

ITEM 13.3 SALEYARDS STRATEGIC OPTIONS

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PURPOSE

To provide an overview of the strategic options available in relation to the Kempsey Shire Council owned saleyards and the recommended next steps.

RECOMMENDATION

- 1 That Council notes the strategic options available in relation to the Kempsey Shire Council owned saleyards.**
- 2 That a workshop involving Councillors, Council management and key external stakeholders be held to discuss the available strategic options.**
- 3 That further analysis be undertaken subsequent to the workshop and a paper with recommended option(s) be presented to a future Council meeting.**

ISSUES

The operation and management of the Kempsey Regional Saleyards (“the Saleyards”) has presented a number of challenges to Kempsey Shire Council in recent years. Council currently owns the saleyard facility and is responsible for providing all infrastructure, ongoing upgrading and maintenance. Over the past 10-15 years, Council has invested more than \$2M in upgrade and infrastructure works to ensure the Saleyards comply with environmental standards, meet WH&S requirements and offer ‘best practice’ facilities capable of processing more than 2,000 head of cattle per day.

The cost of funding this investment, combined with relatively high operating costs has resulted in the Saleyards being loss making since before the 2004-05 financial year. This annual operating deficit has been absorbed by Council over this period. A summary of the financial performance of the Saleyards is attached as [\(Appendix F\)](#). It should also be noted that the costs included in the attached financial summary do not include other indirect overhead costs, such as Council senior management time associated with managing this asset.

Additionally, a number of other immediate challenges facing the Saleyards have been identified. These include:

- The acceleration of direct selling methods;
- Changes to the operating environment;
- Increasing regulations; and
- Ongoing competition from neighbouring saleyards, abattoirs and alternative sale methods.

Furthermore, there is the need for significant further capital expenditure as identified in the GHD Financial Plan (2016) and updated Business Plan. Council has funded historical capital expenditure

via loan funding with the repayment of these loans essentially being a significant contributor to the annual operating deficit of the Saleyards. Existing loans will be fully repaid in the 2018-19 financial year and while the repayment of these loans is projected to result in modest future operating surpluses, future capital expenditure would necessitate sizeable loan borrowings. Any future borrowings to fund capital works at the Saleyards would again result in a sustained period of operating deficits, unless there was a significant improvement in the underlying business operations of the Saleyards (i.e. increased revenue via increased throughput or higher prices, or a combination of both).

Ultimately, commercial operations run by Council, such as Saleyards, need to be financially sustainable. It is not viable for the Saleyards to consistently run at a deficit and for Council to absorb this deficit from its General Fund.

The operational and financial challenges faced by council's in operating and managing saleyards has seen a number of developments in recent years with council's largely either:

- Divesting the operation and management of their saleyards to the private sector (through sale or lease arrangements);
- Investing heavily to modernise the saleyards to deliver high quality animal welfare and work, health and safety outcomes, as well as increased throughput and projected improved financial performance / sustainability¹; or
- Doing nothing, resulting in both a deteriorating and underperforming asset.

Options Analysis

To address the current operating performance of its Saleyards, Council principally has two options:

1. Implement strategies to drive a material increase in revenue from the Saleyards so that the asset is financially sustainable and generates operating surpluses that are sufficient to self-fund repayment of future borrowings that may be incurred to maintain and / or expand the Saleyards.
2. Investigate a range of alternative business models that would deliver improved financial performance of the asset while continuing to deliver the current economic benefits to the Macleay Valley economy and community.

It should also be noted that Council has received two offers in relation to the Saleyards. These include:

- An expression of interest from Kempsey Stock & Land Pty Limited in March 2018 to purchase or lease the saleyard complex should Council decide to move in that direction; and

¹ The Northern Rivers Livestock Exchange (NRLX) owned and operated by Richmond Valley Council is currently undergoing a \$14M upgrade of the saleyard facility having received \$7M grant funding to complete the second stage of the upgrade project. Additionally, Upper Hunter Shire Council has recently received a \$2.8M grant from the Building Better Regions Fund which will partly fund a \$7M project at the Scone Regional Livestock Selling Centre. In both cases the balance of the funding to deliver these upgrades will be via loan borrowings.

- An expression of interest from the AAM Group of companies in December 2017 in leasing the Saleyards to enable their business to assess the viability of a new facility located in the region.

Both offers indicate that there is private sector interest in the Saleyards should this option be pursued.

A summary of the potential operations are analysed in the tables below. The options have been colour coded for ease of understanding with the shading representing the following:

- Blue shaded options (options 1-4) require minimal capital investment and are essentially “as is” options.
- Green shaded options (options 5-9) propose a redevelopment / upgrade of the existing Saleyard facility to expand business operations.
- Purple shaded options (options 10-14) propose a greenfield development to build a state of the Saleyard facility to substantially expand business operations.

Option	Description	Advantages	Disadvantages
1. Do Nothing	Continue to operate Kempsey Regional Saleyards (KRS) as is with minimal capital expenditure (i.e. on an as needs basis)	✓ Avoids large capital investment and funding issues ✓ KRS remains Council owned	❖ Underlying operational issues not addressed ❖ Current operational risks not minimised, mitigated or shifted ❖ May not be aligned to community interests ❖ Asset deterioration and potential breaches of regulations if asset not sufficiently maintained ❖ Negative impact on financial operating result and Fit for the Future Benchmarks over the longer term ❖ Efficiency and effectiveness not promoted ❖ Economic development impacts / opportunities not maximised
2. Immediate Sale and Exit of Kempsey Regional Saleyards	Sell the KRS business operations and assets as a going concern and fully exit.	✓ Avoids large capital investment and funding issues ✓ Improved financial outcomes ✓ Generates sale proceeds that can be used to fund other projects ✓ Minimises risks associated with ownership and ongoing operation of KRS ✓ Allows KSC to focus on core business ✓ Encourages private operator involvement with expertise to deliver an industry standard service	❖ Sale of Council owned asset ❖ Community support may not be positive ❖ Forgoes any potential future operating revenue opportunity
3. Lease of Kempsey Regional Saleyards	Lease the Saleyards with planned capital expenditure on an as needs basis only	✓ Avoids large capital investment and funding issues ✓ Possible improved financial outcomes ✓ Allows KSC to focus on core business ✓ Encourages private operator involvement with expertise to deliver an industry standard service ✓ Possible improved economic benefits to KSC ✓ KRS remains Council owned	❖ Underlying operational issues not fully addressed ❖ Current operational risks not fully minimised, mitigated or shifted ❖ May not be aligned to community interests ❖ Asset deterioration ❖ Financial operating result may not be significantly improved over the longer term (operating result benefit may not be material and capital expenditure will still be KSC responsibility)
4. Joint ownership of Kempsey Regional	As above (Option 1), but KRS subsequently transferred into a	✓ Avoids large capital investment and funding issues ✓ Asset remains community owned	❖ Underlying operational issues not fully addressed ❖ Current operational risks not fully shifted

Option	Description	Advantages	Disadvantages
Saleyards (Co-Operative Model)	special purpose vehicle or co-operative, that is jointly owned by KSC and key local stakeholders (Agents, Producers)		❖ Asset deterioration if limited capital investment ❖ Financial operating result may not be significantly improved over the longer term (operating result benefit may not be material and capital expenditure will still partly be KSC responsibility) ❖ Part sale of Council owned asset – albeit to key local stakeholders ❖ Ability of other stakeholders to invest is unknown ❖ Ownership structural issues
5. Partial Redevelopment / Upgrade – Build, Own & Operate	Capital project to redevelop / upgrade existing facility to expand existing business operations	✓ Redevelopment of key local asset which may deliver economic benefits to KSC ✓ Asset remains Council owned and operated ✓ Delivers improved facility for KSC ✓ Optimises revenue generation and operational efficiency opportunities	❖ Will require sizeable debt funding to deliver project ❖ Ability to (i) access; and (ii) service debt funding questionable ❖ Increased investment risk ❖ Impacts on Fit for the Future Benchmarks (and financial sustainability generally) difficult to assess given uncertain impacts on future operating results ❖ KSC continues to be responsible for running saleyards business and does not have internal capability
6. Partial Redevelopment / Upgrade – Build, Own & Lease	As above (Option 5), but KRS subsequently leased to a private operator to operationally manage in return for stable lease rental payments	✓ Key local asset is upgraded delivering economic benefits to KSC ✓ Asset remains Council owned ✓ Delivers improved facility for KSC ✓ Reduced operational risk ✓ Stable lease income	❖ Will require sizeable debt funding to deliver project ❖ Ability to (i) access; and (ii) service debt funding questionable ❖ Increased investment risk ❖ Ability to attract a lessee willing to pay commercial lease rental on upgraded facility may be difficult
7. Partial Redevelopment / Upgrade – Joint Ownership (Co-Operative Model)	As above (Option 5), but KRS subsequently transferred into a special purpose vehicle or co-operative, that is jointly owned by KSC and key local stakeholders (Agents, Producers)	✓ Key local asset is upgraded delivering economic benefits to KSC ✓ Asset remains community owned ✓ Delivers improved facility for KSC ✓ KSC only required to finance 50a portion of project cost	❖ Part sale of Council owned asset – albeit to key local stakeholders ❖ Ability of other stakeholders to invest capital is unknown ❖ Ownership structural issues ❖ Increased investment risk ❖ KSC assumes the delivery risks associated with large capital-intensive project ❖ Will require debt funding to deliver project ❖ Ability to (i) access; and (ii) service debt funding of this size questionable
8. Partial Redevelopment / Upgrade – Sale & Leaseback	As above (Option 5), but KRS subsequently sold to an institutional investor (e.g. Superannuation Fund) and then leased back by KSC to operationally manage	✓ Key local asset is upgraded delivering economic benefits to KSC ✓ Delivers improved facility for KSC ✓ Generates sale proceeds that can be used to fund other projects ✓ Minimises risks associated with ownership of KRS ✓ Operational management remains with KSC	❖ Sale of Council owned asset ❖ Community support likely to be low ❖ KSC assumes the delivery risks associated with large capital-intensive project ❖ Ability to fund / finance ❖ Number of potential institutional investors unknown and return on investment may result in high lease payments that deem this option uneconomic and unviable
9. Partial Redevelopment / Upgrade – Sale & Exit	As above (Option 5), but KRS subsequently sold to a private operator	✓ Key local asset is upgraded delivering economic benefits to KSC ✓ Delivers improved facility for KSC ✓ Generates sale proceeds that can be used to fund other projects ✓ Minimises risks associated with ownership and ongoing operation of KRS ✓ Allows KSC to focus on core business	❖ Sale of Council owned asset ❖ Community support likely to be low ❖ KSC assumes the delivery risks associated with large capital-intensive project ❖ Ability to fund / finance ❖ Potentially limited purchasers which may impact on sale proceeds – likely purchasers would prefer to undertake redevelopment themselves
10. Greenfield Development –	Major capital project to construct a new	✓ Redevelopment of key local asset which will deliver economic benefits to KSC	❖ Will require significant debt funding to deliver project

Option	Description	Advantages	Disadvantages
Build, Own & Operate	purpose built regional facility on a greenfield site that significantly expands existing business operations	✓ Asset remains Council owned and operated ✓ Delivers “state of the art” facility for KSC ✓ Optimises revenue generation and operational efficiency opportunities	❖ Ability to (i) access; and (ii) service debt funding of this size questionable ❖ Uncertainty that economic benefits exist to support major greenfield development when compared to partial redevelopment option ❖ Significantly increased investment risk ❖ Impacts on Fit for the Future Benchmarks (and financial sustainability generally) difficult to assess given uncertain impacts on future operating results ❖ KSC continues to be responsible for running saleyards business and does not have internal capability
11. Greenfield Development – Build, Own & Lease	As above (Option 10), but Greenfield KRS subsequently leased to a private operator to operationally manage in return for stable lease rental payments	✓ Key local asset is upgraded delivering economic benefits to KSC ✓ Asset remains Council owned ✓ Delivers “state of the art” facility for KSC ✓ Reduced operational risk ✓ Stable lease income	❖ Will require debt funding to deliver project ❖ Ability to (i) access; and (ii) service debt funding of this size questionable ❖ Uncertainty that economic benefits exist to support major greenfield development when compared to partial redevelopment option ❖ Increased investment risk ❖ Ability to attract a lessee willing to pay commercial lease rental
12. Greenfield Development – Joint Ownership (Co-Operative Model)	As above (Option 10), but KRS subsequently transferred into a special purpose vehicle or co-operative, that is jointly owned by KSC and key local stakeholders (Agents, Producers)	✓ Key local asset is upgraded delivering economic benefits to KSC ✓ Asset remains community owned ✓ Delivers “state of the art” facility for KSC ✓ KSC only required to finance a portion of project cost	❖ Part sale of Council owned asset – albeit to key local stakeholders ❖ Ability of other stakeholders to invest capital is unknown ❖ Uncertainty that economic benefits exist to support major greenfield development when compared to partial redevelopment ❖ Ownership structural issues ❖ Increased investment risk ❖ KSC assumes the delivery risks associated with large capital-intensive project ❖ Will require significant debt funding to deliver project ❖ Ability to (i) access; and (ii) service debt funding of this size questionable
13. Greenfield Development – Sale & Leaseback	As above (Option 10), but KRS subsequently sold to an institutional investor (e.g. Superannuation Fund) and then leased back by KSC to operationally manage	✓ Key local asset is upgraded delivering economic benefits to KSC ✓ Delivers “state of the art” facility for KSC ✓ Generates sale proceeds that can be used to fund other projects ✓ Minimises risks associated with ownership of KRS ✓ Operational management remains with KSC	❖ Sale of Council owned asset ❖ Community support likely to be very low ❖ KSC assumes the delivery risks associated with large capital-intensive project ❖ Ability to fund / finance ❖ Uncertainty that economic benefits exist to support major greenfield development when compared to partial redevelopment option ❖ Number of potential institutional investors unknown and return on investment may result in high lease payments that deem this option uneconomic and unviable
14. Greenfield Development – Sale & Exit	As above (Option 10), but KRS subsequently sold to a private operator	✓ Key local asset is upgraded delivering economic benefits to KSC ✓ Delivers “state of the art” facility for KSC ✓ Generates sale proceeds that can be used to fund other projects ✓ Minimises risks associated with ownership and ongoing operation of KRS ✓ Allows KSC to focus on core business	❖ Sale of Council owned asset ❖ Community support likely to be very low ❖ KSC assumes the delivery risks associated with large capital-intensive project ❖ Ability to fund / finance ❖ Uncertainty that economic benefits exist to support major greenfield

Option	Description	Advantages	Disadvantages
			- development when compared to partial redevelopment option ❖ Potentially limited purchasers which may impact on sale proceeds – likely purchasers would prefer to build themselves

BACKGROUND

Kempsey Regional Saleyards is a community asset owned and maintained by Kempsey Shire Council. With around 60-70 sales held per annum, the Saleyards provide a regular venue for livestock buyers and sellers across the region to generate income and undertake herd development activities. The weekday markets are well attended by buyers and sellers, with this number increasing at the Saturday markets.

Local Government has managed Saleyards in the Macleay Valley since the early 1900s and at the current saleyard site since 1969. The Saleyards provide an essential service to beef and dairy industry producers, operators and end users and is located mid-way between Saleyards at Taree and Grafton. Council owns the Kempsey Regional Saleyards facility and is responsible for providing all infrastructure, ongoing upgrading and maintenance.

Under current leasing arrangements, livestock sales are a function of three agents, with Kempsey Stock & Land (KSL) operating under a five-year lease which provides exclusive use on Thursdays and Ray White Rural Kempsey and Midcoast Stock and Station Agency having operating use on Tuesdays. Other interested agents can operate on other days.

Over the past 10-15 years, Kempsey Shire Council has invested more than \$2M in upgrade and infrastructure works to ensure the Saleyards comply with environmental standards, meet WH&S requirements and offer 'best practice' facilities capable of processing more than 2,000 head of cattle per day. Loans associated with these upgrades expire in 2018/2019.

Council has had long-term plans to upgrade the saleyard facility to address effluent disposal issues and improve the selling yards.

While Saleyards have historically formed an integral part of the economic and social fabric of rural communities in Australia, it is acknowledged that improved technology, transportation and regionalisation have driven a consolidation of Saleyards and the growth of alternative selling methods, placing pressure on their financial management.

A number of reviews of the Kempsey Saleyards have been undertaken over the past 10-15 years.

These included:

Review	Outcome
Kempsey Regional Saleyards Infrastructure Review and Feasibility Study (Huefner & Associates Pty Ltd, 2006).	Huefner & Associates Pty Ltd conducted an infrastructure review and feasibility study in 2006. The project included an inspection of the Saleyards, as well as stakeholder consultation with staff, operators and vendors. The report highlighted priority projects which helped shape the capital works program in subsequent years.
Wastewater Treatment Report (ERM 2011)	In 2011 Environmental Resource Management Australia Pty Ltd (ERM) were engaged to undertake a site inspection of the saleyard wastewater treatment system (WWTS) and provide recommendations for system improvements and ongoing management. This study followed the previous WWTS Design Upgrade (ERM 2008) and Operation and Maintenance Manual (ERM 2006).
Kempsey Regional Saleyards, Market Analysis and Financial Modelling (GHD Pty Ltd, 2013)	This 2013 report provided an analysis of factors impacting on the long-term viability of the Kempsey Regional Saleyards, including local cattle numbers, changing selling trends, operating costs etc. The report provided a review of local market conditions and the past financial performance of the Saleyards, which was used to provide projections of future throughput and financial performance under different investment scenarios. The report anticipated an increase in throughput to around 35,000 head, largely due to a second agent (Midcoast Rural) being provided access. Overall the report found the Saleyards were well placed to deliver modest operating profits going forward (depending on future capital improvements). Projections from the report were used to inform the Saleyard Business Plan (below).
2013 Kempsey Regional Saleyards Business Plan	The 2013 Kempsey Regional Saleyards Business Plan highlighted some major immediate challenges currently faced by Kempsey Regional Saleyards, including: • acceleration of direct selling methods; • changes to the operating environment; • increasing regulations; and • ongoing competition from larger neighbouring Saleyards (e.g. Armadale, Grafton, Taree), abattoirs and alternative sale methods.

Review	Outcome
	The report detailed two investment scenarios (low and high investment). The high investment scenario detailed a range of potential upgrades and improvements to the saleyard facilities which may be required into the future, and/or are likely to improve the facilities operations, throughput and profitability.
2016 Kempsey Regional Saleyards Financial Plan	In 2016 GHD were engaged by Kempsey Shire Council to develop a financial plan for the Kempsey Regional Saleyards. After reviewing previous reports, GHD visited the facilities to consider potential upgrades and consult key stakeholders, including Council staff, agents and a selection of producers. Potential improvements were identified, costed and prioritised based on the Council's ability to finance future works. The Financial Plan identified the following recommendations: 1. Implement the capital works program as outlined in the report, while monitoring annual changes to throughput, revenue and expenses against projections. 2. Investigate opportunities to draw on the Environmental Levy or the NSRF to help fund the construction of a roof over delivery yards. 3. Ensure all usage fees are regularly adjusted for CPI. 4. Revisit the business development actions outlined in the Saleyard Business Plan including activities aimed at improving promotion, broaden the Saleyards supply area and improving security/revenue collection. 5. Begin planning and preparations for beyond the current lease agreement. If Council is to hold multi-agent sales, determine how will sales be managed and if additional resources be required? 6. If the Council is not fully committed to managing the facility to its full potential, including the management of multi-agent sales, the Council should seek to outsource management or sell the facility.

At the 16 May 2017 Council meeting it was resolved that a further review of the Saleyards Business Plan be undertaken.