MorrisonLow

Holroyd City Council

Merger v Stand Alone Business Case

Addendum – Scenarios Modelling

June 2015

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1. INTRODUCTION

This addendum provides scenario modelling to complement the previous Merger v Stand Alone Business Case report provided to Holroyd City Council.

The scenarios recognise that a range of potential outcomes are possible from the proposed merger of Holroyd, Parramatta, Auburn, part Ryde and part The Hills Shire.

This report concentrates on the financial impacts of the different scenarios and how these affect the performance of the merged council when measured against the Fit for the Future benchmarks.

2. DESCRIPTION OF SCENARIOS AND ASSUMPTIONS

All scenarios model the merger between Holroyd, Parramatta, Auburn, part Ryde and part The Hills Shire as proposed by the Independent Review Panel.

2.1 Scenario 1 – Base Case "Efficiencies Realised"

This scenario applies a range of financial costs and savings based on research on recent, relevant mergers of councils. Transition costs are, in the context of the five councils, a significant cost in the early and mid-periods of the newly merged council and arise from costs associated with creating the single entity (structure, process, policies, systems and branding), harmonisation of wages, redundancy costs and the implementation of a single IT system. Longer term costs also arise as staff numbers increase, which has been shown to be typical of merged councils and considered to arise as a result of increased services and service levels.

Savings initially arise in the short term through the reduction in the number of senior staff and Councillors. Natural attrition is used to reduce staff numbers in the short term with a focus on removing the duplication of roles across the five councils and creating greater efficiency in operation with reductions modelled in Tier 2 and 3 of the structure, the works units and back of office.

Savings are also projected to arise in relation to procurement and operational expenditure due to the size and increased capacity of the larger council. In the medium and longer term benefits arise through reducing staff numbers by removing the duplication of roles in areas such as finance, HR, IT and management. Savings also arise in creating greater efficiency in operations and some rationalisation of plant, fleet and buildings (one off).

A detailed description of the assumptions is set out in Appendix A.

2.2 Scenario 2 – "Efficiencies not Realised"

Scenario 2 uses the assumptions from the base case but modifies these to assume a scenario where some of the identified savings are not realised. The scenario achieves this by making the following key changes to the base case assumptions;

- No reduction in staff in management layers, the works units and back of office; and
- Not rationalising plant, fleet and buildings

The specific differences between scenarios 1 and 2 are set out in Appendix B.

2.3 Scenario 3 – Limited Savings, Holroyd Assumptions

Scenario 3 has been modelled on assumptions provided to Morrison Low by Holroyd City Council.

Morrison Low has not verified the assumptions provided by Holroyd City Council and nor should this addendum be considered as Morrison Low endorsing or agreeing with the assumptions. Morrison Low has modelled the scenario solely for the purposes of demonstrating how these assumptions differ from the base case. The supporting research and evidence was provided by Professor Brian Dollery. This research and the rationale for the assumptions are set out in Appendix C.

The key changes in the assumptions from the base case scenario are:

Governance Assumptions

- Governance - the Mayor and 14 Councillors are full-time roles and paid as such (using Queensland Local Government Remuneration Tribunal rates)
- Governance - 7 Community Boards have been allowed for at a total cost of $2,541,000 pa.
- Executive Management - GM and four Directors salaries as being 10% higher than the highest salary of any of the individual Council entities. Also, an increase for new support staff equivalent to one staff member per Executive member at a total cost of $455k pa.

Corporate Services Assumptions

- Rationalisation of duplicate services - 5% efficiency gain in year 4

Areas for Further Efficiency Assumptions

- Management – No reduction in costs
- Staff Turnover - .5% natural attrition
- ICT Costs - $120M over the transitional period (increase of 50%)
- Materials and Contracts - Increase of 9% over the base costs from year 5 to reflect an increase in services and service levels
- Works Units (staff) - 6% efficiency gain in year 4
- Works Units (plant and fleet) - 6% reduction in year 4

3. PERFORMANCE AGAINST THE BENCHMARKS

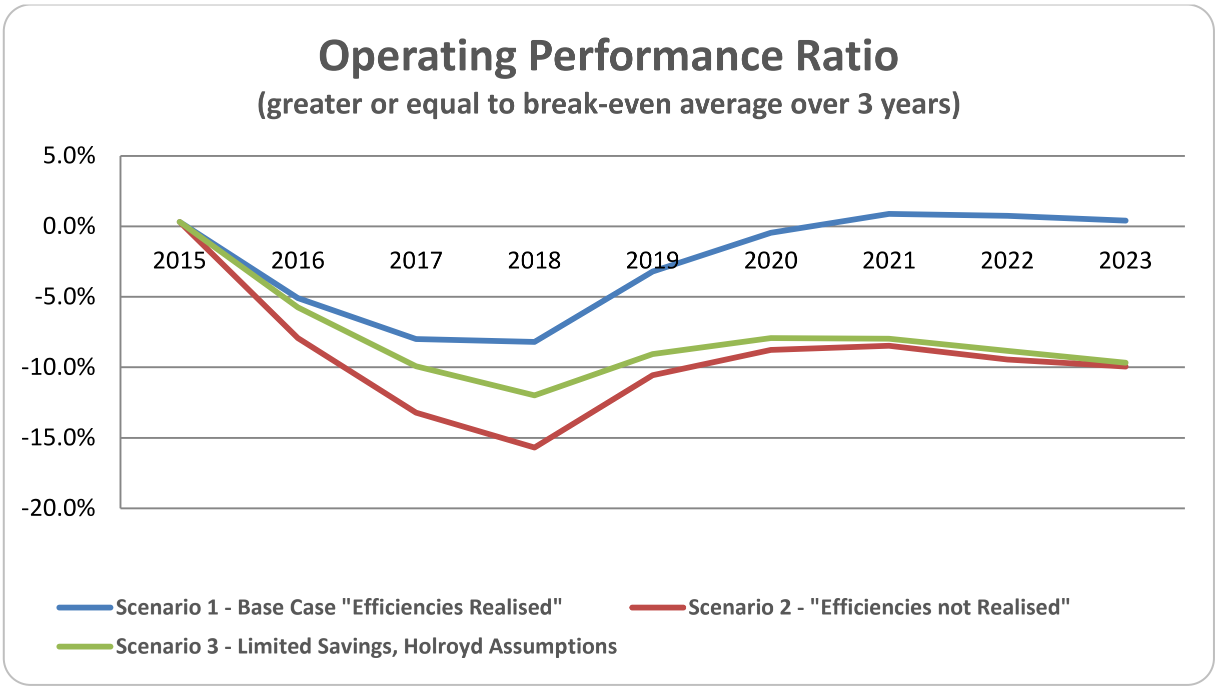
The following section provides a comparison of the performance against the Fit for the Future benchmarks the different scenarios.

Five of the seven benchmarks do not change under the different scenarios. The merged council is the sum of its parts and the combined projections on income, asset expenditure and debt are unchanged by the different scenarios meaning the result stays the same which is as shown in the table below.

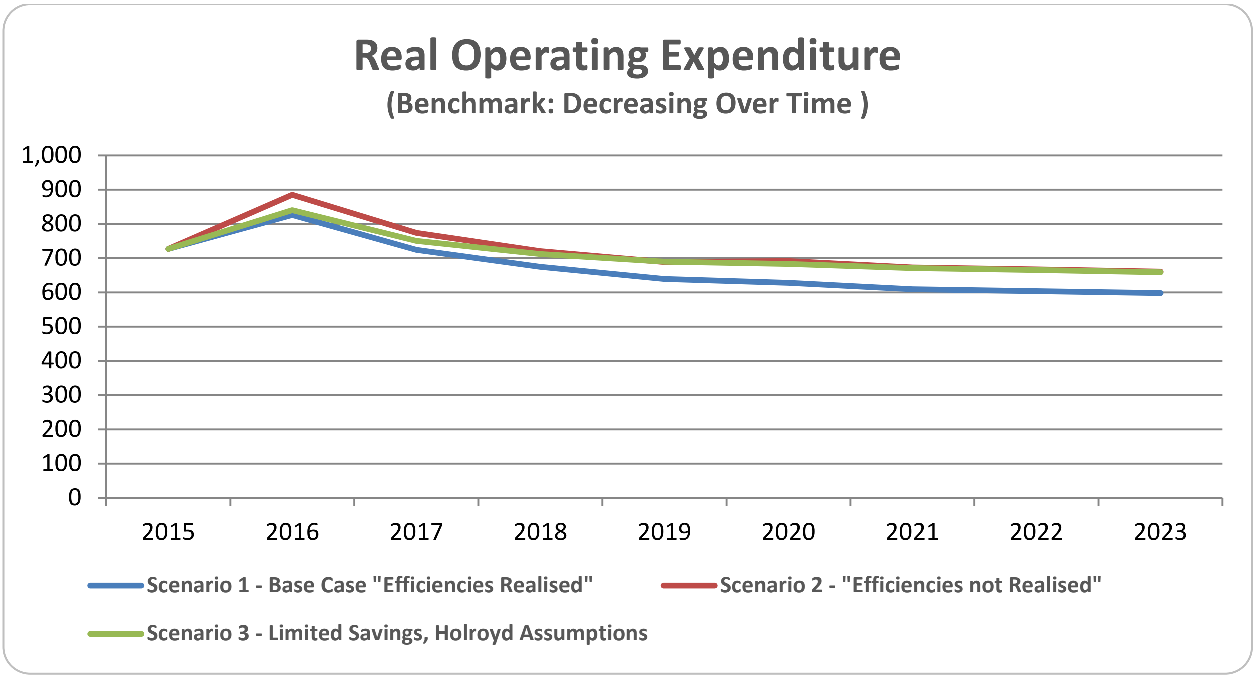
Indicator	At Day One	Merged Council (2020)
Operating Performance	*Does not meet the benchmark*	*Does not meet the benchmark*
Own Source Revenue	*Meets the benchmark*	*Meets the benchmark*
Debt Service Cover	*Meets the benchmark*	*Meets the benchmark*
Asset Maintenance	*Does not meet the benchmark*	*Does not meet the benchmark*
Asset Renewal	*Meets the benchmark*	*Does not meet the benchmark*
Infrastructure Backlog	*Does not meet the benchmark*	*Does not meet the benchmark*
Real Operating Expenditure	*Meets the benchmark*	*Meets the benchmark*

The two benchmarks which are impacted are the Operating Performance Ratio and Real Operating Expenditure Over Time. The Operating Performance Ratio is one of the ratio's which IPART has dictated must be met by 2019/20.

3.1 Operating Performance Ratio



3.2 Real Operating Expenditure Over Time



4. FINANCIAL COSTS AND SAVINGS OF THE MERGER

As per the NSW Treasury Guidelines for business cases, the value of costs and benefits are expressed as net present value under three discount rates, being 4%, 7% and 10%.

The net present value of the financial costs and savings from the potential merger are as follows:

	NPV at 4%	NPV at 7%	NPV at 10%
Scenario 1	$57.5M	$41.8M	$29.7M
Scenario 2	-$139.4M	-$122.9M	-$109.4M
Scenario 3	-$137.8M	-$125.7M	-$115.3M

The net present value of costs and benefits shows

- an overall benefit under Scenario 1 of almost $42 million over the modelling period
- an overall cost under Scenario 2 of almost $123 million over the modelling period
- an overall cost under Scenario 3 of almost $126 million over the modelling period

5. CONCLUSIONS

The comparison of the different scenarios highlights the significantly different outcomes that may be realised from the merger of Holroyd, Parramatta, Auburn, part Ryde and part The Hills Shire as proposed by the Independent Review Panel.

If the assumed efficiencies are realised then over the longer term the merged council meets the operating performance ratio, however the ratio is not meet by 2019/20 as required by IPART. Under either the “efficiencies not realised” or “Holroyd assumptions” scenarios then the operating performance ratio is never met and is well below the benchmark at between -8 and -10%

What the scenario modelling clearly shows is that, leaving aside social and community impacts, the financial viability of the merged council would depend on the organisations ability to make significant efficiency gains through either reducing expenditure or increasing revenue or a combination of both.

APPENDIX A

Base Case Assumptions

Costs and benefits arising from a merger of Holroyd, Parramatta, Auburn, Ryde (Western) and Hills (Part) Councils – detailed assumptions

Costs and benefits identified below form the basis of the modelling referred to throughout the report. Costs outlined below are one off unless stated otherwise whereas benefits continue to accrue each year unless stated otherwise.

Assumptions have been made using the best available information including analysis of various reports on and estimates of merger costs in other similar situations. This has been supplement with professional opinion of Morrison Low staff based on experience including with the Auckland Transition Authority.

Queensland Treasury Corporation August 2009 Report

In an August 2009 report[1] from the Queensland Treasury Corporation reporting on costs associated with the amalgamation of the Western Downs Regional Council, the report said:

> *A net cost outcome in the first local government term is likely as local governments will incur most of their amalgamation costs prior to, and in the two to three years subsequent to, amalgamation. These costs then taper off. However, the savings resulting from amalgamation are likely to gradually increase over time through:*
>
> - *greater efficiency (ie, a reduction in costs through improved economies of scale)*
> - *Improved decision making capability, and*
> - *Improved capacity to deliver services.*
>
> *While Western Downs only identified minor potential future benefits, it is likely that benefits will be generated from a reduction in CEO wages, natural attrition and procurement efficiencies etc, while providing existing services at current service standards. It is noted that Western Downs has been able to extend the delivery of certain services across the local government area.*

Queensland Treasury also provided comment on the reality that local government is different from businesses and that it can be difficult to measure benefits from mergers on a commercial basis:

> *Businesses generally undertake amalgamations and mergers on the basis of a number of factors such as cost savings, increased market share, improved synergies and improved decision making capability. Generally, these factors are measured in the context of reduced staff numbers, reduced operating costs, improved profitability, increased market share and higher share prices.*
>
> *With local government these benefits are more difficult to measure as local governments may utilise savings achieved from improved economies of scale to increase the range and/or to improve the quality of services offered. As a consequence, the cost savings of amalgamation of local governments do not generally show up as improved profitability (ie, operating surpluses). Similarly, improved decision making capability results in more effective decisions and better outcomes to residents but may not be reflected in a local government's bottom line. This is because local governments, unlike the private sector, are not in the business of making profits. Therefore, it is more difficult to measure the cost savings resulting from amalgamation of local governments than it is for corporations as the benefits will generally be utilised by the amalgamated local government in the provision of services.*
>
> *Alan Morton in his report titled Outcomes from Major Structural Change of Local Government, which was released in July 2007, estimated administrative cost savings from the Cairns, Ipswich and Gold Coast amalgamations of 1992/93 were between 1.1 per cent and 3.1 per cent. The report also stated that the South Australian Government estimated savings of 3.0 per cent to 5.0 per cent of expenditure resulting from amalgamation.*

[1] Queensland Treasury Corporation - Review of Amalgamation Costs Funding Submission of Western Downs Regional Council, August 2009

These estimates focused on administrative efficiency rather than the outcomes achieved through improved local government decision making capability. A potential measure of improved local government capability is ratepayer satisfaction. Alan Morton, together with the company Market Facts, undertook a survey of ratepayers of the five amalgamated local governments in 1992/93. The outcome of this survey was very positive and it indicated that over double the number of ratepayers considered the amalgamations were successful compared to those that thought the amalgamations were unsuccessful. This is considered a good outcome considering the main ratepayer concerns surrounding amalgamation are loss of jobs and loss of access to elected officials. QTC has not been asked to comment on improved capability.

The costs and benefits that Morrison Low has modelled for a possible merger of the five councils are described below:

1 Governance and executive team

The formation of a new entity is likely to result in some efficiencies resulting from a new governance model and rationalisation of the existing executive management teams. For the purposes of this review the governance category includes the costs associated with elected members, Council committees and related democratic services and processes, and the executive team.

The table below summarises the expected efficiencies together with the associated timing for governance.

	Staff	Duplicated Services	Elected Members	On Costs
Transition Period	Nil	Nil	Nil	Nil
Short Term (1 to 3 years)	Streamlined Management (General Managers and Directors) Natural attrition (voluntary)	General Managers, Directors, Mayoral/GM support Council/Committee Secretarial Support	Reduced councillors and remuneration	Staff Associated Costs e.g. HR, Accommodation, Computers, Vehicles
Medium Term (3 to 5 years)	Streamlined Management and staff Natural attrition (voluntary)			Staff Associated Costs e.g. HR, Accommodation, Computers, Vehicles
Long Term (5 years plus)				

1.1 Governance ($970K)

The formation on a new entity is expected to result in efficiencies resulting from a new governance model and a reduction in the number of existing Mayors and Councillors. However, this will depend directly on the adopted governance structure including the number of councillors. Estimated governance costs for the new entity have been based on the Mayor and Councillor fees and expenses of the Councils as reported in the Annual Reports 2014. The Independent Review Panel has envisaged a full time Mayor and there will be higher costs associated with such a role than the current Mayor and Councillors receive. It is assumed that there would be 15 Councillors and a Mayor.

1.2 Executive management ($1.5 million)

The formation of a single entity is likely to result in efficiencies due to an overall rationalisation in the total number of executive managers required at the Tier 1 (General Managers) and Tier 2 (Directors). Revised remuneration packages for the new General Manager and Directors for the new entity have been informed and assumed to be similar to that of the City of Sydney executive remuneration packages given the size and scale to that of the proposed new entity.

The General Managers total remuneration for the Councils was based on the councils' respective Annual Reports 2013/14, and the amalgamation to a single entity with a single General Manager has the potential saving of approximately $1.1 million.

In addition there would be a rationalisation of the existing director positions, based on the Annual Reports there are 13 such positions across the councils with the combined remuneration based on the Annual Reports 2013/14. Assuming that the new entity has four director positions, the estimated savings are in the order of $360K.

It is important to note that while ongoing efficiencies of $1.5 million have been identified effective from the short term, there is the one off cost of redundancies of approximately $3.4 million that in our experience is a cost incurred during the transition period. This redundancy cost is based on 38 weeks.

1.3 Rationalisation of services

Under a single entity a number of the existing governance services would be duplicated and there would be an opportunity to investigate rationalising resourcing requirements for a single entity and realise efficiencies in the medium term.

As an example the councils currently have the resources necessary to support the democratic services and processes including council and committee agendas and minutes. Under a new entity there is likely to be a duplication of democratic resources and the new entity would need to determine the number of resources required to deliver this service. The expected efficiencies relative to this area are realised in the Corporate Services Section.

Based on our previous experience one would expect resource efficiencies of between 40 and 60%. The reduction in resources is only likely to occur in the medium term due to the form of employment contracts, however having said that there is the potential not to replace positions vacated in the short term if they are considered to be duplicate positions under the new entity (natural attrition policy). The expected efficiencies relative to this area are realised in the Corporate Services Section.

2 Corporate services

In the formation of a new entity there is likely to be a reduction in staffing numbers across the corporate services in the medium term. The corporate services incorporates most of the organisational and corporate activities such as finance and accounting, human resources, communication, information technology, legal services, procurement, risk management, and records and archive management. Across the councils there is likely to be some element of duplication so there should be efficiency opportunities as it relates to administrative processes and staffing levels.

The potential opportunities for efficiency within the corporate services category are summarised in the table below along with the indicative timing of when the efficiency is likely to materialise.

	Staff	Duplicated Services	Contract/ Procurement	Information Technology	On Costs
Transition Period	Natural attrition (voluntary)	Finance ICT Communications Human Resources Records Customer Services Risk Management			
Short Term (1 to 3 years)	Natural attrition (voluntary)				Staff Associated Costs e.g. HR, Accommodation Computers, Vehicles
Medium Term (3 to 5 years)	Streamlined Management (Tier 3) Natural attrition (voluntary)				Staff Associated Costs e.g. HR, Accommodation Computers, Vehicles
Long Term (6 years plus)					

2.1 Rationalisation of duplicate services ($9.3M)

Consistent with the dis-establishment of five councils and the creation of a single entity, there are a number of back office duplicated services that would be replaced, standardised and simplified. The rationalisation and streamlining of back office services means that there would an opportunity to rationalise financial reporting, business systems, administrative processes and staff numbers. Examples for the rationalisation of corporate services include:

- Finance - A reduction in finance service costs with the rationalisation of financial reporting and financial planning with a single, rather than five Resourcing Strategies, Long Term Financial Plans, Asset Management Strategies, Workforce Management Plans , Annual Plans and Annual Reports needing to be prepared, consulted on and printed. In addition the centralisation of rates, accounts receivable, accounts payable and payroll, including finance systems will reduce resourcing requirements and costs.
- Human Resources (HR) – The size of the HR resource would be commensurate with the number of FTEs in the new entity based on industry benchmarks. The number of HR resources would be expected to reduce proportionately to the reduction in organisational staff numbers.
- Communications – The resourcing would be expected to reduce since there would be a single website and a more integrated approach to communication with less external reporting requirements.
- Customer Services – No reduction in the 'front of house' customer services has been assumed on the basis that all existing customer service centres would remain operative under a single entity and the existing levels of service would be retained. However there is potential to reduce the number of resources in the 'back office' such as the staffing of the call centre.

The potential efficiency in the corporate services category is difficult to determine largely due to the fact that ICT accounts for a large cost through the transition into the new entity both in terms of resources and actual cost. However it is expected that ICT would be implemented in the medium term and due to existing employment contracts, the corporate service efficiencies would therefore only be realised in the medium term. The assumption underpinning the efficiency for corporate services is a 35%[2] reduction in corporate support personnel that has an estimated saving of $9.3 million. On costs are considered to be included as the figure used are based on total employee costs as reported by the councils.

[2] Securing Efficiencies from the Reorganisation of Local Governance in Auckland, Taylor Duigan Barry Ltd, October 2010

There is the potential to reduce FTE numbers in the short term through not replacing positions vacated if they are considered to be duplicate positions through the transition and under the new entity (natural attrition policy). Following the end of the natural attrition period redundancies would be applied to reduce staffing levels outlined above.

In order to achieve the opportunities identified would require detailed scoping, investigation and ownership to ensure that they are implemented and realised post amalgamation. The development of a benefit realisation plan would quantify the cost of implementing any identified efficiencies and establish when such efficiencies are likely to accrue.

Redundancy costs have been modelled based on an average of 26 weeks[3]

3 Areas for further efficiency

Based on the experience from previous amalgamations in local government there are other areas where we would expect there to be opportunity to achieve efficiencies. These areas include management, staff turnover, procurement, business processes, property / accommodation, waste and works units.

	Staff	Duplicated Services	Contract/ Procurement	Information Technology	On Costs
Transition Period					
Short Term (1 to 3 years)	Staff Turnover	Property/ Accommodation, Works Units	Printing, stationary, ICT systems/ licences, legal	ICT Benefits	Staff Associated Costs e.g. HR, Accommodation, Computers, Vehicles
Medium Term (3 to 5 years)	Streamlined Management (Tier 3 & 4)	ICT Resourcing	Waste	ICT Benefits	Staff Associated Costs e.g. HR, Accommodation, Computers, Vehicles
Long Term (5 years plus)					

3.1 Management ($4.5M)

The extent of efficiencies for Tier 3 and Tier 4 is directly dependent on the organisational structure of the new entity, types of services and the manner in which these services are to be delivered in the future, i.e. delivered internally or contracted out.

The Auckland amalgamation resulted in an FTE reduction of almost 60%[2] across the total Tier 1 through to Tier 4 positions. While Section 1 addresses the Tier 1 and Tier 2 efficiencies, there is further opportunity for efficiencies in regard to the Tier 3 and Tier 4 managerial positions although these would only be realised in the medium term.

On the basis that five councils are being disestablished and a single entity created, the assumption is that there will be at least a 30% reduction across the existing Tier 3 and Tier 4 positions achieving an ongoing efficiency of $4.5 million on remuneration and on costs.

Following the end of the natural attrition period redundancies would be applied to reduce staffing levels outlined above.

[3] The Local Government (State) Award provides a sliding scale for redundancy pay-outs from 0 for less than 1 year, 19 weeks for 5 years and 34 weeks for 10years. An average of 26 weeks has therefore been used throughout.

3.2 Staff Turnover ($7.7M)

While the industry average turnover is approximately 9% and on the basis that the new entity adopts a 'natural attrition' policy not to fill positions in the short term, there is an estimated annual efficiency based on applying a modest 4.5% natural attrition.

3.3 ICT Benefits ($7M)

Without a full investigation into the current state of the five councils ICT infrastructure and systems, and without an understanding of the future state the ICT benefits cannot be quantified at this stage. However benefits would include improved customer experience, operational cost saving and reduced capital expenditure, higher quality of IT service and increased resilience of service provision. It is also necessary to model a value for the benefits to balance the costs that have been allowed for in the transition.

The operational cost savings and reduction of capital expenditure would be as a direct result of rationalising the number of IT systems, business applications, security and end user support from five councils to a single entity. The cost of IT and the number of staff resources required to support it would be expected to decrease over time. FTEs are assumed to reduce by 40%[1] over time in line with reduced IT applications and systems. Without the ICT FTE remuneration for the five councils, the 40% efficiency is unable to be determined at this time.

Through the work undertaken as part of the Wellington reorganisation, Stimpson and Co have undertaken a sensitivity analysis on the ICT costs for two options and based on an ICT cost of $90 million have estimated the Net Present Value at $200 million and payback period of 5 years. Without a detailed investigation of systems, processes and the future state of the IT system and support it is not considered possible to model the benefits as arising at a similar rate however to retain consistency with the estimated costs and the basis for them benefits have been modelled as arising over the long term and a rate of $7M per annum.

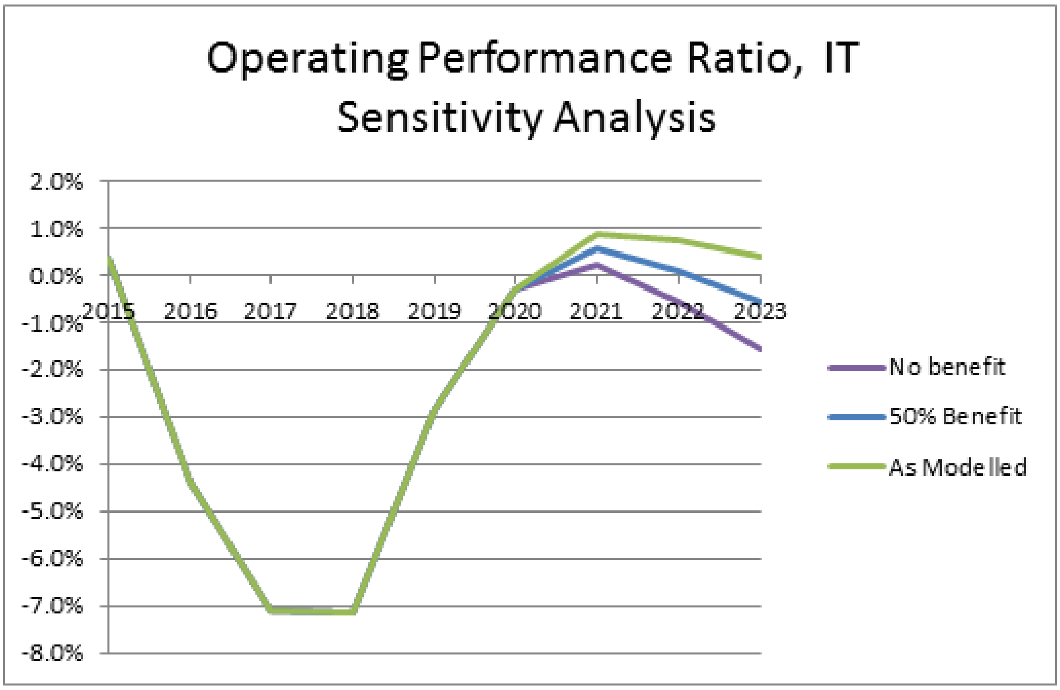
Sensitivity Analysis

Due to the high level of uncertain associated with the realisation of IT benefits one additional scenario has been modelled to demonstrate the overall impact on the financial sustainability of the IT benefits being realised.

The impact on the merged council is set out by reference to the Operating Performance Ratio.

Benefits at 50%

Realising only 50% of the IT benefits affects the merged council's operating performance by approximately $3.5 million per annum from 2021.



3.4 Materials and contracts ($790K - $2.4M)

The opportunity for efficiencies in procurement is created through the consolidation of buying power and the ability to formalise and manage supplier relationships more effectively when moving from five councils to one. An estimate needs to take into account that the councils currently engage in some collective procurement including through NSROC and SHOROC shared and panel contracts but that the process also identified a large number of services contracted out by the councils which are not aligned or co-ordinated.

The increased scale and size of the infrastructure networks managed by the merged council would in our view lead to opportunities to reduce operational expenditure through making better strategic decisions (as distinct from savings arising from procurement).

Based on the analysis during the project and our experience the combined savings have been modelled in the short term at 2% and rising to 3% and then 4% over the medium and longer term.

3.5 Properties ($6 - $8M)

There is an opportunity to rationalise and consolidate the property portfolio through assessing the property needs of the new entity and disposing of those properties no longer required for council purposes. The rationalisation of buildings in the first instance is likely to be corporate accommodation associated with the reduction in staff, other obvious areas would include the work depots (refer to Section 3.7).

The councils have a combined buildings portfolio of over $730M and for the purposes of modelling the merged council it is assumed that the council would dispose of 5% of the building assets in the medium term. In the longer term savings in properties are achievable but should be carried out in a more strategic manner across the combined entity.

3.6 Works units

Staff ($12.2M)

Based on our experience of reviewing a large number of works units across NSW we have found significant savings in all organisations that we have reviewed. As such it is reasonable to assume that a reduction in staff in the order of 20% across the works areas will be easily achieved in the medium term to reflect the duplication of services across the depots.

Redundancy costs have been modelled in for all works staff based on an average of 26 weeks.

Following the end of the natural attrition period redundancies would be applied to reduce staffing levels to those identified above.

Plant and Fleet ($2.8M – one off)

Based on our experience of reviewing a large number of works units across NSW, most councils have significantly more plant and equipment than reasonably required to undertake their day to day functions. As such, it is reasonable to assume that a reduction in plant and fleet in the order of 20% would be achievable should there be an amalgamation of councils.

4 Services and Service Levels

Typically merged councils see an increase in staff associated with rises in services and service levels. Research conducted for the Independent Review Panel noted that each of the councils involved in the 2004 NSW mergers had more staff after the merger than the combined councils together[4] and an average over the period of 2002/3 to 2010/11 of 11.7%.

An allowance has been made for a 2% increase in staff from year 4 onwards (i.e. after the period of natural attrition.

5 Transition costs

The formation of the new entity from the current state of the five councils to one will require a transition to ensure that the new entity is able to function on Day 1. This section identifies tasks to be undertaken and estimates transitional costs that are benchmarked against the Auckland Transition Agency (ATA) results and the costs as estimated by Stimpson & Co.[5] for the proposed Wellington reorganisation.

In the transition to an amalgamated entity there are a number of tasks that need to be undertaken to ensure that the new entity is able to function from Day 1 with minimal disruption to customers and staff. The types of tasks and objectives are summarised in the table below:

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4 Assessing processes and outcomes of the 2004 Local Government Boundary Changes in NSW, Jeff Tate Consulting

5 Report to Local Government Commission on Wellington Reorganisation Transition Costs, Stimpson & Co., 28 November 2014

Governance	• Developing democratic structures (council committees) • Establishing the systems and processes to service and support the democratic structure • Developing the governance procedures and corporate policy and procedures underlying elected member and staff delegations • Developing the organisational structure of the new organisation
Workforce	• Developing the workforce-related change management process including new employment contracts, location and harmonisation of wages • Establishing the Human Resource capacity for the new entity and ensuring all policies, processes and systems are in place for Day 1 • Ensuring that positions required
Finance and Treasury	• Ensuring that the new entity is able to generate the revenue it needs to operate • Ensuring that the new entity is able to satisfy any borrowing requirements • Ensuring the new entity is able to procure goods and services • Developing a methodology for interim rates billing and a strategy for rates harmonisation • Developing a plan for continued statutory and management reporting requirements • Developing a financial framework that complies with legislative requirements
Business Process	• Planning and managing the integration and harmonisation of business processes and systems for Day 1 including customer call centres, financial systems, telephony systems, office infrastructure and software, payroll, consent processing etc. • Developing an initial ICT strategy to support the Day 1 operating environment that includes the identification of those processes and systems that require change • Developing a longer term ICT strategy that provides a roadmap for the future integration and harmonisation of business processes and systems beyond Day 1
Communications	• Ensuring that appropriate communication strategies and processes are in place for the new entity • Developing a communication plan for the transition period that identifies the approach to internal and external communication to ensure that staff and customers are kept informed during the transition period
Legal	• Ensuring any legal risks are identified and managed for the new entity • Ensuring that existing assets, contracts etc. are transferred to the new entity • Ensuring all litigation, claims and liabilities relevant to the new entity are identified and managed
Property and Assets	• Ensuring that all property, assets and facilities are retained by the new entity and are appropriately managed and maintained • Ensuring the ongoing delivery of property related and asset maintenance services are not adversely impacted on by the reorganisation • Facilitating the relocation of staff accommodation requirements as required for Day 1
Planning Services	• Ensuring the new entity is able to meet its statutory planning obligations from Day 1 and beyond • Ensuring that the entity is able to operate efficiently and staff and customers understand the planning environment from Day 1 • Developing a plan to address the statutory planning requirements beyond Day 1

Regulatory Services	• Ensuring that Day 1 regulatory requirements and processes including consenting, licensing and enforcement activities under statute are in place • Ensuring that business as usual is able to continue with minimum impact to customers from Da1 and beyond
Customer Services	• Ensuring no reduction of the customer interaction element – either face to face, by phone, e-mail or in writing from Day 1 and beyond • Ensuring no customer service system failures on Day 1 and beyond • Ensuring that staff and customers are well informed for Day 1 and beyond
Community Services	• Ensuring that the new entity continues to provide community services and facilities • Ensuring that current community service grant and funding recipients have certainty of funding during the short term

Note This is not an exhaustive list but provides an indication of the type of work that needs to be undertaken during the transition period.

The transition costs are those costs incurred, during the period of transition, to enable the establishment of the new entity and to ensure that it is able to function on Day 1. The estimated transition costs for establishment of a new entity are discussed below.

5.1 Transition body ($10M)

In the case of Auckland, the ATA was established to undertake the transition from nine councils to one entity. In order to undertake the transition the ATA employed staff and contractors and it had other operational costs such as rented accommodation, ICT and communications. The cost of the ATA in 2009 was reported at $36 million and it is important to note that a substantial number of staff were seconded to the ATA from the existing councils to assist with undertaking the transition tasks. The cost of these secondments and support costs was at the cost of the existing councils and not the ATA.

The work undertaken for the reorganisation of Wellington identified the cost of the transition body as $20.6 million[4] and on the assumption of FTEs to transition body costs for Wellington, the estimated cost of the transition body for the merger is $11 million. This figure may be understated and is dependent on the governance structure adopted and other unknown factors that may influence the cost of the transition body. The cost of staff secondment and support costs from existing councils to the transition body is not included in the cost estimate.

In this case there will be additional costs associated with 'splitting' Ryde and The Hills including the staff, assets, finances (including investments, debt, liabilities). An allowance of $2M has been made for additional costs over and above the typical transitional costs expects in a merger.

5.2 ICT ($80M)

The costs associated with ICT for the new entity relate to rationalising the five existing councils ICT infrastructure, business applications, security and end user support for the single entity. The full rationalisation of IT systems based on other amalgamation experience will not occur for Day 1 of the new entity and could take anywhere between three to five years to finalise depending on the complexities of the preferred system. However there are some critical aspects for the new entity to function on Day 1 including the ability to make and receive payments, procurement and manage staff so there are ICT costs incurred during the transition.

Estimating the costs for ICT is inherently difficult due to the complexities associated with integrating systems and applications, and not knowing what the new entity may decide on as a future system. With the limited time to undertake this report the ICT costs have thus been based on the proposed Wellington reorganisation. A number of ICT scenarios were explored by Deloitte[6] for Wellington and the WNTA scenario most closely resembles the North Sydney situation has an estimated ICT cost of between $50 million and $80 million.

Given the complexity of splitting Ryde and The Hills, the IT costs have been assumed to be at the higher end of the scale and at $80 million.

5.3 Business Process (existing Council budget)

As part of ensuring the entity is functional on Day 1 is the requirement to redesign the business processes of the existing councils to one that integrates with the ICT systems. This would include the likes of consents, licensing and forms to replace that of the existing councils. In the case of Auckland these tasks were largely undertaken by staff seconded to the transition body, the cost of which was not identified as it was a cost picked up by the nine existing councils.

5.4 Branding ($6M)

The new entity will require its own branding and as part of this a new logo will need to be designed. Once agreed there will be a need to replace some existing signage of the five councils for Day 1 of the new entity on buildings, facilities and vehicles. In addition it will be necessary to replace the existing website, staff uniforms, letterheads, brochures, forms and other items. The estimated cost for branding is $6M based on other amalgamation experience.

5.5 Redundancy Costs ($3M)

This is based on a reduction in from five General Managers to one for a merged council and reduction of senior contracted Staff is based on employment contracts with a redundancy period of 38 weeks, and based on the Councils' respective Annual Reports 2013/14.

5.6 Remuneration Harmonisation ($8.1M)

The remuneration, terms and conditions for staff would need to be reviewed as part of the transition as there is currently a variation in pay rates and conditions across the five councils. In order to estimate the cost of wage parity for moving to a single entity, the average employee costs for similar councils have been compared to that of the combined councils combined as well as between the five councils.

5.7 Elections

There is a possibility of proportional savings in existing council budgets as instead of five separate elections there will be one for the new entity. However the costs of the election are likely to be higher than for future elections as there will need to be additional communication and information provided to voters to inform them of the new arrangements. The costs will also be dependent on the future governance structure, as was the case in the Auckland amalgamation the election costs were more than the budgeted amounts from the previous councils. For the purposes of the transition costs, no additional budget has been allowed for assuming there is sufficient budget in the five councils.

[6] Wellington Local Government Reorganisation Options – Transition Costs and Benefits for Technology Changes, Deloitte, September 2014

Appendix B

Variation from Base Case Assumptions

Changes to Base Case assumptions of the Costs and benefits arising from a merger of Holroyd, Parramatta, Auburn, Ryde (Western) and Hills (Part) Councils

1 Corporate services

1.1 Rationalisation of duplicate services

No reduction in staff for duplicated services meaning no change in staff levels for Finance, HR, Legal, and Communications

Redundancy costs have been modelled based on an average of 26 weeks[7]

2 Areas for further efficiency

2.1 Management

No reduction in staff in management positions e.g. Tier 3 and Tier 4

2.2 Staff Turnover

No natural attrition factored in as the model assumes no reduction in staff numbers is required. There is therefore no logic in applying natural attrition to reduce numbers and the assumption is that staff who leave will be replaced.

2.3 Properties

No rationalisation of council properties

2.4 Works units

Staff

No reduction in staff

Plant and Fleet

No reduction in plant and fleet

[7] The Local Government (State) Award provides a sliding scale for redundancy pay-outs from 0 for less than 1 year, 19 weeks for 5 years and 34 weeks for 10years. An average of 26 weeks has therefore been used throughout.

Appendix C

Research to support Holroyd Council Scenario

Section 1.1 Governance – Modelling the impact of Council Boards

The Assumption of Mayor + 15 Councillors fit with recent experience elsewhere, such as Queensland and Auckland.

However, following the mergers models adopted in Queensland (and Auckland), the Mayor and Councillors would all be fulltime and remunerated at a rate linked to Parliamentary salary scales. Moreover, a full-time Mayor and 15 councillors would also all have secretarial assistance, council' offices, and the like.

In addition, the Independent Panel recommended that very large councils – like the proposed amalgamated entity of Holroyd/ Parramatta /Auburn /Ryde /Hills – would be accompanied by the introduction of community councils/local boards based on the New Zealand model which is suggested by the ILGRP report on page 93 which states that the community board could be established in two situations of which the second listed situation relates to large metropolitan councils:

"To provide representation and some service delivery at suburb or district level within very large metropolitan councils, including following amalgamation, perhaps as a transitional measure in the latter case."

The panel goes onto say that:

" …..in the case of amalgamations the possibility of establishing Community boards should be considered in the formulation of the business case and implementation plan …."

Taking the Auckland example, in its Auckland Remuneration Decision 2013/2014, the Remuneration Board handed down the following remuneration decision for Auckland: in Howick (the highest paid Auckland local board) the local board chair will be paid $88,222 in 2013 and a board member will be paid $40,344, compared with Great Barrier (the lowest paid Auckland local board) where the local board chair will be paid $45,211 and a board member will be paid $21,713. The resultant direct annual costs for board members can be gathered from the fact that Howick has a chair and eight members and Great Barrier has a chair and four members. It is thus evident that Auckland with 21 local boards which have a total of 148 members, as well as an Auckland Council, has considerable costs associated with local boards (as its second tier of local government). In addition, in Auckland, each local board has a three/four person secretariat. Aside from member remuneration, we must also take into account of an Auckland-style secretariat of three/four persons. Given the size of the recently merged Auckland Council, where based on the smaller end of the scale (ie based on The Great Barrier example) local board areas have a population of around 60,000, at almost 450,000 residents Holroyd /Parramatta /Auburn/Ryde/Hills would require at least 7 local boards if the new entity chose to implement the model therefore it would be appropriate to add these costs of amalgamation as an assumption.

With respect to the costs associated with local boards in the recently merged Auckland Council, *Community Level Governance*[8] (2013, p.18) noted that while 'local board areas have a population on average of approximately 70,000, the staffing resource is only some three or four persons for each board to provide advice, and manage the board's administrative processes' and these persons are 'employed directly by Auckland Council and not the local board'. Based on these findings we have adopted a conservative view of 3 additional support staff will be required.

In summary, aside from member remuneration, for 1 Mayor and 15 Councillors plus 7 Local Boards comprising a Chair and 4 members each, we are also taking into account the Auckland-style secretariat of three persons. If each staff member is paid a realistic $60,000, we get remuneration costs of $180,000. If we add 30% on-costs, then this becomes $234,000. Accordingly, secretariat/support staff costs required for each local community board would be around $234,000 per board, without adding the remuneration costs of members. Furthermore, this also excludes the costs of office accommodation and running expenses.

[8] Community Level Governance – What provision should be made and/or mandated in local government legislation MDL (McKinlay Douglas Limited), July 2013

Section 1.2 Executive Management – Senior Management
Empirical literature exists that demonstrates that across the OECD remuneration always rises post-merger. For instance in her Canadian study, Reese (2004)[9] noted that remuneration levels increased in the post-merger period, resulting in a net rise in overall council expenditure so therefore Management costs in aggregate would typically rise given the harmonisation effects and support officers required in those roles.
Section 1.3 Rationalisation of Services
Much work on the impact of amalgamation has been conducted on American Local Government. Extensive summaries of this work has been provided by Leland and Thurmaier (2004;2006)[10], Faulk and Hicks (2011)[11] and Faulk and Grassmueck (2012)[12] In general it has been shown that the mergers have not met expectations in terms of efficiency gains and cost savings based on research conducted by American researchers. For example in an assessment of empirical work on whether consolidation produced greater efficiency, Feiock (2004)[13] concluded that mergers had not met their intended economic objectives, but had rather led to increased expenditures. Similarly Marin and Schiff (2011)[14] found little evidence that municipal consolidation enhanced performance through either improved service provision or reduced or reduced costs for delivering the same service. Leland and Thurmaier (2010)[15] examined 9 cases of amalgamated and comparable unmerged local authorities and concluded that efficiency gains are not a predictable consequence of amalgamation. The bulk of evidence on the outcomes of amalgamation programs in state and territory local governments derive from Australian Public inquiries into local government. Recent Australian national and state inquiries into municipal financial sustainability have established that numerous councils in all Australian local government still face financial problems despite amalgamations. In the light of these findings, Dollery, Byrnes and Crase (2008) have argued that compulsory merger programs have not only failed as a 'silver bullet' for solving systemic financial and other problems in Australian local government, but have also not provided a coordinated regional dimension to local service provision. In addition to these public inquiries, some empirical work on Australian amalgamation programs has been considered in the academic literature, as well as in consultant reports, although largely of a descriptive nature. In Councils in Cooperation, Dollery, Grant and Kortt (2012) provided a detailed evaluation of this work. With some exceptions, such as Soul's (2000) empirical analysis of council size and per capita service costs in NSW, and Consolidation in Local Government (2011), the scholarly literature is pessimistic on the efficacy of amalgamation as a means of improving local government efficiency. In contrast to the marked emphasis the Australian academic literature has placed on a descriptive approach to the assessment of amalgamation through the case studies and the like a new strand of the Australian literature has focused on empirical investigations using state wide data. For example Drew, Kortt and and Dollery (2013a) critically examined the empirical evidence adduced in favour of radical amalgamation of Tasmanian local authorities in Local Government Structural Reform in Tasmania, produced by Deloitte Access Economics (2011), and commissioned by the Property Council of Tasmania. They found that if the DAE model is re-estimated – employing alternative functional forms – then the empirical evidence in support of Tasmania council mergers evaporates. Similarly, Drew, Kortt and Dollery (2013b) examined whether scale economies exist in local government outlays by analysing the expenditure of 152 NSW councils. When the correlation between population and population density was taken into account the evidence in favour of scale economies disappears.

9 Same Governance, Different Day: Does Metropolitan Reorganisation Make A Difference: Reece LA (2004)
10 Case Studies of City County consolidation: Shaping the Local Government Landscape: Leland and Thurmaier (2004 – 2006)
11 Local Government Consolidation in the United States Faulk and Hicks (2011)
12 City County Consolidation and Local Government Faulk and Grassmerack (2012)
13 City County Consolidation Efforts (Selective incentives and Institutional Choice (2004)
14 City County Consolidation Promise Verse Performance Martin L & Schiff (2011)
15 City County Consolidation Promise Made, Promises Kept :Leland and Thurmaier (2011)

In addition, in its final Methodology for Assessment of Councils Fit for the Future Proposals IPART (2015, p.24) itself conceded that mergers will mean greater expenditure until at least the 2019/20 financial year:

'Due to the structural changes required for merged councils, it may not be practical for these councils to meet all of the benchmarks by 2019/20, e.g., there may be less funds available for asset spending during the adjustment phase. We acknowledge that the merger option is presented to achieve scale/capacity objectives over the longer term, and that some short term budgetary adjustment will be required'.

To illustrate the consequence of financial modelling using assumptions we should also review what was uncovered by Drew and Dollery (2013) in their analysis of the financial consequences of the forced amalgamation and then subsequent de-amalgamation of Noosa Shire Council, Caloundra City Council and Maroochy Shire Councils as part of the broader 2008 Queensland local government amalgamation program. In 2008 Noosa Shire Council, Caloundra City Council and Maroochy Shire Council were compulsorily merged into a new Sunshine Coast Regional Council (SCRC). Five years on, unyielding public opposition and a new Queensland Government secured the de- amalgamation of Noosa Shire from the Sunshine Coast Regional Council. As part of their financial analysis, Drew and Dollery (2013) examined the 2007 financial statements of the three former constituent councils and then the consequences of amalgamation on the predicted and actual financial outcomes for the councils involved.

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

Section 2.1 Corporate Services – Rationalisation of duplicate services

Based on Qld experience, it would appear that Council corporate services staff stagnated and didn't decrease until such time as forced redundancies were implemented (refer to Section 3.2 – Staff Turnover below for related evidence). As NSW has staff protections in place for three years, a majority of staff would remain in situ until such time that redundancies are on offer.

Section 3.1 Management – Tier 3 and 4 Management

The empirical literature has shown that municipal amalgamations often result in diseconomies of scale due to over-scaled councils having been formed (drew, Kortt and Dollery (2013) . Point estimates obtained using data envelopment analysis, demonstrates that the proposed merger for Holroyd will see that group entity will be over-scaled by a little over 14%. Thus leading to diseconomies of scale. An important contributing factor for diseconomies of scale is the difficulty in co-ordinating large numbers of employees. Over time these are addressed by the employment of more managers and supervisors which increases that tier of management.

Section 3.2 Staff – Staff Turnover

One empirical test of the assumptions relating to staff expense is to compare audited financial data arising from March 2008 amalgamations of Caloundra City, Maroochy Shire and Noosa Shire Councils into a Sunshine Coast Regional Council (SCRC).

Below is a table that details the employee expenditure prior to the amalgamation (2006 and 2007) and compares this to post amalgamation outcome (2009 to 2012). It should be noted that Queensland legislation prohibited forced redundancies until March 2011. All data is provided in 2012 terms.

Over the first three years of the amalgamated entity employee expenses were in fact higher than the combined pre-merger staff expenses. This suggests that there is little reason to believe that 'Staff turnover" due to natural attrition will have any significant effect of efficiency over the first three years. It is not surprising that natural attrition rates will reduced significantly over the no forced redundancy period when one considers that many staff will delay resignation or retirement in the hope for a redundancy payout at the end of the three years

Table 1 Employee Expense - Sunshine Coast Regional Council

	Real exped. ($'000)	Change from previous years (%)	Change from Base year (%)
Pre- amalgamation			
2006 combined	158,486		
2007 Combined	162,832	2.742%	2.742%
Transition Year			
SCRC and 2008 Combined	163,142	0.1903%	2.938%
Post Amalgamation			
SCRC 2009	174,517	6.972%	10.115%
SCRC 2010	169,245	-3.021%	6.789%
SCRC 2011	149,143	-11.878%	-5.895%
SCRC 2012	151,188	1.371%	-4.605%

Section 3 ICT Benefits

Again using the Sunshine Coast Regional Council as an example, during their amalgamation, the cost of ICT rose substantially during the first years of the merger and in the fourth year of the merger (2012) were still higher than than of the combined councils 2006 costs. See table below:

Table 2 – Expenditure (Less depreciation)

	Real exped. ($'000)	Change from previous years (%)	Change from Base year (%)
Pre- amalgamation			
2006 Combined	349,038		
2007 Combined	367,503	5.290%	5.290%
Transition Year			
SCRC and 2008 Combined	347,243	-5.513%	-0.514%
Post Amalgamation			
SCRC 2009	504,940	45.414%	44.666%
SCRC 2010	409,459	-18.909%	17.311%
SCRC 2011	353,537	-13.658%	1.289%
SCRC 2012	354,155	0.175%	1.466%

Section 3.4 Materials and contracts

The table below presents the data arising from the Sunshine Coast amalgamation for the materials and contract expenditure item (taken from financial audited statements and presented in 2012 terms). It is clear from this there is no reason to expect any reduction in materials and contract expenditure following amalgamation. In fact, the date from the Sunshine Coast amalgamation suggests that significant increases in the order of 24% to 59% can be expected in the short term and further increases in the order of 8% to 9.6% may be expected in the long term.

Table 3 Materials and Contracts Expenditure - Sunshine Coast Regional Council Merger

	Real exped. ($'000)	Change from previous years (%)	Change from Base year (%)
Pre - Amalgamation			
2006 combined	164,963		
2007 Combined	180,585	9.470%	9.470%
Post Amalgamation			
SCRC 2009	262,968		59.410%
SCRC 2010	204,431	-22.260%	23.925%
SCRC 2011	180,799	-11.560%	9.599%
SCRC 2012	178,335	-1.363%	8.106%

Section 3.6 - Work Units and Plant and Fleet

With reference to Table 1 – Employee Expense, there is no reason to expect a reduction in employee expenses in the absence of forced redundancies. Consequently as Plant and Fleet costs are linked to staff numbers, these will not reduce in the first 3 years until redundancies are offered and staffing numbers can potentially reduce.

Section 5.5 Redundancies Cost for Executive Management

No proposal has been made on the structure of the proposed entity. However we maintain that since the Ryde Council and The Hills Council is only in part moving into the merged entity, we would argue that the The Hills Shire Council redundancy costs will not be realised and only one –third of the Ryde council redundancy costs should be factored in. The only redundancy costs that are associated for sure within the entity is the removal of the GM and Senior Management from Parramatta, Auburn and Holroyd and the one-third of Ryde redundancy costs and only .

Additional Information- Transition Body

Table 4: Amalgamation Queensland Council Estimates of Costs of Mergers

Council	Estimated Costs by Council (Aus$)
Bundaberg	$14,705,273
Cairns Regional	N/A
Central Highlands	$21,533,762
Charters Towers	$1,268,268
Gladstone	$ 15,316,400
Goondiwindi	$ 7,117,277
Gympie	$ 2,282,366
Isaac	$12,112,850
Lockyer Valley	$3,647,603
Logan City	$4,884,647
Mackay	$7,575,854
Maranoa	$2,682,547
North Burnett	$7,341,912
Rockhampton	$6,520,353
Scenic Rim	$12,634,356
Somerset	$2,523,929
South Burnett	$5,286,920
Southern Downs	$5,104,919
Sunshine Coast	$13,720,844
Tablelands	$10,751,120

Council	Estimated Costs by Council (Aus$)
Toowoomba	$10,152,954
Townsville	$3,980,997
Western Downs	$8,113,510
Whitsunday	$7,235,105
Total	**$186,493,766**
Mean	**$8,108,425**
Medium	**$7,235,105**

Source: QTC(2009) *Review of Local Government Amalgamation Costs Funding Submissions – Final Summary Report*

Appendix D

Further Assumptions

MorrisonLow

Further Assumptions

Services and service levels remain the same in the merger unless specifically stated otherwise.

Any costs and benefits (financial, social or otherwise) from an extended governance framework e.g. Community Boards have not been allowed for.

Both the City of Ryde and the Hills Shire Council have been split based on the recommendation of the Independent Review Panel recommendation. No detail was provided by the Panel other than the 'western one third of Ryde' and for The Hills, the suburbs south of the M2.

A split has been made using logical boundaries conforming to this with the apportionment of assets, finances and population being made based on the assumed boundary.

For the City of Ryde, the assumptions used are that the merger includes approximately 32% of the population of the existing Ryde Council and 35% of the properties.

For the Hills Shire, the assumptions used are that the merger includes approximately 17% of the population of the existing Hills Shire and 17% of the properties.

The cost of borrowing is based on existing council forecasts and as such no allowance has been made for access to lower interest rate loans that may be available to councils that are deemed 'Fit for the Future'.