

**REPORT TO
LOCAL GOVERNMENT COMMISSION**

**FINANCIAL ANALYSIS
FOR REVIEW OF
OTOROHANGA & WAITOMO DISTRICTS**

*Beattie Rickman
Hamilton
August 2003*

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NOTICE TO READER

Beattie Rickman has prepared this Report for the Local Government Commission for use solely in their review of local government in the Otorohanga and Waitomo Districts. This Report has been prepared based on information provided by the Otorohanga, Waitomo and Waipa District Councils and from publicly available information.

Beattie Rickman makes no representation or warranty as to the correctness, accuracy or completeness of information contained in this Report, accepts no liability for any statements, opinions, information or matters arising out of, contained in or derived from, or for any omissions from, this Report or any other written or oral communications with any party in relation to the Report.

This Report contains high level analysis which includes certain opinions, estimates and forecasts. These involve significant elements of subjective judgement, which may not be correct and/or may not have been tested to the extent which may be required by a party interested in the Report. In addition, there are usually differences between forecasts and actual results, because events and circumstances frequently do not occur as forecast. Differences between forecasts and actual results may be material. Interested parties should conduct their own independent review of the relevant assumptions, calculations, and subjective judgement upon which opinions, estimates and forecasts are based.

We note that we have acted from time to time for all three Councils. However the three Councils were consulted on our appointment.

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August 2003

1. EXECUTIVE SUMMARY

This report had been commissioned by the Local Government Commission to identify, at a **high level**, the likely costs and financial benefits associated with two re-organisation options:

- The union of the Otorohonga and Waitomo Districts to form a new district, and
- The union of the Otorohonga, Waitomo and Waipa Districts to form a new district.

Our approach and methodology is outlined in Section 4. We identified annual costs and savings expected to be incurred/achieved in the longer term and one off costs of achieving the reorganisation offset by savings achieved through the disposal of surplus assets. Our analysis takes into account only the cost savings that would result directly from any reorganisation and does not consider savings that could be achieved by the Councils individually regardless of the reorganisation.

The governance structures for the two options were set by the Commission stipulating in particular Council composition, community boards, centre of operations and service centres. These assumptions along with other material assumptions on which our analysis is based are summarised in Section 5.

In Sections 6 and 7 we detail our analysis. We do not provide our detailed assessment of staff cost savings for privacy reasons.

We have also identified cost savings in the following areas:

- Employment
- Governance
- Information systems
- Computer costs
- Audit
- Legal
- Facilities
- Other

We have identified additional costs in the area of Transfund funding.

Transition costs include:

- Redundancy
- Redundancy support, recruitment and change management
- Financial information, strategy documents and records
- Corporate, regulatory and environmental policies
- Rebranding
- Miscellaneous capital expenditure
- Contingency

Offsetting these one off transition costs are proceeds from the realisation of surplus assets.

Our brief also asked us to consider the viability of Otorohonga and Waitomo District Councils should the reorganisation not proceed. Our comments are included in Section 8. We have benchmarked the two Councils against other similar districts and considered publicly available financial and associated information to assess the current and future affordability of Council services.

Conclusions

Our summary of the savings for an Otorohonga and Waitomo reorganisation is:

	Year 1	Subsequent years	PV 10 years	PV Perpetuity
Estimated annual savings	\$1,007,000	\$1,007,000	\$16,125,000	\$20,239,000
Sale of assets	450,000	-	430,000	430,000
Transition costs	(600,000)	-	(573,000)	(573,000)
Total	\$857,000	\$1,007,000	\$15,982,000	\$20,096,000
Per rateable property (8,936)	\$96	\$113	\$1,788	\$2,248

PV= Present Value-refer page 23 for explanation

Our summary of the savings for an Otorohonga, Waitomo and Waipa reorganisation is:

	Year 1	Subsequent years	PV 10 years	PV Perpetuity
Estimated annual savings	\$2,210,000	\$2,210,000	\$17,275,000	\$44,417,000
Sale of assets	500,000	-	477,000	477,000
Transition costs	(1,400,000)	-	(1,337,000)	(1,337,000)
Total	\$1,310,000	\$2,210,000	\$16,415,000	\$43,577,000
Per rateable property (24,664)	\$53	\$90	\$665	\$1,766

PV= Present Value-refer page 23 for explanation

The tables show that both options for amalgamation are clearly justified on the savings realised in the first year alone. Even without any revenue from property sales the transition costs in year 1 are less than the estimated annual cost savings in year 1 for both options.

Both Otorohonga and Waitomo are small Councils with high rates, fees and charges, and public debt levels when compared with other predominantly rural Councils in the Waikato Region. Any savings that can be achieved through reorganisation, or any other means, will improve the ability of local government in the districts to meet ratepayer expectations.

As part of our high level review we have compared the staffing, expenditure and asset levels of the Councils in New Zealand with populations less than 20,000, a total of 25 Councils. On a population basis Waitomo and Otorohonga rank 11th and 12th smallest respectively of the 25 Councils in New Zealand with populations of less than 20,000. When considering the ratio

of Council staff to population, expenditure and assets Waitomo ranks 4th best of the 25 Councils and Otorohanga only 19th best.

Adding the current Otorohanga and Waitomo Councils together produces a Council that would be ranked 2nd largest out of 24 among the smallest Councils in New Zealand on a population basis and only 12th largest on the ratio of Council staff to population, expenditure and assets. However when comparing a combined Otorohanga and Waitomo Council with the ten largest Councils with populations of less than 20,000, Otorohanga and Waitomo would only rank 8th largest with 68 staff versus an average of close to 50. This indicates that a reorganisation of Otorohanga and Waitomo has the potential to reduce current staff numbers by 10 to 15 positions.

The savings we have identified for both options are primarily employee related, and only those that are obvious savings on a reorganisation. In practice it generally takes a major action such as a reorganisation, and resulting reengineering or restructuring, to achieve significant organisational savings. For example, Waitomo believe that based on their experience over several years a commercially managed reorganisation and associated restructuring could reduce the current combined staff of 68 to approximately 40. This would produce additional savings. Also, in our experience there would be additional savings from economies of scale and increased purchasing power for other expenditure.

We believe that both options proposed by the Local Government Commission would provide significant financial benefits and are worthy of further investigation.

Accordingly we recommend that the Local Government Commission further investigate a reorganisation of Otorohanga and Waitomo on the basis of both proposed options. The preparation of a reorganisation scheme will require careful consideration of funding policies to provide for the equitable sharing of savings between the ratepayers in the existing Districts and for the funding of expenditure by those who benefit.

2. INTRODUCTION

In August 2001 the Waitomo District Council initiated a proposal for the union of the Waitomo District and Otorohanga District to form a King Country District. After due consideration and consultation the Local Government Commission (the Commission) formed the view that a comprehensive review of the structure of local government in the Otorohanga and Waitomo Districts was required.

In November 2002 the Commission engaged Beattie Rickman to provide a high level analysis of the financial implications associated with two reorganisation options:

- The union of the Otorohanga and Waitomo Districts to form a new district, and
- The union of the Otorohanga, Waitomo and Waipa Districts to form a new district.

We prepared a draft report with full workings in May 2003 for consideration of the Councils. There were no material matters brought to our attention by Councils. This report summarises our findings. As it is expected that this will become a public document, it has been necessary to edit our draft report for privacy reasons.

3. TERMS OF REFERENCE

The objective of our engagement is to identify, at a **high level**, the likely costs and financial benefits associated with the two options for local government reorganisation involving the Otorohanga and Waitomo Districts, and to identify which option, if any, should be investigated in further detail. The project will also assess, at a high level, the current and likely future viability of the Otorohanga and Waitomo District Councils.

4. APPROACH AND METHODOLOGY

We have assessed the financial implications of costs and savings under two headings:

- Annual costs or savings that are expected to be incurred/achieved in the longer term.
- Transition costs or savings, the one off costs associated with achieving the reorganisation offset by savings achieved through the disposal of surplus assets.

The net savings as a result of the proposed reorganisation have been calculated as the sum of the annual costs and savings less the net transition costs, being the transition costs less the sale proceeds of any excess assets.

We have assumed that the transition costs and sales proceeds for redundant assets are paid and received respectively one year out and that the annual savings will be achieved in perpetuity.

In calculating the savings, it is necessary to take into account the time value of money to recognise that future dollars, i.e. savings in the future, are worth less than current dollars. Accordingly, in addition to showing the savings per rateable property we have expressed the overall savings from the proposed reorganisation as the net present value of the cash flows.

Reorganisation will not only impact costs but will have a material impact on revenue. The impact on each Council's ratepayers will ultimately depend on the funding policy adopted by any new Council. It was agreed with the Commission that our review of the financial impacts of any reorganisation should be limited to quantifying overall cost savings. Our brief does not include the determination of a new funding policy and accordingly it was not appropriate for us to consider the impact on the ratepayers of the individual Councils. In effect we are assuming that a funding policy will be agreed including targeted rating policies that will maintain equity between the ratepayers of the respective Districts.

In determining the cost savings it was important that we only considered changes in expenditure that will arise directly as a result of the proposed reorganisation. We have ignored cost savings that could be achieved regardless of the reorganisation, for example a change in the level of service. The fact that one Council for example outsources a service and the other conducts the activity in house has no bearing on the conclusions reached in this report.

Accordingly we have assumed that it is business as usual in respect of service levels and have focused our review on the cost of governance, corporate and overhead costs that are allocated to service activities.

The Local Government Act 2002 is likely to impose additional costs on local authorities. The explanatory note to the Bill stated "Local authorities may face additional compliance and transaction costs in decision making. This arises from additional consultation requirements and the development of a long-term council community plan (LTCCP), particularly the first such plan. These costs relate, in part, to the costs of consultation to be undertaken by councils, but may also arise through increased vigilance by communities of their councils. Less cohesive communities, where it will be more difficult to reach agreement, may have higher costs. Requiring specific consultation with Maori may involve some additional compliance and transaction costs in local authority decision making. Once the LTCCP is formulated, however, it is likely to provide better information to business and the public about council intentions, and improved resource allocation. Over time, the consultation and LTCCP proposals are expected to strike a balance with the compliance costs to councils."

One rural Council in the Waikato region has estimated that the Local Government Act 2002 will cost ratepayers at least an additional \$100,000 per year. Any reorganisation should reduce the costs of compliance arising from the 2002 Act. In fact there are likely to be other legislative initiatives and events impacting the Councils in future that could be more cost effectively managed by a larger Council. As any savings in respect of the Local Government Act 2002 would not be a saving of costs currently incurred, we have excluded this from our assessment of savings.

We have prepared this report using information from Management Plans, Annual Estimates and Budgets, Annual Plans and Annual Reports provided for each Council. We have supplemented this information with other publicly available information and discussions with appropriate Council personnel. We received comments on our assessment of staffing levels from the Councils and have met with Otorohanga District Council representatives to discuss our assessment of savings and have considered their views. Waipa and Waitomo District Councils did not accept our initial invitation for more in depth consultation on the basis that they were happy to comment on our draft report.

Otorohanga District Council has expressed concern that Beattie Rickman may have held a preconceived view on the reorganisation based on previous work completed by the partner leading our Local Government consulting group. To allay these concerns it was agreed that a second partner not involved in the previous work become actively involved in the review. A senior management consulting partner with considerable experience in the local government sector reviewed all work and agreed all conclusions reached in formulating the recommendations in this report.

5. ASSUMPTIONS

The Commission set the following underlying assumptions:

Option 1: The union of the Otorohanga and Waitomo Districts to form a new district

- The Council would be based in Otorohanga, with a service centre in Te Kuiti
- Community Boards would be constituted for the Otorohanga, Te Kuiti and Kawhia townships, each with 5 elected members and 1 appointed member.
- 8 members, including the Mayor, would be elected to the Council.

Option 2: The union of the Otorohanga, Waitomo and Waipa Districts to form a new district.

- The Council would be based in Te Awamutu, with a service centres in Cambridge, Otorohanga and Te Kuiti
- Community Boards would be constituted for the Te Awamutu, Cambridge, Otorohanga, Te Kuiti and Kawhia townships, each with 5 elected members and 1 appointed member.
- 12 members, including the Mayor, would be elected to the Council.

We have made the following other material assumptions:

- LTFS documents include all expenditure required to maintain Council's assets and services except for those specifically disclosed, e.g. unfunded depreciation.
- Community Board remuneration for the Te Kuiti Community will be the same as currently paid to the Otorohanga Community Board, which will remain unchanged under both options 1 and 2.
- Staff redundancy payments would average 6 months of salary.
- Following an Otorohanga and Waitomo reorganisation the present Waitomo Administration Building and associated land would be sold.
- Transition costs are paid, and sale proceeds for surplus assets are received, one year out.
- Annual savings will be achieved in perpetuity.
- Cash flows are discounted to present value at a real discount rate of 4.75%.
- All figures are GST exclusive.

Our brief focussed on the financial implications of a reorganisation and as such did not require us to consider the wider economic or social impacts on the communities in the districts that might result from reorganisation, e.g. the economic and social consequences of job losses off-set by the economic benefits from any reduction in rates and charges.

6. COST IMPLICATIONS OF AN OTOROHANGA & WAITOMO REORGANISATION

6.1 Discussion

In August 2002 both Otorohanga and Waitomo prepared their own estimates of the financial implications of a reorganisation of the Otorohanga and Waitomo District Councils. These estimates were based on the 2001/02 annual plans and budgets.

Otorohanga District Council concluded that annually there would be an overall operational rates saving (before transitional costs) of \$262,428.

Otorohanga's business case for the reorganisation is based on 63 staff, compared to the current combined complement of 68. Otorohanga note in their report that they have based their case on bringing Waitomo's contracted professional engineering services in-house "which will not alter the total cost of providing these services". The Otorohanga business case is based on a Council including a Mayor and 10 Councillors (LGC assumption - Mayor and 7 Councillors) and a Piopio Community Board (LGC assumption - no Piopio Community Board).

Of significant note is Otorohanga's treatment of the income received from Waitomo District Council's wholly owned subsidiary Inframax Construction Limited. Otorohanga consider that this income, less associated interest costs, should be excluded from income and instead be used to meet capital expenditure requirements. The impact of this treatment is that Otorohanga have reduced identified savings on reorganisation by this amount. We believe that this treatment is technically incorrect and understates the savings by \$420,000. Therefore it appears that the gross cost savings identified by Otorohanga amount to \$683,000, or an average of approximately \$76 per rateable property. We note that the present value of this level of savings is \$5.3 million over the ten year planning period for local government and in perpetuity is \$13.7 million.

Waitomo District Council concluded that annual operating savings of \$1,858,000 could be achieved. This is an average saving of approximately \$208 per rateable property. We note that the present value of this level of savings is \$14.5 over the ten year planning period for local government and in perpetuity is \$37.3 million.

Waitomo's business case proposes a staffing configuration "based on maximising competencies in every position and maximising productivity through quality of leadership, and personal commitment and loyalty." Waitomo's business case for the reorganisation is based on 48 staff, compared to the current combined complement of 68. The difference between Waitomo's and Otorohanga's proposed staffing accounts for the largest amount of the difference between total estimated savings.

Part of the staffing difference also relates to reduced engineering and asset staff through further contracting out. Other differences are that Waitomo proposes only one community board and a reduced per km rate for roading costs for Otorohanga to bring it into line with Waitomo's average per km cost.

In the discussion included with each Council's estimate of savings they both note that they have adopted existing levels of service and quality.

Otorohanga notes - "Care has been taken to ensure that information presented relates only to savings possible as a consequence of amalgamation. Cost savings arising from a reduction in service level or as a consequence of restructuring have been excluded, as they are not considered true amalgamation savings and could be achieved by either Council independently." This is consistent with our approach.

Waitomo notes - "For the purposes of initial assessment, this proposal adopts existing service levels and quality - i.e. a very conservative position. Significant opportunity exists for further savings from standardising design and delivery of services across the enlarged district and by adopting strategies that consider equity of service delivery to all ratepayers based on business case logic and practice."

In practice it generally takes a major action such as a reorganisation, and resulting reengineering or restructuring, to achieve significant organisational savings. It may be reasonable to exclude the benefits of a restructuring from reorganisation savings on the basis that they theoretically can be achieved without reorganisation. However it will be the very reorganisation that provides the incentive to ensure restructuring takes place and therefore the resulting benefits could arguably be considered to be savings on reorganisation.

Waitomo's estimates would appear to take into account their assessment of staffing levels as a result of a more aggressive commercial management approach, and as such include a level of savings from restructuring that would result from reorganisation. Whilst we have some sympathy for this approach our analysis excludes such savings to the extent that they could be achieved regardless of reorganisation.

6.2 High Level Benchmark Information

A Council's level of staff determines employment costs which are the most significant component of indirect operating costs. Through an "overhead allocation" methodology these costs are allocated to each service that Council provides for the community and the cost of each service includes both direct costs and these indirect costs. A reorganisation will most significantly impact indirect costs, generally through staff savings that arise through economies of scale, duplication of design and service delivery methods, operational efficiencies that can be achieved in a larger organisation and the benefit of increased purchasing power.

As a starting point for our high level review we have compared the staffing, expenditure and asset levels of the Councils in New Zealand with populations less than 20,000, a total of 25 Councils.

A comparison of this nature is somewhat subjective, as the composition of each district (i.e. urban and rural mix), services provided and method of service delivery will impact the number of staff employed. However a comparison can be used as a rough indicator of staff efficiency and therefore overall council operational efficiency.

On a population basis Waitomo and Otorohanga rank 11th and 12th smallest respectively. When considering the ratio of Council staff to population, expenditure and assets, Waitomo ranks 4th best of the 25 Councils and Otorohanga only 19th best. This indicates that Waitomo with 25 staff might be close to "best practice" when compared with its peers while Otorohanga with 43 staff may be well below "best practice".

Adding the current Otorohanga and Waitomo Councils together, without factoring in staff reductions, produces a Council that would be ranked 2nd largest out of 24 on a population basis and only 12th largest on the ratio of Council staff to population, expenditure and assets. However when comparing a combined Otorohanga and Waitomo Council with the ten largest Councils with populations of less than 20,000, Otorohanga and Waitomo would only rank 8th largest with 68 staff versus an average of close to 50. This indicates that a reorganisation of Otorohanga and Waitomo could have the potential to reduce current staff numbers by 10 to 15 positions.

6.3 Analysis

The basis for the estimates detailed in this report are the Council's 2002/03 annual plans and estimates. Since the preparation of their 2002/03 annual plan and estimates Waitomo has undertaken a restructuring that has seen their staff reduced from 35 positions to 25 positions. Our estimates are based on these 25 positions which along with Otorohanga's 43 positions provide a starting point of 68 positions.

For the purposes of this report, employee costs include salary and other direct expenses including professional memberships, ACC, conference and training expenses, vehicle expenses, travel and accommodation, superannuation, FBT etc.

Throughout this report we refer to specific positions that we consider would be surplus on reorganisation. However, consistent with the high level nature of this review, after further consideration it might be more appropriate to remove an alternative position within the same function.

We have determined the following cost changes on reorganisation of the Otorohanga and Waitomo Districts:

i. Governance

Governance currently comprises:

Otorohanga	Waitomo
Mayor	Mayor
Councillors (7)	Councillors (10)
Otorohanga Community Board (5)	
Kawhia Community Board (5)	

The following discussion relates only to the cost of elected members as other costs, including the Otorohanga General Manager which Otorohanga include in governance, are included in the analysis of corporate and overhead costs.

The current direct costs relating to elected members are:

	Otorohanga	Waitomo	Total
	\$	\$	\$
Council			
Mayors Salary	50,000	47,760	97,760
Members Salaries & Meeting Allowances	47,500	80,000	127,500
	<u>97,500</u>	<u>127,760</u>	<u>225,260</u>
Mayors & Members Travelling Expenses	12,000	14,250	26,250
Conference & Zone Expenses	7,000	6,000	13,000
Local Government New Zealand	23,000	25,000	48,000
Printing & Stationery / Newsletter (1)	8,000	15,000	23,000
Sundry Expenses (2)	11,300	33,710	45,010
	<u>158,800</u>	<u>221,720</u>	<u>380,520</u>
Otorohanga Community Board			
Members Remuneration	39,000		39,000
Expenses	1,000		1,000
	<u>40,000</u>		<u>40,000</u>
Kawhia Community Board			
Members Remuneration	5,900		5,900
Expenses	1,000		1,000
	<u>6,900</u>		<u>6,900</u>
Piopio Community Board (3)			
Members Remuneration		7,300	7,300
	<u>\$205,700</u>	<u>\$229,020</u>	<u>\$434,720</u>

- (1) Otorohanga excludes one off costs of \$4,000 in 2002/03 associated with the Commission's Review.
- (2) Otorohanga excludes one off costs of \$20,000 in 2002/03 associated with the Commission's Review.
- (3) The Piopio Community Board has been disestablished during the 2002/03 year.

As noted in the assumptions (see section 5) the Commission has advised that a reorganised Otorohanga and Waitomo District would be governed as follows:

- Council - Mayor and seven members
- Te Kuiti Community Board - 6 members
- Otorohanga Community Board - 6 members
- Kawhia Community Board - 6 members

In 2001 the Higher Salaries Commission (HSC) assumed responsibility for determining remuneration for elected members of Local Government. In late 2002 the HSC determined the total level of remuneration for the elected members of each Council (including 50% of Community Board remuneration) based on criteria including population, expenditure and assets.

The current Waitomo Council has resolved not to increase elected member's remuneration. For the purposes of this review it is appropriate to consider the savings that would result between the HSC determinations for the existing Councils and a new Council. Accordingly we have adjusted the base line expense to the HSC determination and assessed the governance costs of the reorganised Council based on the HSC guidelines.

We have calculated below from the HSC determinations that the total of remuneration for the two Councils as they currently are would be \$337,450.

We have assumed that Community Board remuneration remains at the current levels, including the Te Kuiti Community Board that would be created on reorganisation.

Using the current population, expenditure and assets of the two Districts, before reorganisation, the total remuneration pool for elected members (including the Mayor and 50% of Community Board remuneration) is calculated below in accordance with the HSC determinations to be in the order of \$271,950.

	Otorohanga	Waitomo	Otorohanga & Waitomo Combined	Otorohanga & Waitomo Reorganised
HSC Pool	\$150,000	\$165,000	\$315,000	\$230,000
50% Otorohanga CB	19,500	-	19,500	19,500
50% Kawhia CB	2,950	-	2,950	2,950
50% Te Kuiti CB	-	-	-	19,500
Total Remuneration	<u>\$172,450</u>	<u>\$165,000</u>	<u>\$337,450</u>	<u>\$271,950</u>

The potential saving on reorganisation is the difference between Otorohanga and Waitomo Combined and Otorohanga and Waitomo Reorganised - \$65,500.

Elected members expenses are in addition to this and the changes in cost have been calculated as follows:

Mayor and Council Members Travelling Expenses

Total current cost is \$26,250 for two Mayors (including \$1,500 for the Waitomo Mayor) and seventeen Councillors. This equates to approximately \$1,381 each. We estimate that the cost for the combined Council (Mayor and seven Councillors) would be \$13,500 (Mayor @ \$3,000 plus 7 Councillors @ \$1,500). Therefore there would be a saving of \$12,750.

Conference & Zone Expenses

This cost is currently \$7,000 for Otorohanga and \$6,000 for Waitomo, a total of \$13,000. Other Councils appear to pay a similar level therefore there would be a saving on reorganisation. We estimate that the cost for the combined Council would be \$7,000 and that there would be a saving of \$6,000.

Local Government New Zealand

This cost is currently \$23,000 for Otorohanga and \$25,000 for Waitomo, a total of \$48,000. Other Councils appear to pay a similar level therefore there would be a saving on reorganisation. We estimate that the cost for the combined Council would be \$30,000 and that there would be a saving of \$18,000.

Printing & Stationery / Newsletter

This cost is currently \$8,000 for Otorohanga and \$15,000 for Waitomo, a total of \$23,000. There would be efficiencies as a result of not having to prepare two versions of newsletters and also a larger print run for each newsletter. A saving of 25% is assumed. We estimate that the cost for the combined Council would be \$18,000 and that there would be a saving of \$5,000.

Otorohanga Community Board

Expenses may increase slightly with an increase in members to six. Accordingly we estimate that expenses will increase by \$500 from \$1,000 to \$1,500.

Kawhia Community Board

Expenses may increase slightly with an increase in members to six. Accordingly we estimate that expenses will increase by \$500 from \$1,000 to \$1,500.

Te Kuiti Community Board

We estimate that there would be a new cost of \$1,500.

Sundry Expenses

Total current combined cost is \$45,010 for two Mayors and seventeen Councillors. This equates to approximately \$2,500 each. We estimate that the cost for the combined Council (Mayor and seven Councillors) would be \$20,000 (\$2,500 @ 8) and that the saving would be \$25,010.

Election Expenses and Councilor Training/Induction

Triennial elections have a significant cost, along with Council training and induction. These costs are accounted for in the year incurred although arguably they could be accounted for over the three-year period. The 2002/03 year is not an election year. However, it is appropriate to include an annual saving for these costs.

	Waitomo	Otorohanga	Total
Election	25,000	26,000	51,000
Induction/training	6,000	10,000	16,000
	<u>\$31,000</u>	<u>\$36,000</u>	<u>\$67,000</u>

Annualised this is a cost of \$22,000. Much of the election cost (an estimated 80%) is directly related to the number of electors, which will not change on reorganisation. Therefore election cost savings will not be significant (\$51,000 @ 20%, over three years @ 50% = \$1,700 per year).

With one Council instead of two the saving in induction and training costs is estimated at \$2,000 per year.

We therefore estimate the total of election and training costs at \$3,700 per annum.

Summary

In our opinion the savings in governance costs will be in the order of \$133,000 made up as follows:

	\$
Remuneration	65,500
Travelling Expenses	12,750
Conference & Zone Expenses	6,000
Local Government New Zealand	18,000
Printing & Stationery / Newsletter	5,000
Otorohanga Community Board Expenses	(500)
Kawhia Community Board Expenses	(500)
Te Kuiti Community Board Expenses	(1,500)
Sundry Expenses	25,010
Election Expenses & Councillor Training / Induction	3,700
	<u>\$133,460</u>

ii. Information System Costs

Other Information System costs for Otorohanga and Waitomo amount to approximately \$200,000 including software costs, site and system support, contracts and leases, insurance, repairs and maintenance, electronic data capture and internet/website.

Both Councils operate an NCS financial system. On reorganisation there would be savings in license fees, software upgrades and on-going software support. Also there would be a need to only maintain one GIS system.

Electronically linking a Te Kuiti Service Centre to Otorohanga will require some expenditure however the utilisation of the internet for this should limit the amount of expenditure required. We estimate that by running common systems these costs will reduce by 25%, or a saving in the order of \$50,000. Transition costs (see section 6.4) includes an allowance for miscellaneous expenditure required on reorganisation.

iii. Computer Costs

The requirement for computer terminals is directly related to the number of staff employed. Waitomo's budget for 2002/03 includes a cost for funding computer depreciation of \$85,000. This cost includes the cost of computer terminals,

servers and networking. At that time there were 35 staff, a charge of approximately \$2,500 each, which we have taken as being indicative for both Councils. (We were not able to determine this cost for Otorohanga from their Management Plan and Estimates.) We estimate a reduction in staff on reorganisation of 13, which will reduce this cost by approximately \$32,500 annually.

iv Corporate Support Costs

In the Support Services and Finance and Administration areas of both Waitomo and Otorohanga there are a number of other direct costs that are likely to reduce as a result of reorganisation. These include:

	Waitomo	Otorohanga	Total
	\$	\$	\$
Audit	55,000	46,000	101,000
Insurance	34,400	33,000	67,400
Valuation Services	52,000	50,000	102,000
Legal Expenses	40,000	55,200	95,200

Audit

The audit fee paid by Waipa is \$65,000. Based on this cost we estimate an audit for the combined Council of \$60,000, a saving in the order of \$41,000.

Insurance

We believe that there is unlikely to be much of a cost saving on reorganisation.

Valuation Services

The valuation fees paid by Waipa are \$201,000 for 15,728 rateable properties. Waitomo and Otorohanga have a total of 8,936. On this basis the combined level of valuation fees is appropriate and little saving is likely.

Legal Expenses

Most of Otorohanga's legal costs result from the provision of in-house legal services (total direct costs \$47,000) while Waitomo's are sourced externally. External legal fees for Otorohanga are \$8,000 and Waitomo \$40,000.

On the basis that an in-house legal service is retained on reorganisation, we estimate a cost saving in the order of 25% of the current Waitomo legal cost, or \$10,000.

v. Administration Building - Waitomo

The Commission has determined that for the basis of our review a reorganised Otorohanga and Waitomo Council would be headquartered at Otorohanga. With the resulting reduction in staff and shift of staff from the Te Kuiti Administration Building to the Borough Building (as the Te Kuiti Service Centre) or Otorohanga, the Te Kuiti Administration Building would be surplus. Set out below is a

calculation of estimated savings based on the costs shown in Waitomo's 2002/03 Annual Plan:

Unavoidable Costs, ie people related

Electricity & Gas	21,000
Repairs & Maintenance (50%)	6,498
Office Cleaning (75%)	16,875
Total Unavoidable Costs	<u>44,373</u>

Avoidable Costs, ie building related

Insurance	7,720
Repairs & Maintenance (50%)	6,497
Car Park/Sheds/Lab	2,800
Office Cleaning (25%)	5,625
Security/Compliance Costs	4,900
Rates	3,900
Depreciation	32,432
Total Avoidable Costs	<u>63,874</u>

Total Costs	108,247
Less: Lease Income	9,936
Net Cost	<u>\$98,311</u>

These costs are based on a staff of 35, at least three of who are not located in the Administration Building. We have estimated that 13 positions would be surplus on reorganisation, a reduced building requirement to the combined Councils equivalent to 50% of the Te Kuiti Administration Building. This would provide a saving in the order of \$76,000 being avoidable costs plus 50% of unavoidable costs (the remaining 50% would continue to be incurred at another location, either the Borough Building or Otorohanga Council Building) less lease income.

The Waitomo Administration Building and surrounding land is recorded at a current valuation of \$700,000. This value has been independently confirmed as an indicative market value. The Government Valuation is \$570,000. As the property would likely be surplus on reorganisation, it could be sold. Additionally with a reduction of 13 staff on reorganisation there would be other office equipment and furnishings that could be sold.

We have estimated that after sale costs \$450,000 could be realised on reorganisation.

vi. Other Savings

Reorganisation would create a larger organisation with theoretically greater purchasing power and potential for efficiencies. This should result in some cost savings for consumable type expenditure including telephone and tolls, photocopying, subscriptions and publications, personnel management and appraisal, which is primarily related to the number of staff.

With a reduction in Waitomo staff from 35 to 25 during the 2002/03 year these costs will already reduce. Reducing the combined staff of Waitomo and Otorohanga on reorganisation will result in further savings.

Using Waitomo costs for these expenses (approximately \$100,000 in 2002/03) as a basis we have estimated a saving in the order of \$20,000. (We could not determine all of these costs from Otorohanga's Management Plan and Estimates.)

vii. Transfund Subsidies for Roothing

Reorganisation of Otorohanga and Waitomo would have some impact on the level of roading subsidies received from Transfund. Discussions with Transfund indicate that the level of subsidy would reduce slightly in the event of a reorganisation. They estimate that based on the level of expenditure in the 2002/03 year the reduction would have been approximately \$62,000.

viii. Staff Costs

We assess that there would be a reduction of 13 positions on reorganisation with a resulting saving of \$706,000.

6.4 Transition Costs

Transition costs would arise from the implementation of either of the options identified by the Commission. These costs would include:

- Redundancy payments to staff and redundancy support
- Recruitment and change management
- Disposing of surplus assets
- Combining financial information
- Combining Strategy documents including LTFS (LTCCP), Funding Policy and Treasury Management Policy
- Combining other records
- Combining District Plans
- Aligning corporate, regulatory and environmental policies
- Rebranding

In respect of a reorganisation of Otorohanga and Waipa we have estimated transition costs as follows:

Redundancy

On the basis of current employment conditions we have provided for redundancies on the basis of an average redundancy payment of 6 months pay - \$300,000

Redundancy support, recruitment and change management

\$100,000.

Asset Disposal

These costs have been taken into account when considering the proceeds estimated above.

Financial Information

Both Waitomo and Otorohanga use the NCS financial system. While some work would be required to combine information it would not be extensive.

Strategy documents including LTFS (LTCCP), Funding Policy and Treasury Management Policy

Some work would be required to combine these documents in the short-term, with the major work being undertaken as part of a regular review.

Estimate for combining financial information, strategy documents including LTFS (LTCCP), Funding Policy and Treasury Management Policy and other records
\$50,000

Combining District Plans

The reorganised district could operate two District Plans on a geographic basis until the normal five yearly review. The cost of then preparing one District Plan would be covered by the five yearly review.

Aligning corporate, regulatory and environmental policies

Some immediate work would be required to align these policies. Estimated cost - One person for 6 months, say \$25,000.

Rebranding

\$25,000

Miscellaneous capital expenditure

\$50,000

This is a PC sum for the fitout of the Te Kuiti service centre, meeting room for the Te Kuiti Community Board (using existing Council furniture) and other costs associated with establishing the Te Kuiti Service Centre including electronically linking the service centre to Otorohanga.

Summary of Transition Costs

	\$
Redundancy	300,000
Redundancy support, recruitment & change management	100,000
Financial information, strategy documents & records	50,000
Corporate, regulatory and environmental policies	25,000
Rebranding	25,000
Miscellaneous capital expenditure	50,000
Contingency	50,000
Total	<u><u>\$600,000</u></u>

6.5 Total Estimated Savings

On reorganisation we have estimated that there would be the following net cost savings:

	\$
Employee Costs	706,000
Other Costs	
Governance	133,000
Information System	50,000
Computer Costs	33,000
Audit	41,000
Legal	10,000
Administration Building	76,000
Other	20,000
Transfund subsidies	<u>(62,000)</u>
Estimated Annual Savings	<u>\$1,007,00</u>
Estimated Transition Costs	<u>\$600,000</u>
Estimated Proceeds from Sale of Assets	<u>\$450,000</u>

The total saving is the net present value of the annual cost savings in perpetuity less the net transition costs, being the transition costs less the proceeds from sale of assets.

Future cash flows should be discounted to present value using an appropriate opportunity cost of capital. This would normally be derived assuming an appropriate capital structure (debt and equity) to develop a weighted average cost of capital for the organisation. Local authorities do not have equity holders in the normal commercial sense, although arguably ratepayers are a proxy for the shareholder of a normal commercial enterprise.

A likely use of any savings from any reorganisation would be to repay or avoid debt which would otherwise have been necessary to fund future capital expenditure. Accordingly, one option is to utilise the cost of borrowing as an appropriate discount rate.

Utilising the current interest rate for Council borrowings, we derive a real pre-tax discount rate of 4.5%.

An alternative approach to the calculation of the discount rate is to assume the benefits of the organisation will ultimately flow through to the ratepayer, as reduced rates or improved service levels. An appropriate discount rate in this instance would be the opportunity cost of capital to the ratepayer. One measure of this would be the returns that the ratepayer could expect in the longer term from a balanced investment portfolio. The discount rate based on a return from a balanced investment portfolio (real) is likely to be in the vicinity of 5%.

We have used the average of the above two options, 4.75%. We note that the higher the discount rate, the lower the present value of future cash flows, or in this case, the net savings.

We have considered two present value scenarios, firstly the present value of savings during the ten year planning period of local government and secondly the present value of the savings in for perpetuity.

Our summary of the savings for an Otorohanga and Waitomo reorganisation is:

	Year 1	Subsequent years	PV 10 years	PV Perpetuity
Estimated annual savings	\$1,007,000	\$1,007,000	\$16,125,000	\$20,239,000
Sale of assets	450,000	-	430,000	430,000
Transition costs	(600,000)	-	(573,000)	(573,000)
Total	\$857,000	\$1,007,000	\$15,982,000	\$20,096,000
Per rateable property (8,936)	\$96	\$113	\$1,788	\$2,248

7. COST IMPLICATIONS OF AN OTOROHANGA, WAITOMO & WAIPA REORGANISATION

7.1 Discussion

Having completed our assessment of cost savings resulting from an Otorohanga and Waitomo reorganisation we have then used that as a base for determining the further impact of a reorganisation with Waipa. To use a cost management analogy, we have looked at an Otorohanga and Waitomo reorganisation on a "full cost" basis and an Otorohanga, Waitomo and Waipa reorganisation on a "marginal cost" basis. This approach is appropriate given the significance of the Waipa District as is evident from the following information taken from each Councils 2002/03 Annual Plan:

	Waipa	Otorohanga	Waitomo
Population	40,293	9,279	9,473
Rateable Properties	15,728	4,439	4,497
Revenue (Forecast 2002/03)	33,863,000	10,601,000	12,692,000
Net Assets (Forecast 30/6/03)	480,952,000	136,353,000	186,302,000
Public Debt (Forecast 30/6/03)	\$24,376,000	\$9,812,000	\$11,628,000

Our approach has primarily involved considering the overall resources of the Waipa District Council and determining the resources that would need to be added from the Otorohanga and Waitomo District Councils to meet Otorohanga and Waitomo service requirements. In some areas, e.g. finance, these requirements would be limited whereas in other areas, e.g. asset management and regulatory, the requirements would be more extensive.

The starting point for our estimates are the 55 positions which we consider would be the position requirements following a reorganisation of the Otorohanga and Waitomo Districts.

7.2 Analysis

i. Governance

As noted in the assumptions (see section 5) the Commission has advised that a reorganised Otorohanga, Waitomo and Waipa District would be governed as follows:

- Council - Mayor and eleven members (same as current Waipa)
- Te Awamutu Community Board - 6 members (currently 9 members)
- Cambridge Community Board - 6 members (currently 8 members)
- Te Kuiti Community Board - 6 members
- Otorohanga Community Board - 6 members
- Kawhia Community Board - 6 members

Elected member's remuneration would be as follows:

HSC pool based on the current population, expenditure and assets of the three Districts (including the Mayor and 50% of Community Board remuneration) would be in the order of	475,000
Hearing and Iwi Committees – advised by Waipa	35,000
Te Awamutu Community Board – Current remuneration \$40,890 for 9 members, therefore six members = \$27,260 @ 50%	13,630
Cambridge Community Board - Current remuneration \$40,890 for 8 members, therefore six members \$30,670 @ 50%	15,335
Te Kuiti Community Board – as for Otorohanga/Waitomo reorganisation	19,500
Otorohanga Community Board - as for Otorohanga/Waitomo reorganisation	19,500
Kawhia Community Board - as for Otorohanga/Waitomo reorganisation	2,950
Total Elected Member's remuneration	\$580,915

This cost needs to be compared with the elected member's remuneration cost already determined for an Otorohanga and Waitomo reorganisation and what the Waipa cost is taking into account the HSC formula.

The remuneration for a reorganised Otorohanga and Waitomo council has been determined at \$271,950.

Waipa advise their remuneration pool, under the new HSC formula, will be \$415,128 (HSC \$340,128 + \$75,000) including Community Board remuneration and Hearing and Iwi Committee fees.

The \$271,950 and \$415,128 together equal \$687,078. This means a saving of \$106,163 (\$687,078 - \$580,915).

Elected members expenses are in addition to their remuneration and savings have been assessed as follows:

Mayor and Council Members Travelling Expenses

The estimated cost for an Otorohanga and Waitomo reorganisation was \$13,500. While the Otorohanga/Waitomo Council would disappear there would be some additional travel expenses associated with some members of the new Otorohanga, Waitomo and Waipa Council. We have estimated that approximately 50% would be saved, say \$6,000.

Conference & Zone Expenses

The estimated cost for an Otorohanga and Waitomo reorganisation was \$7,000. This cost would be saved on an Otorohanga, Waitomo and Waipa reorganisation.

Local Government New Zealand

The estimated cost for an Otorohanga and Waitomo reorganisation was \$30,000. We estimate that \$25,000 of this would be saved on an Otorohanga, Waitomo and Waipa reorganisation.

Printing & Stationery/Newsletter

The estimated cost for an Otorohanga and Waitomo reorganisation was \$18,000. There would be efficiencies as a result of not having to prepare two versions of newsletters and also a larger print run for each newsletter. A saving in the order of \$5,000 is assumed.

Te Awamutu Community Board and Cambridge Community Board expenses

These expenses are not significant and would change little on reorganisation.

Sundry Expenses

The estimated cost for an Otorohanga and Waitomo reorganisation was \$20,000. We estimate that these costs would be saved on an Otorohanga, Waitomo and Waipa reorganisation.

Election Expenses and Councilor Training/Induction

Triennial elections have a significant cost, along with Council training and induction. These costs are accounted for in the year incurred although arguably they could be accounted for over the three-year period. The 2002/03 year is not an election year however it is appropriate to include an annual saving for these costs. The costs for Waitomo and Otorohanga are set out in section 6 and include \$51,000 for the election and \$16,000 for Councilor training and induction.

Much of the election cost (an estimated 80%) is directly related to the number of electors, which will not change on reorganisation. Therefore election cost savings will not be significant (\$51,000 @ 20%, over three years = \$3,400 per

year less \$1,700 already included as a saving in the Otorohanga and Waitomo reorganisation).

However with an Otorohanga, Waitomo and Waipa reorganisation most of the Induction/training costs would be saved (\$16,000 @ 80%, over three years = \$4,200 less \$2,000 already included as a saving in the Otorohanga and Waitomo reorganisation). The total annual saving would therefore be \$3,700.

Summary of savings in Governance Costs

	\$
Remuneration	106,000
Travelling Expenses	6,000
Conference & Zone Expenses	7,000
Local Government New Zealand	25,000
Printing & Stationery / Newsletter	5,000
Sundry Expenses	20,000
Induction/Training costs	4,000
Total Savings	<u>\$173,000</u>

ii. Information System Costs

Other Information System costs for Otorohanga and Waitomo amount to approximately \$200,000 including software costs, site and system support, contracts and leases, insurance, repairs and maintenance, electronic data capture and internet/website.

We estimated that by running common systems these costs might reduce by 25% on reorganisation of Waitomo and Otorohanga. On reorganisation of Otorohanga, Waitomo and Waipa we estimate that a further 25%, or in the order of \$50,000 would be saved.

iii. Computer Costs

The requirement for computer terminals, servers and networking is directly related to the number of staff employed. Using the cost of funding depreciation for Waitomo for the 2002/03 year of \$85,000 as set out in section 6.reorganisation of Otorohanga, Waitomo and Waipa would see a reduction of staff 14 staff which would, using Waitomo's cost, result in a saving of approximately \$35,000 annually.

iv. Corporate Support Costs

In the Support Services and Finance and Administration areas of both Waitomo and Otorohanga there are a number of other direct costs that are likely to reduce as a result of further reorganisation with Waipa. These include:

	Waitomo	Otorohanga	Total
Audit	\$55,000	\$46,000	\$101,000
Legal Expenses	\$40,000	\$55,200	\$95,200

We have not considered whether there would be any savings of current Waipa costs.

Audit

The audit fee paid by Waipa is \$65,000, Otorohanga \$46,000 and Waitomo \$55,000. We estimated an audit fee for the combined Otorohanga and Waitomo Council of \$60,000. We estimate an audit fee for the Waipa/Otorohanga/Waitomo Council of \$95,000 and therefore a further saving in the order of \$30,000. (Current Waipa fee \$65,000 + estimated Otorohanga and Waitomo fee \$60,000 - estimated Waipa, Otorohanga and Waitomo fee \$95,000.)

Legal Expenses

Most of Otorohanga's legal costs result from the provision of in-house legal services (total direct costs \$47,000) while Waitomo's are sourced externally. External legal fees for Otorohanga are \$8,000 and Waitomo \$40,000.

On the basis that an in-house legal service is retained on reorganisation, we estimate a further cost saving in the order of 25% of the current Waitomo legal cost, or \$10,000.

v. Council Building - Otorohanga

The Commission has determined that for the basis of our review a reorganised Otorohanga, Waitomo and Waipa Council would be headquartered at Te Awamutu. Based on our estimates on a reorganisation of Otorohanga, Waitomo and Waipa approximately 40 positions would remain from the Otorohanga and Waitomo Councils. This is equivalent to the current Otorohanga staffing complement. Accordingly the costs associated with Otorohanga would remain, both at the existing building and in Te Kuiti, or split between Otorohanga, Te Kuiti and Te Awamutu.

In order to determine the accommodation savings associated with reducing positions by a further 14 we have taken the remaining costs associated with the Waitomo Administration Building, which would not all have been saved on an Otorohanga and Waitomo reorganisation as set out in section 6. These cost amount to \$22,000.

Additionally with a reduction of 14 further staff positions on an Otorohanga, Waitomo and Waipa reorganisation there would be other office equipment and furniture that could be sold. We have estimated additional sale proceeds of \$50,000.

vi. Other Savings

Reorganisation would create a larger organisation with theoretically greater purchasing power and potential for efficiencies. This should result in some cost

savings for consumable type expenditure including telephone and tolls, photocopying, subscriptions and publications, personnel management and appraisal which is primarily related to the number of staff.

Using Waitomo costs (approximately \$100,000) as a basis, we could not determine all of these costs from Otorohanga's Management Plan and Estimates, we have estimated additional savings of \$20,000.

vii. Transfund Subsidies for Roading

Reorganisation of Otorohanga, Waitomo and Waipa would have some impact on the level of roading subsidies received from Transfund. Discussions with Transfund indicate that the level of subsidy would reduce slightly in the event of a reorganisation. They estimate that based on the level of expenditure in the 2002/03 year the total reduction (over all three Councils) would have been approximately \$117,000, an additional cost of \$55,000.

viii. Staff Costs

Based on our discussions and analysis assessing an Otorohanga and Waitomo reorganisation, and our further discussions with Waipa District Council, we have estimated a reduction of a further 14 positions with an annual cost saving of \$920,000.

7.3 Transition Costs

The nature of transition costs are discussed in section 6.4. In the event of an Otorohanga, Waitomo and Waipa reorganisation, transition costs in addition to those set out in section 6.4 are likely to include:

Redundancy

On the basis of current employment conditions we have provided for redundancies on the basis of an average redundancy payment of 6 months pay for an additional 14 staff - \$400,000.

Redundancy support, recruitment and change management

\$100,000.

Financial Information

While both Waitomo and Otorohanga use the same financial system it is different to the system used by Waipa.

Strategy documents including LTFS (LTCCP), Funding Policy and Treasury Management Policy

Some work would be required to combine these documents in the short-term, with the major work being undertaken as part of a regular review.

Estimate for combining financial information, strategy documents including LTFS (LTCCP), Funding Policy and Treasury Management Policy and other records
\$150,000.

Combining District Plans

The reorganised district could operate three District Plans on a geographic basis until the normal five yearly review. The cost of then preparing one District Plan would be included in the five yearly review.

Aligning corporate, regulatory and environmental policies

Some immediate work would be required to align these policies. Estimated additional cost - \$25,000.

Rebranding

\$25,000

Miscellaneous capital expenditure

\$50,000

This is a PC sum to accommodate the reorganisation including electronically linking Otorohanga and Te Kuiti to Te Awamutu.

Summary of Additional Transition Costs

	\$
Redundancy	400,000
Redundancy support, recruitment & change management	100,000
Financial information, strategy documents & records	150,000
Corporate, regulatory and environmental policies	25,000
Rebranding	25,000
Miscellaneous capital expenditure	50,000
Contingency	50,000
Total	<u><u>\$800,000</u></u>

7.4 Total Estimated Savings

On an Otorohanga, Waitomo and Waipa reorganisation we have estimated that there would be the following cost savings (as detailed in sections 6 and 7):

	Otorohanga & Waitomo		Waipa Incremental		Otorohanga, Waitomo & Waipa	
	Positions	\$	Positions	\$	Positions	\$
Employee Costs	13	706,000	14	920,000	27	1,626,000
Other Costs						
Governance	-	133,000	-	173,000	-	306,000
Information System	-	50,000	-	50,000	-	100,000
Computer Costs	-	33,000	-	33,000	-	66,000
Audit	-	41,000	-	30,000	-	71,000
Legal	-	10,000	-	10,000	-	20,000
Admin Building	-	76,000	-	22,000	-	98,000
Other	-	20,000	-	20,000	-	40,000
Transfund Subsidies	-	(62,000)	-	(55,000)	-	(117,000)
Est Annual Savings	13	\$1,007,000	14	\$1,203,000	27	\$2,210,000
Est Transition Costs		\$600,000		\$800,000		\$1,400,000
Est Proceeds from Sale of Assets		\$450,000		\$50,000		\$500,000

Our summary of the savings for an Otorohanga, Waitomo and Waipa reorganisation is:

	Year 1	Subsequent years	PV 10 years	PV Perpetuity
Estimated annual savings	\$2,210,000	\$2,210,000	\$17,275,000	\$44,417,000
Sale of assets	500,000	-	477,000	477,000
Transition costs	(1,400,000)	-	(1,337,000)	(1,337,000)
Total	\$1,310,000	\$2,210,000	\$16,415,000	\$43,577,000
Per rateable property (24,664)	\$53	\$90	\$665	\$1,766

8. VIABILITY

The Commission asked us to include a high-level assessment of the current and likely future viability of the Otorohanga District Council and of the Waitomo District Council.

Our approach to this assessment has been twofold:

- Firstly to use publicly available financial and associated information to make an assessment of the current and future affordability of Council services, and
- Secondly to consider other information including information from Statistics New Zealand.

Set out in the Table 1 is information taken from the 2002/03 Annual Plans for the seven predominantly rural Councils in the Waikato Region. The table shows the level of rates and fees and charges levied, the operating surplus and the level of public debt for each Council.

This information is also shown on a per rateable property basis which the Councils have been ranked on.

Set out in Table 2 is the same information taken from Otorohanga and Waitomo's current Long Term Financial Strategies. It forecasts the level of rates, fees and charges levied, the projected operating surplus and the level of public debt for each Council for the subsequent ten years.

TABLE 1 - COMPARISON OF PREDOMINANTLY RURAL COUNCILS IN THE WAIKATO REGION

	Rateable Properties	Rates & Charges	Rates & Charges / Rateable Property	Rank	Projected Surplus	Projected Surplus / Rateable Property	Rank	Public Debt (Forecast 30/0/03)	Public Debt / Rateable Property	Rank
Waikato	16,277	\$26,228,000	\$1,611	6	\$6,666,000	\$410	7	\$3,735,000	\$229	6
Matamata Piako	11,486	18,808,000	1,637	5	382,000	33	2	922,000	80	7
Hauraki	8,355	15,291,000	1,830	1	1,202,000	144	3	1,950,000	233	5
South Waikato	9,546	14,136,000	1,481	7	2,266,000	237	5	6,658,000	697	4
Waitomo	4,497	7,984,000	1,775	2	(22,000)	(5)	1	11,628,000	2,586	1
Otorohanga	4,439	7,390,840	1,665	3	958,890	216	4	9,812,414	2,211	2
Waipa	15,728	25,940,000	1,649	4	4,836,000	307	6	24,376,000	1,550	3
Average	10,047	16,539,691	1,646		2,326,984	232		8,440,202	840	

Notes on Rates & Charges

Waikato - Includes General Rates (including UAGC), Separate Rates, Fees and Charges and Water by Meter

Matamata Piako - Includes General Rates, UAGC, Uniform Charges, Hall Rates and User Charges

Hauraki - Includes General Rates, Recoveries and Separate Rates less Roothing

South Waikato - Includes General Rates, Uniform General Charges, Rates & Charges and Fees & Charges

Waitomo - Includes Rates Income plus Fees and Charges

Otorohanga - Includes Rates Income plus User Fees and Charges

Waipa - Includes Rates plus Revenue less Roothing & Network Management and Support Services

TABLE 2 - INFORMATION FROM CURRENT LONG TERM FINANCIAL STRATEGY (\$'000)

Year end	Otorohanga						Waitomo					
	Rates & Charges	Rates & Charges per Rateable Property	Capex	Capex to Rateable Property	Public Debt	Public Debt to Rateable Property	Rates & Charges	Rates & Charges to Rateable Property	Capex	Capex to Rateable Property	Public Debt	Public Debt to Rateable Property
2003	7,391	1,665	4,212	949	9,812	2,210	9,394	2,089	4,098	911	15,496	3,446
2004	7,446	1,677	3,804	857	10,327	2,326	9,269	2,061	3,515	782	15,859	3,527
2005	7,383	1,663	3,574	805	11,051	2,489	9,280	2,064	3,143	699	15,748	3,502
2006	7,696	1,795	2,703	609	10,788	2,430	9,399	2,090	4,632	1,030	17,148	3,813
2007	7,904	1,781	4,287	966	11,230	2,530	9,373	2,084	4,086	909	18,685	4,155
2008	8,323	1,874	3,720	838	11,241	2,532	9,383	2,087	2,145	477	18,303	4,070
2009	8,385	1,889	2,995	675	10,491	2,363	9,402	2,091	2,158	479	17,953	3,992
2010	8,448	1,903	3,060	689	9,589	2,160	9,417	2,094	2,139	476	17,593	3,912
2011	8,498	1,914	3,063	690	8,724	1,965	9,381	2,086	2,133	474	17,267	3,840
2012	8,683	1,956	3,271	737	7,758	1,748						

Notes

Rateable Properties as per 2002/03 Annual Plan

Waitomo District

The Waitomo District has a population of 9,473, down 2.8% (New Zealand up 3.3%) on the 1996 census. Nearly 40% of the population are Maori (New Zealand 15%) and 26% of people earn over \$30,000 per annum (New Zealand 31%). Nearly 1,500 people (or 22% of people over 15) receive a government benefit (New Zealand 20%). 61% of private dwellings in the District are owned (New Zealand 68%). The majority of people in the District work in agricultural occupations.

Table 1 shows that of the seven predominantly rural Councils in the Waikato Region, the Waitomo District Council has, per rateable property:

- the second highest level of rates, fees and charges (\$1,775 v average \$1,646)
- the lowest operating surplus (\$5 loss v average \$232 surplus)
- the highest level of public debt (\$2,586 v average \$840)

Waitomo's current Long Term Financial Strategy includes the following comments:

- The small size of the District's rating base limits the options for economies of scale.
- Council must continue to look for the most cost-effective way to provide quality services.
- There is a need for substantial capital investment in deteriorating and aging infrastructural assets within rural communities, some of which have declining populations.
- The costs of providing essential services to some communities are beyond the affordability of residents.
- The community cannot afford rate increases beyond the level of inflation.
- Council has minimum capital reserves and, therefore, annual expenditure must be carefully planned and managed.
- Council can only afford to fund depreciation on what are considered to be essential assets.
- Total unfunded depreciation is approximately \$370,000 including \$130,000 for the Te Kuiti Cultural and Arts Centre.
- Te Waitere and Benneydale sanitation are subsidised by the remainder of the District.

Table 2 shows Waitomo's high level of rates, fees and charges per rateable property will continue to increase from \$1,775 and reach \$2,094 in 2010. This increase excludes the impact of inflation. The high level of public debt per rateable property will continue to increase from \$2,586 and reach \$4,155 in 2007.

The Waitomo Council continues to address their financial position and the affordability of rates, fees and charges. Initial estimates for the 2003/04 Annual Plan indicate that by giving further consideration to planned Piopio and Te Kuiti

sanitation upgrades, the level of rates and debt could be maintained close to current levels.

All indicators, financial and non-financial, show that the Waitomo District Council is already under considerable financial pressure. The District has a high level of rating, fees and charges, which are forecast to continue to increase. Future capital expenditure, and therefore public debt requirements, are significant. The economy of the District is based largely on the agricultural sector which has enjoyed reasonably buoyant times recently. A downturn in this sector, including the current pressure on farm commodity prices, will impact Waitomo's ability to raise the funds it requires. Waitomo's ability to generate reserves for contingencies and unexpected expenditure requirements is limited and will continue to be so. A continuing decline in population will also impact Council's ability to meet its revenue requirements.

Waitomo owns 100% of Inframax Construction Ltd which provides income of approximately \$600,000 annually. The market value of Inframax is estimated by the directors to be in excess of its net asset value, currently \$7.2 million. Realisation of this investment may improve the longer-term financial position of Waitomo.

Otorohanga District

The Otorohanga District has a population of 9,279, down 3.9% (New Zealand as a whole up 3.3%) on the 1996 census. Nearly 30% of the population are Maori (New Zealand 15%) and 28% of people earn over \$30,000 per annum (New Zealand 31%). Nearly 1,300 people (or 19% of people over 15) receive a government benefit (New Zealand 20%). 62% of private dwellings in the District are owned (New Zealand 68%). The majority of people in the District work in agricultural occupations.

Table 1 shows that of the seven predominantly rural Councils in the Waikato Region, the Otorohanga District Council has, per rateable property:

- the third highest level of rates, fees and charges (\$1,665 v average \$1,646)
- the third highest operating surplus (\$216 v average \$232)
- the second highest level of public debt (\$2,211 v average \$840)

Table 2 shows Otorohanga's reasonably high level of rates, fees and charges per rateable property will continue to increase from \$1,665 and reach \$1,956 in 2012. This increase excludes the impact of inflation. The high level of public debt per rateable property will continue to increase from \$2,211 and reach \$2,532 in 2008 before declining to be below the current by 2010.

The affordability of the forecast rate, fees and charges increases must be of concern to Council. With a high level of rates, fees and charges and public debt, Otorohanga's ability to meet its revenue requirements could be impacted by a downturn in the agricultural sector and a continued decline in population.

By all measures (population, rateable properties, assets and expenditure etc) both Otorohanga and Waitomo are small Councils. Both Councils have high rating, fees and charges, and public debt levels when compared with other predominantly rural Councils in the Waikato Region.

These key indicators are forecast to increase and together with declining populations and exposure to volatility of the agricultural sector will place pressure on their ability to generate the level of revenue they require and maintain service levels. Any savings that can be achieved through reorganisation, or any other means, will improve the ability of local government in the districts to meet ratepayer expectations.

9. CONCLUSION

Both Otorohanga and Waitomo are small Councils with high rates, fees and charges, and public debt levels when compared with other predominantly rural Councils in the Waikato Region. Any savings that can be achieved through reorganisation, or any other means, will improve the ability of local government in the districts to meet ratepayer expectations.

A Council's staffing levels determines employee costs which are the most significant component of indirect operating costs. A reorganisation will significantly impact indirect costs, generally through staff savings that arise through economies of scale, synergies of design and service delivery methods, and the operational efficiencies that can be achieved in a larger organisation.

As part of our high level review we have compared the staffing, expenditure and asset levels of the Councils in New Zealand with populations less than 20,000, a total of 25 Councils. On a population basis Waitomo and Otorohanga rank 11th and 12th smallest respectively of the 25 Councils in New Zealand with populations of less than 20,000. When considering the ratio of Council staff to population, expenditure and assets Waitomo ranks 4th best of the 25 Councils and Otorohanga only 19th best.

Adding the current Otorohanga and Waitomo Councils together produces a Council that would be ranked 2nd out of 24 on a population basis and 12th on the ratio of Council staff to population, expenditure and assets. However when comparing a combined Otorohanga and Waitomo Council with the ten largest Councils with populations of less than 20,000, Otorohanga and Waitomo would only rank 8th with 68 staff versus an average of close to 50. This indicates that a reorganisation of Otorohanga and Waitomo has the potential to reduce current staff numbers by 10 to 15 positions.

In 2002 both Otorohanga District Council and Waitomo District Council prepared their own estimates of the financial implications of a reorganisation. Otorohanga proposed a staffing complement of 63 versus the current combined staff of 68 while Waitomo proposed 48.

We have estimated that the financial implications of a an Otorohanga and Waitomo reorganisation would be:

Reduction in staff positions	13
Estimated annual savings – year 1	\$857,000
Estimated average annual savings per rateable property	\$96
Estimated annual savings – subsequent years	\$1,007,000
Estimated average annual savings per rateable property	\$113
Net present value of savings – for ten years	\$15,982,000
Average net present value per rateable property	\$1,788
Net present value of savings – in perpetuity	\$20,096,000
Average net present value per rateable property	\$2,248

Having completed our assessment of cost savings resulting from an Otorohanga and Waitomo reorganisation we used that as a base for determining the further impact of a reorganisation with Waipa. Our approach primarily involved considering the overall resources of the Waipa District Council and determining the resources that would need to be added from the Otorohanga and Waitomo District Councils, after reorganisation, to meet Otorohanga and Waitomo service requirements.

We have estimated that the financial implications of a an Otorohanga, Waitomo and Waipa reorganisation would be:

Reduction in staff positions	27
Estimated annual savings – year 1	\$1,310,000
Estimated average annual savings per rateable property	\$53
Estimated annual savings – subsequent years	\$2,210,000
Estimated average annual savings per rateable property	\$90
Net present value of savings – for ten years	\$17,275,000
Average net present value per rateable property	\$665
Net present value of savings – in perpetuity	\$43,577,000
Average net present value per rateable property	\$1,766

The savings we have identified for both options are primarily employee related, and only those that are obvious savings on a reorganisation. In practice it generally takes a major action such as a reorganisation, and resulting reengineering or restructuring, to achieve significant organisational savings. For example, Waitomo believe that based on their experience over several years a commercially managed reorganisation and associated restructuring could reduce the current combined staff of 68 to approximately 40. This would produce additional savings. Also, in our experience there would be additional savings from economies of scale and increased purchasing power for other expenditure.

Also, as discussed in section 4 we have not provided for any possible savings in the costs that will be incurred in the future to meet the requirements of the Local Government Act 2002. Accordingly we believe that the savings shown above are the minimum savings that would be achieved on reorganisation.

Based on the assumptions outlined in section 5 we believe that both options proposed by the Local Government Commission would provide significant financial benefits and are worthy of further investigation.

Accordingly we recommend that the Local Government Commission further investigate a reorganisation of Otorohanga and Waitomo on the basis of both proposed options. The preparation of a reorganisation scheme will require careful consideration of funding policies to provide for the equitable sharing of savings between the ratepayers in the existing Districts and for the funding of expenditure by those who benefit.