

28 October 2010

**Securing Efficiencies
from the
Reorganisation of
Local Governance in Auckland**

October 2010

Auckland Transition Agency

Disclaimer

This report has been prepared by Taylor Duignan Barry Limited (TDB) with care and diligence and the statements and opinions given by TDB in this report are given in good faith and in the belief that such statements and opinions are correct and not misleading. However, no responsibility is accepted by TDB or any of its officers, employees or agents for errors or omissions however arising in the preparation of this report or for any consequences of reliance on its content or conclusions. Any person or entity wishing to access our report or its conclusions should have the entire report made available to them.

This report is concerned with the potential efficiencies arising from reorganisation of local government in Auckland (Reorganisation). The report has been developed on the basis of information supplied to TDB by the Auckland Transition Agency (ATA), in particular the Planning Document (Plan) for the Auckland Council prepared by the ATA.

The ATA has developed an organisational structure for the new Auckland Council, made staff appointments and put in place financial reporting functions to support the new structure. The new management team has, in many cases, only recently been appointed and the new Council's approach regarding detailed efficiency plans will be developed after the new Auckland Council comes into force on 1 November 2010. Thus this report provides a high-level rather than a detailed analysis of the potential for efficiency gains beyond those already initiated by the ATA. This limitation should be taken into account when considering this report and implies that actual efficiencies achievable may differ materially from the estimates set out in this report.

Table of contents

1. EXECUTIVE SUMMARY	5
2. STRUCTURE OF THIS REPORT	9
3. AUCKLAND COUNCIL – CONTEXT	10
3.1 INTRODUCTION.....	10
3.2 FORMATION OF THE NEW AUCKLAND COUNCIL	10
3.3 AUCKLAND COUNCIL EXPENDITURE BY ACTIVITY	11
3.4 AUCKLAND COUNCIL EXPENDITURE BY MAJOR EXPENSE CATEGORY	11
3.5 PRELIMINARY ASSESSMENT OF EFFICIENCIES IN REPORT TO ROYAL COMMISSION ON AUCKLAND GOVERNANCE	12
3.6 CONCLUSION.....	14
4. EFFICIENCIES FROM THE AUCKLAND REORGANISATION	15
4.1 INTRODUCTION.....	15
4.2 DUPLICATION OF STAFFING	15
4.3 RATIONALISATION OF SOME ADMINISTRATIVE PROCESSES	16
4.4 EFFICIENCIES INITIATED BY THE ATA.....	16
4.5 FURTHER POTENTIAL EFFICIENCIES	18
4.6 CONCLUSION.....	20
5. MECHANISMS FOR SECURING EFFICIENCY GAINS AND ACHIEVING A HIGH-PRODUCTIVITY ORGANISATION	22
5.1 INTRODUCTION.....	22
5.2 STREAM 1: DELIVERING SERVICES AT LEAST COST	23
5.3 STREAM 1: PHASE 2 - GENERIC APPROACHES TO COST REDUCTION	24
5.4 STREAM 1: PHASE 3 - TARGETED REVIEWS OF COST EFFECTIVENESS	24
6. STREAM 1: CHANGES IN BUSINESS PROCESSES, SUPPORT FUNCTIONS AND PROCUREMENT	26
6.1 INTRODUCTION.....	26
6.2 GERSHON REVIEW.....	26
6.3 NEW SOUTH WALES SHARED SERVICES REFORMS 2010	26
6.4 SIMPLIFICATION/STANDARDISATION OF BUSINESS PRACTICES.....	27
6.5 PROCUREMENT.....	27
6.6 CONCLUSION.....	28
7. STREAM 1: GAINS FROM ENHANCED ASSET MANAGEMENT PRACTICES	29
7.1 INTRODUCTION.....	29
7.2 ACHIEVING BETTER PERFORMANCE ACROSS THE ENTIRE PORTFOLIO	29
7.3 LAND AND BUILDINGS	30
7.4 RATIONALISATION OF PROPERTY FOR COUNCIL USE	30
7.5 RATIONALISATION OF IT SPEND	30
7.6 MAJOR CAPITAL PROJECTS	31
7.7 OUTSOURCING/PROCESS RE-ENGINEERING	32
7.8 CONCLUSION.....	32
8. STREAM 2: REVIEWING THE LEVEL AND QUALITY OF THE COUNCIL’S FUTURE ACTIVITIES	34
8.1 INTRODUCTION.....	34
8.2 REVIEWS TO REDUCE RISKS ON ALIGNMENT OF COUNCIL PRACTICES	34
8.3 UNITED KINGDOM EXPENDITURE REVIEW	35
8.4 NEW AND IMPROVED BUDGETARY PROCESSES	35
8.5 BENCHMARKING/MEDIUM TERM TARGETS	36
8.6 CONCLUSIONS	36
9. GOVERNANCE PROCESSES TO SUPPORT ACHIEVEMENT OF A HIGH PRODUCTIVITY AND EFFICIENT COUNCIL	37

9.1 INTRODUCTION.....37
9.2 ALIGNED MOTIVATION AND INCENTIVES37
9.3 CLEAR GOALS.....37
9.4 CLOSE COOPERATION BETWEEN MAJOR STAKEHOLDERS38
9.5 EMPOWERED CHANGE AGENTS38
9.6 BENEFITS REALISATION PLAN.....38
9.7 EFFECTIVE COMMUNICATION38
9.8 CONCLUSION.....39

1. Executive summary

This report has been prepared for the Auckland Transition Agency (ATA) by Taylor Duignan Barry Limited (TDB) to assist the new Auckland Council in the process of securing efficiencies arising from the reorganisation of local governance in Auckland (Reorganisation). The report reviews the progress made in achieving efficiencies against earlier estimates¹ and analyses further opportunities, the processes for achieving them and the associated risks.

The first phase of the transition is now complete. The ATA has established the organisational “architecture” of the new Auckland Council, hired a senior management team and installed financial, information communications technology (ICT) and other systems to support the Auckland Council’s operations. Additionally, the ATA has designed and populated six new Council-Controlled Organisations (CCOs) which are subsidiaries of the Auckland Council and will play critical roles in providing social, economic, environmental and cultural services to Auckland’s communities. The ATA had a very compressed timeframe of around 16 months in which to plan and manage the transition and its brief did not extend to a fundamental review of business processes, policies or the nature of the services provided by the Auckland councils.

In undertaking the Reorganisation, the ATA has had to ensure that the local government organisations maintained service levels while at the same time, in establishing the new structures, the duplication of management and supervisory positions has been minimised and some processes have been rationalised.

The ATA, in developing and staffing the new organisation, has initiated efficiencies resulting in some \$95M p.a. in savings from the Reorganisation – around \$75M of which will be realised in 2011/12 with the full \$95M p.a. being realised from 2012/13 onwards. These efficiencies comprise staff expense savings of \$91M p.a. and savings from removal of duplicated services of around \$4M p.a. The efficiencies captured by the ATA are in line with the “Medium” assessed level of total efficiency gains in our 2009 Report of \$95M p.a. (see footnote 1). Furthermore, these savings will be fully delivered by 1 July 2012, whereas our 2009 Report assumed the assessed level of efficiencies would not be fully delivered until 1 January 2015.

As required by its empowering legislation, the ATA has prepared a Planning Document (Plan) which will be the initial Long Term Plan (2010 to 2019) of the Auckland Council when it comes into operation on 1 November 2010. The Plan is a consolidation of the various plans of the former city, regional and district councils being replaced by the Auckland Council, adjusted to take account of the new organisational structure and rationalisation of some processes by the ATA.

¹ In February 2009, TDB prepared a financial analysis (2009 Report) for the Royal Commission on Auckland Governance of the Commission’s preferred option for reorganisation of the eight councils in the area now constituting the Auckland Council region (the Auckland councils), including an evaluation of the efficiencies achievable from the Reorganisation. Overall, the indicative range of total efficiency gains were estimated to lie in the range of \$76M p.a. to \$113M p.a. which represented approximately 2.5% – 3.5% of the total expenditure the Auckland councils planned for 2008/09 (of around \$3.2B).

Among the other factors influencing the Plan forecast are the spending priorities of the former councils, the costs and savings associated with the transition, council projects timed to coincide with the 2011 Rugby World Cup (RWC), the establishment of 21 local boards, weathertightness provisions and inflation.

The Plan² incorporates the savings arising from efficiencies initiated by the ATA which as noted above total \$95M p.a. with \$75M to be realised in 2011/12. In addition to these efficiencies, the Plan also incorporates achievement of further reductions in Council funded operating expenditure (OPEX) of some \$47M in 2011/12. These reductions are to be achieved by efficiencies/cost savings over and above those initiated by the ATA. Thus the Plan is based on expenditure reductions, compared to the plans of the previous councils, of \$122M in 2011/12, \$47M being additional to the savings initiated by the ATA.

The \$47M further expenditure reduction reflects the ATA's assessment of the additional cost savings that the Auckland Council could be expected to realise in 2011/12. The efficiencies to achieve this amount of savings have yet to be specifically identified and implemented. The ATA believes that in part this global estimate of savings could be achieved by applying; tighter budgeting, removal of duplicated costs and as a result of OPEX being lower than forecast due to actual capital expenditure (CAPEX) after 1 November 2010 being lower than planned. (We discuss how budget caps can be used to promote efficiencies in section 5.3 of this report.)

The Plan provides for a rate increase for 2011/2012 of 3.9%. The plans of the previous eight councils when consolidated without taking into account efficiencies initiated or planned by the ATA, would have required a weighted average rate increase of 6.0% for 2011/12. Thus the forecast rates requirement for 2011/2012 is reduced by 2.1% as a result of the Reorganisation³ efficiencies incorporated in the Plan, net of transition costs, weathertightness provisions and costs associated with the RWC etc. This is not however a full reflection of the efficiencies achieved by the Reorganisation for a further reason, since in addition to a lower rates level, regulatory fees and water charges have been reduced compared to the plans of the previous councils. The impact of the gross level of efficiencies initiated by the ATA (that is before transition costs) would, all other things being equal, have reduced the rates bill in 2011/12 by around 5%.

The ATA did not in general introduce changes in procurement and business processes since it largely carried over to the new organisation the arrangements under which the previous councils operated. Changes in these areas could be expected to deliver significant efficiencies. From 1 November 2010 the achievement of such efficiencies will be the responsibility of the new Auckland Council itself.

Although the forecast 3.9% rates increase is lower than the average increase projected by the previous Auckland councils, this report identifies ways in which further efficiencies over and above those initiated by the ATA could be sought by the Auckland Council. We discuss the opportunities in terms of two streams of activity where Stream 1 pursues efficiencies in the cost of providing services while Stream 2 supports the Council's review of the levels of services to be provided and the extent of user charges.

² As provided to TDB as at the date of this report.

³ Including the \$47M of additional savings in OPEX for 2011/12.

Within Stream 1, we suggest the next phase of work (Phase 2 since the ATA has undertaken phase 1) would be to identify potential savings from aspects of alignment and standardisation, thus reaping benefits from increased scale. Phase 2 would also involve developing benchmark and cost information that would inform what we describe as Phase 3 work where best practice business systems are implemented and systems are significantly re-engineered. Stream 2 - the Council's decisions on service levels and user-charge financing - will interact with the Stream 1 phases, connecting choices and options for service delivery with business redesign.

As analysed in section 4.5 of this report, TDB believes that there is an opportunity to secure significant additional efficiencies over and above those initiated by the ATA. Since saving in procurement and those relating to property relate to CAPEX as well as to OPEX our estimates of savings in this and our 2009 Report cover both forms of expenditure. The estimate in our 2009 Report, adjusted to exclude those efficiencies that the ATA has already initiated, implies the further opportunities for efficiencies should deliver savings indicatively in the range of \$80M p.a. to \$100M p.a. progressively achievable over the short to medium term. The \$47M savings in 2011/12 incorporated in the Plan are to be obtained from these further opportunities for efficiencies over and above those already initiated by the ATA.

The opportunities include:

- savings in “on-costs” following staff reductions – including office accommodation expenses, office supplies and furniture requirements;
- further efficiencies in procurement – through consolidation of buying power and formalizing and managing supplier relationships;
- enhanced asset management practices in terms of managing and programming CAPEX within the Council and its CCOs;⁴
- further streamlining of business processes – simplification and standardisation of business processes;
- rationalisation and consolidation of the property portfolio – enhancing the returns and disposal of properties no longer required for Council's purposes;
- online servicing of customers' needs; and
- other efficiencies, including for example, those arising from a consolidation of the treasury function.

Achievement of these potential efficiencies would require detailed investigation and ownership by the relevant business units that need to implement programs to realise them. A detailed and resourced benefit realisation plan would be required to quantify when the efficiencies would accrue including accounting for any costs of implementation. We expect that realisation of most of these savings could be completed within 3 to 5 years from 1 November 2010.

⁴ The new Auckland Council is estimated to have a total of \$29.5B in non-current assets by 2011/12, comprised primarily of some \$11B in property, plant and equipment and a further \$17B investment in subsidiaries. Efficiencies are being achieved through the establishment of six substantive CCOs and CAPEX and OPEX savings are expected as the number of legacy IT systems are rationalised, albeit that there may be up-front investments to achieve this, including parallel running of systems.

If savings of \$80M p.a. to \$100M p.a., including CAPEX and OPEX savings, are made over and above the \$95M p.a. in savings from efficiencies initiated by the ATA, the total annualised savings would be \$175M p.a. to \$195M p.a. over the medium term. These are estimates of efficiencies arising from the amalgamation of the previous councils and overall opportunities for efficiencies are likely to be significantly larger than this estimate if efficiencies additional to those related to amalgamation are pursued.

The potential savings of \$175M p.a. to \$195M p.a. is a gross amount before taking into account any offsetting costs incurred in achieving these savings. On a gross basis, the savings would equate to around 10-11%⁵ of the rates bill that might otherwise have applied for 2015/16. The extent to which this overall potential gross saving from the Reorganisation of the Auckland region councils is reflected in lower rates than would have applied without the Reorganisation would depend on the extent to which the savings manifest themselves as lower user charges or are offset by decisions to increase expenditure on; enhanced service levels, new services or to accelerate other capital works.⁶

In summary, the Reorganisation provides an opportunity for the new Auckland Council to critically review what the Council should best do and how it can best do it. Achieving sustainable gains in efficiency is likely to require a multi-pronged strategy as outlined in Phase 3 of Stream 1 (best practice service models are identified and implemented) and Stream 2 (reviewing the level and quality of future activities). The need for such reviews is magnified as the new Auckland Council considers potential alignment of service levels, remuneration, user charges and rating bases across the Auckland Region - since this process has the potential to result in significant cost or rate increases if not carefully managed.

In our experience, the key measures to secure enhanced performance are likely to involve a combination of; strong leadership, empowering the right people, improved processes and a clear medium-term financial strategy involving commitments to constraints on increases in the levels of rates and debt over time. Most important will be maintaining the credibility of the Council as it drives for greater efficiencies across the services it delivers to the community.

⁵ Total rates funding in 2015/16 of \$1.65B per Plan, Volume 5, page 11, adjusted to reflect the efficiencies already incorporated in the forecast.

⁶ It will also depend on the level of associated restructuring expenses and their treatment in terms of the revenue and funding policies adopted by the new Auckland Council.

2. Structure of this report

This report is structured as follows:

Section 3 provides background on the formation of the new Auckland Council and the planned expenditure by activity and major expense category, in order to provide a context for assessing potential efficiency gains. It also summarises our preliminary estimates of efficiencies provided to the Royal Commission on Auckland Governance;

Section 4 outlines the Reorganisation activities undertaken by the ATA and resultant efficiencies which have been incorporated in the Auckland Council's 2011/12 budgeted expenditure. It examines the potential for further efficiencies and the impact on the level of rates;

Section 5 discusses potential mechanisms for achieving efficiency gains by the new Auckland Council drawing on New Zealand and offshore experience of efficiency programs in the public sector;

Section 6 discusses ways of pursuing efficiencies through changes to business processes and procurement;

Section 7 outlines mechanisms to enhance asset management practices;

Section 8 outlines the need to consider reviews of the activities undertaken by the new Auckland Council, including mitigating the risks around the alignment of service levels and charging across the region. The UK experience is referenced, together with budgetary processes and the role of medium-term targets; and

Section 9 identifies governance and other processes that the new Auckland Council could adopt to approve and monitor efficiency programs.

3. Auckland Council – context

3.1 Introduction

This section outlines the process underlying the formation of the Auckland Council and provides context for subsequent analysis by outlining the planned level and patterns of expenditure. This section concludes by summarising the assessment undertaken by TDB of the preferred option of the Royal Commission on Auckland Governance (the Commission) on reform of local government in Auckland.

3.2 Formation of the new Auckland Council

In 2007, the government established the Commission to examine governance arrangements in the Auckland Region. Following release of its findings in March 2009, the government decided to disestablish the existing city, district and regional councils and replace them with a single local authority – the new Auckland Council. The Auckland Council was established pursuant to the Local Government (Tamaki Makaurau Reorganisation) Act 2009 (Act) which provided for reorganisation of local governance in Auckland (Reorganisation).

The new Auckland Council comes into existence on 1 November 2010, following local body elections that were held on 9 October 2010. It replaces the previous eight local authorities of the Auckland Region including the; Auckland City Council, Auckland Regional Council, Franklin District Council, Manukau City Council, North Shore City Council, Papakura District Council, Rodney District Council and Waitakere City Council.

The Act established the Auckland Transition Agency (ATA or the Transition Agency) “to plan and manage all matters in relation to the reorganisation to ensure that the Auckland Council is ready to function on and from 1 November 2010.”⁷

The ATA is required to compile a Planning Document (Plan) that consolidates the various plans of the former regional, city and district councils being replaced by the Auckland Council. Once the Plan has been completed, the law requires the ATA to hand it to the Auckland Council by 31 October 2010.

The ATA has commissioned TDB to prepare this report which is to be handed over to the Auckland Council along with the Plan. The purpose of this report is to assist the new Auckland Council in securing the potential efficiencies arising from Reorganisation of the eight councils in the Auckland region – i.e., efficiencies beyond those already captured by the ATA.

⁷ s13(1)(a) of the Act.
www.tdb.co.nz

3.3 Auckland Council expenditure by activity

The following table⁸ depicts planned OPEX by activities funded by the Auckland Council for 2011/12. It therefore includes expenditure undertaken by CCOs only where the OPEX is funded from the Auckland Council (via operating grants):

Table 1: Auckland Council expenditure in 2011/12 by activity

	Plan 2011/2012 \$M	Plan 2011/2012 % total
Activity		
Community	210	11.8
Lifestyle and culture	422	23.6
Economic development	61	3.4
Planning and regulation	314	17.6
Environmental management	50	2.8
Solid waste	93	5.2
Water supply and wastewater	133	7.5
Stormwater	112	6.3
Transport	328	18.4
Commercial activities	17	1.0
Governance	45	2.5
Total cost of service	1,785	100.0

Provision of community, lifestyle and cultural facilities and planning/regulation activities together account for around 50% of the total planned OPEX funded by the Auckland Council in 2011/12 of \$1.8B.

These activities represent around 70% of the OPEX directly undertaken by the Auckland Council i.e. when OPEX relating to water and wastewater supply and transport are excluded, on the basis that these mostly represent transfers to CCOs.

3.4 Auckland Council Expenditure by major expense category

3.4.1 Operating expenditure (OPEX)

OPEX planned by the Auckland Council for 2011/12 is shown disaggregated by major expense category in the table below.⁹ The table includes the expenditure undertaken by CCOs which is funded by Council:

⁸ Plan: Volume 5, page 10.

⁹ Plan: Volume 5, page 15.

Table 2: Auckland Council expenditure in 2011/12 by expense category

	Plan 2011/2012	Plan 2011/2012
	\$M	% total
Employee benefits	422	23.3
Depreciation and amortisation	201	11.1
Finance costs	203	11.2
Other expenses	985	54.4
Total operating expenditure	1,811	100.0

It is assumed that interest payments and depreciation (comprising some 22% of OPEX) which reflect past CAPEX cannot be directly reduced by efficiencies resulting from the Reorganisation¹⁰ (although in the longer term the Reorganisation may influence depreciation and interest costs). Therefore these costs are separated from the remaining expenses which are potentially “amenable” to efficiency gains. Up to 78% of the Auckland council’s OPEX (which totals \$1.4B p.a. in 2011/12) could be influenced by efficiencies resulting from the Reorganisation. The Plan incorporates efficiencies initiated and planned by the ATA.

3.4.2 Capital expenditure (CAPEX)

Gross CAPEX incurred by the Auckland Council Group is planned to total \$1.4B in 2011/12, and to reduce to around \$1.2B in each of the subsequent 7 years. CAPEX funded by the Council is forecast to be around \$800M in 2011/12.

3.5 Preliminary assessment of efficiencies in report to Royal Commission on Auckland Governance

In February 2009, TDB prepared a report¹² (2009 Report) for the Commission in order to provide a preliminary financial analysis of the Commission’s preferred option¹³ for re-organisation of the eight councils in the Auckland region. This analysis included an evaluation of the efficiencies achievable from the re-organisation¹⁴. The financial analysis was based on the Auckland councils’ 2008 Annual Plans and on the levels and patterns of expenditure planned for the 2008/09 financial year.

¹⁰ These costs can be reduced by changes in the policies of the Auckland Council in the future, including decisions on the level and timing of CAPEX and on funding policies for CAPEX.

¹² “Financial Analysis: Re-organisation of the Councils in the Auckland Region,” 9 February 2009.

¹³ The Commission’s preferred option was based on the creation of a unitary Auckland Council which would undertake regional planning and infrastructure planning and delivery (except local roading). Six subsidiary local councils would have provided local service delivery including management of local roads, community assets and the processing of planning applications and performance of certain regulatory functions.

¹⁴ An efficiency gain arises from the reduction in the costs of producing the same level of goods or services.

In assessing the level of potential efficiency gains, TDB based its analysis on the following assumptions:

- sector reports for the water and wastewater industry where estimates of efficiency gains had been made;
- for procurement, savings of 5% of the relevant expenditures;
- for those functions to which a unified service delivery environment could be applied, efficiencies of 10%-15% of the relevant expenditures;
- only 80% of the assessed potential level of efficiencies were incorporated into our analysis on the basis that a focus on the highest value opportunities would increase the probability of them being captured; and
- a high quality implementation.

With respect to the Commission’s preferred option, the indicative range of annual assessed efficiency gains when fully realised were as follows:

Table 3: TDB’s analysis of the Commission’s preferred option for reorganisation of Auckland Local Governance

Commission’s preferred option indicative range of efficiency gains	Low	High	Medium
	\$M p.a.	\$M p.a.	\$M p.a.
CAPEX efficiency gains	22	37	30
OPEX efficiency gains	54	77	65
Total efficiency gains	76	113	95

Overall, the indicative range of total efficiency gains were estimated to lie in the range of \$76M p.a. to \$113M p.a. when fully realised, which represented approximately 2.5% – 3.5% of the total expenditure of the Auckland councils planned for 2008/09 (of around \$3.2B). The indicative level of CAPEX efficiency gains was estimated to be in the range of \$22M p.a. to \$37M p.a. which represented approximately 2-3% of the total CAPEX (of almost \$1.3B) planned by the Auckland councils for 2008/09. The indicative level of OPEX efficiency gains were estimated to be in the range of \$54M p.a. to \$77M p.a., which would have represented approximately 3-4% of the total OPEX (of almost \$2B) planned by the Auckland councils for 2008/09.

The reorganisation efficiencies were assumed to be progressively realised from 1 January 2012 through to 1 January 2015 when they would be fully realised.

As will be outlined in the following section 4, the Reorganisation subsequently approved by government made two changes to the Commission’s preferred option that materially increased the level and enhanced the speed with which the potential efficiencies could be achieved.

3.6 Conclusion

The ATA has commissioned TDB to prepare this Report which is to be handed over to the Auckland Council along with the Plan. The purpose of this Report is to assist the new Auckland Council in securing the potential efficiencies arising from Reorganisation of the eight councils in the Auckland region, beyond those already initiated by the ATA.

Up to 78% of the Auckland Council's OPEX of \$1.4B p.a. in 2011/12 could be influenced by efficiencies resulting from the Reorganisation. Gross CAPEX incurred by the Auckland Council Group is planned to total \$1.4B in 2011/12, and to reduce to around \$1.2B in each of the subsequent 7 years.

In our 2009 Report, TDB's preliminary estimate of the efficiencies potentially available from a high quality reorganisation of the eight Auckland councils ranged from \$76M p.a. to \$113M p.a. when fully realised.

4. Efficiencies from the Auckland reorganisation

4.1 Introduction

This section reviews the efficiencies secured by the ATA - principally relating to removing duplication of staffing positions and secondarily to removing duplication of administrative requirements - and compares this to TDB's assessment of potential efficiencies provided in our 2009 Report. This section also explores the opportunities for efficiencies in addition to those initiated by the ATA and the potential implications for the level of rates revenue required by the new Auckland Council.

The key task of the ATA was to ensure that the Auckland Council was ready to function from 1 November 2010. This included the requirement to develop an organisational structure and plan to manage the transition of assets and staff from the constituent local government organisations to give effect to the new local governance arrangements for Auckland.¹⁵ In exercising its powers, a requirement on the ATA has been that "key local government projects in Auckland are not to (be) hindered or interrupted."¹⁶ The ATA had an extremely compressed timeframe of around 16 months in which to plan and manage the transition and its brief did not extend to a fundamental review of business processes, policies or the nature of the services provided by the Auckland councils. It did however secure significant efficiencies in undertaking the Reorganisation.

4.2 Duplication of staffing

On 28 September 2010, the ATA announced the number of staff who will be employed by the new Auckland Council, as follows:

- the number of staff working for the current councils and their subsidiaries is reducing from 9,430 full-time equivalent employees (FTEs) 12 months ago to 8,207 by 1 November 2010. That is a reduction of 1,223 FTEs – or around 13%;
- the number of employees will fall further in the months that follow, taking the 'business as usual' size of the organisation to 7,907 FTEs by 1 July 2012. That is a total reduction of 1,523 employees – or around 16%;
- the annual wage bill for the Auckland Council will fall from \$604M p.a. (at 1 November 2009) to \$537.5M p.a. at 1 November 2010 – a reduction of \$66.5 M p.a.; and
- the numbers employed will further reduce as some 300 FTEs on transition-related and project work leave the organisation, leaving an annual salary bill of \$513M by 1 July 2012 – or a reduction of \$91M p.a. on 2009's figures.

¹⁵ 13(2)(a) and(b) of the Act.

¹⁶ 13(3)(c) of the Act.

The planned total reduction of 1,523 FTEs by 1 July 2012 has been achieved through elimination of duplicated positions, rather than as the result of changes in business practices. Almost all of the reduction to date has occurred in managerial/supervisory positions – with the 1,187 reduction in FTEs at these levels representing almost 60% of the total Tier 1 through Tier 4 positions (FTEs) existing as at 1 November 2009. The overall number of employees at Tier 5 and lower (largely “front-line” or public-facing staff, for example in customer service roles) have remained virtually unchanged - at around 7,400 FTEs.

Given that the reduction in the number of staff on transition-related and project work will occur progressively throughout 2011/12 and is weighted toward the end of the financial year, staff efficiencies initiated by the ATA are expected to yield OPEX savings of around \$71M in 2011/12.

There will also be further substantial savings in; office accommodation, office supplies and furniture expenses as a consequence of the staff reductions. Section 7 discusses rationalisation of assets, including office accommodation.

4.3 Rationalisation of some administrative processes

Consistent with the dis-establishment of eight organisations and replacement with one entity, there are considerable direct savings in a number of specific administrative processes, including:

- one, rather than eight, Long-Term Council Community Plans (LTCCPs) need to be prepared, consulted on and printed;
- one audit process, albeit that it would involve a larger entity; and
- rationalisation of insurance providers, etc.

These efficiencies are estimated to amount to around \$4M p.a. which will be fully realised in 2011/12. Having regard to the \$71M in staff savings expected to be realised in 2011/12, total efficiencies initiated by the ATA are estimated to result in savings of \$75M in 2011/12.

In addition to these identified and initiated efficiencies, the ATA has provided for a further approximately \$47M p.a. of efficiency gains to be delivered by the new Auckland Council in the 2011/12 financial year. These efficiency gains have yet to be specifically identified and initiated. This matter is discussed in section 4.5.

4.4 Efficiencies initiated by the ATA.

The ATA has initiated plans that will yield efficiencies of some \$95M p.a. when fully realised, comprising personnel savings of \$91M p.a. and non-personnel savings of around \$4M p.a. These efficiencies relate solely to reductions in OPEX. Some \$75M p.a. of the total efficiencies will be realised in 2011/12 with the full \$95M p.a. being realised from 2012/13 onwards. The efficiencies initiated by the ATA under the Reorganisation compared to those assessed in our 2009 Report to arise from the structure proposed by the Commission are as follows:

- they are in line with the “Medium” assessed level of total efficiency gains of \$95M p.a.;
- exceed the “High” level of assumed efficiencies sourced from OPEX of \$77M p.a. by \$18M p.a.; and
- the gains are expected to be delivered in full by 1 July 2012, two-and-a-half years ahead of the assessed date of 1 January 2015.

Decisions by the government with respect to the Reorganisation contributed in part to increasing the level and accelerating the speed with which efficiencies could be achieved relative to the preferred option proposed by the Commission which was the basis for our 2009 Report:

- on the issue of the second-tier of local governance, the government decided to institute local boards rather than six local councils as proposed by the Commission. The significance of this is that the Reorganisation eliminates the need to retain the management support for separate local councils and replaces this with shared support for local boards, saving in overheads and enhancing the seamless provision of services by the Auckland Council; and
- in respect to timing, “the Government did not accept the Royal Commission’s recommendations that the rationalisation occur after October 2010. The 4-year implementation time frame was considered too long. Tolerance for change and disruption in Auckland will only last for a short time and implementation needs to proceed at a rapid pace”.¹⁷ This decision contributed to accelerating the attainment of efficiencies earlier than anticipated by the Commission and includes the establishment of six new council-controlled organisations ready to function as of 1 November 2010 rather than being established by the Auckland Council at some future stage as envisaged by the Commission.

The efficiencies initiated by the ATA relate primarily to staff savings, contributing \$91M p.a. of the total efficiencies of \$95M p.a. to be delivered in 2012/13. The analysis in our 2009 report did not focus on efficiencies by “line-item” (i.e. staff/other etc). Rather the focus was on an activity basis and whether shared services or procurement initiatives were likely to be the prime driver of potential efficiencies. Staff savings drive shared services and the Regulatory/Planning/Governance activities were considered to be the most amenable to shared services efficiencies. Efficiencies in these activities were assessed to be in the range of \$14M to \$28M p.a. These efficiencies compare to the \$91M p.a. in staff savings that the ATA plans to achieve in 2012/13.

¹⁷ Regulatory Impact Statement: Local Government (Auckland Reorganisation) Bill 35-1 (2009), Government Bill.

4.5 Further potential efficiencies

4.5.1 ATA has initiated substantial OPEX efficiencies regarding staffing

The ATA has initiated staff efficiencies of \$91M p.a. which are well in excess of that which was anticipated in our 2009 Report. On the other hand, much of the non-staffing efficiencies forecast in our 2009 Report are yet to be initiated. Given that it has only had 16 months to achieve the Reorganisation, compared to the four-year timeframe envisaged by the Commission, the ATA was not well placed to obtain much of these non-staffing efficiencies, since its prime responsibility was delivering an amalgamated organisation capable of maintaining business-as-usual services from 1 November 2010. Whilst the ATA did eliminate duplicated administrative costs, amounting to some \$4M p.a., the areas in which additional efficiencies can be sought include changes in business processes and in procurement where we would expect there to be substantial opportunity to achieve efficiencies.

4.5.2 Further efficiencies assumed

In the Plan, the ATA has provided for further savings to be realised by the new Auckland Council during 2011/12 of around \$47M in OPEX over and above the \$75M in savings attributable to efficiencies initiated by the ATA and deliverable in that year. The further savings are made up of three components:

- efficiencies from areas such as procurement and business processes where the ATA believes that the new Auckland Council might achieve and deliver in its first full year of operation. Whilst reductions in training and ACC costs have been removed in-line with the staff reductions, lower staffing levels have not yet been recognised in lower costs such as for; office accommodation, office supplies and furniture. We understand that early establishment of a team to identify further savings and productivity benefits has been identified as a priority by incoming management;
- savings that the ATA believes are achievable by applying tighter budgeting thereby eliminating built-in excess costs (specific costs have not been identified). In addition, there will be duplicated costs between the previous councils that will no longer be required. The elimination of such costs would not impact on the ability to deliver services; and
- the ATA has also identified that the Auckland councils have often underspent on CAPEX - because the capacity to deliver all the planned projects has typically been over-estimated. Delivering less CAPEX than planned would reduce the interest and depreciation expenses and the consequential OPEX in the year in which those assets would otherwise have been commissioned. The consequential reduction in rates of underspending on assets is understood to average around 14% of the cost of the assets that would otherwise have been commissioned. No information is available on the extent of underspending in CAPEX.

Savings from the latter two sources have not been quantified, but they would, to the extent achievable, reduce the level of further efficiencies that would otherwise be required to deliver the \$47M reduction in Auckland Council OPEX assumed in the Plan for 2011/12.

In terms of current council funding policies, any restructuring costs by way of OPEX are treated as expenditure in the year that they are incurred. Thus any restructuring expenses by way of OPEX incurred in 2011/12 to achieve efficiencies would therefore need to be offset by higher gross savings than \$47M in order to achieve the assumed net \$47M savings in expenditure.

4.5.3 Implications for the level of rates in 2011/12

The total rates requirement of the new Auckland Council of \$1.4B in 2011/12 is the outcome after applying the revenue and financing policies of the previous eight councils¹⁸. The average forecast rates rise in 2011/12 is 3.9%, being some 2.1% lower than the rates rise of 6.0% forecast by the previous councils¹⁹.

The ATA has initiated total efficiencies of \$95M p.a. to be fully delivered in 2012/13 onwards. Due to the buildup of savings during 2011/12 largely falling in the latter part of the year, the monetary savings for 2011/12 will be \$75M. This reduction in OPEX of \$75M in 2011/12²⁰ would, all other things being equal, have reduced the rates bill by up to 5%.²¹

As noted, the ATA has also provided for a global reduction in OPEX relating to targeted further, but as yet unidentified, efficiencies of some \$47M in 2011/12 in addition to the efficiencies initiated by the ATA itself.

Offsetting items which have added to expenditure in 2011/12 include funding transition costs, funding the mayoral office and local boards and the additional OPEX associated with the RWC. The latter item is estimated by the ATA to have increased rates by some 2% in 2011/12.

Expenditure in 2011/12 includes the cost of some 300 staff on transition-related and project work associated with the implementation of the Reorganisation with these costs being eliminated as the assignments are completed. This temporary, transition-related and project expenditure in 2011/12 equates to around 1.5% of rates revenue.

In the absence of the additional OPEX associated with the RWC and the temporary costs associated with transition-related and project work, the rates rise in 2011/12 could have been close to zero (assuming the \$47M of unspecified saving is achieved).

¹⁸ "Revenue and financing policy – this is based on the policies that were in place in the previous eight councils as at 1 July 2010. It reflects the legislative and reorganisation changes, including changes to regulatory fees, funding of transition costs and the new council-controlled organisation structure." Plan: Volume 5.

¹⁹ The rates rise is after accounting for growth in the ratepayer base - Plan, Volume 5.

²⁰ Having regard for the part-year impact of the reduction in transition-related contracting expenses.

²¹ Not all of the reduction in OPEX has been used to reduce rates – there have also been reductions in regulatory user charges.

4.5.4 Opportunity for attainment of further efficiencies

Our 2009 report assessed total efficiencies in the range of \$76M p.a. to \$113M p.a. once fully realised. Given that the shared services/staff savings contributed an estimated \$14M p.a. to \$28M p.a. of the total efficiencies - some \$62M p.a. to \$85M p.a. related to areas other than staff remuneration. These efficiencies are likely to be driven primarily by procurement efficiencies. Research from Deloitte which was presented by the Employers and Manufacturers Association to the Commission²² estimated that there could be \$91M p.a. in efficiencies from procurement savings. This suggests that most of the potential efficiencies envisaged in our 2009 Report, have yet to be achieved. Additional efficiencies could be derived from business process re-engineering and enhanced asset management practices, but we are not in a position to estimate these.

TDB believes that there is an opportunity to secure significant additional efficiencies over and above those initiated by the ATA. Since saving in procurement and those relating to property relate to CAPEX as well as to OPEX our estimates of savings in this and our previous report cover both forms of expenditure and indicatively range from \$80M p.a. to \$100M p.a.. These are estimates of efficiencies arising from the amalgamation of the previous councils and overall opportunities for efficiencies are likely to be significantly larger than this estimate if efficiencies additional to those related to amalgamation are pursued.

Achievement of these potential efficiencies would require detailed investigation and ownership by the relevant business units that need to implement programs to realise them. A detailed and resourced benefit realisation plan would be required to quantify when the efficiencies would accrue including accounting for any costs of implementation. We expect that realisation of most of these savings could be completed within 3 to 5 years from 1 November 2010.

4.6 Conclusion

Our 2009 Report included an evaluation of the efficiencies achievable from the re-organisation of local governance arrangements in Auckland. Overall, the indicative range of total efficiency gains were estimated to lie in the range of \$76M p.a. to \$113M p.a. which represented approximately 2.5% – 3.5% of the total expenditure of the Auckland councils planned for 2008/09 (of around \$3.2B).

The ATA has initiated some \$95M p.a. in efficiencies from Reorganisation of the eight councils – around \$75M of which will be realised in 2011/12 with the full \$95M p.a. being realised from 2012/13 onwards. The efficiencies initiated by the ATA are in line with the “Medium” assessed level of total efficiency gains in our 2009 Report of \$95M p.a. Furthermore, these savings will be fully realised by 1 July 2012, whereas our 2009 Report assumed the Medium level of efficiencies would not be fully realised until 1 January 2015.

TDB believes that there is an opportunity to secure significant additional efficiencies over and above those initiated by the ATA. Since saving in procurement and those relating to property relate to CAPEX as well as to OPEX our estimates of savings in this and our 2009 Report cover both forms of expenditure and indicatively range from \$80M p.a. to \$100M p.a..

²² Supplementary papers to the Commission “Financial benefits of consolidation”, 23 June 2008. Procurement efficiencies were based on Auckland councils’ 2007/08 Annual Plans and would approximate \$100M p.a. in 2011/12 having regard to inflation over the intervening four year period.

Achievement of these potential efficiencies would require detailed investigation and ownership by the relevant business units that need to implement programs to realise them. A detailed and resourced benefit realisation plan would be required to quantify when the efficiencies would accrue including accounting for any costs of implementation. We expect that realisation of most of these savings could be completed within 3 to 5 years from 1 November 2010.

If savings of \$80M p.a. to \$100M p.a., including CAPEX as well as OPEX savings, are made over and above the \$95M p.a. in savings from efficiencies initiated by the ATA, the total annualised savings would be \$175M p.a. to \$195M p.a. The potential savings of \$175M p.a. to \$195M p.a. is a gross amount before taking into account any offsetting costs incurred in achieving these savings. On a gross basis, the savings would equate to around 10-11%²³ of the rates bill that might otherwise have applied for 2015/16. The extent to which this overall potential gross saving from the Reorganisation of the Auckland region councils is reflected in lower rates than would have applied without the Reorganisation would depend on the extent to which the savings manifest themselves as lower user charges or are offset by decisions to increase expenditure on; enhanced service levels, new services or to accelerate other capital works.²⁴

These are estimates of efficiencies arising from the amalgamation of the previous councils and overall opportunities for efficiencies are likely to be significantly larger than this estimate if efficiencies additional to those related to amalgamation are pursued.

The extent to which the overall potential gross savings from the Reorganisation of the Auckland region councils is reflected in lower rates than would have been applied without the Reorganisation would depend on the extent to which the savings manifested themselves as either lower water or other user charges or lower borrowing requirements.²⁵

²³ Total rates funding in 2015/16 of \$1.65B per Plan, Volume 5, page 11, adjusted to reflect the efficiencies already incorporated in the forecast.

²⁴ It will also depend on the level of associated restructuring expenses and their treatment in terms of the revenue and funding policies adopted by the new Auckland Council. It is recognized that lower CAPEX levels would not directly reduce the rates requirement, but would, over time, reduce OPEX and therefore rates as a consequence of lower; interest, depreciation and operating costs.

²⁵ It will also depend on the level of associated restructuring expenses and their treatment in terms of the revenue and funding policies adopted by the new Auckland Council.

5. Mechanisms for securing efficiency gains and achieving a high-productivity organisation

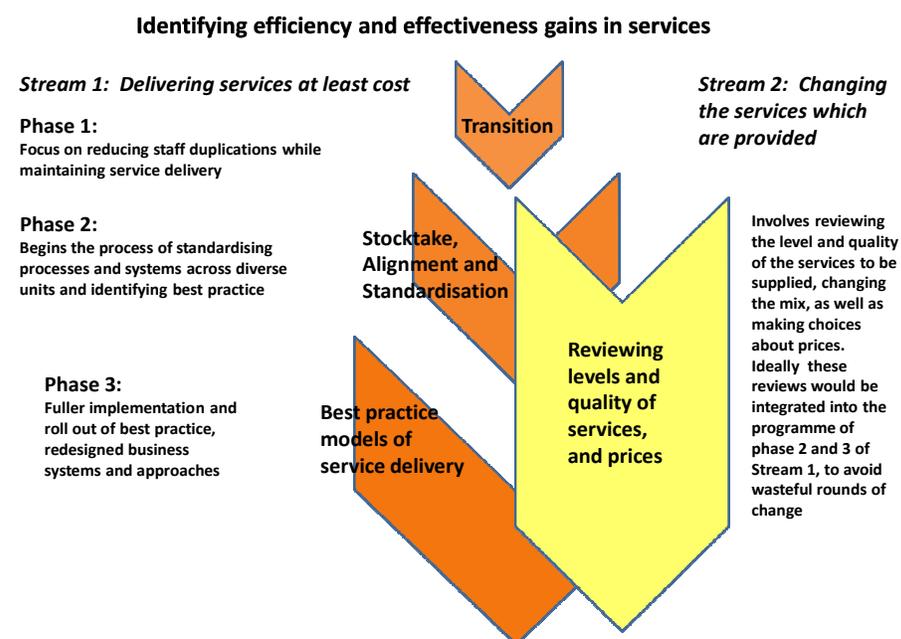
5.1 Introduction

The remainder of this report looks ahead: identifying areas and methods where further efficiency and effectiveness gains could be achieved. It builds on the work that the ATA has already initiated in the transition phase, where staffing and other costs have been reduced, delivering some \$95M p.a. in ongoing savings in 2012/13 onwards. We consider now the steps the Council could take to achieve ongoing efficiency gains and high performance levels across the new organisation.

Phase 1 in the reforms to establish a super-city involved the ATA moving to achieve efficiencies through the reorganisation process. It has generally left existing systems, processes and the attached resources in place across the joined-up service units.

Now that the Council is about to be formed we identify the further challenges and opportunities for the new Council as it seeks to achieve ongoing efficiency improvements across the region. As set out in the diagram below, they can be seen as involving two separate but closely interconnected streams of work:

Figure 1: Identifying efficiencies and effectiveness gains in services



- Stream 1: delivering services at least cost. The choices and tools are generally under Council executive control. The work can be categorised as fitting into two separate phases, where Phase 2 involves collecting information on the costs of the various components of the system that have been inherited, beginning to standardise processes and aligning key contracts and resources so that changes can be made. Phase 3 uses the cost and benchmarking information from Phase 2, along with other reviews and sources of best practice, to identify and then implement significant systems re-engineering.

- Stream 2: reviewing existing service quality, level and price to identify whether another service mix delivers preferred outcomes at lower cost. While some of the choices are within council management control, many of the options and trade-offs will require public choices to be made.

Streams 1 and 2 interact. Major investments in systems redesign should have some review under Stream 2 as well. We would expect a dynamic set of interactions to occur between the workstreams; not all business system redesign will need major reviews of service choices, nor should a whole set of sensible business improvements be interminably deferred while new options for service mix are discussed.

The next parts of this report firstly address Stream 1 issues, then Stream 2 issues, along with a summary section on more general lessons about the ways in which the streams can be governed so as to best deliver the desired outcomes.

5.2 Stream 1: delivering services at least cost

The ATA has made substantial progress during the Reorganisation process in streamlining the back-office functions of the former Auckland councils. The attention of the new Auckland Council could now turn to improving the efficiency of the front-line operations it inherits from its eight previous councils. Logically this can be tackled in two further phases (where Phase 1 has already been conducted by the ATA).

Phase 2: this would initially involve clearly understanding the cost of existing services and moving then to standardise and align activities. In many cases operations have been simply combined together, with differing operating rules (or even by-laws), different business processes and IT systems, staff employed on different remuneration regimes, differing degrees of contracting out - for core processes or reference to expert advice. In this phase small and quick opportunities for improvement would be made, as well as initial steps to start aligning key processes, identifying the crucial dates where systems change could most usefully occur (e.g. when external contracts run out or new IT investments are required). The core business information and its use in benchmarking - within units and across to similar activities carried out externally - would prepare the ground for Phase 3. This could take up to a further 18 months.

Phase 3: major opportunities for business system redesign would be identified on the basis of best practice models. Benchmarking information would be used to inform the business case for the new system/investment that may be required (or shift for instance to contracting out). The opportunities will generally not be able to be identified or exploited immediately, but should be addressed over the next 3-5 years. Work in this phase would need to be carried out in conjunction with Stream 2 where discussions over the desired service mix would take place.

The next section considers generic tools for cost reduction, while options for improving the efficiency of the Council's operations in specific areas such as procurement, business processes and asset management are discussed in sections 6 and 7 below.

5.3 Stream 1: Phase 2 - generic approaches to cost reduction

At the macro level, the Council's quest for efficiency gains could be made easier by establishing top-down, across-the-board targets. Such an approach is applied often in the public sector. The approach could involve setting an overall target for expenditure or expenditure growth rates across the organisation. The central government in New Zealand, for example, adopted such an approach in the late 1980s and early 1990s.

In the case of the Auckland Council, the Council could, for example, agree to maintain levels of expenditure constant in nominal levels for the next three years. With inflation projected to be around 2.5% p.a.²⁶ over the period, the Council's real level of expenditure would be reduced at a rate equal to the rate of inflation (i.e., by around 2.5% p.a.).

The above approach would not take into account population growth and an alternative would be to allow nominal expenditure to grow at the rate of population growth. In that case the Council's real per capita expenditure would be reduced at a rate equal to the rate of inflation. If the rates base (i.e. the revenue collected at constant nominal levels of rates) was growing in line with population growth then the reduction in real per capita expenditure would allow rates to be kept unchanged in nominal levels. Rate payers would benefit because their rates would remain the same dollar amount i.e. would fall in real terms.

Such a macro-level target, if it is credible and adhered to by the Council, could deliver substantial savings in the short term. With total Council funded spending on OPEX other than depreciation and interest of around \$1.4B p.a., efficiency gains of 2.5% p.a. would equate to on-going savings of around \$100M p.a. in nominal terms by the end of the three year period.

However, there are risks with such a macro-level approach. The expenditure constraints could be achieved by reducing service levels without any accompanying improvements in efficiency. Alternatively, the expenditure constraints may be accompanied by downgrades in the quality of the services. In addition, the expenditure targets could be achieved in ways that simply defer expenditure and lead to greater problems in the future (e.g., by deferring necessary expenditure on the maintenance of assets).

5.4 Stream 1: Phase 3 - targeted reviews of cost effectiveness

While top-down, across-the-board targets can deliver efficiency gains in the short term, more fundamental reforms are likely to be required to sustain the gains in efficiency over the longer term. A further lift can be achieved when substantial business process re-engineering occurs, and new models of service delivery are adopted.

As discussed more fully in a following section of this report, on Stream 2, before substantial investment is made in new systems and processes (often involving up-front investments), choices should be made on the levels and quality of service, utilizing the information base developed in the prior phase. The Auckland Council inherits a diverse range of service provision and of funding particularly the use of user charges between the areas covered by the eight previous councils and the Auckland Council will need to decide the extent and form of a move towards more uniform policies. There is tension between taking the time required to make well thought through decisions regarding moving to more uniform provision on the one hand and reforming how services are delivered on the other.

²⁶ The NZIER's latest consensus forecast for the inflation rate (CPI) for the period 2011/12 and 2012/13 is 2.6% p.a. Refer http://www.nzier.org.nz/Site/Publications/Consensus_forecasts.aspx.

Developing these changes and reforms requires focus and expertise. Without such reforms, addressed in the rest of this report, the underlying pressures for expenditure growth are likely to re-emerge quite quickly. For example, the areas that are subject to fiscal constraint are likely to find ways of getting around the constraints by a variety of different ways, such as loading additional expenditure into new spending proposals. They also may seek to shift costs to demand-driven areas of expenditure or to other areas that are outside the direct fiscal constraints (such as those areas funded directly by users).

6. Stream 1: changes in business processes, support functions and procurement

6.1 Introduction

Future changes in business processes, back-office support functions and procurement, could be expected to deliver significant efficiencies. This section examines the UK experience at achieving efficiencies in the public sector, draws on recent evidence used in New South Wales, and then addresses mechanisms and approaches whereby procurement efficiencies could be extracted.

6.2 Gershon Review

An example of efficiencies achieved in the public sector environment is the outcome of the “Independent Review of (the UK) Public Sector Efficiency – Releasing resources to the front line”, undertaken by Sir Peter Gershon (Gershon Review). Sir Peter was engaged by the UK government in August 2003 and his report above was published in July 2004. The report targetted cumulative efficiencies of STG 20B (7.5% of departmental expenditure limits) to be achieved during the three year period, 2005/06 through 2007/08. These targets were set having in mind the need to ensure that savings were not delivered at the expense of impacting on service delivery. The resultant efficiencies were to be “recycled’ to release resources for front line public service delivery – so this exercise was not used to reduce overall levels of expenditure.

The HM Treasury has subsequently reported that the Gershon Review resulted in assessed annual efficiency gains of STG 26.5B across the public sector - approximately 9.5B pounds of which (35% of the total) related to procurement and approximately 6.5B pounds of which (25% of the total) related to freeing up more productive time of front-line staff through IT investments. With respect to Local Government, the target level of efficiency savings over the three year period to 2007/08 of 6.5B pounds (a cumulative 7.5% efficiency gain) was exceeded – 8.2B pounds was recorded as having being achieved²⁷.

In its most recent Budget, the UK Government has announced that it proposes to achieve even further savings: “we have gone further than we thought possible in cutting back-office costs.....and the administrative budgets of every main government department cut by a third”²⁸.

6.3 New South Wales shared services reforms 2010

Amalgamation also provides opportunities for common approaches and systems across a range of corporate areas, achieving benefits beyond procurement and business system change. Over time, common systems and platforms can be developed and applied to HR, transaction processing (billing and booking), vehicles and fleet management and IT. Greater unit size allows the development of more specialised staff, potentially reducing the need for external consultancies, and enabling more efficient process optimisation. Property can be rationalised.

²⁷ 2004 Spending Review: final report on the efficiency programme,” HM Treasury, November 2008.

²⁸ 2010 Spending Review Speech, UK Chancellor Rt. Hon George Osborne, 20 October.

A recent study prepared for the New South Wales Department of Premier and Cabinet³⁰ quoted a review of 193 organisations in the public and private sectors which indicated that 61% had actually achieved savings of over 20% from shared services operations. But typically scale matters a lot in achieving savings, and even the new Council would be towards the lower end of size for the organisations covered so we would expect that benefits may not rise to the same level.

6.4 Simplification/standardisation of business practices

On-line servicing of consumers of Council services would not only unlock significant efficiency gains for the Auckland Council but also enhance the customer experience in that contact could be made when it suited the “client.” The Gershon Report noted that in the UK, “recent research carried out by Deloitte on behalf of OPDM concluded that universal implementation of e-procurement alone by all local authorities would secure savings of STG 1.1B pounds”.³¹

This e-procurement opportunity is maximised where underlying processes are simplified and rationalised. There is also a need to align the processes and systems across the Auckland Region. Alignment in terms of consistency of processing and outcome would have significant benefits in reducing the transactions and compliance costs of those interacting with the Auckland Council.

6.5 Procurement

6.5.1 Introduction

At least 50% of the Auckland Council’s OPEX relates to expenses other than remuneration, interest and depreciation – these total some \$1B p.a. based on Auckland Council funded expenditures alone. In addition, CAPEX funded by the Auckland Council totals some \$0.8B p.a. A global survey of mergers and acquisitions undertaken by Booz-Allen & Hamilton³² reports procurement savings ranging from 3 to 5%, rising to 20 to 25% dependent on the cost category. This section outlines how these efficiencies might be secured.

6.5.2 Formation of Consolidated Purchasing Group (CPG)

The ATA has developed a procurement service delivery model to be deployed by the new Auckland Council which includes the establishment of a CPG. This Group will have ownership of leadership activities to provide guidance, direction and support for procurement execution and monitoring activities to ensure compliance with the procurement guidelines. The degree of ownership for other procurement activities will be dependent on category and based on:

³⁰ July 2010:

http://www.gcio.nsw.gov.au/100715_Blue_Print_for_Corporate_and_Shared_Services_in_the_NSW_Government.pdf

³¹ “Releasing resources to the front line – Independent Review of Public Sector Efficiency,” Sir Peter Gershon, CBE, July 2004 (page 56).

³² “Making Acquisitions Work: Capturing Value After the Deal”, by Harbison, Viscio and Asin, Booz-Allen & Hamilton, 1999.

- the potential benefits of centralizing (i.e. reducing duplication and achieving economies of scale); and
- the need for specialist business knowledge.

Establishment of the CPG with appropriate specialist resourcing should enhance the capability of the Auckland Council and support the attainment of procurement efficiencies.

6.5.3 Consolidation of buying power

Whilst each of the larger contributing councils were substantial entities which, in their own right, should have had leverage with their suppliers, Reorganisation should enable these scale benefits to be extended over the spending formerly controlled by the smaller constituent councils. Savings might accrue through scale enabling acquisition of specialist and more specialist human and other resources in substitution for costlier consultancy services. Savings might also accrue from the fact that in aggregation of the Auckland Council's utility needs there may be ways in which the Auckland Council's expenditure could be lowered through better planning and co-ordination with utility providers.

6.5.4 Rationalising number of suppliers

There will be greater transactions costs in dealing with a larger pool of suppliers and for suppliers in multiple tendering rounds. Developing panels of preferred suppliers might be one mechanism to reduce tendering costs whilst maintaining contestability.

6.5.5 Formalising and managing supplier relationships

The greater scale of the Auckland Council facilitates the establishment of more specialisation and focus on particular categories of expenditure. This specialisation should facilitate a better understanding of suppliers' capabilities and in turn, improve their understanding of the Auckland Council's requirements, which should lead to better outcomes.

6.5.6 Catalogue-based purchasing

Catalogue purchasing facilitates on-line requisitioning. Standardisation of the products required by the Auckland Council not only reduces the transaction costs but facilitates the buying power through scale economies for suppliers.

6.6 Conclusion

Changes in procurement and business processes could be expected to deliver significant efficiencies to the new Auckland Council. On-line servicing of consumers of Council services would not only unlock significant efficiency gains for the Auckland Council but also enhance the customer experience in that contact could be made when it suited the "client."

The ATA has developed a procurement service delivery model to be deployed by the new Auckland Council which includes the establishment of a CPG which should enhance the capability of the Auckland Council and support the attainment of procurement efficiencies. Procurement efficiencies derive from consolidation of buying power, rationalising the number of suppliers, formalising and managing supplier relationships and catalogue purchasing.

7. Stream 1: Gains from enhanced asset management practices

7.1 Introduction

The new Auckland Council is estimated to have a total of \$29.5B in non-current assets by 2011/12, comprised primarily of some \$11B in property, plant and equipment and a further \$17B investment in subsidiaries. Gross capital expenditure funded by the Auckland Council is projected to be around \$0.7B p.a. over the next 10 years. Services delivered by these assets are important and pervasive and even small changes in the performance of these assets or improvements in the quality of asset acquisition and reductions in whole of life costings could have material impacts on the quality of life for people and businesses within Auckland and on the cost to the Auckland Council.

We now consider some of the major assets and consider the scope for efficiency and effectiveness gains.

7.2 Achieving better performance across the entire portfolio

The reforms have initiated changes to the way that Council manages its assets. The establishment of six substantive CCOs ready to function on 1 November 2010 is a significant move towards more efficient management of operational activities. The intention is that the overall direction for these CCOs will be set in the Council's long-term plan, including the CCO accountability policy³³ and that a separate Governance and Monitoring department and Advisory Board will assist the Council in monitoring the performance of the CCOs.

It is difficult to assess the performance impact of these changes in quantitative terms, but clearly improvements have the potential to make large impacts on Council financial flows (either directly through reductions in OPEX funding or through returns on the invested capital). But the Boards are newly in place, key accountability expectations have not yet been developed, and the performance monitoring regime needs to be put in place.

Our view is that improved performance in CCOs is an important focus area over the next few years. Considerable effort and expertise within CCOs and in the monitoring department will be required if potential gains are to be realised. Many of the generic areas of efficiency gain are applicable (e.g. procurement) but more important is the scope for process re-engineering (especially where services have simply been amalgamated, e.g. parking services) and in lifting the value for money outcomes from major investment projects. Several key asset areas are discussed below.

³³ The accountability policy will set out how the Council will hold the CCOs accountable for meeting its objectives and priorities.

7.3 Land and buildings

The primary focus of Phase 1 with respect to the \$11B property, plant and equipment assets has been to make an initial separation of property not required for ongoing council service delivery, and to clarify the focus of agencies working with substantial property assets. This has involved the establishment of several refocused CCOs, including:

- Auckland Council Property (ACP). TDB understands that upon establishment, ACP will manage some \$700M in property assets, comprising some 820 individual properties, generally being properties that are not immediately being used for service delivery or infrastructure by the Auckland Council. ACP is to obtain a return on these properties by renting them out where that is feasible; and
- Auckland Waterfront Development Agency. This CCO will be responsible for leading waterfront development, with a clear initial focus on the completion of RWC 2011 related projects. Its portfolio is estimated to comprise \$259M of property, plant and equipment and \$202M of investment property in 2011/12.

Phase 2 is beginning. Volume 4 of the Plan sets out, for instance, a table of performance measures for these two CCOs where the first measure is to “manage the assets in a way that optimises financial returns”. As yet there are no recent performance measures and the target set for 30 June 2011 is to establish a baseline. Without more detailed information on the composition of the portfolio and an understanding of the reasons property is held (for example is it held in anticipation of a specific project planned further out than 12 months) it is impossible to establish an appropriate benchmark. But we observe, on the basis of aggregate numbers, that current annual rental returns from the portfolio managed by ACP of \$700M of non-core property are about \$16M (or \$24M gross). This annual return of 2.3% is well below the borrowing costs for the Council so there would appear to be considerable scope for efficiency gains.

7.4 Rationalisation of property for Council use

Within the time available we have not separately reviewed estimates of either existing surplus properties, or estimates of space freed up following staffing level and location changes. But clearly a 16% reduction in staff numbers (by 1 July 2012) can be expected to result in consequential reductions in space requirements. We understand that some property rationalisation benefits are incorporated in Council budgets from Q4 2011/12.

As departments and business units work through the next phase of stocktaking and standardisation further surplus properties should be identified, or reallocated to highest and best uses. The Phase 3 work program may involve another round of rationalisation, particularly if significantly changed business models are adopted, for instance involving contracting out for service functions or major shifts to on-line application and processing.

7.5 Rationalisation of IT spend

Understandably the Auckland Council will inherit a wide range of IT systems and applications. Phase 1 has involved the introduction of a more common financials package but by and large most existing systems and contracts have been left in place.

Phase 2 could be expected to result in a much better identification of the full set of existing systems, benchmark data on performance, and evidence on their fitness for use, both within a business area and across business areas (for instance a booking system within one area that has the capability for much wider application). The adoption of more common platforms and applications will reduce, over time, capital costs on software and hardware as well as maintenance and support. Making these decisions will require careful business case development as typically higher initial costs are involved.

As part of Phase 2, and increasingly as part of Phase 3, changed IT systems and processes will emerge as enablers of business process re-engineering. For instance, shifts to greater on-line consent processing may emerge as a way of delivering productivity benefits to clients and the Council, but any changes such as this would require a whole-of-process review and evaluation of alternatives, and carefully developed implementation plans to secure the full benefits of change.

7.6 Major capital projects

Securing improvements in capital spending will yield large direct benefits in reduced borrowing, as well as reduced operational expenses through depreciation and maintenance. We note though that capital spending decisions involve a whole-of-life calculation including clear evaluations of the service delivery benefits, so there will be times when the most efficient decisions involve increased initial spending.

Several main avenues exist for improving the effectiveness of capital spending, many of which are practiced to some extent in some part of the amalgamated council (including CCOs where much of the investment occurs). They include:

- improved option identification and analysis;
- tighter project management and budgeting;
- improved identification and consideration of whole-of-life costs for investments, especially where subsequent costs may be borne across council units or people and businesses outside the entity making the capital decision;
- choosing carefully among procurement approaches, each of which offer ways to manage development and operation opportunities and risk (for example alliances, BOOT schemes, or Public Private Partnerships (PPPs)); and
- rethinking contracting approaches and timeframes, especially where contracts involve one party investing in relatively specific investments which would be costly to shift to alternative uses (for example investment in tunneling equipment or waste treatment facilities).

Phase 1 work has identified a trend of consistent underspending/under-delivery on capital projects. This has consequential operating cost implications in following years through depreciation and maintenance costs. Tightening budgets and forecasts so they better match expected delivery will produce some savings.

The next two phases could be expected to be applied progressively over the next 2-3 years. Best practice should be identified in each area, along with developing teams of people with requisite skills so that approaches can be transferred as appropriate to new areas. It will though require careful evaluation and benchmarking of performance: under what circumstances is it more efficient to contract out road construction with a long-life maintenance contract, and how can incentives be effectively designed to ensure adequate competitive and efficiency pressures emerge in an alliance model (which also can offer greater scope for identifying value-creating opportunities)?³⁴

7.7 Outsourcing/process re-engineering

Variations exist across amalgamated operations of the Council/CCOs in the extent of outsourcing and the areas to which it has been applied, reflecting variations in practice amongst the regions, for example in waste management, CCO IT services, parking operations, and road maintenance. Under Phase 1 these variations remain. Phase 2 could identify the areas of variation and those which offer possible scope for efficiencies (perhaps through external benchmarking) as well as clearly establishing current cost performance baselines and more clearly setting service expectations. In some cases it will take time to align contracting, or to standardise terms and operations (e.g. differing by-laws relating to parking). Phase 3 would involve processes which identified target cost and performance levels based on best practice models, either in one part of the Council/CCO or by comparison externally, and implementing the change processes where required to secure further effectiveness and efficiency improvements.

Given that in many cases Phase 1 has not involved substantive reviews of how services are delivered, the scope for efficiency gains remains. Potential for significant process re-engineering exists, for instance, in consenting or in the split functions of road access/operation/maintenance. It could be that integrated planning and programming of works, both within and across sectors could reduce costs for Council and operators e.g. better coordination of capital works, operations and maintenance within roading as well as better coordination of utility access to roads corridors resulting in roads being dug up only once.

7.8 Conclusion

The new Auckland Council is estimated to have a total of \$29.5B in non-current assets by 2011/12, comprised primarily of some \$11B in property, plant and equipment and a further \$17B investment in subsidiaries.

³⁴ From NZTA website: <http://www.nzta.govt.nz/projects/mackays-to-peka-peka/about.html>

An alliance model is considered to be the most suitable method for highly complex projects as it allows the partners to:

- work on a number of areas at once, overlap project phases and promote efficiencies; through early constructor involvement;
- deliver major projects with greater speed and innovation; and
- work together to achieve the best transport and community outcomes.

The establishment of six substantive CCOs is a significant move towards more efficient management of operational activities.

There is potential for rationalisation of the property portfolio following consolidation of staffing levels and enhancement of the returns from the portfolio of non-core property assets. There will be CAPEX and OPEX savings as the number of legacy systems are rationalised, albeit that there may be up-front investments including parallel running of systems.

8. Stream 2: Reviewing the level and quality of the Council's future activities

8.1 Introduction

A central task facing the Auckland Council will be to decide what level and quality of services will be provided across the region and how these services will be funded. The new Council will inherit a wide range of different policies and practices in terms of service levels and funding approaches including the key issue of user charges from the previous councils. The new Council would presumably aim to move to more uniform policies on what services levels are provided and how they are funded across the now-single region subject to variations in residents' preferences in different areas as expressed through local boards. This move towards more uniform provision and funding policies will provide the opportunity for the Council to review the different activities that the Council funds to bring them up to best international practice in terms of efficiency and performance.

8.2 Reviews to reduce risks on alignment of council practices

Indeed, without such a review there is a real risk that the reorganisation will lead not to best-practice but to inefficiencies and substantial increases in expenditure. This risk arises from two key pressures that are likely to emerge from the reorganisation:

- firstly, where a service was provided or was rates funded by some, but not all, of the eight former Councils there are likely to be pressures to extend the provision of the service or rates funding of it across the entire region covered by the new Council. The Council's expenditure would increase - potentially substantially - if it seeks to provide in all parts of its region all of the services that were provided in some areas previously or if it adopts rates funding of all the services that various of the previous councils funded from user charges (e.g., swimming pools); and
- a second, related risk arises from staff remuneration arrangements where history has resulted in staff performing similar functions in the different councils being on differing pay and conditions. When moving to more standardised remuneration arrangement the risk is that re-alignment will be at the highest cost levels. Such a result could increase significantly the rates that ratepayers have to pay over time and undermine the drive for greater efficiencies across the Council's operations.

Thus the reviews are critical if the efficiency and performance levels of the Auckland Council are to increase, rather than decrease, over time. The reviews would systematically compare the quantity and quality of services funded by the eight previous Councils. Where an activity was not funded by a previous council (or where the level of expenditure per capita was much lower than for other councils), the question could be asked at what level the new Council should fund the activity.

As noted the Council will need to decide its timetable for reviewing its policies regarding service levels and rates funding taking into account its objectives regarding moving towards more uniformity across the region. Equally importantly the Council will need to take into account that in principle it will be more cost efficient to apply measures to achieve efficiencies in procurement and business processes to services where the level and funding policies have been settled than to situations where changes to levels and funding are yet to be considered.

8.3 United Kingdom Expenditure Review

The United Kingdom's central government is currently going through a major efficiency-seeking exercise and has adopted a bottom-up approach to reviewing major items of expenditure. The UK government last year recorded, in the wake of the global financial crisis, a deficit of 12% of GDP. The UK government has announced plans to reduce core government spending in almost all areas by 19% over the next four years.³⁵

Key elements of the UK government's stated approach include:

- to go back to first principles and ask what is the role of the government in the different areas it operates in?
- to be prepared to abolish whole programs (rather than adopt uniform across-the-board percentage cuts) where it considers the case for a role for government is not compelling;
- where the government continues to have a core provider role (e.g., in schooling and justice), to introduce internal markets and PPPs to encourage efficiencies; and
- to devolve responsibility for decision making to a greater extent to the local level (e.g., introducing elections for local crime and police commissioners).³⁶

The new Council could adapt some of these elements in undertaking a bottom-up, first-principles based review of the major different functions that the Council undertakes in order to assist in achieving its efficiency targets.

8.4 New and improved budgetary processes

There is also an opportunity to achieve efficiency gains through new and improved budgetary processes and systems. Such financial reforms could include in particular:

- detailed expenditure reviews of major activities done periodically with the reviews linked to the Council's budget processes and decisions;
- increased focus on results in budget decision making including better specification of the desired outputs and performance levels that the Council expects from its service delivery agencies;
- benchmarking of performance levels against comparable organisations;
- bringing in people from the private sector to lead reviews of major areas of expenditure (as the central government is currently doing with Value for Money reviews in such areas as Defence);

³⁵ The National Health Service and foreign aid have been excluded from the review.

³⁶ The elected commissioners will set the police budget, determine police force priorities, and have the power to hire, and when necessary fire, their chief constable. The government will also publish local crime data and mandate beat meetings so that people can challenge the performance of their neighbourhood policing teams. Refer <http://www.homeoffice.gov.uk/publications/consultations/policing-21st-century/>.

- getting panels together, involving clients/business people with systems skills or the ability to offer insights into new ways of doing things, to generate new ideas;
- a review of the role of user charges amongst the Council's activities;
- increased financial disciplines on the Council's commercial activities; and
- improved monitoring and evaluation focused on key expectations and tailored to the Council's budget decision making.

8.5 Benchmarking/medium term targets

The potential for benchmarking of activities raises the question of what target the new Council has for efficiency levels. For example, is the target to achieve efficiency levels in line with the average levels achieved by comparable organisations. Or is it to be as efficient as the top quarter of the comparable entities. If Auckland wants to be the best city in the region, it will be important to address this question and have a medium-term financial strategy for achieving the goal.

Such a medium-term fiscal strategy is likely to include, if the goal is improvements in efficiency, medium-term targets whereby the Council commits to constraints on future rates and debt levels. To be credible and to change behaviour across the Council's activities it needs to be understood that the constraints are binding.

8.6 Conclusions

There are no simple solutions or magic bullets for achieving ongoing efficiency gains in the public sector. Finding savings and securing them is hard work, especially if there is little reward available to those involved in achieving the efficiency gains. Achieving improvements in efficiency will be an ongoing challenge for the new Council if Auckland is to achieve its goal of being a world-class city.

The establishment of the new Auckland Council provides an opportunity for the Council to review critically what the Council should best do and how it can best do it. While rapid gains in efficiency can be made in Stream 1 under Phase 2 (improving the efficiency of existing activities, initially within the constraints of existing systems, contracts and processes) through such measures as across-the-board constraints on expenditure, caution needs to be taken that such gains are not at the expense of longer-term gains. Achieving sustainable gains in efficiency is likely to require a multi-pronged strategy as outlined in Phase 3 of Stream 1 (best practice service models are identified and implemented) and Stream 2 (reviewing the level and quality of future activities). In our experience, the key measures in such a strategy are likely to involve a combination of strong leadership, empowering the right people, improved processes and a clear medium-term financial strategy involving commitments to constraints on increases in the levels of rates and debt over time. Most important will be maintaining the credibility of the Council as it drives for greater efficiencies across the services it delivers to the community.

9. Governance processes to support achievement of a high productivity and efficient Council

9.1 Introduction

Phase 1 is now complete, having delivered a revised structure for the Council and removal of duplications. It has largely delivered the anticipated first round of savings, driven organisationally by a group independent of both the previous councils and the new Council (although obviously working closely with them).

Looking ahead to the next steps in the process makes it clear that achieving the even greater service and efficiency improvements is a harder and longer task. In our view there are several critical ingredients for success:

- aligned motivation and incentives;
- clear goals;
- close cooperation between major stakeholders;
- empowered change agents;
- developing a clear benefits realisation plan; and
- effective communications about goals and progress.

9.2 Aligned motivation and incentives

The Council depends on its staff to deliver services: the staff must own and drive any process that is enduring and widespread. Having amalgamated groups of staff with widely differing traditions and expectations is just the beginning of what will be a major cultural change, where the goal will be to achieve a common ethic about working in Auckland's best interest, using tools and approaches common across the region. Ensuring staff are given motivation, training and tools for this will clearly be a major task for the new leadership team, reinforced by aligned performance expectations and management tools. Encouraging appropriate risk taking to identify and enable more effective options and systems will be a key enabler of a change that delivers an Auckland Council that is the most productive in New Zealand.

9.3 Clear goals

Phase 1 established some initial financial savings targets along with clearly demarcated delivery timetables. This report does not provide a simple template for the next two phases, the information simply does not yet exist although evidence from other areas and countries provides some confidence that a significant step up in productivity can be achieved through a 3-5 year process.

It will, though, be important that the Council develops clear goals and a timetable to achieve this performance lift. It is too easy to become distracted by day-to-day pressures. Early stages in Phase 2, over the next 6 months, could involve the use of initial benchmarking information to set the initial steps for performance improvement to be delivered through the third phase.

9.4 Close cooperation between major stakeholders

Many of the potential improvements to service delivery and effectiveness involve changes, for example, to modes of delivery or might require trade-offs between service attributes when the true costs of some features are uncovered. Finding ways that enable ideas and views to be exchanged, and encourage innovative solutions to be developed will allow the Council to develop and adopt good ideas and processes more quickly. This level of engagement will be even more important for the issues tackled in Stream 2, where many public choices will be required.

9.5 Empowered change agents

The challenges of identifying and delivering new business processes and changed patterns of asset acquisition and delivery are significant. Experience with many other change exercises (in both public and private sectors) highlights the need for some separation between the managers tasked with ensuring service delivery is maintained, and those teams tasked with identifying and delivering change. Changes will potentially distract incumbent managers from their delivery task, and will often challenge some parts of their operation. We recommend that the Council leadership clearly establish a separate position for driving and securing further productivity improvements, along with adequate skilled staffing in a team supporting that position.

9.6 Benefits realisation plan

Often ambitious mergers in the public and private sector start with large but generically estimated potential benefits. Where the estimates of the benefits are not derived from specific actions or embedded within line-item expenditure areas, the resultant lack of ownership results in under-delivery. The Plan makes good progress in delivering initial savings in specified areas, but looking ahead progress will require a benefits realisation plan which establishes ownership, resourcing, identification, resolution of resource conflict with business-as-usual, and regional coordination activities.

9.7 Effective communication

Change typically succeeds well where the need for it is well understood. We recommend that as the Council moves through Phases 2 and 3, it establishes clear processes around communicating the various issues, alternatives, options, decisions, progress and achievements.

9.8 Conclusion

Looking ahead to the next steps of the process makes it clear that achieving the even greater service and efficiency improvements is a harder and longer task. In our view there are several critical ingredients for success:

- aligned motivation and incentives;
- clear goals;
- close cooperation between major stakeholders;
- empowered change agents;
- developing a clear benefits realisation plan; and
- effective communications about goals and progress.