MorrisonLow

PARKES SHIRE COUNCIL

Fit for the Future Modelling of a Merger Scenario between Parkes Shire Council and Lachlan Shire Council

June 2015

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Document Status

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1 INTRODUCTION

1.1 Fit for the Future

Three years ago, local councils from throughout NSW gathered for a summit, Destination 2036, to plan how local government could meet the challenges of the future. As a result, councils agreed that change was needed and that they wanted to be strong and sustainable and to make a positive difference in their respective communities. However, there were various views as to how this could be achieved and in April 2012 the State Government appointed an independent expert panel to carry out a review of the sector. That Independent Local Government Review Panel consulted widely in developing its final recommendations which were presented to the Government in late 2013.

The Panel concluded that for councils to become strong and sustainable, both the NSW Government and the local government sector would have to play a part. The State indicated its preparedness to change the way it works with councils and to support them through meaningful reform. Local councils must also be prepared to consider new ways of working and new structural arrangements. The Fit for the Future (FFTF) program brings these changes together to lay the foundations for a stronger system of local government and stronger local communities.

The Fit for the Future program requires councils to actively assess their scale and capacity in achieving long term sustainability and for councils to submit proposals to the government indicating how they will achieve these objectives.

Parkes Shire Council has commissioned Morrison Low to undertake a high level assessment of a merger between Parkes and Lachlan Shire Councils, using a broad range of factors (financial, social, environmental) in order for the council to understand the implications of the merger of the two councils proposed by the Independent Local Government Review Panel. The Lachlan Shire Council is not party to this investigation. This report uses publicly available information from each Council.

The modelling is prepared using publicly available information and augmented by information provided by Parkes Shire Council.

Where the data is inconsistent or unclear it has not been included and will be recorded as either ‘no data’ or ‘no result’.

1.2 Providing information to enable councils to individually make their decisions

The modelling is intended to assist Parkes Shire Council to understand what the benefits and dis-benefits of the merger of the Councils may be. It has involved analysing historic, current and forecast performance as well as drawing in information from other jurisdictions in which we have been involved in local government reform (for example, transitional costs).

The project is not intended to advise Council of the best option, although it may naturally fall out of the modelling. The project simply provides the information that will enable Council to determine its individual course of action, undertake informed consultation with its community, and ultimately form the basis of the Council’s submission.

1.3 Constraints

The data provided within the model is drawn from a variety of sources (including the Council directly) however it is acknowledged that the timeframe limits our capacity to refine both the available data and the model itself to a fine level of detail. For consistency across the Councils, publicly available information has formed the basis of the analysis.

The asset data for this report has been sourced from Council's Special Schedule 7 report as part of the annual financial statements. It is acknowledged that each Council utilises a different methodology to calculate the cost to satisfactory and the required maintenance expenditure. As such, it is not possible to have a direct comparison between the Councils. Ideally we would normalise these numbers utilising a consistent approach across the Councils to allow a like for like comparison. In this instance we are unable to compile asset data in a similar format to facilitate this approach. It is acknowledged that while both Councils are likely to have adopted a different approach to Special Schedule 7, the numbers represent each Council's best estimate of the cost to satisfactory and the required maintenance expenditure. We would recommend that a more detailed analysis of the asset information be undertaken to validate or test the Council's published information should this merger investigation proceed further.

Notwithstanding these constraints, we have had great support from the staff, providing quick responses to our requests for information. We thank the executives and staff of Parkes Council for their input and cooperation.

1.4 Assessment of business case

IPART recently announced draft assessment criteria for the standalone, merger and rural council improvement plans and business cases. Councils are expected to consider the ILGRP options proposed for each council. The ILGRP proposed a merger of Parkes and Lachlan.

We noted that for a merger to proceed, all participant councils are required to formally resolve to proceed with the merger and complete a Merger Template. If one council chooses not to participate in a merger, all councils must complete an Improvement Plan Template.

2 SCOPE

2.1 Multiple scenarios

The shared modelling project was undertaken on the basis of evaluating the following options.

1. **Status Quo**

   The baseline is measured against what each Council has reported the current and future financial position to be. The analysis is based on the published financial statements and long term financial plans of the Councils.

2. **Meeting the Benchmarks**

   This scenario answers the question as to what each Council would need to do to meet the Fit for the Future benchmarks. It does not address the question of scale and capacity and concentrates on the seven government benchmarks.

   The scenario is built up by separately considering the operating result, asset renewal, asset maintenance, and the infrastructure backlog. It identifies what, if any, funding gap exists but it does not identify how the gap is to be resolved as that is a question for each individual Council.

3. **Merged Council**

   This scenario models a merger of the two Councils and assesses the advantages and disadvantages of this against a series of criteria. The agreed criteria include financial and non-financial indicators and go beyond the government's Fit for the Future benchmarks to incorporate communities of interest and the alignment between the council organisations.

The scenarios assess the advantages and disadvantages of this approach including the financial costs and benefits.

2.2 Reporting

This concise report is intended to provide a body of information that the Council will then use to determine what is in the best interests of the Council and community. As such it does not seek to recommend any one option over another option.

The report compares options and highlights advantages and disadvantages. The relative weighting that is then applied to each matter is a subject for Council.

3 MERGER MODELLING

The following details our assessment of the outcomes of merger modelling.

3.1 Scale and capacity

The government has made it clear that the starting point for every council is scale and capacity.

In the case of Parkes Shire Council the Independent Panel position is that Parkes could be a council in Central West JO or merge with Lachlan Shire Council. The ILGRP did not identify a preferred option and therefore was of the view that scale and capacity for Parkes could equally arise through being a standalone council in a Joint Orangisation or through a merger.

IPART has published further guidelines on how scale and capacity will be evaluated and, at this stage, the methodology is more subjective than objective.

While a merger would, in our view, increase strategic capacity against most of the test criteria this is unlikely to be significant when compared to Parkes on its own.

Council must still make an argument that they can meet the scale and capacity tests.

3.2 Fit for the Future benchmarks comparison

The government has established a set of Fit for the Future benchmarks which all councils are being assessed against. We have undertaken a detailed analysis of the financial and asset management approaches on the following basis:

- Parkes Shire Council: A base case
- Lachlan Shire Council: A base case
- A Merged Council: Analysed on the base case basis

The following table summarises the results of that analysis.

Table 1 Overall comparison of options against Fit for the Future benchmarks

Council	Lachlan Council	Parkes Council	Merged Council	
			Day one	Modelling period
Operating Performance	No	Yes from 2018	No	Yes from 2020
Own Source Revenue	No	Yes	No	No
Debt Service Cover	Yes	Yes	Yes	Yes
Asset Maintenance	No	No	No	No
Asset Renewal	Yes from 2018	Yes	Yes	Yes
Infrastructure Backlog	No	Yes	No	No
Real Operating Expenditure	No	Yes	Yes	No

3.3 What is required to meet the benchmarks

Parkes exceeds most of the Fit for the Future benchmarks throughout the modelling period, from now until 2023, while Lachlan does not. A substantial asset funding gap exists in Lachlan and no asset funding gap in Parkes. Lachlan Council is also showing an operating performance funding deficit for the modelling period which does not provide discretionary funding to address the asset funding gap.

Parkes has no infrastructure backlog after year one and can afford to reduce renewal investment accordingly. Lachlan has a significant infrastructure backlog for the entire modelling period. Both Councils spend less than required on maintenance albeit for Parkes the amount is only slightly below the benchmark and easily addressed by reducing expenditure on renewals in favour of maintenance.

The table below identifies the extent of the funding gap for each Council to address the infrastructure benchmarks and asset maintenance ratio and bringing the infrastructure backlog[1] to the benchmark of 2% within five years. Note there is no gap for Parkes, however Lachlan would need to spend $17,250m each year for five years to meet the asset benchmarks.

Table 2 Summary of infrastructure funding gap

Council[2]	Average funding required per annum (5 years) ($000)	Average funding required per annum (5 years+) ($000)
Lachlan Council	-17,250	-4,280
Parkes Council	2715	2817

[1] Based on condition 3 being satisfactory and as calculated using the Morrison Low methodology

[2] Infrastructure funding gap does not take into account any potential SRV applications

The table below identifies the average annual gap or surplus between operating revenue and operating expenditure (as per the operating performance ratio guidelines) over the time period within each Council's LTFP. Lachlan has an average deficit of $64,000 and Parkes a surplus of $514,000 over the period modelled.

Table 3 Operating performance funding gap

Council	Average gap ($000)
Lachlan Council	-64
Parkes Council	514

3.4 Merged council

3.4.1 Scale and capacity

On the basis that the Independent Panel proposed a merger as one of the options for Parkes it can be assumed that the merged council would achieve the scale and capacity requirements as intended by the ILGRP. We note the standalone option would also satisfy this criteria on this principle.

As part of this research we would normally explore a comparison between the two Councils, the merged council and another current council in NSW. Unfortunately there is no reasonable comparison council with both the population and area to give the proposed merged council reasonable sense of scale and performance.

	Parkes	Lachlan	Merged
Full time equivalent staff	189	131	320
Geographic area (km^2)	5954	14965	20,920
Population	15154	6735	21889
Annual expenditure	33722	35827	69549

3.4.2 Funding shortfall

The merged council is the sum of its parts. This means that the asset and financial position of each council directly contributes to the overall asset and financial position of the merged council. As with the individual councils, the merged council generally meets all of the asset related benchmarks. There is a significant funding gap in order to address the asset renewal and infrastructure backlog ratios which is set out in the table below. The merged council would need to spend $14 million per annum for the first five years in order to meet the benchmarks, and thereafter a further $2.1m per annum to maintain compliance with the asset benchmarks.

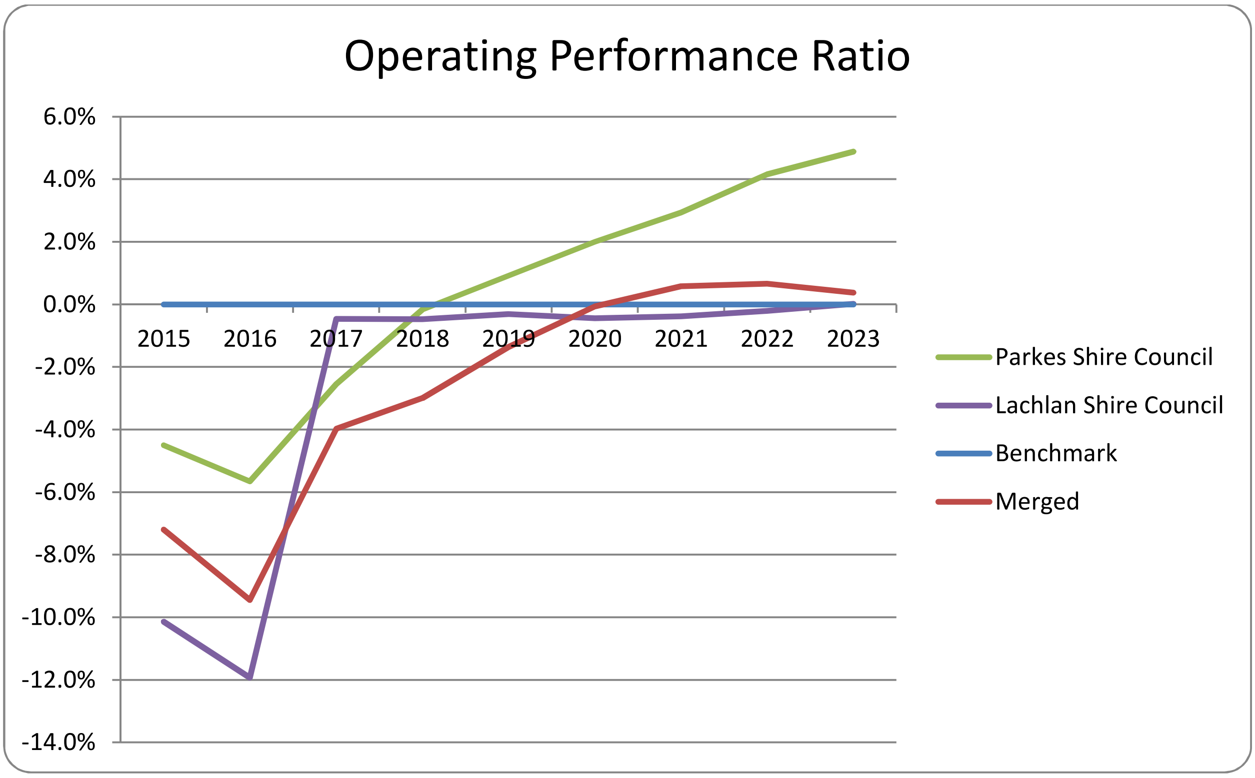
The merged council also has an average operating performance gap of $26,000 per annum which means that it will be running a deficit and therefore has limited ability to address the asset maintenance gap. The impact of the establishment costs affect the merged Council Operating Performance Ratio in 2016.

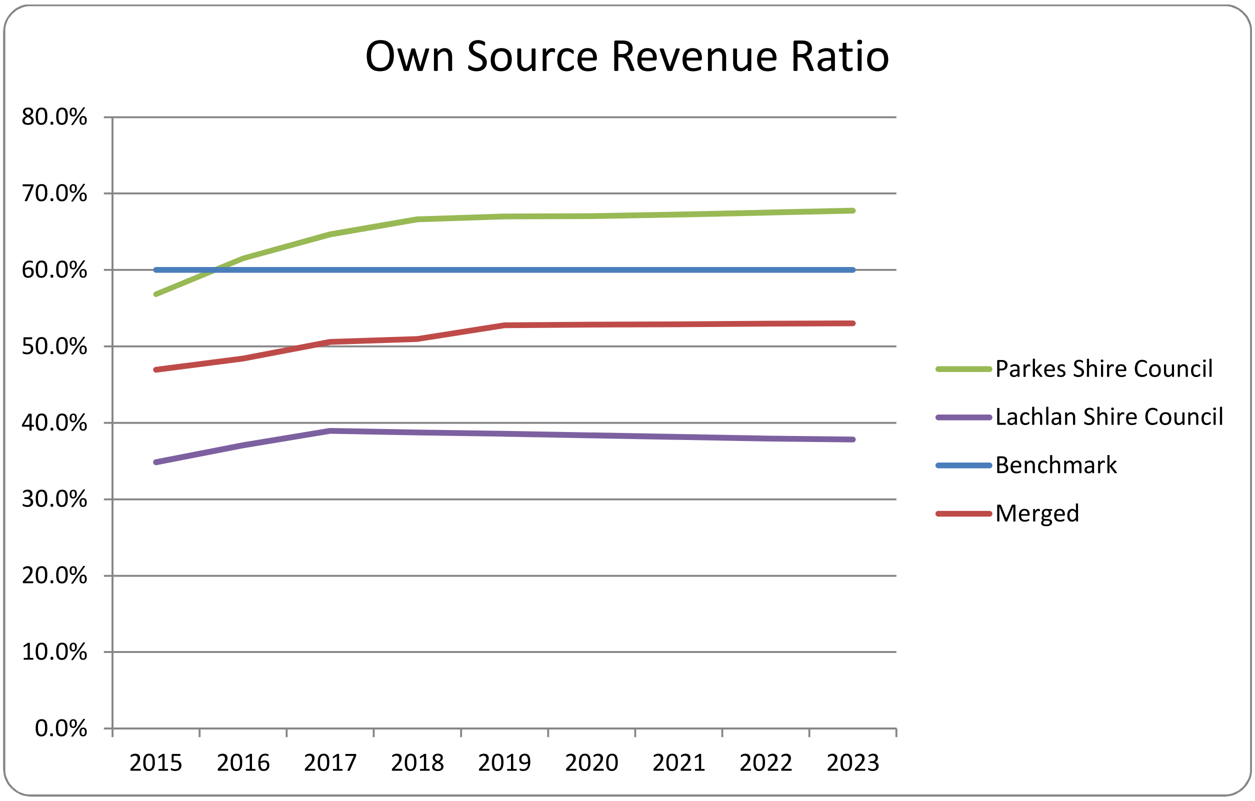
Table 4 Merged council asset funding gap

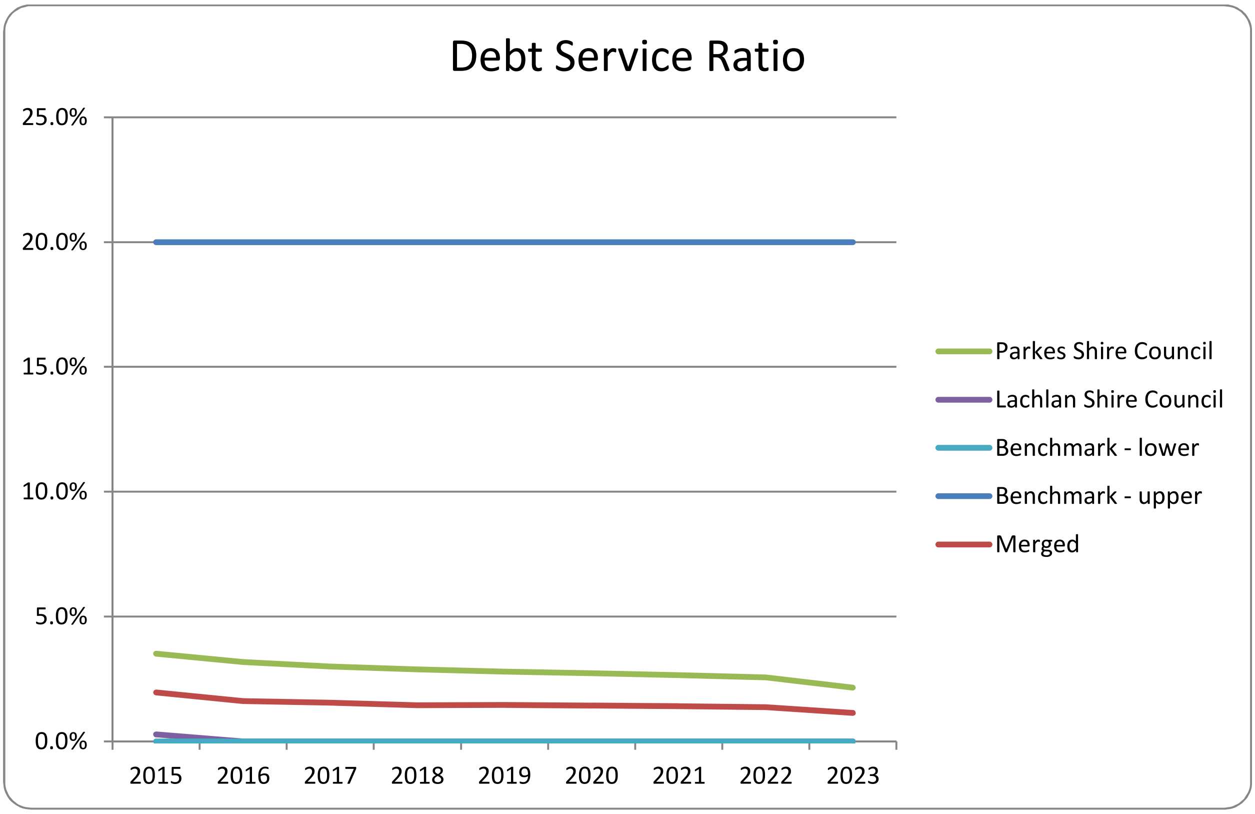
Council	Average funding required per annum (5 years) ($000)	Average funding required per annum (5 years+) ($000)
Merged Council	-13,910	-2,103

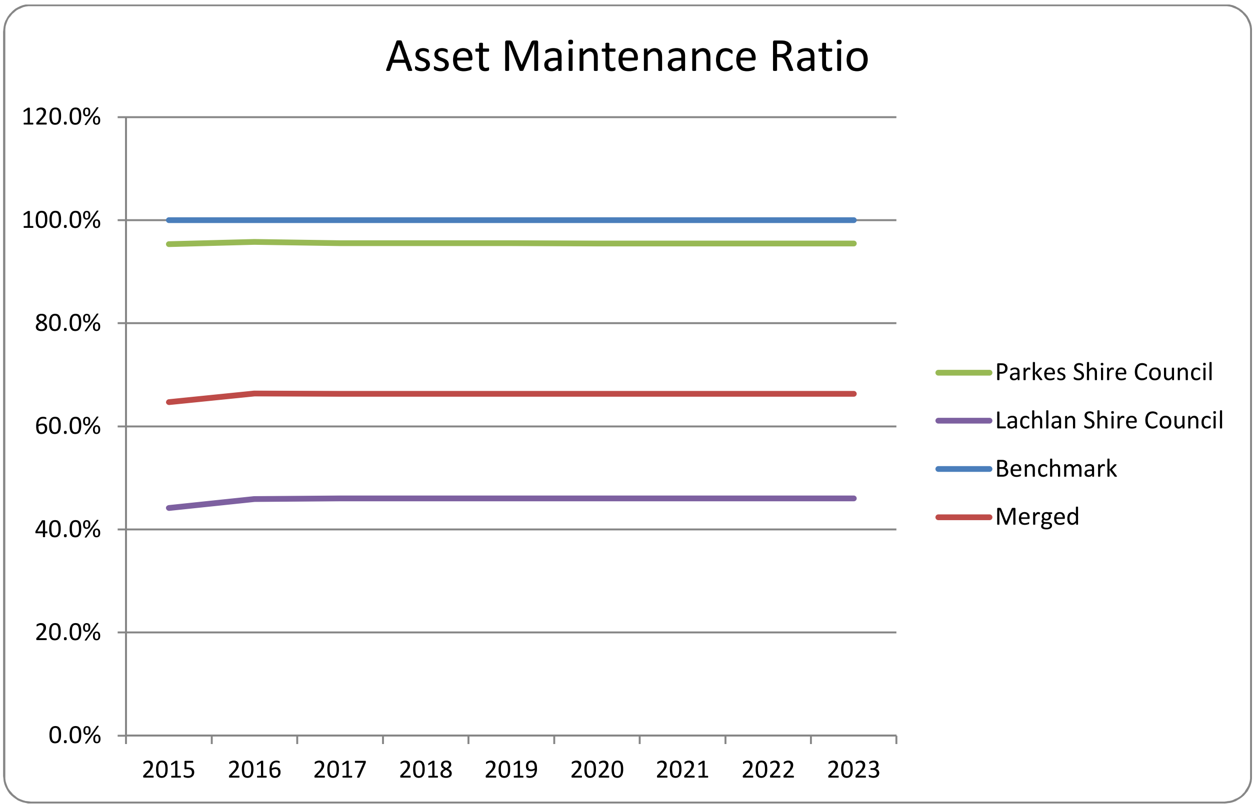
3.4.3 Fit for the Future benchmarks

The following charts display performance over time by the individual Councils and merged council against each of the Fit for the Future benchmarks. These charts were summarised in Table 1.

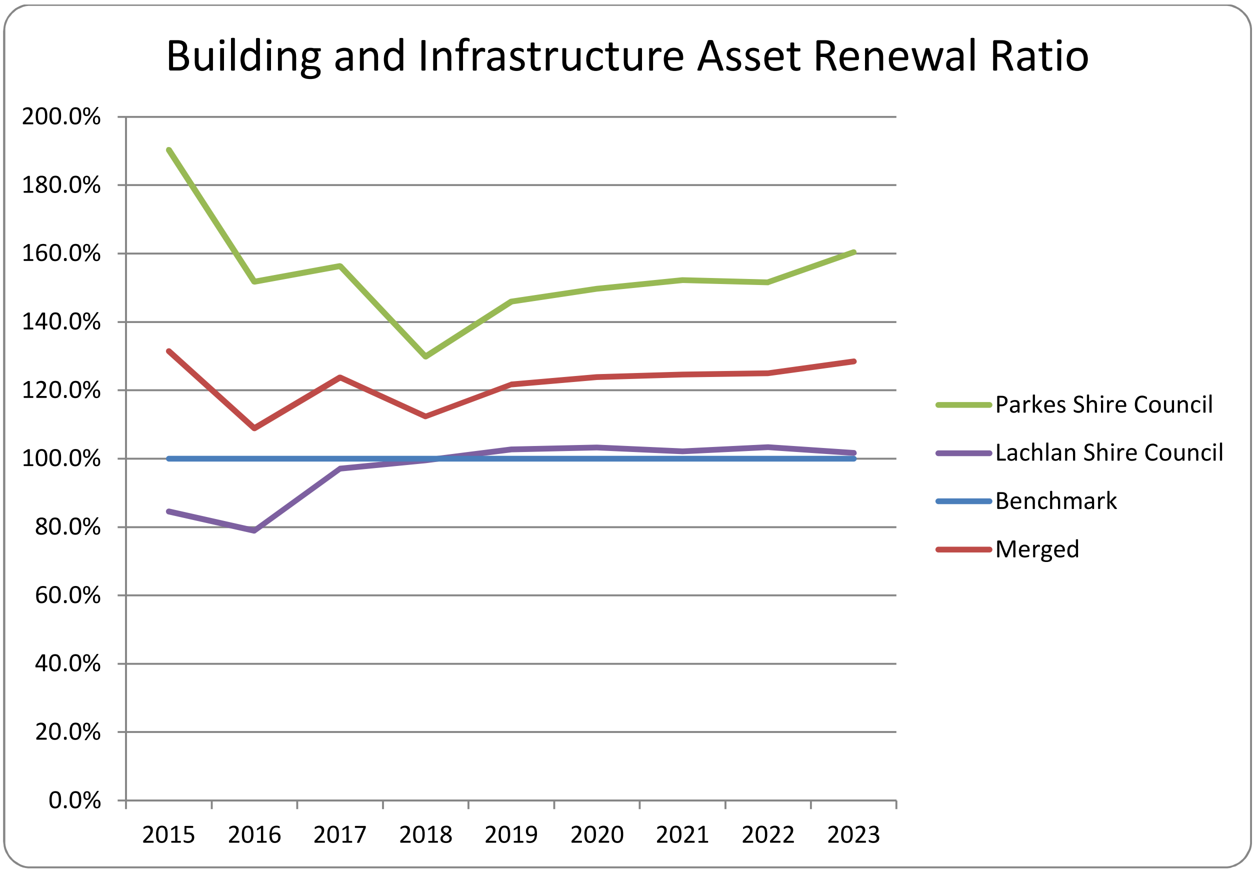



Own Source Revenue Ratio
80.0%
70.0%
60.0%
50.0%
40.0%
30.0%
20.0%
10.0%
0.0%
2015
2016
2017
2018
2019
2020
2021
2022
2023
Parkes Shire Council
Lachlan Shire Council
Benchmark
Merged

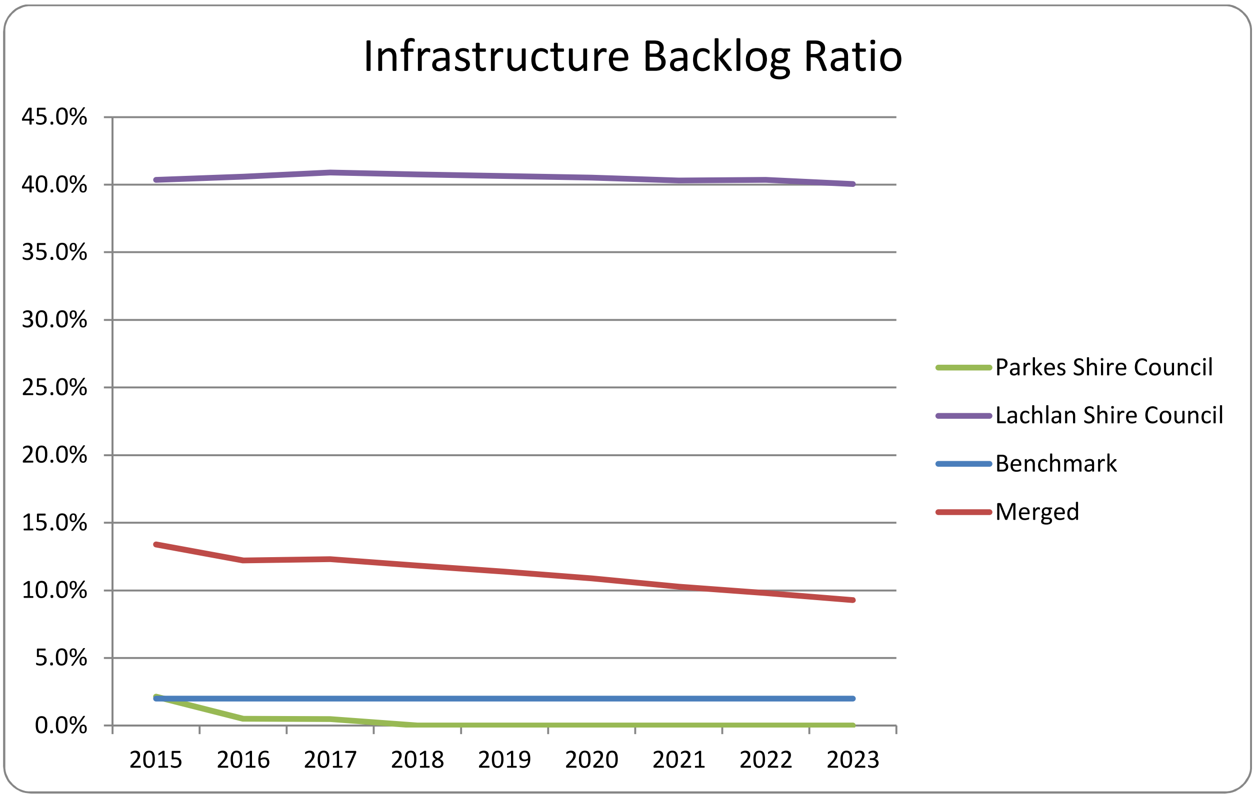

Debt Service Ratio
25.0%
20.0%
15.0%
10.0%
5.0%
0.0%
2015
2016
2017
2018
2019
2020
2021
2022
2023
Parkes Shire Council
Lachlan Shire Council
Benchmark - lower
Benchmark - upper
Merged



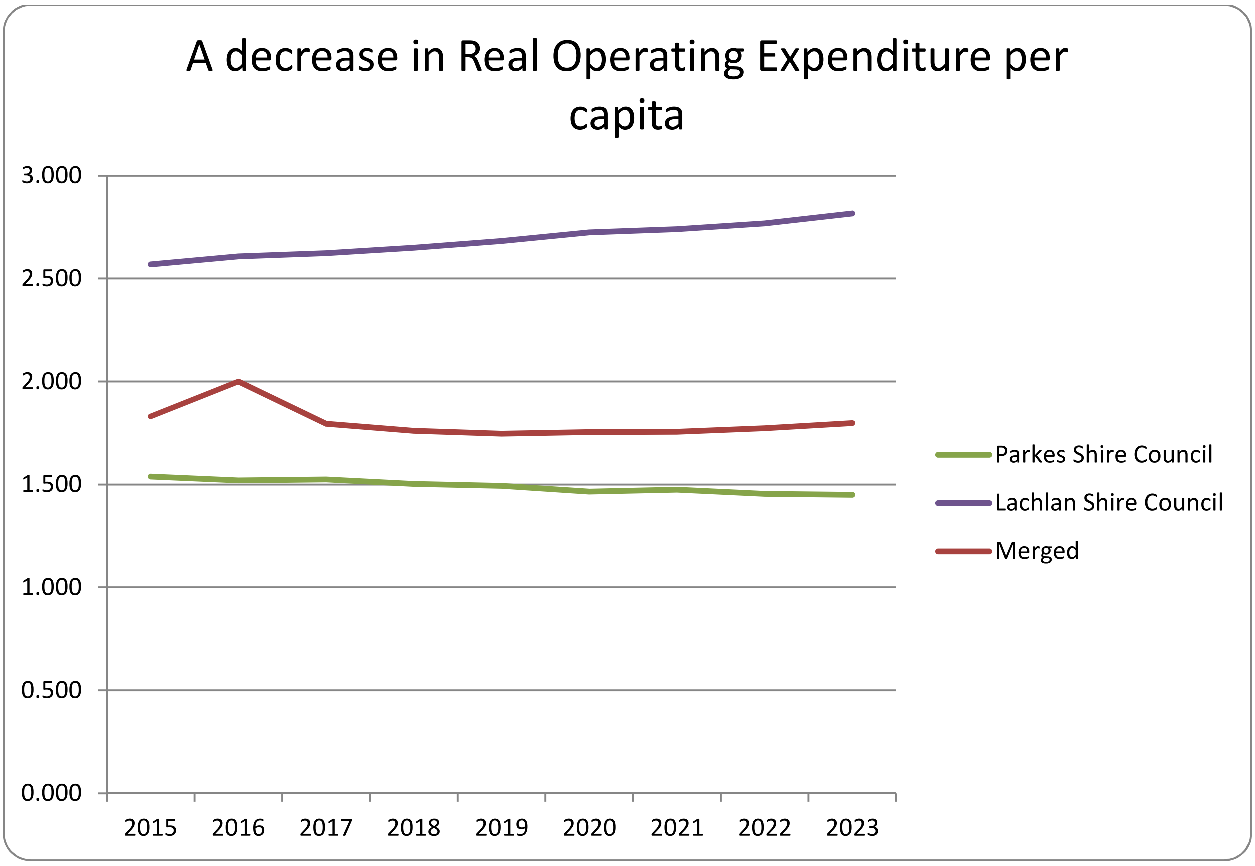
Asset Maintenance Ratio
120.0%
100.0%
80.0%
60.0%
40.0%
20.0%
0.0%
2015
2016
2017
2018
2019
2020
2021
2022
2023
Parkes Shire Council
Lachlan Shire Council
Benchmark
Merged



Building and Infrastructure Asset Renewal Ratio
200.0%
180.0%
160.0%
140.0%
120.0%
100.0%
80.0%
60.0%
40.0%
20.0%
0.0%
2015
2016
2017
2018
2019
2020
2021
2022
2023
Parkes Shire Council
Lachlan Shire Council
Benchmark
Merged



Infrastructure Backlog Ratio
45.0%
40.0%
35.0%
30.0%
25.0%
20.0%
15.0%
10.0%
5.0%
0.0%
2015
2016
2017
2018
2019
2020
2021
2022
2023
Parkes Shire Council
Lachlan Shire Council
Benchmark
Merged



A decrease in Real Operating Expenditure per capita
3.000
2.500
2.000
1.500
1.000
0.500
0.000
2015
2016
2017
2018
2019
2020
2021
2022
2023
Parkes Shire Council
Lachlan Shire Council
Merged

3.4.4 Debt

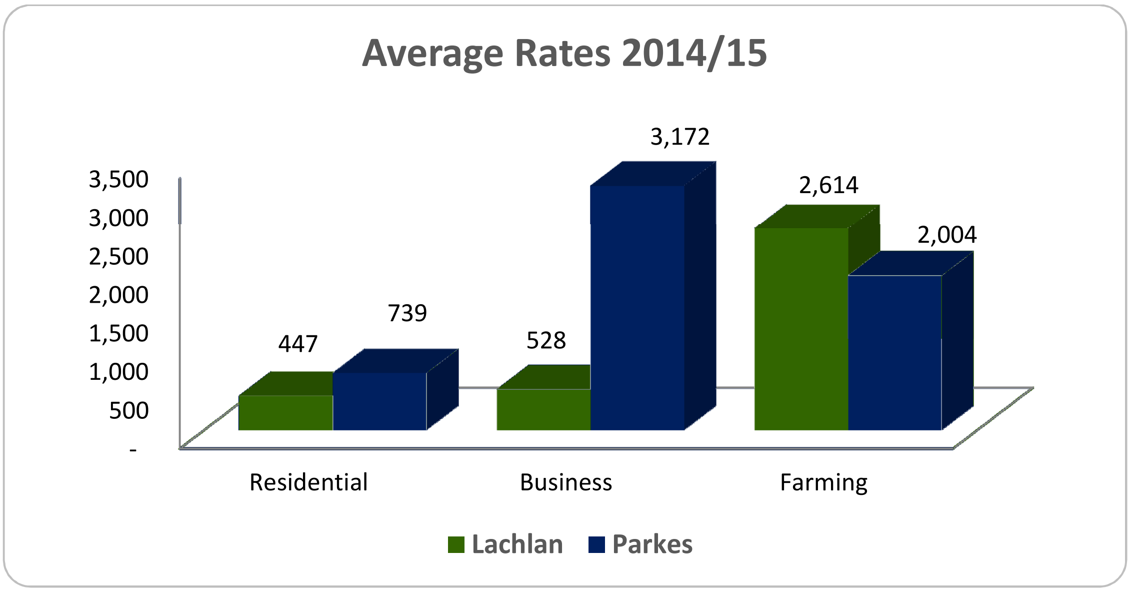
Debt is not an issue for either Council. Parkes has a low debt level and Lachlan no reported debt.

Table 5 Comparison of debt[3]

Council	Debt ($000)	Debt Service Ratio	Debt per Capita ($)
Lachlan Council	$0	0%	$0
Parkes Council	$6,469	3.4%	$430
Combined	$6,469	1.7%	$300

3.4.5 Rates

Both Councils have very dissimilar rating models, levying rates differently across their communities. This is not surprising given that Parkes has a strong urbanised rural service centre and Lachlan is dominated more by farming. The average rates differ significantly between each Council as shown below. If the two Councils were to merge then a new rating model would be required to equitably apportion rates.



3.4.6 Environment and community aspirations

At a broad level, the two LEPs reflect the more complex nature of the Parkes Shire economy in comparison to the rural-focussed economy of Lachlan Shire. Both Councils take a facilitative approach to development within their Shires.

3 Based on 2014 Actual

Residential Zones permit a broad range of residential forms in both Shires. Lachlan Shire applies an RU5 – Village Zone to the principal centre (Condobolin) while Parkes applies an R1 – General Residential Zone to its main centre, Parkes. In addition to residential uses, both zones allow a wide range of support uses.

Both Councils apply an R5 Large Lot Residential Zone to the outskirts of their major centres allowing "rural-residential" growth on the interface between the town centres and broad scale agriculture.

The major commercial heart of Parkes benefits from B2 Local Centre and B4 Mixed Use Zones encouraging retail and commercial activity and recognising its higher order economic role. In Condobolin, these uses are accommodated in the RU5 Village zone.

Aim	Lachlan	Parkes
Agricultural Land	To protect, conserve and enhance agricultural land through the proper management, conservation and development of natural and man-made resources.	To protect, enhance and conserve agricultural land through the proper management, development and conservation of natural and man-made resources.
Lifestyle	To encourage the provision of a range of housing, employment and recreation facilities to meet the needs of existing and future residents of Lachlan.	To encourage a range of housing, employment, recreation and facilities to meet the needs of existing and future residents of Parkes.
Services	To promote the efficient and equitable provision of public services, infrastructure and amenities.	To promote the efficient and equitable provision of public services, infrastructure and amenities.
Environmental and Cultural Heritage	To protect, conserve and enhance the environmental and cultural heritage of Lachlan.	To conserve, protect and enhance the environmental and cultural heritage of Parkes.
Growth	To encourage the sustainable growth of Lachlan.	To encourage the sustainable growth of the villages of Parkes.

Parkes LEP zones land specifically for industrial activity (IN 1 General Industrial) and contains a number of Special Uses (SP1) Zones identifying large sites for activities such as heavy freight. These zones are absent in Lachlan Shire.

Most of the Aims of the two LEPs are identical or very similar.

Differences in the Aims of the two LEPs relate to the higher order economic role of the Parkes Town Centre compared to Condobolin and the importance of the mining sector to Parkes Shire.

Aim	Lachlan	Parkes
Land Supply	To encourage development that is matched by adequate land supply for long-term needs and that is linked with key services and infrastructure.	To encourage industrial development that is matched by adequate land supply for long-term needs, is linked with key services and infrastructure, provides for a diversity of employment and increases the number of skilled jobs in Parkes.

Major Centre Role	Nil	To promote the town of Parkes as a major commercial and community service centre. To raise the profile of Parkes to broaden the economic base, improve its attractiveness as a tourist destination, encourage longer stays and greater local spending and promote a wider understanding of Parkes as a place to live and invest.
Mining	Nil	To acknowledge the contribution of mining to Parkes and the role of Parkes as a mining centre for the region.

3.4.7 Representation

Both Councils currently have ten Councillors. If, under a merged council, this level of representation was retained it would see an increase in the number of residents represented by each Councillor for both areas.

Table 6 Comparison of representation

Council	Representation (population / councillor)
Parkes Shire Council	1510
Lachlan Shire Council	680
Merged	2190

3.4.8 Community profile and communities of interest

The communities are comparable across many of the key indicators, as reported in the 2011 census:

- Both areas have similar age profiles, with median ages of 39.1 (Parkes) and 40 (Lachlan) respectively. The region has similar household types, and both areas have low multicultural diversity and a lower education profile.
- Industry profiles for the two regions differ. Parkes' largest industry is retail (11.6%), with Health and Social Services (11.3%) and Agriculture, Forestry and Fishing (11.3%) the next largest sectors. Lachlan's industry profile however is dominated by Agriculture, Forestry and Fishing (36.1%).
- There is a high level of interdependence between the two regions economically, particularly with regards to workforce, with the majority of residents of both regions likely to work and reside in these locations.
- The labour market in each community is comparable, showing Parkes with 4.9% unemployment, and Lachlan at 4.7%. Both communities also show similar low levels of participation at below 60%.

- Participation in education is also comparable, with Parkes seeing 30% of residents having Year 12 as the highest year of completion, and Lachlan 29%. Further, post school qualifications are also similar though Parkes shows a slightly higher level of postgraduate level degree (0.9% compared to 0.5% for Lachlan). Certificate level qualifications also show some variation at 21.6% for Parkes compared to 16.9% for Lachlan.
- In the period from 2011 – 2031 Parkes is projected to see an increase in its population, up 2.8%, whereas Lachlan is projected to see a considerable decline in population growth over the period, down by 17.9%.
- While both communities have Indigenous populations well above the New South Wales average of 3%, Aboriginal and Torres Strait Islander people represent 16.5% of Lachlan's population, as compared to 8.3% for Parkes.

3.4.9 Organisation alignment

3.4.9.1 Policy alignment

A high level analysis of the vision and key directions in the community strategic plans identifies the areas of relative emphasis for each council area.

Parkes and Lachlan Shire Councils have adopted very similar styles in expressing their respective vision and associated themes for their local areas. Both have brief vision statements and values, and elaborate on these with a series of focus areas around which their community strategic plans have been created. There is a strong consistency and commonality in the foundations of the two CSPs.

In general terms, the themes address priority areas including education, community strength and wellbeing, the natural environment, the local economy and employment, infrastructure and the built environment and strong and effective governance. Parkes specifically identifies the desire to operate as a National Logistics Hub within its plan. Lachlan's CSP includes a strong focus on engaging with and supporting the Indigenous community of the region, which reflects the high percentage of the population who identify as Aboriginal and/or Torres Strait Islander.

The Councils' reflection of their values shows similarities as well with key values of openness, initiative, respect and teamwork included in both.

The comparison is presented visually below through Word Clouds in the figures below.

Figure 1 Summary of Parkes Community Strategic Plan

Figure 2 Summary of Lachlan Community Strategic Plan

3.4.9.2 Cultural Alignment

While it is difficult to compare the internal cultures of the council organisations in this exercise, there are both subjective and objective indicators that give an insight into how aligned or misaligned the organisations cultures can be.

Communities

Often an organisations culture develops as a direct influence of the community it serves. There are a number of indicators of cultural alignment of local government areas including the social and cultural diversity of the community (discussed in this report under communities of interest), the community aspirations and values and how the community views its relationship with Council.

While there can be quite specific local needs and community aspirations, there are themes that emerge from a comparison of the visions for their communities that are expressed by the Councils in their community strategic plans.

Corporate Organisations

Both organisations are structured similarly. Each council operates a three directorate structure organising functions along similar lines. Parkes includes a specific function outside these directorates for governance and corporate strategy.

Organisational size can impact on culture in a range of ways, such as diversity of skills and workforce characteristics, level of specialisation vs. multifunctional roles, capacity to undertake a greater range of functions and services, and partnership and advocacy capacity with other levels of government.

Workforce size is comparable across the two Councils though Parkes is carrying a significant number of vacancies as at the end of 2013 -14 (30 vacancies). Lachlan's workforce experiences 17.5% turnover, whereas Parkes is very low at 2.9%. The industry average sits at approximately 9%.

Lachlan's gender mix sees 36.75% of staff being women. Women dominate administrative roles, and men focused on outdoor/operational roles. Parkes gender mix is less representative, with only 29.5% of the workforce being women. Parkes also indicate a desire to increase the representation of other areas of its workforce including Indigenous people.

Parkes has an ageing workforce, with 46.3% identified as critical positions over the age of 45. This is comparable with Lachlan whose over 45 workforce is at just over 40 percent.

The following table shows some key differences and similarities between the workforces.

	Parkes	Lachlan
FTE (including vacancies)	189	131
Percentage of employee costs allocated to training	1.79%	1.69%
Total annual employee cost ($000) per FTE	$55.69	$59.16
Total annual expense ($000) per FTE	$178.42	$273.49

By measuring training and development expenditure against both total expenditure and full time equivalent staff numbers we can assess each of the Council's approach to staff development. Both Councils spend similar amounts on training and development, slightly less than the recommended industry average.

The annual employee costs, per employee are also very similar. Variances can be due in part to salaries and wages but is also as a result of the organisational structure and type of roles the Council has. Organisations whose costs vary substantially can prove more problematic to merge as harmonisation issues can impact on relationships and behaviours.

A crude indicator of staff productivity can be the portion of the operating costs spent per staff member. There is a variation between the two Councils in this regard, with Parkes having a much lower expense per FTE. While we identify this as an indicator we do not recommend taking these figures at face value as they can be influenced by factors such as the maturity of the workforce and the fluctuating nature of total expenditure year on year and capital projects. Ideally they should be compared over time.

Corporate values

Councils will naturally take a different approach to developing their own corporate culture but generally each is underpinned by a set of organisational values.

Parkes Council lists their corporate values as including - Safety, Innovation, Respect, Community, Integrity and Teamwork. Specific corporate values for Lachlan could not be identified, however in their Community Strategic Plan note their behaviours will be driven by the following: that they will Lead, influence and inspire, Take the initiative and act, Accept and value each other and work together, Respect the environment, Embrace new ideas and build pride and resilience. These values are broadly comparable with Parkes.

In any event most council's would have a relatively common set of corporate values that are heavily influenced by the public nature of their role and service focus.

Corporate Policies

A review of the policy registers can identify some interesting philosophical differences and issues that have been given priorities (at some point in time) by the different Councils. While policies change from time to time they can both reflect and influence the organisational culture that is tasked with implementing them.

A desktop review of both Councils' policies shows that each has a range of policies that cover most traditional government functions and responsibilities. Parkes' policy register is extensive with many 'operational policies' that frame expected outcomes and limit officer discretion. Lachlan's policy register is much smaller.

Any merger plan must have a strategy that specifically addresses organisational culture.

3.4.10 Services

The range of services and facilities provided by any council to its community can vary significantly from place to place. Not only do the types of services vary, but the levels of service will often be quite different from council to council.

The reasons for these variations are numerous. For many councils the suite of services that they offer in the present day is a reflection of decisions made by councils past. Those decisions are generally based on community desires and needs, funding availability or strategic business choices.

Given the limitations on this investigation we have not undertaken any service analysis but if we were to we would expect to find considerable differences in the service offering, service delivery methods and service levels. Some of these differences will be for the reasons list above but also the very fact that one Council serves a large urban population and is a regional service centre where as the other focuses more on servicing its rural community.

These variations pose one of the greatest risks to the merger and realising any benefits. We know from prior experience the newly merged councils are often challenged to deliver services equally across the region creating a trend to increase service levels for residents who receive a lower service. Rarely do service levels decrease. Any trend to increase services and service levels will rapidly reduce any merger benefits. Any merger plan should include a thorough review of services to determine differences in delivery and cost implications.

3.4.11 Costs and savings of the merger

The costs and savings of the merger arise throughout the period being modelled. The costs and savings should not be considered in isolation. They only form part of the information on which a decision should be made and in particular they should be considered in conjunction with the infrastructure funding gap identified above.

Initially in the transition from two councils into one there are costs associated with creating the single entity (structure, process, policies, systems and branding), costs continue to arise through redundancies of senior staff and the implementation of a single IT system across the new council which has significant cost implications. Costs of the merger continue to arise in the medium and longer term largely from redundancy costs (one off) but increasingly from an overall increase in staff numbers which is 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 required in comparison to the councils combined. Natural attrition is initially applied meaning that overall staff numbers fall in the short term, although the reduction is a small one. Savings are also projected to arise in relation to procurement and operational expenditure due to the size and increased capacity of the larger council but again these are modest. In the medium and longer term benefits arise through reducing the overall staff numbers with a focus on removing the duplication of roles and creating greater efficiency in operations and some rationalisation of plant (one off).

The operating performance of the merged council (excluding grants and contributions for capital purposes) is negative in every year of the period being modelled.

The NPV of the total costs and savings over the period being modelled (2023[4]) has been calculated and set out below and identifies a net benefit to the councils and community arising from the merger.

4 2023 is the period being modelled to match the time covered by both council LTFPs

Table 7 Summary of costs and savings

NPV at 4%	NPV at 7%	NPV at 10%
-$16,524,350	-$14,294,720	-$12,443,600

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.

The costs and benefits that Morrison Low has modelled for a possible merger of Parkes and Lachlan 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 following table 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 ($90 - $110k)

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 10 councillors for the new merged council.

1.2 General Manager ($300K)

The formation of a single entity will result savings in executive management costs as there will only be one General Manager and an assumed executive of four. We have not investigated if both Councils tier two staff are senior staff and therefore not protected employees. Revised remuneration packages for the new entity have been informed and assumed to be on par with similar sized councils.

It is important to note that while ongoing efficiencies of $300k have been identified effective from the short term, there is the one off cost of redundancies of an estimated $1.25m. This redundancy cost is based on 38 weeks and makes allowance for the potential of all tier one and two staff being made redundant.

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.

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.

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

2.1 Rationalisation of duplicate services ($350k)

Consistent with the dis-establishment of two 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.

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 starting point for the assumption underpinning the efficiency for corporate services was a 15%[5] reduction in corporate support personnel based on previous mergers. However, a review of the organisational charts of the two councils means that in this case our view is that there is very limited opportunity for reductions in corporate services. On costs are considered to be included as the figure used are based on total employee costs as reported by the councils.

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 to those outlines 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.

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

Redundancy costs have been modelled on an average of 26 weeks[6].

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 ($400k)

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.

On the basis that two Councils are being disestablished and a single entity created there is typically opportunity for a reduction in Tier 3 management positions in particular and in this case we have allowed for a $400k or 17.5% reduction in management positions.

3.2 Staff Turnover ($500k)

While the average turnover varies significantly between both Councils 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 2.5% natural attrition.

3.3 ICT Benefits ($400k)

Without a full investigation into the current state of the two 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.

[6] 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 10 years. An average of 26 weeks has therefore been used throughout the modelling.

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 two 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%[7] over time in line with reduced IT applications and systems. Without the ICT FTE remuneration for the two 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. Research into the Queensland amalgamtions indentified ICT solutions as representing 47% of all merger costs. 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 $400K per annum.

3.4 Materials and contracts (1%)

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 two councils to one.

The increased scale and size of the infrastructure networks managed by the 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 our work in other councils, we have forecast savings of 1%.

3.5 Properties ($0)

Typically 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.

However the nature of the two Councils, the geography and the limited opportunities to reduce staff numbers means that in our view that no allowance should be made for the rationalisation of buildings.

3.6 Works units

Staff (10% reduction in staff))

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 10% 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.

[7] Report to the Local Government Commission on Potential Savings of a Range of Options for the Re-organisation of Local Government in the Wellington Region, Brian Smith Advisory Services Limited, November 2014

Plant and Fleet (5% reduction, 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 it day to day functions. Having considered the utilisation rates of the two councils a reduction in plant and fleet in the order of 5% would be achievable should there be an amalgamation of the 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[8] 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 two 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.[9] 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:

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 are filled.
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

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

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

	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 ($1.5m)

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[10] including an assessment of the merger costs for the three rural councils of the Wairarapa. Queensland Treasury Corporation also identified a cost for both establishing corporate office accommodation and external contracts to handle the additional workload of creating and implanting the new Council structure of approximately $750,000 in 2009.

On the assumption of FTEs to transition body costs for Wellington, the estimated cost of the transition body for the councils is $1.5 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.

5.2 ICT ($4m)

The costs associated with ICT for the new entity relate to rationalising the 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. Two approaches were considered; the first being the costs to transition the new council to a single system(s) across the board. The second was to take a ‘best of breed approach’ and use the best existing systems and migrate data across.

The significant costs involved in the first option mean that it is not considered appropriate for a merger of Parkes and Lachlan. Comparatively the costs remain high for the second option as well as the difficulties in migrating data and working through system capabilities etc will still incur costs. Given the respective size of the Councils and the populations they serve in the context of the studies cited it is considered that the most likely costs are in the region of $4 million.

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

The estimated cost are spread across the initial years of the councils operations with the majority falling in the first two years.

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 two 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 ($750k)

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 the existing signage of the two Councils for Day 1 of the new entity on buildings, facilities and vehicles. In addition it will be necessary to replace the existing staff uniforms, letterheads, brochures, forms and other items. The estimated cost for branding is $750K based on other amalgamation experience.

5.5 Redundancy Costs ($1.25m)

This is based on a reduction from two general managers to one for a merged council and a reduction in tier two staff. This estimate is based on employment contracts with a redundancy period of 38 weeks, and a reduction in directors from six to four.

5.6 Remuneration Harmonisation (negligible)

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 two councils. Given the significant number of vacancies which were unfilled in Parkes across the year, it has been difficult to determine a value for this cost. High level analysis however indicates there would be limited costs associated with harmonisation across the two workforces.

5.7 Elections ($0k)

There is a possibility of proportional savings in existing council budgets as instead of two 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 two councils.

3.4.12 Risks arising from merger

There are significant potential risks arising from the merger both in a financial and non-financial sense. The obvious financial risks are that the transitional costs may be more significant than set out in the business case or that the efficiencies projected in the business case are not delivered. The business case is high level and implementation costs and attaining the savings will be difficult to achieve.

If, for example, the council chooses not to follow through with the projected efficiencies, this will affect the financial viability of the merged council. Similarly, decisions made subsequent to the merger about the rationalisation of facilities and services may not reduce the cost base of the merged organisation as originally planned.

Careful consideration of the issue of cultural integration will be required and the most consistent remedy to these particular risks is in our view strong and consistent leadership. Corporate culture misalignment during the post-merger integration phase often means the employees will dig in, form cliques and protect the old culture. In addition to decreased morale and an increased staff turnover rate, culture misalignment reduces business performance. It also prolongs the time it takes for the predicted efficiencies to be achieved.

The integration of services with differing service levels often leads to standardising those service levels at the highest level of the services that are being integrated. This is quite often a response to a natural desire to deliver the best possible services to communities as well as the need to balance service levels to community expectations across the whole area. However it does pose the risk of increased delivery costs and/or lost savings opportunities. Similarly, introducing services that are not currently delivered in one or more of the former council areas to the whole of the new council area will incur additional costs.

Further risks exist with developing an acceptable (to the communities) rating model.

Alongside these typical risks arising from a merger, any reduced financial performance would be likely to lead to the new council having to review services and service levels to seek significant further efficiency gains and/or increase rates to address the operating deficit.

4 SUMMARY

Lachlan	Parkes	Merged Council
• Meets two of seven benchmarks • Asset funding gap per annum to meet benchmarks in 5 yrs – $17.3m • Average operating deficit – $64k	• Meets six of seven benchmarks • No asset funding gap • Average operating surplus – $514k	• Meets three of seven benchmarks • Asset funding gap per annum to meet benchmarks in 5 yrs – $13.9m • Average operating deficit – $26k • $14.3m in benefits (incl $5m grant) over modelling period • Decrease in representation • New rating apportionment required • Community, service level and organisational differences to resolve • Risks to realising benefits