

Council becomes a Contractor

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Abstract

Local Government faces pressures from rate pegging, cost shifting from state government, growing community expectations and aging infrastructure. Operating a commercialised business unit that delivers competitive services to council as well as generating additional revenues is a means of improving financial sustainability, increasing service levels and delivering other community benefits. This paper discusses the development of the business unit of Tumut Shire Council, Snowy Works and Services, over the past seven years and also reviews lessons learned from a study tour of five 'council-controlled trading organisations' which have been operating in New Zealand for the past 15 years.

Key Words

Business Unit, Commercialisation, Service Provision, National Competition Policy, Snowy Works and Services, Tumut, New Zealand

Introduction

Tumut Shire is located between the Australian Capital Territory and Wagga Wagga City, on the western side of the Snowy Mountains. Its area is 4,500 sq km with a population of around 11,500.

Almost two thirds of the Shire is non rateable, being primarily State Forest or National Park.

Principal economic activities in the Shire are plantation timber growing and processing; horticulture (primarily apples); tourism; grazing; electricity generation (via the Snowy Scheme) and storage of waters for power generation and downstream irrigation.

The towns in the Shire are (in order of size) Tumut (6500 people), Batlow (1400), Adelong (1000), Talbingo (350), Brungle (100) and Cabramurra (100), which is the highest town in Australia, owned by Snowy Hydro.

Tumut Shire Council employs around 130 FTE staff. In July 2002, Council established Snowy Works and Services as the 'business arm' from Council's works department.

The SnowyWS Board was established as a committee of Council under section 355 of the Local Government Act. The Board included two Councillors, the General Manager and Manager of Finance for Tumut Shire Council, a Community Representative, the CEO of SnowyWS and a SnowyWS Staff Representative.

An Instrument of Delegation from Council outlined the functions, powers and duties of the Board. A partnering agreement set out the scope of services to be delivered by SnowyWS to the other Council departments and the nature of the relationship – basically SnowyWS was the preferred supplier of all services, paid on a cost recovery basis.

We opened our own bank account, began invoicing Council for work done and paying them commercial rates for the use of depots, gravel pits and plant. This effectively 'ring

fenced' the unit so we could account for external works on a full cost recovery basis.

The unit became 'self contained' with finance, HR and administration staff transferred to an office at the main depot. Only IT services were still supplied by Council (which were paid for).

Over the next seven years, SnowyWS has become one of the very limited number of local government-owned commercialised service providers in Australia.

This paper reviews the phases in the development of the unit, lessons learned and the key benefits the unit provides to Council and the community.

Development Phases of SnowyWS

Phase 1 – Establishment

Council engaged consultants to review possible structures, formulate plans, facilitate staff consultation and set out the basic structure of the unit. Staff also visited other service providers.

A key mistake at this stage was the decision by Council to restrict staff numbers. This made 'year one' very difficult to set up the systems necessary for the unit to function effectively.

Phase 2 – Culture Change and Identity

The following three years saw an increasing development of our own identity, as well as culture change – staff thinking commercially, appreciating customers and costs, etc.

Something to consider in this phase is the development of the Asset Owner / purchaser function of Council. If all the effort goes into the business unit, those working in the 'Asset Owner' functions can feel like they are left out or that the service provider is empire building.

Through this phase, the biggest failing was the lack of review of the consultant's Strategic Business Plan by the Board. This arguably led to many of our later hurdles.

Phase 3 – Stretch Goals and Growing Pains

Because the Board was not reviewing strategy, it was being formulated as we went and Council, the Board and I failed to appreciate fully the consequences of this.

In 'year 5' (2006/07), Council's works program was reduced substantially and the RTA (usually our major external customer) advised that there would be no capital works on their roads we maintained under contract.

We potentially had insufficient work to retain our existing resources.

I responded to this issue by targeting competitively a tender for a major subdivision in Tumut. Three weeks after being advised that we were successful the RTA rang and asked if we could complete a major road reconstruction project on a vital community transport link (of course I said yes).

Now not short of work, we pressed on, also taking on a fortnight's work for Forests NSW (that turned into five) and working all the while on a major utilities contract for Snowy Hydro we had won a few months earlier.

Without fully considering it I had set a fairly aggressive strategy for the unit. Trouble was we didn't have the capacity to effectively control operations, let alone formulate a clear strategy.

Pretty soon we had growing pains... and with them increased commercial risk.

On the up side, the 'stretch goals' I had set were a catalyst for change: both cultural and organisational. Our staff stepped up to the plate magnificently.

We were so busy that people didn't argue 'that's not my job', they just got in and lent a hand. People didn't argue about taking on more responsibility, they were proud of what we were achieving.

The exposure to the market was invaluable. Everyone started to appreciate the need to focus on finances and customer requirements to succeed, to continuously improve our processes.

From many perspectives it was our most successful year to date: the largest dividend, excellent plant utilisation and significant revenue growth. We also learned a lot, improved key parts of our systems, and started to appreciate what we were capable of.

But something had to change. Councils should not be in the business of taking risks... and we were getting riskier.

Phase 4 – Why are we here?

The lack of strategic review and involvement by the Board and Council in the past meant we were now 'starting from scratch' to develop a shared understanding of what the key objectives of the unit were and what direction we were headed.

In August 2007, Council resolved to engage consultants Morrison Low to carry out a strategic review of SnowyWS.

Malcolm Morrison, who carried out the review, suggested that given that there are no real parallels to SnowyWS in Australian local government, a delegation from the board should visit New Zealand.

Malcolm had been part of New Zealand's outsourcing of road works that occurred in the early 1990's and still works with many councils over there as well as in Australia.

He arranged visits for us with five council-controlled trading organisations and the councils who own them in February 2008.

The delegation included Cr James Hayes (Deputy Mayor of Tumut Shire Council and Chairman of the SnowyWS Board), Chris Adams (General Manager of Council), Allan Tonkin (Manager of Corporate Services at Council) and myself. I'd like to thank the

Engineering Foundation for funding my portion of the tour.

New Zealand Study Tour

The Council-Controlled Trading Organisations (CCTOs) we visited are not guaranteed work from their councils and have survived the last 15 years on their own.

Government grants for roads are significantly higher than in Australia (making up two thirds or more of many council's roads budgets). In the mid 1990's, the New Zealand government legislated the compulsory tendering of all road works with government funding in an effort to improve the competitiveness of service provision.

Councils were forced to set up companies that could tender on the work or divest themselves of their operational workforce, plant and so on. The transition period was around three years.

The five councils and CCTOs were:

- Infracon and Tararua District Council
- QRS and Wairoa District Council
- CityCare and Christchurch City Council
- Whitestone and Waitaki District Council
- Inframax and Waitomo District Council



General Lessons Learned

All of the CCTOs had benefited from the strategic direction and management of a commercial board with the appropriate range of skills, and the commercial orientation provided by a company structure.

All had recognised the need to grow to become more competitive, many having grown by acquisition or merger.

The 'Long Term Community Consultation Plans' introduced a few years ago (that focus on asset management and sustainability) were a reaction against the deferred maintenance which resulted from the 'compete on price, cheat on quality' environment that is created when legislation requires 'lowest cost conforming' tender acceptance.

Most maintenance contracts were based on a schedule of rates. Performance-based contracts were not popular due to difficulties with administration.

Transit New Zealand's national highway maintenance contracts are sized beyond the capability of individual CCTOs. However construction projects are let on the basis of individual projects, which were a key market for most CCTOs.

Two companies (Works Infrastructure, which incidentally started life as the New Zealand Department of Works, and Fulton Hogan) appear to hold a major portion of the civil construction market across the country.

All CCTOs had started out with councillors on the board, and all had moved away from this due to the 'irresolvable conflict' that wearing these two hats created.

It seems like councils eventually became comfortable setting performance targets in the 'Statement of Business Intent' and leaving the professional boards to run the business.

Of the 40 or 50 CCTOs that were established in the 1990s, the five we visited were among

only 15 or so that remain. From second-hand observations and comments, it appears that those CCTOs that did not survive either:

- Were bought up by other CCTOs or privately-owned companies who wished to expand;
- Failed to develop a commercial focus and understand what was required to succeed in the market;
- Failed to retain their key contracts such as those with their parent council; or
- Were in less remote areas, more easily penetrated by the larger players. A related issue is the impact of relying upon these larger players for supplies of gravel, sealing and asphalt.

The “5 Why’s” of owning a Commercialised Service Provider

At the end of the strategic review process, five key benefits became clear and these are what was presented to Council supporting the further development of SnowyWS.

Competitiveness of Service Provision

Increasing turnover increases plant utilisation and reduces overheads, which mean lower costs for council.

Exposing staff to the ‘real world’ market gets them thinking more about costs, customers and performance.

While this is difficult to quantify, its importance should not be underestimated. The culture change in our staff since SnowyWS was established has delivered real increases in competitiveness as well as enhancing people’s pride and therefore retention rates.

We have also implemented innovative employment conditions such as ‘Winter TOIL’ where staff can elect to take Time Off In Lieu of overtime at overtime rates (i.e. double time = 2 hours TOIL), which has addressed issues with

having insufficient work in winter, while at the same time improving conditions for staff.

Supplementing shortfalls in Council’s works programs with external works has helped SnowyWS handle variations in Council’s program of up to 50%.

We have been able to generate additional revenues for Council during these ‘slow’ years and then have the resources available to deliver large capital programs when Council has additional grant funds to spend.

Contribution to the Community

A local business delivering services increases local jobs, payments to local suppliers and provides competition, giving the community better value for money when they buy these services.

SnowyWS contributes significantly to local community projects and has donated over \$270,000 in the last seven years.

Increase in Council’s Revenue Base

Local government is facing aging infrastructure, additional responsibilities from state government cost shifting and tougher legislation, as well as higher community expectations.

Yet their income is restricted by rate pegging, so alternative revenue sources are vital.

SnowyWS has generated substantial dividends for Council over the years from external works and importantly satisfies the requirements of a ‘category 1’ business under National Competition Policy.

Ensuring Emergency Response Capability

This is something that came through loud and clear in New Zealand, where many councils had suffered significant floods in recent years. Unless you control the resources and have them locally, you risk not having them when you need them.

While trying to minimise commercial impacts of doing so, SnowyWS has 'dropped everything' to respond to emergencies in the local area on a number of occasions in the past few years.

Flexibility to Respond to Changes in the Operating Environment

If local government is to survive, we must be adaptable, and be able to demonstrate sustainability, competitiveness, innovation, best value and all the other buzzwords.

SnowyWS makes Tumut Shire Council more adaptable in that it has more options to respond – for example, with proposed changes to local water utilities: Council can demonstrate we are competitive since we have won a number of similar tenders on the open market. Or, if these services were to be put out to contract, SnowyWS would be well positioned to tender on this work and thus retain local jobs.

Council is also far more financially sustainable, delivers more competitive services, is arguably more innovative and provides best value than a 'traditional' council.

Phase 5 – Moving Forward

To return to the 'development phases' of SnowyWS: we are now happily in our latest development phase that I call 'moving forward'.

Council has resolved to appoint two additional staff and will soon consider the appointment of additional Board members with commercial skills.

We will also be reviewing the Strategic Business Plan, Partnering Agreement with Council and the Instrument of Delegation to the Board.

Things done well and lessons to learn

The main things we've done well are:

- Stepped out of the comfort zone (stretch goals are a catalyst for change);

- Engaged and developed staff – helped them understand where we're headed;
- Worked on good relationships with Council's Asset owners: they are our biggest customer;
- Ensured there is transparency in finances.

The key lessons to learn are:

- It is essential that councillors develop a clear understanding of objectives in establishing the unit;
- Strategy must be continuously reviewed;
- Commercial skills are essential on the Board.

Conclusion

Local government should not be in the business of taking risks.

We are, however, in the business of delivering services and that means we have capabilities in water, wastewater, roads, bridges, parks, plant maintenance and whatever else.

And we don't ever have enough money.

So to me, running a commercialised business arm aligns perfectly with local government's reason for being.

But you need to recognise that you are running a business. Council's role is (like other functions of local government) setting objectives via the management plan. Matching this from the business side must be the skills required to manage risks and operate commercially.

Biography

Ben Lawson has worked with Tumut Shire Council for almost ten years, half of this in the role of CEO of Snowy Works and Services, Council's business arm. Ben comes from a long line of engineers – back to his great, great grandfather. He is a certified practicing engineer and has a B.E. Civil (Hons.), M.E. and MBA. Ben has also chaired the South West Group of the IPWEA for the past four years and acted as Secretary for a couple of years prior to that.

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