

Working Paper Series

08-2008

October 2008

Shared Service in Australian Local Government: A Proposed Taxonomy

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Abstract: Disappointment with the results of forced amalgamation programs across almost all Australian local government jurisdictions has created great interest in shared service models as an alternative method of improving the operational efficiency of local councils. While an embryonic literature on shared service provision in the Australian municipal milieu does exist, much remains to be done, including the development of a satisfactory typology for shared services applicable to real-world experience in Australian local government. This short note seeks to fill this gap in the literature by developing a typology of local government shared service provision.

Keywords: Amalgamation; local government; shared services

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Introduction

Australian local government has experienced a period of intense structural reform under the guise of forced amalgamation in all states and territories, with the sole exception of Western Australia. However, a host of recent inquiries into financial sustainability in local government has emphatically established that a large number of local councils in all local government jurisdictions continue to face daunting financial problems, centred mostly on local infrastructure depletion crisis¹. This has served to demonstrate that compulsory council merger programs have not served as a 'silver bullet' for these systemic funding problems (Dollery *et al.* 2007; Dollery *et al.* 2008a). This has led to a search for different methods of improving the operational efficiency of local councils. In the realm of structural change, interest has focused on shared service models as an alternative to forced amalgamation and this approach has been endorsed in all of the national and state inquiries.

Although much remains to be done, some scholarly effort has already been directed at the question of shared services in the Australian local government milieu. For example, Allan (2001; 2003) and Dollery *et al.* (2006a) have considered the economic and political foundations for shared services in local government service provision for groups of cooperating councils, including local autonomy, scale economies and economies of scope. Similarly, Dollery *et al.* (2008c) have studied shared services at the state level in Queensland. Dollery and Akimov (2007; 2008) have also examined Australian and international evidence on shared services. In addition, a useful literature exists

¹ At the state level, we have seen the South Australian Financial Sustainability Review Board's (FSRB) (2005) *Rising to the Challenge*, the Independent Inquiry into the Financial Sustainability of NSW Local Government's (LGI) (2006), the Queensland Local Government Association's (LGAQ) (2005; 2006) *Size, Shape and Sustainability (SSS)* project, the Western Australian Local Government Association's (WALGA) (2006; 2008) *Systemic Sustainability Study* Inquiry, as well as the Local Government Association of Tasmania's (LGAT) (2007) *A Review of the Financial Sustainability of Local Government in Tasmania*. At the national level, we have seen the Hawker Report (2003) and the PriceWaterhouseCoopers (PWC) (2006) *National Financial Sustainability Study of Local Government*.

on specific Australian ‘case studies’, which encompasses the New England Regional Alliance of Councils (Dollery *et al.* 2005), joint board models (Dollery and Johnson 2007), the Walkerville model (Dollery and Byrnes 2006), the Gilgandra model (Dollery *et al.* 2006b) and the Riverina East Regional Organization of Councils (Dollery *et al.* 2004; 2005). Finally, a parallel Australian literature deals with the use of market instruments in delivering local government services. While outsourcing, contracting out and other for-profit modes of delivery do not meet the definition of *bona fide* shared services, this literature nonetheless sheds light on many of the economic characteristics of shared service models².

However, Australian work on shared service provision in local government remains deficient in several respects. Perhaps the most serious omission resides in the lack of a conceptually sound typology of local government shared services models. This neglect has had some unfortunate consequences, not least the conflation of *bona fide* shared services with for-profit outsourcing in local government service provision in some local government policy circles, especially in Queensland (Dollery *et al.* 2008b). The present short note seeks to remedy this omission by developing a typology of shared service models suited to Australian local government circumstances.

The note has four main parts. Section 2 provides a synoptic discussion of the conceptual basis for shared service models in local government. Section 3 outlines some earlier attempts at classifying the structural features of

² Scholars have examined both the theoretical foundations of this mode of service production and delivery and empirical evidence on its results (see, for instance, Domberger and Jensen 1997), which has a significant Australian strand, including recent valuable contributions by Hodge (1996) and Johnston and Gudergan (2007). In this Australian literature, earlier optimism (see, for instance, Domberger and Hall 1996) has given way to greater pessimism (see, for example, Bisman 2008) on the outcomes of the exercise. With some notable exceptions (see, for instance, Rimmer 1993), this literature has focused on the public sector as a whole, rather than local government *per se*.

Australian local government. Section 4 proposes a new taxonomic approach to Australian local government shared service models. The note ends with some brief concluding remarks in section 5.

Conceptual Basis for Shared Services

Oakerson (1999, 7) drew a fundamental distinction between local service 'provision' and local service 'production'. The provision of local services involves determining whether to provide a particular service, the regulation of local activities, local revenue raising, the quantity and quality of local services provided, and how these services should be produced. By contrast, production involves the creation of a product or a service rather than its financial provision.

The separation of provision from production allows for choice between different modes of producing services. Oakerson (1999, 17-18) has identified seven generic possibilities for linking provision with production:

- 'In-house production' occurs where a local council arranges its own production. For example, an individual council organizes its own production units along traditional grounds;
- 'Coordinated production' takes place where councils coordinate production activities. For instance, the building inspection departments of two adjacent councils cooperate on activities affecting both jurisdictions;
- 'Joint production' where two adjoining councils organize a single production unit. For example, joint rates notices processing;
- 'Intergovernmental contracting' takes the form of one council contracting services from another council or state or federal government agency;
- 'Private contracting' where a private firm undertakes production for a council;

- ‘Franchising’ where a council gives a commercial producer the exclusive right to produce a given service from which residents can purchase the service; and
- ‘Vouchering’ where a council sets standards and the level of provision, but allows households to select their own producer using a voucher.

If we define shared services as cooperative arrangements between local councils, and state local government associations, and between local councils and other tiers of government, then following Oakerson’s (1999) typology, only ‘coordinated production’, ‘joint production’, ‘intergovernmental contracting’ constitute shared services in local government.

By contrast, ‘private contracting’, ‘franchising’ and ‘vouchering’ do not meet the definition of shared services since they involve contractual arrangements not only outside of local government, but also outside of the entire public sector. This means that they possess additional economic and political attributes derived from their for-profit nature to shared services aimed at reaping the advantages of scale and scope. For instance, unlike local councils, private contractors seek to maximise profits from contractual relationships with councils. This gives them strong incentives to reduce costs wherever possible. In practice, this can result in lower service quality, less responsiveness to the public, and fewer workers delivering a given service. Given the difficulties involved in monitoring complex local government services, this usually means contracting councils are not able to retain control over service provision. For these and other reasons, contractual arrangements with private firms they cannot be normally regarded as shared service models (Dollery *et al.* 2008b).

Alternative Shared Service Models

Two theoretical efforts aimed at classifying local government in terms of generic municipal models have been developed, which are applicable to Australian circumstances, with one of these aimed directly at shared service

models. These typologies provide a useful foundation for the taxonomy developed in this note.

Dollery and Johnson (2005)

The Dollery and Johnson (2005) typology comprises seven alternative models of local governance:

- Existing small councils possess the most operational and political autonomy as well as highest degree of decentralization and are thus located at one end of a continuum;
- The next most autonomous and decentralized model resides in voluntary arrangements between geographically adjacent councils to share resources on an *ad hoc* basis whenever and wherever the perceived need arises;
- Regional Organizations of Councils constitute a formalization of the *ad hoc* resource sharing model which provides shared services to member councils;
- Area integration models retain autonomous existing councils with their current boundaries, but create a shared administration;
- Virtual local government consists of several small adjacent 'virtual' councils with a common administrative structure or 'shared service centre' that provides the administrative capacity to implement policies decided by councils, with service delivery itself contracted out either to private companies or to the shared service centre;
- The agency model in which all service functions are run by state government agencies, with elected councils acting as advisory bodies to determine the mix of services; and
- The most extreme form of centralization occurs when several small councils are amalgamated into a single large municipality.

The Dollery and Johnson (2005) taxonomy allows us to locate shared services within its categories. Thus, under the Dollery and Johnson (2005) taxonomy, *ad hoc* resource sharing models, Regional Organisations of Council, area integration models, virtual local councils and agency models all represent

institutional vehicles for accommodating shared services to a greater or lesser degree.

Tomkinson (2007)

A more precise typology of shared service arrangements has been proposed by Tomkinson (2007) in *Shared Services in Local Government*, based on recent British experience, which contains four alternative shared service models:

- The Intra-Service Model includes limited shared services options, such as 'regional procurement models' which provide procurement and purchasing services to member councils. The Intra-Service Model most closely approximates the *ad hoc* resource sharing structure in the Dollery and Johnson (2005) typology;
- The Service Model embodies a degree of formality which enables the participating group of councils to cede control to the council which takes on the role of the 'lead council' in terms of budgetary control, service specification, statutory service responsibilities, etc. The Service Model does not fit easily into the Dollery and Johnson (2005) taxonomy. However, it seems to most closely resemble the *ad hoc* resource sharing model with a greater degree of formality;
- The Corporatist Model involves two or more councils forming a joint arrangement to deliver a specific service or services at a mutually agreed standard in which both the costs and benefits are borne by all partner councils on a negotiated basis. In general, this means the creation of a joint governing body to sit between the sharing councils and the delivery body which is wholly owned by these councils. The Corporatist Model aligns perhaps most closely with Regional Organisations of Council in the Dollery and Johnson (2005) taxonomy;
- The Supra-Corporate Model enables two or more participating councils to set up a separate Special Purpose Vehicle to deliver a specified service or services on behalf of member councils. This vehicle could take a variety of organisational forms, such as a joint venture company, a company limited by shares or by guarantee, a not-for-profit

organisation and limited liability partnerships. In the Dollery and Johnson (2005) taxonomy, both area integration models and Regional Organizations of Councils approximate the Supra-Corporate Model.

New Typology of Shared Services in Local Government

While the taxonomies contained in Dollery and Johnson (2005) and Tomkinson (2007) represent useful methods for considering shared services in Australian local government, they share the common shortcoming of inaccurately describing shared service practice in contemporary Australian local government. Accordingly, a new tripartite typology is proposed which seeks to more precisely correlate its categories real-world Australian local government experience.

Horizontal Shared Service Models

We can propose the 'horizontal shared service model' as the most common form of shared services in contemporary Australian local government. These standard shared service arrangements involve partnerships between local councils, typically geographically bordering on one another, which range from simple *ad hoc* resource sharing between two or more local councils to fully-fledged area integration models following the Dollery and Johnson (2005) typology. While these shared service arrangements take a multitude of different forms, with widely varied governance models and patterns of ownership, they have in common that the shared services, shared resources, shared equipment and shared facilities involved are fully owned by the member councils. Thus not only are the activities and procedures of the shared service entity completely controlled by its members councils, but all costs, income, profit and risk fall ultimately upon these councils. In other words, shared service arrangements falling under horizontal shared service models are wholly operated and owned by local councils.

Vertical Shared Service Models

The second most common type of shared service arrangement evident in Australian local government may be termed the ‘vertical shared service model’ since it involves cooperation between all or some local councils in a given state jurisdiction and the state local government association in that state. Vertical shared service models usually involve the state local government association offering a defined service to member councils either as a normal part of its ongoing contribution to members or on a ‘fee-for-service’ basis. We can classify these arrangements as *bona fide* shared service models since, in principle at least, a state local government association is an entity wholly owned and controlled by its state member councils. While vertical shared service models exist in all Australian state and territory local government jurisdictions, they are the most highly developed in Queensland (Dollery *et al.* 2008c).

Intergovernmental Contracting Shared Service Models

The third discrete local government shared services category we can identify is the ‘intergovernmental contracting’ – a category borrowed directly from Oakerson (1999) Under this kind of arrangement, local councils *voluntarily* carry out various functions on behalf of public agencies from state and federal government. We can differentiate between various different types of intergovernmental contracting shared service models. For instance, the most common form of this model occurs where individual councils contract on an *ad hoc* basis with state agencies to undertake specific tasks, such as highway maintenance on behalf of the Roads and Traffic Authority in New South Wales.

In recent times a second subset of the intergovernmental contracting shared service models has emerged under the auspices of Intergovernmental Agreements between state and local government in various state jurisdictions. For example, the Municipal Association of Victoria has negotiated a Victorian State-Local Government Agreement which holds that local government has

the right to decide whether or not to accept delivery of a function or service for the Victorian government and that it can negotiate on service standards, financial arrangements, implementation terms, as well as other conditions of the delivery of services.

Finally, sometimes local councils also provide certain services on behalf of Commonwealth government agencies, often in regional, rural and remote local government jurisdictions.

It is important to stress that the three sub-categories falling under the intergovernmental contracting shared service model must be divorced from those functions and services that local councils are forced to undertake at the behest of higher tiers of government, regardless of financial and other considerations. This form of shared services obviously occurs under duress and thus represents a type of cost shifting (Dollery *et al.* 2008d).

A crucial common theme running through these three models of local government shared services resides in the fact they all involve full ownership and control by local government of the resources involved, the functions and services provided and the costs and benefits contingent on the activities in question. These characteristics substantially reduce the risks associated with these shared service partnerships and maintain local council autonomy. In essence, shared service models thus rule out partnerships with for-profit private organisations since such relationships inevitably involve at least some loss of ownership and control.

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