

# Local Government Reform in New Zealand



**Joe Wallis**

(Professor of Otago University)

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## 1. Introduction

The radical changes in the structure and management of local government that were set in motion in New Zealand by the Local Government Amendment Act of 1989 cannot be understood outside the context of the comprehensive process of economic reform that was being advanced, in a selectively radical fashion, first by a centre-left Labour government over the 1984-1990 period and then by a centre-right National administration over its first term between 1990 and 1993. The coherence of this process was sustained by the strong policy leadership collectively supplied by a reformist network comprising the New Zealand Treasury, reformist factions in both major political parties and a group of "change agents" who oversaw the restructuring of public institutions (Kelsey, 1995; Easton, 1997; Wallis, 1999). These key players were bound together by a shared commitment to advance reform according to principles the Treasury derived from a policy paradigm it constructed from a number of economic theories (public choice, agency theory, the new institutional economics and "new classical macroeconomics) that tended to highlight problems of government failure. As the dominant source of policy advice to Cabinet, the Treasury could play a "gatekeeper" role, screening policy proposals according to whether or not they advanced parallel processes of liberalization, stabilization and privatization that were expected to limit the scope for government failure in the form of rent-seeking, agency capture, bureaucratic empire-building and "populist" interference in the setting of monetary and fiscal policy. Although the Treasury could, in this respect, be regarded as the domestic guardian of the "Washington consensus" so that New Zealand pursued a reform direction similar to that being prescribed for other countries by the World Bank and IMF, it also devised bold and innovative proposals of its own, particularly in the area of public sector management.

The Treasury set out the blueprint for reform in this area in its briefing papers

to the Labour government after it was re-elected in 1987. These recommended that public management reform be developed from a broad system-wide perspective derived primarily from agency theory and public choice that focused on "the lack of management incentives" that lay at root of pervasive government failure rather than on "the symptoms of dysfunctionality . . . such as financial waste, excessive rules and poor performance" (Bale and Dale, 1998). Cabinet consideration of these briefing papers gave Michael Bassett, the Minister of Local Government, the opportunity to highlight those aspects of local government structure and management that were inconsistent with the model that the Treasury was seeking to apply to core government departments. In particular, the following weaknesses were identified:

- (a) the confusion between councillors and senior management about their roles;
- (b) a built-in bias towards inefficiency resulting from the absence of contestability in the provision of council services, most of which were provided 'in-house';
- (c) confusion between the commercial and non-commercial objectives in the management of council trading activities;
- (d) the lack of appropriate incentives and accountability arrangements to enable elected representatives to hold managers accountable for resource use; and
- (e) the diseconomies of scale in resource use and recruitment of quality management of too many small authorities (McKinlay, 1994, p.6).

Accordingly, when the Cabinet responded to the share market crash by introducing an urgent economic reform package in December 1987, Bassett succeeded in having a proposal to reform local government to address these problems included in this package.

He was well prepared to take advantage of this "window of opportunity" since during the 1985-7 period, he had developed a close working relationship with Brian Elwood, the chair of the Local Government Commission (LGC). Elwood had

contacted councillors from every local authority to engage them in the process of reviewing their boundaries, functions, powers and relationships. By making clear to respondents that "no change was not going to be an acceptable response" (Bassett, 1996, p.33), Elwood was able to "flush out" those councillors whose resistance to reform could be anticipated and overcome as well as identify potential supporters who were willing to constructively contribute to proposals for change.

Realizing that "delay had defeated all previous attempts at reform" (Bassett, 1996, p.34), Bassett and Elwood adopted a number of tactics to "fast track" local government reform after 1987. Firstly, they worked to a timetable that required the changes to be in place within the Labour Government's second term since "to let the reforms spill beyond another general election in 1990 risked turning restructuring into a national election issue" (p.34). Secondly, as a result of the preparatory work done between 1985 and 1987, they now knew what they wanted to achieve and could afford to minimize the time available for further consultation. A Local Government Bill was drawn up and introduced in Parliament on 22 March 1988 which announced that new structures would be in place before local body election day on 14 October 1989 and gave the LGC sweeping powers to achieve this goal. This body could then proceed with its task of establishing new boundaries for local authorities while the officials working under Bassett could craft legislation specifying the principles under which these authorities were to be managed and made publicly accountable for their decisions. The third tactic the reformers deployed thus involved the simultaneous formulation of proposals for legislative and structural changes. Bassett was thus able to push through the Local Government Amendment Bill specifying new management and accountability mechanisms on 23 May 1989, 15 days before he received from the LGC their proposed boundary changes that were to apply from the October elections.

For Bassett, then, the reform process was like a military campaign in which speed, control of the commanding heights of the policy process and a refusal to be deflected

from the achievement of clear objectives were of the essence. Such "blitzkrieg" tactics were being deployed by his Cabinet colleagues in a number of other policy areas to drive through radical reforms and have been severely criticized for their tendency to circumvent and undermine public trust in the democratic policy process in New Zealand (Kelsey, 1995; Easton, 1997). Both Bassett and Elwood appear, however, to take the view that the ends justified the means and considered that through these tactics they were able to succeed where others failed in putting in place reforms that largely realized their overarching goal which was "to balance democratization of process and the efficient and effective use of limited resources" (Elwood, 1996, p.312).

This paper will examine the content of these reforms, consider some of their outcomes and then deploy an "advocacy coalition framework" (Sabatier, 1991) to consider the main contours of the debate about the "unfinished business" of local government reform in New Zealand in the 1990s. It will conclude by considering the relevance of this reform experience to other countries, particularly those that seek to embody "Asian values" in the practice of public administration.

## 2. The 1989 Reforms to Local Government in New Zealand

### **Amalgamation and Local Democracy**

The reduction in the number and variety of local bodies represents the most striking achievement of the reformers. From 1876 (when the two tier, central-local government structure was established in New Zealand) until 1989, local government was allowed to develop in a way that perpetuated its institutional weaknesses. The proliferation of small authorities and the ad hoc formation of special authorities meant that "the more authorities there were, the more their overlapping functional

boundaries were a recipe for weakness and the stronger central government became" (Bassett, 1996, p.30). The issue of amalgamation did, from time to time, rise to prominence on the policy agenda but supporters of the status quo were invariably able to mount sufficient resistance to block this first step to modernizing this level of government. This resistance was effective not just because it reflected the pressures of local parochialism but also because "the functions of local government were so limited relative to central government that there was little to be gained from a more rational structure" (Easton, 1997, p.187). Thus despite the emergence of reasonably broad bi-partisan support for local government amalgamation following the formation of the Local Government Commission in 1946 neither major political party was prepared to take the risk of pushing through this reform.

However, by using the tactics described earlier Bassett and Elwood succeeded where their predecessors failed in rationalizing the structure of local government so that from 1989

- the number of regional councils was reduced from twenty-two to thirteen with provision being made for the direct election of these bodies;
- the number of city and district councils (designated "territorial authorities") was reduced from 200 to seventy-four; and
- the number of ad hoc or special purpose bodies was reduced from over 400 to seven.

The structure of local government that emerged from this rationalization "should be regarded as an entity in which regional councils and territorial authorities have separate but complementary functions, rather than as two levels of sub-national government where one is subordinate to the other" (Boston, 1996, p.184).

The functions devolved to regional councils are largely regulatory in nature. Once these bodies had been established in their new form they could be vested with many of the environmental regulation functions set out in the Resource Management

Act of 1991<sup>1)</sup> as well as continuing to carry out functions set out in the Soil Conservation and Rivers Control Act of 1941. By contrast territorial authorities have a much broader mandate to contribute to the social, economic and infrastructure development of their communities. It is important to note that both types of local body are "creatures of statute" (Bush, 1992, p.104). They have never been conferred "a power of general competence" and accordingly can only exercise those powers and functions specifically provided in statute. The purposes of local government set out in the 1989 Act<sup>2)</sup> are nevertheless sufficiently broad to enable some territorial authorities to forge a more activist role their communities the last decade<sup>3)</sup>.

The architects of local reform were very conscious of the criticism that is frequently directed toward any amalgamation initiative which is that larger authorities can weaken local democracy by increasing the potential distance between

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1) Their functions have thus come to include:

- management of the effects of use of freshwater, coastal waters and land;
- biosecurity control of regional plant and animal pests;
- river management, flood control and mitigation of erosion;
- regional land transport planning and contracting of passenger services;
- harbour navigation and safety, marine pollution and oil spills; and
- regional civil defence preparedness.

2) This section states that the purposes of local government are to provide:

- (a) Recognition of the existence of different communities in New Zealand;
- (b) Recognition of the identities and values of those communities;
- (c) Definition and enforcement of appropriate rights within those communities;
- (d) Scope for communities to make choices between different kinds of local public facilities and services;
- (e) For the operation of trading undertakings on a competitively neutral basis;
- (f) For the delivery of appropriate facilities and services on behalf of central government;
- (g) Recognition of communities of interest;
- (h) For the efficient and effective exercise of the functions, duties, and powers of the components of local government;
- (i) For the effective participation of local persons in local government.

3) As Boston (1986, p.167) observes:

"Despite the lack of a power of general competence, territorial authorities have, in practice, rarely been inhibited by the doctrine of ultra vires from undertaking functions. Rather, it has been the reluctance of either ratepayers or central government to provide finance that has been the limiting factor."

citizens and their representatives on elected councils. To counter this criticism they were careful to ensure that the boundaries of the new councils encompassed identifiable "communities of interest" as well as devising various institutional mechanisms to safeguard the "localness" in local government and strengthen the democratic accountability of the new bodies. In particular:

- "community boards" (with an advisory role only) were established within larger territorial authorities to give smaller communities a 'voice' in local government;
- a system of postal voting and ward elections in areas with a population above 20000 was introduced; and
- "open government" at the local level was promoted through legislation which required that the meetings of councils and their committees be open to the public and, in what was a major innovation, stipulated that councils consult with, and respond back to, their ratepayers and electors about their annual plans and performance.

Despite the significant compliance costs these consultative and reporting requirements predictably came to impose, particularly on smaller authorities, the reformers appear to have believed that they had an intrinsic value in providing the public with a greater opportunity to participate in local decision making and in making officeholders more accountable for their performance - a principle that was carried over into the managerial and financial reforms which constituted the second major arm of the 1989 reforms. 4)

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4) It is perhaps an indication of Elwood's sensitivity to claims that the breakneck speed of the 1987-9 reform process flouted democratic ideals that he continues to insist that their outcome was to strengthen local democracy:

"Short of making decisions on the basis of binding referenda or opinion polls it is difficult to identify anywhere a regime of greater accountability resting upon a democratically elected governing body. New Zealand local government operates within an accountability regime which is a standard to which others can aspire. It works to the extent that there is a public interest in participating. What is important is not so much that thousands within each local area could participate but don't, but that the obligation upon councils



## Managerial and Financial Reform and Organizational Restructuring

According to Schick (1998), the enormous number of public management reforms implemented in New Zealand since 1988 "add up to an integrated concept of how government should work" – a concept that can be encapsulated in the phrase "Government by contract" (p.124). A wide range of contractualist instruments were introduced to establish and strengthen contract-like relationships in which bureaucrats function as agents either of elected officials, funding agencies or civil servants placed further up the hierarchy of government. Although the legal status of these contracts varies, with only some being legally binding, their general aim has been to specify as precisely as possible the resources that one side will provide and the performance the other side will produce.

It is interesting to compare the way this contractualist approach was applied at the central and local government level. At both levels senior administrators lost their permanent tenure and were appointed for fixed terms up to five years, renewable for a further three years depending on performance. Now known as "chief executives" (CEs) they negotiated performance agreements with their principals. In the case of the CE's of central government departments their principals were their portfolio Ministers and it was made clear that the latter were responsible for outcomes and could only hold CE's accountable for the delivery of clearly specified "outputs". The rationale for this distinction was that while outcomes are often not within the control of the CE they can be held accountable for outputs which can be relatively well-defined in advance.

In the case of the CE's of local authorities, the principals were the members of the elected council. These bodies constituted both the legislative and executive arms of local government effectively Parliament and Cabinet. Moreover they lacked the

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to operate in a way that provides an opportunity for participation, keeps the system functioning in an open manner and is at all times capable of being brought to account" (Elwood, 1996, p.314).

internal cohesiveness of Cabinet since their members were not bound by the conventional of collective responsibility for decision making. The 1989 reforms sought to clarify the roles of the elected council on the one hand and the appointed CE on the other by decoupling the council from the day-to day management of the authority and empowering the CE to perform a comprehensive range of implementation, advisory and management functions. While these measures encouraged a "policy-administration dichotomy", they could not establish the same distinction between "outcomes" and "outputs" that was effected at central government level, since local CEs were clearly responsible for a range of outcomes and outputs. They were nevertheless given the same discretion over input decisions that were accorded to the CEs of government departments.

To create the conditions under which formal contracts between principals and agents in the public sector could be most readily negotiated and enforced, a comprehensive overhaul of budgetary and accounting systems and a radical process of organizational restructuring was undertaken at both central and local government level after 1989. As far as financial management was concerned, the 1989 Act's provisions essentially followed the reforms introduced in central government by the Public Finance Act of 1989. To generate the information and incentives required to control and monitor spending by output class there has been a shift to an accrual basis for financial statements, the budget and appropriations. This represented a dramatic change from the situation that typified most local authorities before 1989 where "accounts were prepared on a cash basis for the entity as a whole, and were virtually meaningless as a source of information on its activities" (McKinlay, 1994, p.21).

The impetus for restructuring was provided by the 1989 local government reforms which required that the structure of local authorities be changed to ensure (i) the separation of regulatory functions from other functions through the structuring of committees and the allocation of management responsibilities; (ii) the

encouragement of corporatization through the transfer to "Local Authority Trading Enterprises" of "commercial" activities; and (iii) the concentration of administrative authority in the new post of chief executive. The reformers were seeking to establish a structure at both central and local government level of single objective, manageable units with a clear linear accountability. Resources could then be more closely matched with tasks.

As was the case with similar reforms being pushed through at central government level, the intent was not just to ameliorate the inherent problems associated with specifying non-market outputs but also to make it easier local authorities to fully privatize those commercial activities that had been transferred LATES and to contract out, through a tendering process, those activities which it would continue to fund but not provide "in-house". The discretion to take these privatization and contracting-out options was nevertheless left with elected councils. Many councils did however take these options in the early 1990s with the result that the Department of Internal Affairs (1994) found that from 1989 to July 1994 delivery of local government services exclusively by council departments had declined from 70 to 26 per cent with delivery by external providers rising from 22 to 48 per cent and by "business units"<sup>5)</sup> rising from 2 to 18 per cent.

As a result of the cumulative effect of the restructuring, privatization and contracting-out activities the structural form of a typical local body nowadays is fundamentally different to what it was before 1989. This is graphically illustrated in Figures 1 and 2 (in appendix). Figure 1 shows that before the reforms the organization of local authorities was characterized by vertically integrated departments with the lines of accountability between officers and the council often

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5) The Department of Internal Affairs (1994, p.vii) defines business units as "a clearly defined unit in the authority's organisation whose staff are directly employed by the authority but which operates as a self-contained business contracting to deliver services for other council departments and units. It may also be undertake work for outside organisations".

being blurred. By contrast, Figure 2 indicates that with managerial accountability being focussed on the direct contractual relationship between the council and the CE, vertical lines of accountability can be established between this officer and those functionally distinct council departments and business units placed under his management. However, as Boston (1996, p.193) points out, it is not entirely without paradox that "the movement away from service delivery by council departments to a mix of delivery methods has, as in central government, fragmented the political accountability of the council".

The territorial boundaries and management disciplines set in place by the 1989 reforms have remained largely unchanged during the 1990s. It is therefore possible to empirically assess the impact this new framework has had on quantifiable indicators of the strength of local democracy and the level and functional composition of local authority expenditure during this decade.

### **Some Outcomes of the Local Government Reforms**

For the reformers the application of the New Zealand model of contractualist governance held out the promise of enhancing operational efficiencies so that public sector expenditure and the relative size of central and local government could be reduced without at the same time reducing the quantity and quality of services delivered. At first sight Tables 1 and 2 (see appendix) might suggest that this promise has been unfulfilled. Table 1 compares the average percentage shift in the inflation-adjusted value of final expenditure by central government, local government and households over three periods: 1978-84 (the period immediately before major public sector reforms); 1985-1990 (the period during which the reforms were implemented); and 1991-7 (the period immediately after the reforms). It can be seen that while public sector reforms appear to have induced a downward (albeit modest) trend in the rate of increase of central government expenditure, the same cannot be

said of local government in respect of which spending increased by 2.7 per cent in real terms over the 1990s after falling 0.9 per cent in the period immediately preceding the reform of this sector<sup>6</sup>). Table 2 nevertheless shows that the impact of these trends on the relative size of local government has been negligible, with local government's share of GDP rising 0.4 per cent between 1978 and 1984 and remaining stable at around 2.4 per cent thereafter.

The relatively disappointing impact of the reforms on both the level of spending and relative size of the local government sector nevertheless requires explanation. One view, which will be elaborated in the next section, is that local authorities are far more prone to the varieties of government failure than central government departments. The application of reforms designed to apply contractualist solutions to problems of government failure could therefore be expected to have a more discernable impact at the central than at the local level. Another view is that as a result of the 1989 reforms, additional functions could be either devolved to or acquired by local authorities who also had to bear the costs of implementing and complying with the managerial and accountability changes imposed by these reforms. The fact that local authorities have been able to absorb these additional costs without significantly increasing their spending or the burden on ratepayers can thus be viewed as an achievement.

From this perspective the positive impact of the 1989 reforms should be evaluated more in terms of the way they enhanced the capacity of local authorities to take on more functions than in terms of any overall contraction in the size of this sector. The Resource Management Act of 1991 could thus devolve to local authorities increased statutory responsibility for environmental regulation. In addition some local authorities have been able to step into the gaps caused by the withdrawal,

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6) Inspection of the annual figures reveals an erratic pattern in local government spending since 1989. According to McDermott and Forgie (1999) "this supports the view that reform carries with it significant and unpredictable costs that take some time to work through the sector" (p.251).

during the 1990s, of the central government from the delivery of certain welfare services by assuming a broader responsibility for community development. Furthermore, there has been a growth, particularly in urban areas, in the demands on social infrastructure so that some local authorities have been able to step up their involvement in the provision, for example, of improved cultural and recreational facilities.

McDermott and Forgie (1999) have attempted to quantify these developments by examining changes in the functional composition of expenditure in fifteen councils covering both urban and rural areas in the Lower North Island over the period 1993-1997. Table 3 summarizes their findings. The sources for this table were the annual reports of the councils, which indicate the following shifts in the allocation of total spending between the four main functional categories:

- The "costs of democracy" increased slightly indicating that councils were investing more in the reporting, monitoring and consultation activities associated with shift to more "open local government".
- The greater expenditure on regulation is consistent with the growing responsibility of councils for environmental regulation.
- The significant contraction in spending on services to property (the provision of physical infrastructure, including roads, water, sewerage disposal as well as garbage collection) would be consistent with the trend to privatize some of these traditional infrastructural activities but could also reflect the efficiencies gained from the contracting out of their delivery.
- The expansion in spending on services to the community more than offset the reduction in the preceding category "confirming the proposition that any potential for contraction of local government has been offset by a realignment of functions" (McDermott and Forgie, 1999, p.254).

It could be inferred, then, that the 1989 reforms enhanced the capacity of local governments in a way that enabled them to play a more activist role in the social

and economic development of their communities. The debate that ensued in the 1990s about the desirability of this trend and the future direction for local government reform must now be examined.

### 3. The Unfinished Business of Reform: An Advocacy Coalition Framework

During the 1990s the debate about the "unfinished business" of local government reform in New Zealand appears to have taken place in a "policy subsystem" that exhibits the distinctive characteristics highlighted by the American political scientist, Paul Sabatier (1991). Sabatier views the basic unit of policy analysis as being a "policy subsystem" that brings together those members of the policymaking community who have sufficient specialized information about a particular policy area to be able to understand substantive debates, at a relatively technical level, about the relative merits and significance of the alternative policy directions being proposed in this area. He thus views policy development as being primarily shaped by a "politics of ideas" through which a stable line-up of opposing "advocacy coalitions" can emerge under the following conditions: (i) the participants in a policy subsystem come to have a hierarchy of beliefs reflected in their unwillingness to revise "policy core" as distinct from "secondary" beliefs in response to new information; (ii) advocacy coalitions come to be identifiable by the "policy core beliefs" that their members share in common; (iii) the main controversies in a policy subsystem involve disputes about the core beliefs of opposing coalitions; and (iv) these disputes should typically not be capable of uncontested resolution through scientific methods or according to the standards of independent professional forums but should tend to be perpetuated as each side buttresses its position by using substantive policy information in an advocacy fashion.

This appears to have been the case in the local government policy subsystem in New Zealand in the 1990s during which a coalition advocating minimalist local government has lined itself up against a coalition advocating a more activist role for local authorities within their communities of interest. Neither coalition advocates a return to the status quo existing before the 1989 reforms so that their main point of contention concerns the direction in which local government policy should move on the basis of changes implemented through these reforms. The differences between the core beliefs of these two advocacy coalitions and the way they shape their policy positions, as set out in Table 4, must now be examined in more detail.

### **The Minimalist Advocacy Coalition**

The Minimalist Advocacy Coalition (MAC) appears to draw together those politicians, central government "technocrats" and representatives of manufacturer and exporter interests who are concerned that the failure of some local authorities to focus on their "core activities" and significantly reduce the burden of rates is adversely affecting the international competitiveness of New Zealand producers. The leading player in this group is the "Business Roundtable" (BR), a self-selected lobby group which includes in its membership (which is by invitation only) the chief executives of some of New Zealand's largest companies. Since setting up an office in Wellington in 1986 under the direction of a former Treasury official, Roger Kerr, the BR has persistently advocated a downsizing of the role of government in the economy, issuing a stream of position papers that highlight areas, such as local government, where it considers that the logic of the reform process pursued between 1984 and 1993 has not been pushed through to "its ultimate destination". Since the BR derives its arguments from the same theories of government failure that the Treasury used to rationalize this change in policy direction, it is essentially "pushing against an open door" when it comes to bringing them to the attention of New



Zealand's policy elite.

Underlying these theories is the core belief that people can be assumed to act in ways that best advance their own interests. If the public sector is then viewed as vertical "chain of principal-agent relationships (Moe, 1984, p.765), this means that the agents in this chain will behave in a fiscally irresponsible way when weak accountability arrangements allow them scope to do so. The BR has thus sought to prod central government into an ongoing process of evaluating the institutional arrangements through which it performs and devolves its functions to ensure that they minimize the scope for agency failure and fiscal irresponsibility.

A clear hierarchy of institutional preferences is usually applied with local authorities being ranked below privately owned public companies and single-purpose government agencies respectively. Where feasible, the privatization of the commercial activities of both central and local government is invariably recommended. This recommendation is not typically based on empirical evidence. This is by no means clear-cut and certainly differs depending on the nature of the activity<sup>7)</sup>. Rather it is based on the logic of agency theory that leads to the conclusion that significant business assets are best held in public company form since individual shareholders (the principals) can sell their shares to new owners if they consider that managers (the agents) are not acting in their best interests. Where ownership remains in public hands, there is more scope for agency failure, since Ministers within central government or councillors within local government have to act as proxy for the true owners, taxpayers or ratepayers, who, in turn, have no right to exit from their investment by selling to a third party.

The New Zealand model of contractualist governance does, however, limit the scope for further agency failure in single-purpose agencies where a designated Chief

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7) As McKinlay (1999) points out "there is much less confidence that private ownership is inherently superior in natural monopoly industries such as electricity transmission or distribution than it is for activities which are more naturally contestable such as telecommunications or banking" (p.87).

Executive (CE) can be made contractually accountable for the delivery of a specific output. Unfortunately, despite every effort by the architects of the 1989 reforms to apply this model to local government, the potential for agency failure remains greatest at this level of government. The accountability of elected councillors may be weakened by the following factors:

- There is a low turnout at elections, usually no more than 50 percent, despite postal voting.
- Few voters can identify more than a handful of candidates on ballot papers.
- Often candidates do not have a party affiliation, so that voters cannot use the information that is normally provided by party platforms to make their choice.
- Mayors and chairpersons do not necessarily lead the political party or parties with a majority on a council or command the support of a majority of councillors and are therefore sometimes unable to implement the manifestos on which they were elected.

There may thus be considerable scope for elected councils to use "log-rolling" tactics to push their pet projects through committees. They can thereby enhance their re-election prospects by claiming credit for the implementation of these projects while at the same time avoiding blame for the upward drift in government spending that can occur when the other councillors also behave in a fiscally irresponsible way.

The architects of the 1989 reforms sought to ameliorate the potential fiscal irresponsibility of elected councils by concentrating administrative authority in the new post of CE. Local authorities are, however, multi-purpose organizations and their CEs cannot, like their counterparts in central government departments, be made accountable to political representatives for the delivery of contractually specified outputs. Where their accountability is weak, there is scope for CEs to engage in "empire-building" activities. Even when they are faced with a fiscally responsible

council, the information asymmetries that are inherent in their position can still give them the capacity to expand budgets. It is often unnecessary, though, for CEs to use their superior information to engage in "councillor capture" since their relationships with councils are usually not sustainable unless they are based on some minimal level of co-operation. This became evident in the first five years after the reforms during which 36 out of the 86 local authorities replaced their CE with the most frequently cited reason being "a breakdown in the relationship between the chief executive and the council" (Audit Office, 1994, p.7). The emergence of greater co-operation and reduced turnover in recent years is, however, unlikely to be viewed positively by the MAC which remains concerned by the possibility that high-spending "iron triangles" between activist councils, empire-building CEs and rent-seeking interest groups could emerge at the local level of New Zealand government.

The position this coalition takes on most issues of local government policy is shaped by the residuality principle which holds "that local government should be selected only where the benefits of such an option exceed all other institutional arrangements" (Bassett, 1987, p.63). The MAC is prepared to concede that local authorities may have a comparative institutional advantage in "administering necessary local regulations" and in funding (but not typically providing) genuinely local public goods such as library services and rubbish collection whose benefits do not extend significantly beyond a particular community. However, as the BR (1995, pp.19-20) points out: even where councils possess better information on the value that their communities place on such goods, relatively weak accountability arrangements may not give them sufficient incentive "to use that knowledge to the benefit of their communities".

Together with the other members of the MAC, the BR has repeatedly called on local authorities to focus on their "core traditional business" and expressed alarm at

the trend for some activist councils to expand into non-traditional activities such as the promotion of community and social development and the mobilization of local resistance to the drive to commercialize public health care provision. The ire of the BR has been directed, in particular, toward the Christchurch City Council which has steadfastly resisted pressure to privatize a number of its LATEs- justifying its continued ownership of these businesses on the grounds that privatization would prevent it from using future profits to reduce the overall rate burden. The growing impatience of the BRT with the intransigent activism of such councils is reflected in the hard-line nature of its most recent call for central government intervention to tightly proscribe the activities of local authorities:

"Activities such as the provision of water and roading infrastructure should be commercialised. Local authorities should be required to focus on the public good activities that are the proper business of government at the local level, and prohibited from engaging in the provision of private goods and services" (Kerr, 1999, p.5).

Such measures would involve a significant departure from the intent of the 1989 reforms which was clearly to leave such decisions in the hands of democratically elected councils.

While there is no indication that current or prospective future governments are prepared to go this far, some attempt was made to address the MAC's concerns that councils were failing to "apply sound economic principles in deciding what activities to engage in and how their spending should be funded." (ibid.) through the additional reporting requirements imposed by the Local Government Amendment Act of 1996. The Act requires local authorities to prepare two major policy documents: a long-term financial strategy and a funding policy.

Through their long-term financial strategies, councils are now required *inter alia* to specify for at least the next ten years the estimated expenses to fund the range

of activities in which they expect to be involved, the justification for undertaking them and the cash flow they expect to receive from all sources. The intent was to discipline the authorities to reflect carefully on the options for undertaking particular activities including whether they need to be involved in some of them at all. Through this discipline it was hoped that the authorities would internalize the residuality principle or could, at least, be called to account for their failure to do so during the process of submitting this document to public scrutiny.

The other major requirement of the 1996 Act that authorities prepare a funding policy document also seems to have been a response to concerns expressed by the MAC. Table 5 shows the breakdown of local authority revenue in the period just prior to the passage of this legislation.

The MAC had repeatedly expressed the view that councils were continuing to use their main source of revenue, property rates, to engage in a number of forms of cross-subsidization. In particular, they argued that the burden on residential ratepayers was being relieved by cross-subsidization from business ratepayers. Moreover, they pointed out that as councils took on new activities in response to the needs of local citizens they were, to some degree, cross-subsidizing non-ratepayers out of the rates levied on property owners. Although the Act did not proscribe cross-subsidization by subjecting funding to the benefits principle of taxation advocated by the MAC, it did require authorities to go through the discipline of reflecting on how far this principle could be applied by setting out the steps according to funding policy documents were to be prepared.

Essentially these documents require local authorities to ascertain the extent to which particular goods and services public goods, private goods or some mixture. Private goods should be paid for by end-users while the rates applied to finance public goods are to be allocated in proportion in proportion to the benefit which different groups in the community derive from the service. Once local authorities

have made their judgement, on economic principles, as to the nature and distribution of the benefits of their activities, they are required to make transparent any further adjustments with respect to matters such as fairness or equity or the policy of the local authority.

The partial and incomplete success the MAC has experienced in shaping local government policy development in the 1990s can be attributed, at least in part to the mobilization of an activist advocacy coalition (AAC) that has been able to mount an increasingly cogent and intellectually coherent challenge to the core beliefs underlying the residuality and benefits principles of devolution and funding.

### **The Activist Advocacy Coalition**

The Activist Advocacy Coalition (AAC) mainly comprises representatives of those councils that have sought to play a more activist role in local governance as well as officials within government departments like Social Welfare and Internal Affairs that have sought to "bring back balance" and counter Treasury hegemony over policy development by highlighting the role local authorities and community-based voluntary organizations can play in the preservation and development of "social capital". The main source of position documents that express this view is Local Government New Zealand. The ensuing discussion will draw on papers and monographs written by Mike Reid and Peter McKinlay which have been circulated by this association to promote its position on local government policy.

Like the MAC, the AAC seeks to build on the historic achievements of the 1989 reforms. However, unlike the MAC, the AAC does not see these reforms as facilitating a rational downsizing of local government. Rather it sees them as increasing "the capacity of local government to deal with complex issues and meet local expectations" (Reid, 1999. p. 168). The core beliefs of the AAC derive from an "autonomist" view of local government as a sphere of government in its own right

that derives its legitimacy from its effectiveness in meeting community expectations and local needs. This can be contrasted with the "functionalist" perspective the MAC derives from agency theory that regards "local government as an agency of the state drawing its authority and mandate from the centre" (ibid). Its autonomist perspective leads the AAC to endorse the activist tendency of some local councils, particularly in urban areas, to move from a traditional focus on providing infrastructure and other "core" activities towards playing "a lead role in working with their communities to define the economic and social outcomes they seek, and to develop the means for achieving them" (McKinley, 1999, p.99).

"Governance" is thus seen by the AAC as the primary role of local authorities. In an earlier article, Reid (1994, p.2) set out what he saw to be the four elements of "local governance":

- the guardianship of difference;
- the protection of future selves;
- the advancement of "positive rights"; and
- the provision of civic leadership.

This writer argues that "good local governance" will be based on the "participatory model" which recognizes that there is more than one "public" and thus seeks to take account of the diversity of interests in a geographic community (including those of citizens beyond the current generation), by bringing groups (including those under-represented by the political process) together in deliberative fora where issues and concerns are sought out and given full expression. The governance role can thus be seen as being synonymous with a catalytic, participatory style of leadership that forges a common vision for the community in a way that cannot be "contracted out, delegated to appointed boards of management or ultimately privatized" (p.5).

The AAC thus takes a positive view of local councils seeing them as having a comparative institutional advantage in the supply of local governance since they are multipurpose agencies who interact with other local agencies and groups on issues that cross sectoral boundaries and which are defined by the needs of localities or places. The public sector reforms implemented in New Zealand since the late 1980s have in their view strengthened this institutional advantage, particularly with respect to the co-ordination and advocacy roles of local government. The CEs of local authorities came to distinguished from the CEs of government departments in that they were given a holistic responsibility for the entire range of their institution's activities and could thus play an increasingly important role in co-ordinating the activities of central agencies whose narrow, contractually determined, focus could otherwise lead to fragmentation and overlap in their provision of public services to local citizens. In addition, the dismantling by the 1993 health reforms of other locally based democratic structures such as Area Health Boards has increased the importance of local government as a vehicle for articulating local concerns since it has become "the only democratically accountable body representing geographic communities" (Reid, 1999, p.168).

The autonomist view of local government appears to be based on fundamentally different assumptions about the motivation of local authority decision-makers to those derived from public choice and agency theory. Instead of presuming them to be agents who will take advantage of weaknesses in the accountability system to behave in a fiscally irresponsible way, the autonomist view sees them as trying to cope responsibly with a number of conflicting pressures, demands and expectations and focuses on factors that enhance their coping capacity. These factors are best viewed from a bottom-up perspective (Sabatier, 1986) that highlights the importance of "implementation networks" that link local, regional and national actors involved in the planning, financing and execution of the relevant government and non-



government programs. This perspective is, however, somewhat alien to the trained economists from the New Zealand Treasury who typically act as gatekeepers at the top level of the policy process. The AAC has thus shown considerable interest in recent developments in the theory of social capital since they seem to provide a conceptual framework that can be used to rationalize a bottom-up emphasis on implementation networks in terms intelligible to these gatekeepers.

Putnam (1993) defines social capital as the features of social life that enable participants to act together more effectively to pursue shared objectives. Its key components are "networks of civic engagement", "norms of generalized reciprocity" and relations of social trust. Drawing from game theory, this writer argues that through repeated interaction in networks that "are primarily 'horizontal' bringing together agents of equivalent status and power", norms are "inculcated and sustained by modeling and socialization (including civic education) and by sanctions" (Putnam, 1993, pp.171-2). The most important of these norms is generalized reciprocity which "refers to a continuing relationship of exchange that is at any time unrequited or imbalanced, but that involves mutual expectations that a benefit granted now should be repaid in the future" (p.172). The establishment of this norm will allow "dense networks of social exchange" to form in which "people can be confident that trusting will be requited, not exploited" (p.172). In his study of regional governments in Italy, Putnam attributed regional variations in public sector efficacy to the density of associational life, finding, for example, that the more likely a region's citizens are to join football clubs and choral societies, the faster the regional government is in reimbursing health care claims. This finding has attracted considerable interest in the economics profession, being cited with approval by Fukuyama (1995) and being subject to rigorous empirical analysis by Knack and Keefer (1997) who found that the determinants of the social capital variables are stronger in countries where "low social polarization, and formal institutional rules that constrain the government from

acting arbitrarily, are associated with the development of co-operative norms and trust" (p.1283).

Both Putnam (1993) and Fukuyama (1995) emphasize that social capital is a precondition for effective governance but that intervention to enhance social capital can have perverse consequences. As Fukuyama puts it, "while governments can enact policies that have the effect of depleting social capital, they have great difficulties in understanding how to build it up again" (p.11). The AAC takes a more optimistic view of the role local governments, in particular, can play in encouraging the preconditions that allow for social capital formation. Reid (1997, pp.106-7) thus acknowledges that social capital is "primarily constructed at the community level" but suggests that local governments can contribute to its formation by:

- providing opportunities for citizens and communities to influence the outcomes of local issues and decisions;
- providing facilities and types of infrastructure that allow voluntary associations to develop and flourish;
- providing assistance through grants, advice and training to people involved in developing local service delivery networks;
- undertaking monitoring, research and data collection on the strength of the local voluntary sector;
- co-ordinating the delivery of services and funding between agencies, voluntary associations and firms to ensure local needs are being addressed; and
- giving voice and legitimacy to community concerns about the level and range of local services, especially where they are provided by central government agencies.

A key dimension of this strategy is that the network relationships that local authorities seek to build with other agencies, voluntary organizations and community

groups should be in the form of horizontal partnerships rather than vertical principal-agent or patron-client relationships. However, if the partnerships local authorities forge with voluntary associations are to preserve and enhance social capital, then it is important that the local authority avoids treating them like any other service provider and recognizes the distinctiveness of the voluntary or membership nature of these organizations. Reid (1997, p.114) argues that for this to occur there are at least two factors that need to be protected:

- the freedom of these associations to determine their priorities according to the preferences of their members;
- the primary accountability they have back to their own members rather than to an external funding or sponsoring body.

The local authority should therefore see itself as funding community-driven initiatives rather than purchasing contractually specified outputs from the voluntary organizations concerned.

The AAC acknowledges that their emphasis on the role local authorities can play in community governance and social capital formation is reflected in some features of government policy in this area. Section 598 of the 1989 Act does, for example, give councils powers to promote community welfare either themselves, or by making grants to any organization or group who shares this goal within their "community of interest". In addition the central government has since 1996 sought to co-operate with local authorities in a number of community-based initiatives. Of these only the Safer Community Council (SCC) Program constitutes a genuine partnership initiative. Through this scheme local authorities can apply to the Crime Prevention Unit that operates within the Department of the Prime Minister and Cabinet for annual grants of up to \$40000 to enable them to establish SCCs that typically include within their membership a wide range of community groups and government agencies (most commonly Police, Corrections and Social Welfare) with an interest in

devising local solutions to local problems of crime prevention. Other instances where government departments have sought some involvement by local authorities in the delivery of services include a community "workfare scheme" and the "Welfare to Well-being" and "Strengthening Families" initiatives of the Department of Social Welfare (DSW). In these cases devolution is pursued through co-option rather than partnership with councils being co-opted into a local liasory role in the case of the DSW initiatives and having to make work available for those former beneficiaries who qualify for the community wage program. There are also numerous cases of unintended devolution that have arisen where councils have sought to fill gaps created by central government withdrawal from their communities. Most notably local authorities have, throughout the 1990s, become increasingly involved in health services advocacy and planning while some have even sought to keep hospitals and clinics open in the face of central decisions to close them down.

The major concern of the AAC is that this process of devolution is occurring in an ad hoc manner in the absence of any overarching policy framework to organize and structure central-local governance relations. Reid (1999) has proposed that the devolution of government functions to the local level should be governed by the subsidiarity principle. The most notable international application of this principle is by the European Union in its relations with individual nation states. In New Zealand, however, the 1988 Royal Commission on Social Policy's recommendation that "no organization should be bigger than necessary and nothing should be done by a larger and higher unit than can be done a lower and smaller unit" has had little influence on government policy. Reid argues, nevertheless, that this subsidiarity principle can be used to formulate a checklist of the key criteria for determining the location of accountability not only between different spheres of government but also between governments and communities. Specifically he contends that any checklist (such as that set out in Table 6) "needs to address the distribution of benefit; information

needs and complexity; the relative importance of local knowledge and national consistency; the degree of national significance; the importance of critical mass and value of local discretion" (1999, p.180). Thus while this principle can be contrasted with the residuality principle advocated by the MAC in that it implies a presumption for rather than against the devolution of responsibilities to local government, its application would require an empirical assessment of the capability of different levels of government to undertake particular activities. According to McKinlay (1998) some caution may need to be exercised in this regard there is a wide variance in capacity across New Zealand's territorial local authorities so that a " decision to delegate a function to local authorities generally may carry with it the risk that the performance of some will fall beneath some acceptable level" (p.14). The emphasis which the members of the AAC characteristically place on the importance of social capital is reflected in this writer's insistence that central government should pay careful attention to forming and preserving relationships of mutual trust with those local authorities to whom it chooses to devolve power:

"For government to have the freedom it may want to allocate functions in an optimal way, it is important that the parties to whom those functions may be allocated can have confidence in the basis of allocation. This means clear and shared understandings of what is being transferred and who will be expected to bear the costs. It means assuring the parties who may receive the allocation that they will not be exposed to the political risk which can arise, for example if government reduces its financial commitment once a program has become well established in new hands" (p.31).

Through its repeated calls on central government to reshape its relations with local authorities according to the principles of subsidiarity and trust, the AAC presents a fundamentally different vision of the way forward for local government policy to that espoused by the MAC. The implications of a possible stalemate

between these two advocacy coalitions and the relevance of their competing visions to other countries, particularly those, which seek to preserve "Asian values" in public administration, will be considered by way of conclusion to this paper.

#### 4. Conclusion

Something of a stalemate has emerged in local government policy in New Zealand during the 1990s, with neither the MAC nor the AAC being able to claim complete success in advancing their reform goals. The concerns of the MAC were only partially addressed by the 1996 Act, since while this sought to make local authorities more accountable for their funding policies and long term strategies, it still allowed them to pursue an activist course if that is what their democratically elected councils desired. However, the ad hoc nature of government devolution policy and the divergent views different government departments have on this issue, has inhibited many councils from undertaking an activist role to the degree recommended by the AAC.

Compared to the radical reforms of the late 1980s, policy changes in local government have been very incremental during the 1990s. It would seem that a fundamental re-assessment is only likely to be induced by some future crisis, although this is more likely to be precipitated by problems arising from aging infrastructure rather than the fiscal problems that drove radical reform during the 1984-1993 period.

The 1990s have, nevertheless, been a period during which international interest in the New Zealand model of contractualist governance has been high. Schick (1998, pp.123-4) observes that although the World Bank and other international organizations have showcased this model at various conferences while some of its

architects have "crisscrossed the globe" extolling its virtues and "dozens of countries" have sent delegations to Wellington to gain first-hand knowledge of how it is applied in practice "only a few developed countries (such as Iceland and Singapore) have adopted selected features of the model; others (such as Sweden and the United Kingdom) have embraced a managerial ethic without subscribing to the hard-edged contractualism that differentiates New Zealand's reforms from those tried elsewhere." He attributes this reluctance to the fact that its combination of managerial discretion and strict output accountability is singularly inappropriate in developing countries where public administration is still characterized by a high degree of informality.

The New Zealand model's emphasis on vertical lines of accountability and arms-length contractual relationships may, however, also render it inappropriate in developed Asian countries where governance relationships tend to be more horizontal, with attention being paid to norms of reciprocity that sustain relatively high levels of social trust. Despite the pressure being placed on these countries to strengthen accountability in the public and corporate sector in the aftermath of the "Asian financial crisis", it would seem that the wholesale introduction of an extreme type of contractualism could not only encounter cultural resistance but also potentially damage the social capital that has enabled them to solve problems in a comparatively co-operative manner in the past. This paper has shown that there have been clear limits to the application of this approach at the local government level, while the scope for expanding capacity at this level in the future is likely to require greater attention to the processes that encourage the formation of social capital in horizontal networks of civic engagement.

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Table 1

## Average Percentage Shifts in Final Expenditure, 1978-1997(1997 Dollars)

	1978-84	1985-90	1991-7
Central Government	3.0	1.5	-0.11
Local Government	6.1	-0.9	2.7
Households	1.9	1.9	2.4

Table 2

## Changes in Final Expenditure in Relation to Gross Domestic Product, 1978-97

	1978 %	1984 %	1990 %	1997 %
Central Government	15.5	16.4	17.2	15.0
Local Government	2.0	2.4	2.3	2.4
Household Consumption	67.0	65.9	71.1	73.6
Saving	14.2			7.5
Non-Profit Services	1.0	0.9	1.2	1.5
GDP	100.0	100.0	100.0	100.0

Table 3

## Patterns of Change in Council Functions, Lower North Island 1993/4 1997 (1997 Dollars)

Functions	1993/4 \$m (%)	1997 \$m (%)	Shifts 1993/4-7 \$m (%)
Democracy	19.0 (3.3%)	20.9 (3.6%)	1.9 (10.0%)
Regulation	49.9 (8.7%)	52.6 (9.0%)	2.7 (5.4%)
Services to Property	339.9 (59.7%)	315.5 (53.8%)	-24.4 (-6.7%)
Services to Community	161.7 (28.3%)	196.7 (33.6%)	35.0 (21.6%)
Total	572.5 (100%)	585.7 (100%)	13.2 (2.3%)

**Table 4**  
**Rival Advocacy Coalitions in the Local Government Policy Subsystem**

	<b>Minimalist Advocacy Coalition</b>	<b>Activist Advocacy Coalition</b>
<b>Key Players</b>	Business Roundtable, manufacturers, "centralist" politicians and some smaller rural councils.	Local Government Association, Department of Social Welfare, Department of Internal Affairs, voluntary organisations, large urban councils.
<b>Underlying Theories</b>	Public choice, agency theory, the "new institutional economics".	"Bottom-up" theories of governance;  Social capital theory.
<b>Assumptions About Agents</b>	Fiscally irresponsible when accountability is weak	Responsibly concerned with capacity to cope with multiple pressures
<b>Institutional Preferences</b>	<ol style="list-style-type: none"> <li>1. Public company</li> <li>2. State owned enterprise with single profit goal</li> <li>3. Central government department strictly accountable for specific output</li> <li>4. Local government</li> </ol>	Democratically elected local body in horizontal partnership with a range of government agencies and non-government organisations
<b>Proposed Directions for Local Government Policy</b>	<ol style="list-style-type: none"> <li>1. Statutory obligation to focus on "core" activities according to "residuality" principle.</li> <li>2. Funding according to "benefits" principle.</li> </ol>	<ol style="list-style-type: none"> <li>1. Devolution according to principle of "subsidiarity".</li> <li>2. Predictable funding as the basis for central-local trust.</li> </ol>

**Table 5:**  
**Main revenue sources of local authorities (1994-5)**

Source	%
Rates	57
Sales and other income	19
Grants, subsidies and levies	10
Investment income	8
Fees and fines	4
Petroleum tax	2

Source: Statistics New Zealand

**Table 6**  
**Reid's Allocation Criteria Based on Subsidiarity Principle**

Factor	Explanation
Distribution of benefit	Accountability should be devolved to the level of government coterminous with area of benefit or "community of interest" of an activity.
Information needs and complexity	Local accountability is required where service specification requires complex information that is costly to obtain nationally.
Local knowledge	Accountability should be local where service specification requires local knowledge.
National consistency	National accountability may be appropriate where the service is required to achieve nationally consistent outcomes.
Degree of national significance	Where the risks of failure have national, accountability may be best placed nationally.
Critical mass	Achieving economies of scale might recommend national or regional accountability.
Local discretion	Where local discretion is important because it deals with the determination and resolution of local values, accountability should lie with local government