

Greater Sheboygan Committee

November 24, 2009

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Analysis and Evaluation of:

“NorthStar Economics Fiscal Flow and Funding Analysis for Mead Public Library”

Narrow Assumptions Drive Narrow and Limited Conclusions Recently, NorthStar Economics (a consulting firm) completed an analysis for the Mead Public Library (MPL). The NorthStar Economics (NSE) study is in large part a forward looking document, as one of its major goals is to assess the financial impact on MPL, should the Library sever its relationship Eastern Shores Library System (ESLS).

The basis for any forward looking (projected) study is the core set of assumptions chosen to create the future scenario. In addition, thorough forward looking studies consider multiple sets of assumptions.

Of major concern about the NSE study is that it is based on a very narrow set of assumptions. The primary narrow assumption is that MPL would continue to operate all functions, in the same manner, and at the same level after severing its relationship with ESLS, as it now does as a member of ESLS. Why is that the only assumption chosen?

If it is assumed there is a certain level of costs involved in operating the Library in the manner in which it operates today and those operations and costs would continue outside of ESLS, then the NSE study is correct. Choosing that very limited assumption automatically drives an increased cost conclusion. The results are determined by the deliberate choice of assumption.

A thorough and complete analysis would have outlined multiple assumptions and described multiple options to respond to those assumptions.

As an example, MPL currently provides five day a week delivery of incoming/outgoing materials via ESLS. The NSE study assumes five day a week delivery would continue outside of ESLS with associated increased costs. No consideration was given to cost saving via shifting to 3, 2 or even 1 day a week delivery. The only other option considered was delivery via USPS at an enormous increase in cost. Also, it appears the NSE study assumes MPL would continue to supply interlibrary materials to all libraries it does now and does not give any consideration to potential reduction in volume of materials.

While the cost issue of materials delivery is not the largest one considered, it is an easily understood example of how narrow the NSE study is and how its limited focus drives limited conclusions. A true cost analysis would address options to deal with increased costs if MPL is operated outside of ESLS.

Lack of Cost Differentiation

The NSE study lacks significant differentiation between one-time costs and on-going costs. This is a serious fault in the study and leads to easy misinterpretation of the conclusions. The NSE study indicates there would be an annual minimum cost of \$350,000 to exit ESLS, assuming MPL buys its own software and equipment to replace those provided by ESLS. This number, however, is an inappropriate aggregation of one-time and on-going costs

It is recognized that if MPL were to sever its relationship with ESLS, it would have to acquire its own Integrated Library System software/hardware. There are two components to acquiring a new ILS; one-time, up front costs and on-going annual costs.

As an example, one of the ILS systems considered has a one-time, up front cost of \$200,000. The NSE study assumes this would be paid for over 5 years at \$47,000 per year (including financing costs). The \$47,000 amount is included in the \$350,000 minimum annual exit cost. As such it would appear the \$350,000 annual cost is a given amount indefinitely. No where in the NSE study is there a specific listing of one-time versus on-going expense. At best this is a very poor approach to financial analysis and at worst it is misleading to the casual reader.

The NSE study also offers the option of purchasing needed service from ESLS at an annual cost of \$300,000. As the study is structured, this appears to be the least expensive option.

The study should have differentiated costs as follows:

Option A: Purchase services from ESLS on an indefinite, annual basis: \$300,000

Option B Part 1:	One time cost to acquire software & equipment:	\$XXX,XXX
Option B Part 2:	On going annual costs thereafter	\$XXX,XXX

It may be less expensive in the long run to purchase needed software and equipment up front and then pay only annual costs thereafter. The structure of the NSE report makes it appear the cost of leaving ESLS is, at least, \$ 300,000.

On a five year basis, the Option A cost to purchase services from ESLS would be \$1,500,000 (5 X \$300,000). Option B (assuming up front costs of \$200,000 and on-going annual costs of \$150,00 for 5 years) would be \$950,000. Assuming the numbers are reasonably accurate, MPL could save \$550,000 by NOT purchasing services from ESLS. Yet, the NSE study supports the purchasing services as the best option. An error of this size is not insignificant.

Costs, Fees and Overhead

- The NSE study estimates an administrative overhead cost to replace ESLS, but shows no reduction in administrative overhead cost related to belonging to ESLS. In fact, no overhead cost is allocated to being part of ESLS currently.

- If the MPL would exit ESLS, but continue to provide interlibrary service to other parts of Sheboygan County, no effort was made to fully cost those services (and charge for full reimbursement) and therefore reduce MPL's operational costs.
- Sheboygan County provides over \$1 million in funding to ESLS. Of that amount, approximately \$500,000 is transferred to MPL by ESLS. If MPL were to exit ESLS, would the County still provide \$1 million of funding to ESLS? Any reduction in County funding to ESLS needs to be considered as a reduction in library costs to taxpayers.
- MPL has been the primary provider of interlibrary functions to other libraries within ESLS. The NSE study assumes MPL would have only additional costs by exiting ESLS. It neglects any potential for revenue generation by providing services outside of ESLS.

Summation

The NSE study is a great disappointment. It had the potential to be a useful study that would have added to the discussion. However, its narrow assumptions drive a narrow conclusion. It does not address multiple options and it is not representative of sound financial cost analysis. The obvious errors and omissions indicate this was not the right consultant and the methodology used was inappropriate. It should also be noted that all problem areas in the NSE study were not related in this document due to space limitations.