	Total expenditure	Population	Possibility of scale economies
KPMG (1998)	New South Wales	Total expenditure	Population	Potential scale economies
Local Government Commission (1986)	Victoria	Per capita administrative costs, excluding overheads	Population	Economies of scale in administrative expenditure
Musgrave et. al.	New South Wales	Total expenditure per capita, excluding new fixed capital expenditure	Population	Limited evidence of 'economies of size'
Office of Local Government (1993)	Victoria	Total expenditure per capita	Population	Economies of scale

Author	Jurisdiction	Dependent variable	Explanatory variable	Economies of scale?
SA Department of Local Government (1988)	South Australia	Total expenditure on administration; overheads; household herbage; road construction and maintenance; recreation and cultural and level of outside grants and subsidies received	Population; area and total road length	Scale economies found in administration, overhead, drainage, roads and grants, and subsidies received
Soul (2000)	New South Wales	Gross expenditure per capital and expenditure per capita on economies services	Population	Evidence of economies and diseconomies of scale
Victoria Grants Commission (1985)	Victoria	Per capita expenditure on administration, street cleaning, community and regional development, recreation and culture, debt servicing and capital equipment	Population	Economies of scale in all functions

Source: Byrnes and Dollery (2002)

E.2 Case studies of domestic and international boundary reform experience

Systems of government – including local government – vary significantly across jurisdictions. For example, China has five levels of government, federations (e.g. Australia) have three, and unitary states (e.g. New Zealand) have two.

Systems of similar levels of government can also vary substantially. In New Zealand, for example, community boards are established underneath the local authority. In Paris, local government has a hybrid structure, with each municipal *arrondissement* having an elected council and mayor. A selection of the councillors from each *arrondissement* forms the Council of Paris, which elects its own mayor.

Even in the Anglosphere, with shared political heritage and culture, there are vast differences in the role of local government. For example, within Australia and New Zealand, local government is mainly involved in mainly providing services to property, whereas in other countries such as the United Kingdom and Canada, local government has a broader remit, for example, in the provision of public housing.

Varying systems of local government mean that experience from local government reform cannot necessarily be directly translated to the Australian or NSW context. These insights are, however, critical to:

- understand the broader context to local government reform and identify learnings and limitations associated with reform experiences; and
- inform assumptions to underpin the analysis of boundary reform options with respect to both financial and non-financial impacts.

The following sections provide detailed case studies of local government reform experiences in international jurisdictions.

E.2.1 City of Toronto

Toronto is the provisional capital of Ontario, and most populous city in Canada. With around half its population of 2.6 million born overseas, Toronto is the commercial capital of Canada. It is consistently rated as one of the most liveable cities in the world.³⁹

Background

In 1998, the seven municipalities that governed Toronto were amalgamated to form the City of Toronto.⁴⁰ The amalgamation went ahead despite widespread local opposition, and was primarily driven by the Provincial Government and a desire to achieve cost efficiencies. Following amalgamation, the entity had an annual budget of nearly \$6.0 billion and around 20,000 employees. The proposed amalgamation was announced in 1996, legislated the following year and finally implemented in January 1998. In addition to the amalgamation, the province

³⁹ Toronto Star 2013, 'Toronto fourth most liveable city in the world: Economist', Toronto Star, August 28, accessed 12 December 2013,

http://www.thestar.com/news/canada/2013/08/28/toronto_fourth_most_livable_city_in_world_economist.html.

⁴⁰ City of Toronto 2001, *Building the new City of Toronto: Three year status report on amalgamation January 1998-December 2000*, Toronto, accessed 3 December 2013, <http://www.toronto.ca/pdf/amalrpt.pdf>.

legislated for the province to transfer responsibilities for some service provision to the municipality.

Financial sustainability

Prior to this amalgamation, a shared services model was operating among the municipalities. Consequently, around 27 per cent of gross expenditure was linked to amalgamating programs. The remaining 73 per cent was linked to programs that had previously been part of the shared services arrangement.

For the amalgamating programs, there was a 10 per cent savings target to be achieved. In the third year after the amalgamation, annual savings reached nine per cent, or about CAD \$136 million of annual expenditure, from an annual saving of three per cent in the first year and eight per cent in the second year.

The majority of amalgamation savings were achieved through reduction in the staffing establishment. Of a workforce of nearly 20,000 full time equivalent (FTE) staff in the amalgamating workforce, there was a reduction between 1998 and 2000 of:

- nine per cent in total positions;
- 14 per cent in administration and support positions;
- 34 per cent in management positions; and
- 60 per cent in executive management positions.

Of the nine per cent total reduction to the staffing establishment, around one-third of these occurred in management or executive management positions.

Although there were substantial benefits to the amalgamation program, there were also significant costs, including:

- upfront costs, which accounted for 4.7 per cent of annual expenditure, including for:
 - facility consolidation and modification (30 per cent);
 - consolidation of business information systems (30 per cent);
 - redundancy costs (27 per cent);
 - retraining of staff (two per cent); and
 - other costs (e.g. consulting studies and the implementation of new collective agreements) (11 per cent).
- recurrent costs, including for:
 - harmonisation of service levels between councils (0.3 per cent of annual expenditure); and
 - financing costs the upfront amalgamation costs (0.5 per cent of annual expenditure for 10 years).

Service delivery

In October 2000, three years after the amalgamation, 87 per cent of residents polled for the Toronto Star believed that the amalgamation was the right decision, and 66 per cent believed amalgamation provides better government than the previous system.⁴¹

The Council described the process as an “*urban success story*”, citing residents that reported that programs and services had not been interrupted and had been enhanced in some areas.⁴² However, it argued that a local services realignment, which saw the Province give more responsibility to the local government, and which accompanied the amalgamation, was not working. It asserted that it had led to a deterioration of the financial sustainability of Council’s operations, as the additional responsibility for service given to municipalities was not matched by increased authority to raise revenue.

Representation and governance

Prior to the amalgamation, there were 106 elected officials across the seven councils. Immediately following the amalgamation, there were 57 elected officials, which was subsequently reduced to 44, due to legislation passed by the Provincial Government. The rationale for this reduction was to increase financial efficiency. The reduction in council size necessitated the redrawing of new ward boundaries.

To complement the reduction in the number of elected representatives, the legislation that created the City of Toronto allowed for the creation of Community Councils. Six Community Councils were created to address purely local issues, such as fence by-laws and the removal of trees. Council found that very few matters before Community Councils were reviewed by the full Council.

Consequently, while the reduction in the total number of elected representatives declined, which would imply a reduction in the quality of local presentation; dedicated representatives were assigned to deal with local issues. Additionally, the larger council would have had greater power in lobbying for and coordinating with the other levels of government to advance the region’s interests.

E.2.2 Auckland Council

Auckland is the commercial capital of New Zealand, with a population of around 1.5 million people, which accounts for about one-third of the nation’s total. Auckland is situated on the coast of the Pacific Ocean and is one of the few cities in the world to have two harbours. Like Toronto, Auckland also regularly features in lists of cities ranked for their liveability.

Background

In March 2009, the Royal Commission on Auckland Governance recommended that Auckland’s eight city, regional, and district councils amalgamate into a single Auckland Council. The stated was to enable Auckland to reach its full potential as the core driver of national economic growth. The reforms were based on four principles that guided the Commission’s recommendations:

⁴¹ *Ibid.*

⁴² *Ibid.*

- **common identity and purpose** through governance arrangements should encompass the interests of the region;
- **effectiveness** of cost, service delivery, local democracy and community engagement;
- **transparency and accountability** of governance structures; and
- **responsiveness** to respect and accommodate diversity.

The reforms were implemented over an 18 month period and have impacted the national reform agenda being implemented by the New Zealand Government. The Auckland Transition Agency (ATA) was responsible for managing and overseeing the transition process of amalgamating the eight local authorities.

Financial sustainability

The primary motivation for the reforms was not financial, however, Council reported NZD \$81 million in efficiencies in the first year of the transition, or about three per cent of expenditure. It is also forecasting NZD \$1.7 billion in efficiency savings over the next 10 years.

Efficiency gains were achieved through the rationalisation of procurement processes. For example, prior to amalgamation, there were 78 park contracts maintained by the various entities. This has now been merged to 12. The Council expects that there will be additional savings from the consolidation of services and delivery channels. Enhanced business information system integration is seen as a key enabler of achieving these savings, as this can reduce the multiple licence fees that are payable when multiple entities are independently operating.

In addition to savings generated by the Council, the ATA created the organisational structure for the Council, which resulted in a 16 per cent reduction in staff and an annual salary saving of just over three per cent of expenditure.

The two streams of savings were distinct. One was derived from efficiencies gained through the rationalisation of assets, procurement processes and services. The other came from the efficiencies in labour that was made possible from the first stream of savings. The combined six per cent rate saving would equate to a reduction in rates of around 10 per cent.

A report by the Controller and Auditor General of New Zealand found that there was “*limited experience and knowledge about the likely ongoing cost of the new Council’s operations.*” Council’s 2013/14 Annual Plan observed that the cost of amalgamation was \$78 million, or around three per cent of expenditure, however, this cost was not further disaggregated into upfront and recurrent costs.

Service delivery

Auckland Council has a model whereby council-controlled organisations are responsible for the delivery of services and activities, including road maintenance, public transport, water, and waste water.

The report by the Controller and Auditor General of New Zealand two years after the transition found that in most cases, service delivery standards had been maintained or improved.

The key improvement in service delivery, according to the ATA, was a new planning system that enabled an integrated planning framework. There was also a standardisation of services and a lowering of fees and charges to the minimum rate of the previous eight entities.

Governance and representation

The local government reforms introduced a two-tier governance structure. This structure comprised:

- Auckland Council, which is responsible for the management of strategic and regional issues; and
- 21 local boards to be responsible for:
 - community engagement;
 - shaping and monitoring local services; and
 - bringing local perspectives to region-wide policies and plans.

The reforms also led to a reduction in the number of elected representatives in the region (see Table E.3). While there was a reduction in the number of elected representatives, the impact on the effectiveness of representation was balanced by the:

- formation of a more powerful regional council that could better advocate for the region’s interests; and
- retention of local boards, which gave residents access to platform to voice concern about local issues.

Table E.3: Local government governance arrangements in Auckland

Auckland Council governance	Former governance arrangements of local authorities
<ul style="list-style-type: none"> • 1 Council • 21 Local Boards 	<ul style="list-style-type: none"> • 1 Regional Council • 7 Territorial Councils • 30 community boards
<ul style="list-style-type: none"> • 1 Mayor • 20 Councillors • 149 Local Board Members 	<ul style="list-style-type: none"> • 1 Chair of the Regional Council • 7 Mayors • 13 Regional Councillors • 96 Territorial Authority Councillors • 145 Community Board Members
<ul style="list-style-type: none"> • 7 Council controlled organisations (CCOs) • 9 legacy CCOs 	<ul style="list-style-type: none"> • 41 CCOs

Source: Controller and Auditor-General (2012)

E.3 Domestic experience

Local government in Australia has been subject to various reform programs over the last several decades. In March 2013, nearly 30 reviews and reform initiatives were underway or about to commence in jurisdictions in Australia and New Zealand. The frequency of attempted reform has helped to establish a substantial literature on local government reform, although there is less information on the impacts of reform.

The focus of local government reform has often centred on the amalgamation of rural and regional councils, which tend to be the least financially sustainable. Although there has been a clear financial motivation for rural local government reform, these proposals have attracted greater opposition and scrutiny given the heightened economic and social importance of regional councils to their constituents.

Rural and regional councils tend to be geographically larger and less populated compared to Sydney councils. This may make the learnings from assessments of the impact of amalgamations on councils in rural and regional Australia less applicable in the context a metropolitan Sydney council.

E.3.1 Reform of Victorian local government (1993)

Background

In 1993, the Kennett Government commenced a program of local government reform that resulted in the number of councils in the state declining from 210 to 78, including a halving of the number of councils in the Melbourne metropolitan area. The motive for the reforms was to increase the sustainability of local government. The reforms were largely forced on councils, with the transition characterised by the sacking of 1,600 elected councillors and their replacement with appointed commissioners.

Financial sustainability

The Kennett Government's key motivation for the reforms was to increase the efficiency of local government, and this was part of a broader microeconomic reform agenda. In particular, councils were mandated to:

- implement a 20 per cent reduction in rates;
- put at least 50 per cent of council services out to tender; and
- reduce expenditure by 10 per cent between 1995 and 1997.

A Ministerial Review of the reform several years after implementation estimated that these changes helped contribute to a saving of \$323 million in 1995-96.⁴³

Service delivery

Surveys and interviews with 26 representative councils involved in the reforms found the process of amalgamation was easier to design and implement when councils were of similar

⁴³ Hallam, R. 1996, Minister's Review, *Local Government in 1995: First Fruits of Reform*, Victorian Department of Local Government, Melbourne.

geographic and population size and provided similar types of services.⁴⁴ The research also found that leadership and planning of amalgamations, along with the performance management of staff were essential in responding to these programs.

Governance and representation

The number of councils in Victoria was reduced from 210 to 78 through a reform process that was announced in 1994 and concluded with elections for new councillors in 1996. Additionally, the maximum number of elected representatives for each council was reduced from 21 to 12. Finally, all councillors were elected for common three year terms rather than annual elections for one-third of councillors, with postal voting introduced. The Ministerial Review of the reforms focused more on efficiencies achieved, rather than the impact of efficiencies on representation.

E.3.2 Boundary reforms in Queensland (2008)

Background

In 2008, reforms resulted in around three-quarters of Queensland's local government areas being amalgamated. The reforms were initiated by the Bligh Government and motivated by the poor financial sustainability of local governments. The forced amalgamations generated significant community opposition, and resulted in the number of councils in Queensland declining from 157 to 73.

Financial sustainability

A survey was conducted in 2009 of Mayors and Chief Executive Officers (CEOs) that elicited responses from 29 of the affected councils about the potential of the boundary reforms to impact the operations and financial performance of the councils.

The survey found that 27 per cent of respondents expected redundancies, once a state government moratorium ended. Of the respondents from South-East Queensland (SEQ), where population densities tend to be higher compared to the rest of the state, only 10 per cent of respondents expected redundancies. Of the 27 per cent that expected workforce redundancies, 71 per cent expected it to be a five per cent reduction.

Despite the relative lack of belief that efficiencies could be made through the consolidation of staffing, 61 per cent of respondents said efficiencies could be achieved through the rationalisation of plant fleets and depot locations. This rose to 81 per cent among respondents from SEQ councils, where plant and depot rationalisation would likely be more feasible due to the smaller geographies of affected councils.

Mayors were evenly split about whether there were net benefits associated with amalgamations, however, 32 per cent of the CEOs of councils believed there would be a net benefit. Provincial councils were most positive, while regional councils were least positive about the benefits of amalgamations.

In a free response section that assessed the greatest gains from amalgamations, 43 per cent of respondents nominated either cost efficiencies or a strengthened financial capacity. Nearly one-

⁴⁴ Martin, J. 1999, *Leadership in Local Government Reform: Strategic Direction v Administrative Compliance*, Australian Journal of Public Administration, vol. 58, iss. 2, pp. 24-37

third of respondents said the greatest benefit of amalgamation was increased cost efficiencies, while an additional 12 per cent nominated strengthened financial capacity to deliver services.

Service delivery

The survey found that a key gain from amalgamations was the improvement of planning and development, with 33 per cent of respondents nominating this as the most significant benefit. Larger councils may be better able to manage the planning requirements placed upon them by the Department of Planning, such as requirements for greenfield sites, according to consultations with Hornsby Shire Council.

The survey found that larger councils generally only attracted better quality staff when they were non-SEQ councils.

Governance and representation

The reduction in the number of councils would have reduced the number of elected representatives.

The most common difficulty with amalgamations, cited by respondents, was community expectations and identity, and organisational cultural issues, with 30 per cent citing each issue.

E.3.3 Implementation of boundary reforms in Metropolitan Perth, Western Australia (2015)

Background

In 2012, the Metropolitan Local Government Review Panel concluded a review of local government in Metropolitan Perth. Within the report, the motivation for reform is underpinned by the need to meet increased pressures in the provision of essential community services to Perth's growing population. In response to the report, the WA Government announced plans for boundary reforms in Metropolitan Perth, including a reduction in the number of local governments from 30 to 15, starting from July 2015.

The report provides a number of insights into the potential impacts associated with the reforms, however, it is important to note that it will be important to undertake post-implementation reviews to understand the extent of benefits realisation and effectiveness.

Financial sustainability

The Metropolitan Local Government Review Panel commissioned an independent analysis of the financial position of local governments. The analysis provided a five year snapshot of the sustainability of the 30 local governments in the metropolitan area. The results from the analysis suggested that around one-third of councils in the area had financial viability concerns, with:

- one of the council's performance classified as 'unsustainable'; and
- a further ten classified as having a 'declining' financial position over the five year period.

The financial analysis also indicated that:

- larger local governments tended to exhibit strong and consistent performance; and

- the most sustainable local governments tended to have stronger links to commercial and residential rateable properties.

Through the analysis, many of the smaller local governments were identified to be experiencing a declining financial position, however, this decline was the result of single events in some of these local governments, including:

- capital outlays, for example the construction of a library; and
- other expenditure, for example the destruction of council chambers and offices due to fire.

The review highlighted that the implementation of the boundary reforms had the potential to improve the financial position of local governments and suggested the potential for efficiencies from increased economies of scale as a result of the reforms.

Service delivery

With respect to service delivery, the review suggested that the reforms have the potential to:

- generate a more equitable distribution of resources and service delivery to residents;
- contribute to reduced duplication in service delivery and other costs; and
- increase the infrastructure used to deliver services.

Together, these potential benefits suggest that the reforms will help local government to deliver better, and more financially sustainable, services to residents.

In respect to implementation, the review noted that extensive planning would be required to ensure minimum disruption to front line services.

Governance and representation

The review highlighted that boundary reform would lead to a reduction in the number of local governments, and therefore may contribute to concerns within the community associated with a reduction in community engagement. Although boundary reforms will lead to a reduction in community representatives, the review suggested that community engagement could be improved, or even increased, through the reforms through the appropriate use of mechanisms such as community advisory committees. Such mechanisms may better empower local governments to:

- improve communication and engagement with local communities, and therefore improve local representation of residents; and
- enable tailored service delivery based on community needs.

The review also noted broader potential benefits associated with the greater scale of fewer local governments, for example:

- greater strategic capacity of local governments; and
- greater capacity to attract and retain high quality professional staff.