

Implementing mergers and consolidation across the public sector

The hard work's only just beginning

A view from practitioners about the challenges ahead



The burning platform

Deficit reduction and radical reform

The coalition government has made deficit reduction its number one priority. At the same time, it is pursuing radical reform programmes in health, in schools and in police and has an ambitious agenda to build a Big Society – putting people and localities at the heart of decision making and services, and fundamentally challenging perceptions about the role and structure of government. With politicians setting an expectation of achieving ‘more for less’, there is no doubt that the period ahead is going to be tough and turbulent.

The required structural changes across the UK public sector include a merger and consolidation programme that is certainly the most ambitious ever undertaken by a UK government. Public sector boards and senior managers need to be ready to respond – with pace and focus – to an unprecedented challenge in terms of how to make it happen.

The hard work on implementation is therefore only just beginning. While few precedents exist and little practical guidance on successful implementation is available, there is copious evidence that reorganisation

and restructuring often result in failure. This is not a problem unique to the public sector. Indeed, a review of the literature shows that between 50-80% of private sector mergers disappoint, with many destroying shareholder value.

The ambitious scale of the programme inevitably brings cost and risk attached to implementation, along with the potential to deliver huge benefits.

This report looks at how those charged with implementation currently perceive the challenges ahead and offers some practical insights on a way forward, to help improve the probability of successful implementation of these ambitious reforms.

Central government departments and quangos

As a key driver of change and reform, central government has a crucial role to play in setting the policy direction and providing oversight for structural reform across the whole of the public sector. The Cabinet Office and HM Treasury are operating through the newly established Efficiency & Reform Group (ERG) to drive this change through. A specific ERG initiative is the public

bodies reform programme, which will stimulate a significant level of merger and consolidation activity. New enabling legislation is an important component of this plan and will help facilitate the process of reducing the number and cost of public bodies.

The potential benefits of the government’s public bodies reform programme are huge and, importantly, much greater than the direct cost savings that will come from rationalisation of the bodies themselves. The real prize will be simplification of administrative processes, systems and management that currently form a complex maze from Whitehall to the front line of service delivery. This all too often blurs accountability and adds cost but very little value to public services.

Those quangos that continue will be subject to tighter governance arrangements and are likely to experience substantial funding cuts, forcing a re-think of their remit and operating model.

Health

The NHS White Paper, *Equity and Excellence: Liberating the NHS*, sets out the government's intention to reform the funding and organisational structure of the NHS. The key driver to these changes is the devolution of power and responsibility for commissioning to consortia of GP practices, with the abolition of both strategic health authorities (SHAs) and primary care trusts (PCTs) over the next three years. At present, it is unclear as to how commissioning responsibilities will be transferred. It is clear however that there will be a significant amount of merger and consolidation activity.

Some activity is already underway, with the separation of commissioning and provider functions of all PCTs by March 2011 and a growing number of acute and mental health reconfigurations.

The Transforming Community Services programme, launched by the Department of Health in January 2009, provides a driver for the disposal of provider arms by PCTs. Predominantly, disposals are through vertical integration (acquisition)

by NHS acute and mental health foundation trusts and NHS trusts, although some are proceeding to stand-alone solutions through the establishment of social enterprises and a small number of community trusts.

There is predicted to be a growing number of acute and mental health reconfigurations, through disposals to the private sector and foundation trusts. Potentially as many as 50 existing NHS trusts will achieve foundation trust status without informal or formal reconfiguration. Some of these will be sold, others merged and others forced to consider federated models to reduce risk.

While the provision of frontline services continues to be a political imperative, it will be impossible to provide savings without significant service redesign. Merger and consolidation activity has the potential to release significant management cost savings through back office reconfigurations, but all savings will need to be underpinned by radical changes to NHS staff terms and conditions if they are to have any real financial impact.

Higher and further education

Within the further education sector there have been a number of mergers in recent years, including, for example, the merger of three colleges in Leeds resulting in Leeds City College, to become the third largest college in the country. The college now has centralised functions, but provides services from a number of the original college sites. One of the obstacles to mergers within further education is the need for provision to be within a certain distance from target learners. This makes merger options more available to urban colleges than to those covering the wider geography of rural areas.

In the past, significant funds have been made available for such mergers and were frequently instigated by the former Learning and Skills Council, to address specific issues such as the quality of provision for learners. It is not expected that such funds will be available to the same extent in the future and there may be a greater need for the impetus to come from the colleges themselves rather than the funder/regulator. With the additional uncertainty over the future existence and role of the Young People Learning

Agency (YPLA) and the Skills Funding Agency (SFA) it is likely that the process will be more difficult in the short-term.

In the higher education sector, where institutions have more autonomy than further education institutions, higher levels of merger and collaborative working are anticipated. Much of this is based on the expectation that more higher education institutions (HEIs) will suffer from financial distress, especially those which have not built up levels of cash-backed reserves to see them through the leaner years. Such mergers can be challenging as institutions have strong brand identity linked to the particular type of learning and/or research they provide. Often, those institutions that may have complementary brands and teaching/research strengths, are not geographically close, making many of the benefits of merger more difficult to achieve. With this in mind, much of the focus to date has been on collaborative working.

Shared service agreements are being explored by a number of organisations. The Higher Education Funding Council for England (HEFCE) and the University & Colleges Admissions

Service (UCAS) published the results of a combined study in June 2009 exploring the possibilities of various institutions in London taking part in shared services for applications and admissions. The study identified both significant projected savings and support from the related organisations for such arrangements. Many cities have more than one HEI in the locality and while the target student audiences may be very different, these institutions working together on shared services is likely to be an increasingly popular option as cost pressures rise.

Social housing

After a relatively quiet period for mergers in the housing sector we are beginning to see more activity. The sector is not a stranger to mergers and the experience of housing associations will be invaluable to other not for profit organisations.

Historically, numerous group structures have been created whereby an umbrella group has the individual entities remaining as subsidiaries. This has had its benefits as it allows the individual identities to remain, while reducing costs through shared administration and increasing

such opportunities through economies of scale.

Recently, some groups have collapsed this structure, flattening it out and creating a single board. This was primarily in response to concerns over the costs of servicing numerous boards and the issues that can occur in the governance of these structures, in addition to internal competition. However, it also takes place after the identities of the subsidiaries have become more closely aligned. This 'two stage' approach may, therefore, be a consideration for other sectors where cultural fit is a major obstacle.

All elements of housing associations' public funding are now under threat and the pressure on associations will be greater than ever before to reduce costs, so that they remain financially strong and can continue to deliver more affordable housing as well as developing further the delivery of high quality services. This, combined with the reduction in the availability of financing for new projects and the pressures on servicing existing debt make the economies of scale associated with mergers attractive.

Local authorities

Many local authorities have been on business transformation journeys as a response to previous efficiency agendas. The scale of the government's saving targets means that more radical and innovative solutions will be required if current service levels are to be maintained.

There are already a growing number of examples of shared management arrangements, shared services, and the shared use of assets with local authority and other public sector partners. While these are all areas of consolidation – and we expect more authorities to adopt such arrangements – we are now seeing some authorities consider all-out mergers, as a response to the scale of savings required and to maximise the opportunities for realising efficiencies so that services and Council Tax levels can be protected.

It is also likely that local government will follow the lead of authorities such as Torbay Council and Westminster City Council in adopting a strategic commissioning model, with the authority focusing on the commissioning of services from the most appropriate provider – this could be the local authority itself, or via providers from the wider public, private or third sectors.

The government's Big Society agenda will provide impetus to this transition, in particular the development of civil society – social enterprises, charities, and community groups – with a greater service provider role, and an increase in the devolution of service design to the community level. In addition, there is likely to be a de-commissioning of some discretionary services to manage significantly lower levels of funding, allied to the development of the capacity of voluntary organisations to mitigate service delivery loss, and the use of innovative approaches to financing, such as Social Impact Bonds.

The ability of public service providers across a locality to take a strategic approach to area based budgeting, investment decisions and the management and delivery of services will increase, as localities respond to the government's restructuring of public services, such as the abolition of PCTs, the introduction of local economic partnerships, and the increase in academies and free schools. Whether such arrangements are informal collaborations, or formal mergers, it is likely that the government will empower both of these options.

Charities

The charity sector is accustomed to mergers, with some larger-scale mergers in recent years including those which resulted in CLIC Sargent and Age UK. The Charity Commission is supportive of both collaborative working and more formal mergers, providing that such actions are in the interests of the charities involved and a specialist team is in place to assist and provide advice on the more formal aspects of such arrangements.

There are various versions of collaborative working currently in place across the sector. These range from relatively informal shared resources on individual projects (perhaps through a service level agreement), through to federations (where one charity may act on behalf of a group of member charities), in addition to group structures where legal structures are put in place to bring individual charities together.

The Charity Commission's latest research indicates that 59% of charities have been affected by the economic downturn, and, while charities are becoming more optimistic that circumstances may soon improve, the same research indicates that 47% of charities expect the sector to be behind commercial organisations in hitting the recovery curve.

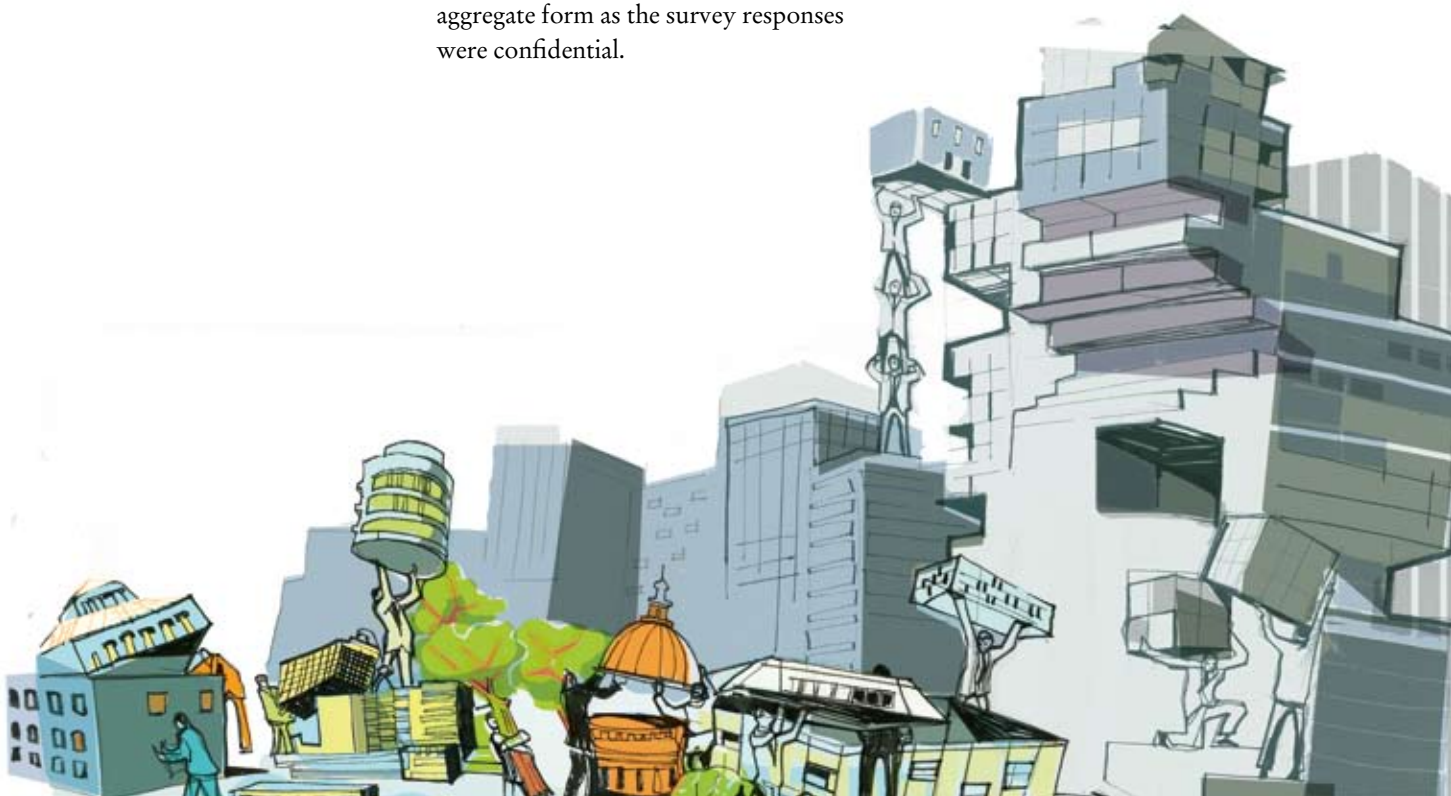
Combined with the direct financial effects of the downturn, the Big Society agenda and the stated intention for the migration of public services to the voluntary sector indicate an increased role for those charities that work together to become more responsive and more able to deal with greater demands on their services. The requirement for public funds to be dealt with transparently and within an effective governance structure often means that public sector bodies prefer to contract with larger organisations, creating a further driver towards merger and collaborative working.

About the research

To help understand the views of those that will be tasked to deliver the vision and reforms set out by the government, Grant Thornton with the Guardian commissioned a national survey of around 600 directors and senior managers, together with a number of individual interviews.

These research findings provide a practical insight into the concerns, challenges and opportunities faced by those about to deliver the reforms. They also gather the lessons learnt from practitioners who have already experienced mergers and consolidation.

The results are presented in aggregate form as the survey responses were confidential.



Implementing the vision

Recognising the challenge ahead

Our survey results highlight the opportunities and complexities of the challenges ahead for those implementing reform and seeking cost savings across government, as well as the optimism, nervousness and concerns from public sector managers.

While the political ambition to reduce costs and implement radical reform is a strong driver for change across the public sector, the personal incentives may be less clear cut and stakeholder relationships are often complex. Critical areas to get right include:

- **Plan** – ensure that the appropriate people, skills and plans are in place, available to support implementation. Seek specialist advice (legal, financial) when appropriate to avoid any unintended consequences and costly mistakes
- **Cost** – consider the full cost of implementation and ensure that a budget has been agreed and is in place before implementation begins
- **People** – focus on the integration of organisational cultures and ways of working, as well keeping staff and other stakeholders informed throughout the process
- **Leadership** – take the tough decisions early, making sure that the leadership team is in place to take ownership of the process and that clear incentives are in place for management to deliver change
- **Benefits** – be clear about the benefits, risks, and timescales of change.

I can think of two key issues for any successful merger. One is having a plan, a vision of a variety of work streams associated with systems and processes that are implemented, monitored and reviewed on a regular basis. You have to have a systematic approach to that vision to make it work. The second key issue is communication. It's a people business. You've got to make sure people understand where we're going and why we're going there. Obviously, staff feel uncertainty around any proposed merger.

Peter Roberts,
Principal & Chief
Executive of Leeds
City College

It was important to have: a very clear process underpinning the merger; a formal management team dotting all the 'i's'; and a clear commitment to making it happen. Our chief executive had undertaken mergers before and was absolutely driving the change programme. Having a person in a senior role who could bring in that experience was crucial.

Michelle Mitchell,
Charity Director,
Age UK

A focus on restructuring, merging and consolidation to deliver savings

Fifty-eight per cent of respondents state that they would expect their organisations to seek cost savings and efficiencies through a focus on restructuring, merger and consolidation activities.

Only 5% of respondents believe that the focus of work to deliver cost savings and efficiencies will be on outsourcing or private sector partnering.

These mergers will have a strategic element, but I believe that it's really the efficiencies at this stage that are giving it the drive to happen.

Nick Walkley,
Chief Executive,
London Borough
of Barnet

Providing an opportunity to realise wider benefits

The survey reveals that 74% of respondents are positive about mergers and consolidation as a means to reduce cost, but also recognise the opportunities that mergers create are not just about cost reduction.

Only 6% are doubtful about the potential benefits, but this is overshadowed by the 49% stating it is an opportunity to develop more strategic and smarter systems, and the 47% that saw mergers as providing an opportunity to innovate.

Fig. 1. As your organisation seeks savings and efficiencies, where in the next 12 months will the greatest focus be?

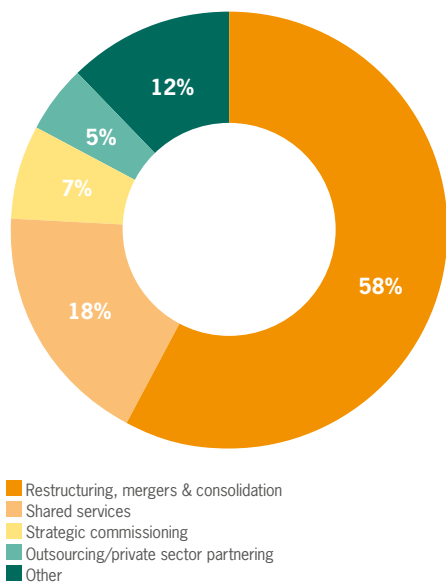
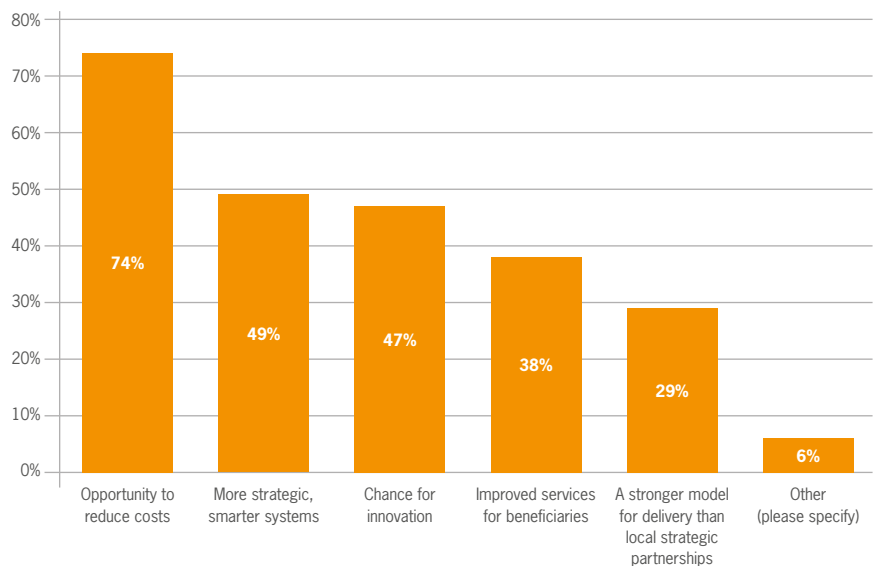


Fig. 2. What are the opportunities for organisations undertaking a merger or consolidation?



Savings are often exaggerated during the lead-in period to justify the merger, but with no evidence that anticipated benefits are achieved or to identify whether additional unpredicted costs were incurred.

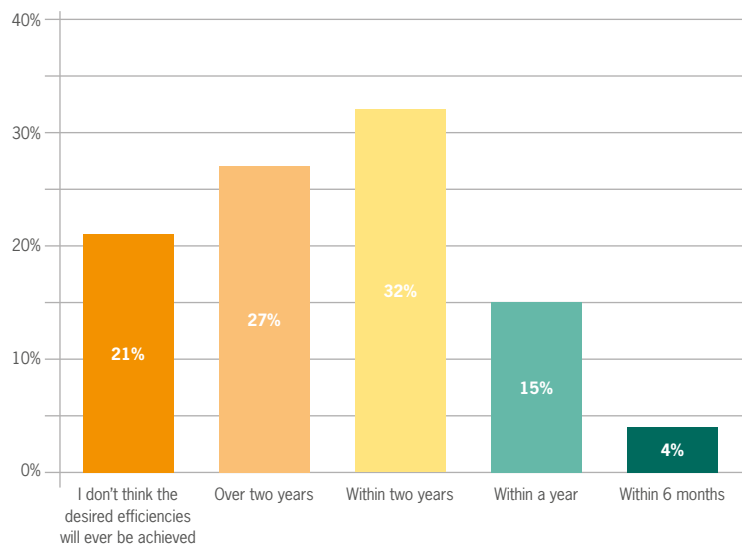
Survey respondent

The anticipated pace of change

The survey indicates that public sector managers anticipate a relatively rapid pace of change, with 51% stating that the benefits of merger activity will be achieved within two years or less after a merger has taken place. (4% believe that efficiencies will take effect within six months, a further 15% within a year, and 32% within two years.)

Experience suggests that respondents may be over-optimistic about what can be achieved within realistic timescales. Implementing change across the public sector has unique challenges and complexities that will have to be tackled to ensure a successful outcome. The evidence suggests change often leads to costly mistakes and unintended consequences where it has been pushed through too quickly without sufficient planning and budgeting.

Fig. 3. After a merger, how long do you expect it to take for the desired efficiencies to be achieved?



Restructuring and redundancies were done in a very consultative way while keeping up the pace. It was obviously a difficult and uncertain time, but we were very successful in having a staff focus and understanding their expectations – people are intelligent and understand the challenges, so it's not about spinning things. We lost around 200 jobs – over half were voluntary and only a handful were compulsory.

Michelle Mitchell,
Charity Director,
Age UK

The impact of previous mergers

Overall, the majority of respondents are negative about the impacts of previous mergers. Fifty-six per cent highlight that staff suffer the most, compared to the 30% who state that previous mergers have had a positive impact on efficiency.

Any level of change and cost cutting will always create a level of uncertainty for staff. Their needs have to be given careful attention and priority through the merger process to ensure a successful outcome.

Maintaining business as usual through the merger process is always challenging. If this is not managed carefully it can not only be disruptive in the short-term, but also risks causing longer-term reputational damage. Organisations need to consider what mitigating actions and interventions are required to motivate staff and maintain quality of service.

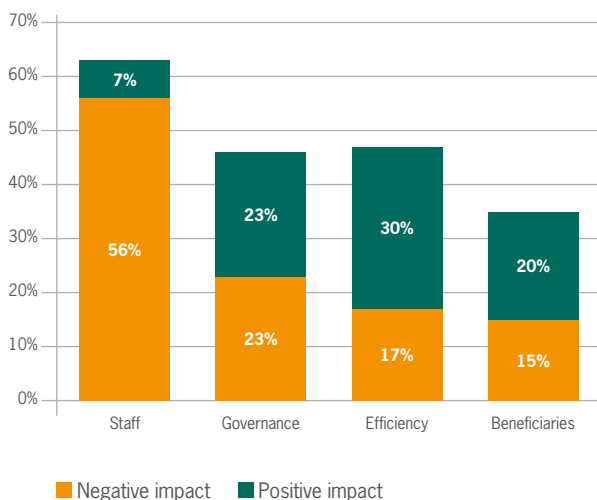
Research highlights that the importance of clear staff engagement and providing visible and accessible leadership are effective ways to keep staff informed

about progress and can help alleviate staff concerns and lessen the impact on morale. In addition, providing access to an appropriate level of human resource expertise to answer questions and alleviate staff concerns can help lessen the negative impact of a merger on your staff.

Staff are almost always negatively impacted upon through mergers. Not only through the higher likelihood of redundancies, but the increased pressures on staff to deliver much more with reduced resource.

Survey respondent

Fig. 4. In the main, what kind of impact do you believe previous sector mergers and consolidation have had?



The key is to be upfront and take a long-term view over several years. We wanted the single back office and as much possible to be out of London, with fewer offices. All staff knew that upfront. A lot of restructuring will be done by them for you, if staff share that long-term vision and decide whether they want to stay or not.

Trevor Beattie,
Director of Place Making
at the HCA

Former head of setup during the merger with English Partnerships in December 2008

The greatest impact on efficiency in the longer-term

The negative impact of previous mergers on staff is reflected within the survey results about what might have the biggest long-term impact in meeting the new efficiency agenda.

A reduction in workforce numbers is expected to have most impact on efficiency in the long-term (five years). While this aligns with ministers' views about the public sector now having to do 'more with less', the survey results also suggest that the driver for longer-term

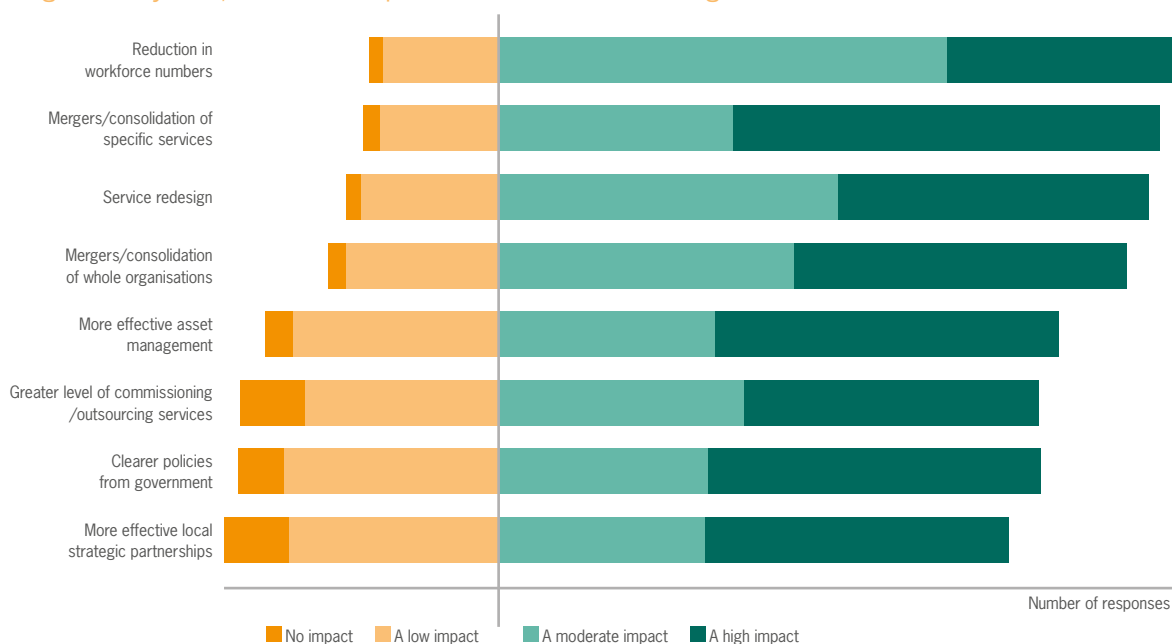
efficiency savings should also start challenging how organisations deliver public services and could stimulate more collaborative approaches to service provision.

When looking at cumulative responses for high and moderate impact, mergers of specific services rank alongside a reduction in workforce numbers as a key area that will have an impact on efficiency over the coming years.

This suggests that there are opportunities to realise savings by reducing levels of overlap in activity

and refocusing service provision delivery around outcomes. Collaborative and partnership approaches to deliver have been proven to be effective at reducing cost, but also enhancing the quality of outcomes delivered. Such approaches should be considered early when considering the options for merging and consolidating to reduce cost.

Fig. 5. To meet the agenda for greater efficiency in the long-term (5 years), how much impact will each of the following have?



The challenge of achieving the required benefits

While respondents are clear that there are opportunities and benefits associated with mergers such as reducing cost, developing smarter systems, and an opportunity to innovate, the results also highlight that achieving the desired results will be challenging to deliver.

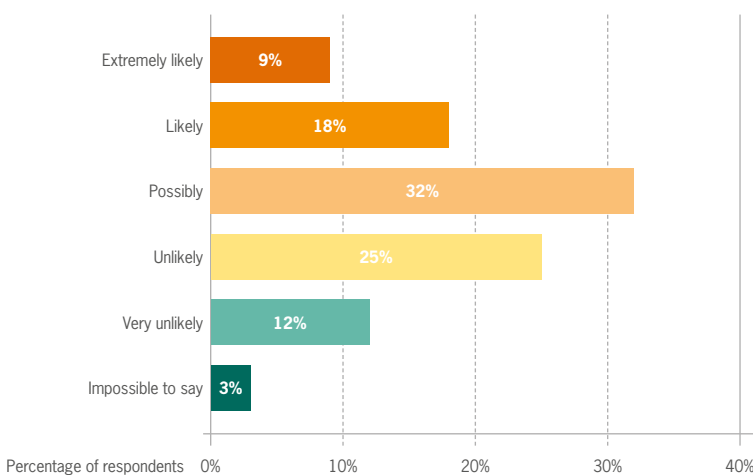
Only 27% of survey respondents are positive about the ability to achieve savings through mergers, stating that it is likely or extremely likely that the potential savings from a merger will be achieved. However, this is outweighed by the 37% who believe that it is unlikely or very unlikely that the desired savings will be achieved.

A merger may be the consequence of a decision depending on where you are trying to get to, but it's not the end in itself.

If you can work with staff and colleagues about establishing what the end game is, while it can be disruptive and challenging, you tend to get to where you intended because you involved people at the start.

Owen Williams,
Chief Executive of
Calderdale Council

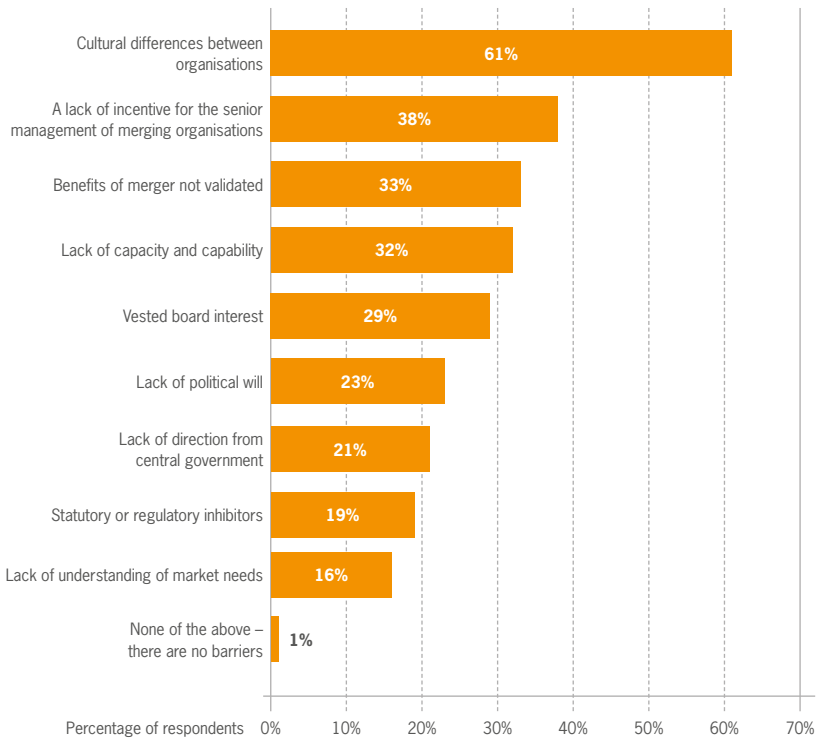
Fig. 6. How likely do you think that the potential savings required by your organisation will be achieved from a merger or consolidation?



Staff have different cultures which take time to bring together, and in the meantime there are risks of confusion, misunderstanding and error.

Survey respondent

Fig. 7. In your sector, what are the main barriers to organisations undertaking mergers and consolidations?



The main barriers

Cultural differences between organisations are perceived as by far the biggest challenges in undertaking a merger, with 61% stating it is the main barrier to a successful merger.

Thirty-eight per cent state that the lack of incentives for senior management is the second biggest barrier to delivering a successful outcome. Within our tightening fiscal environment those driving change will need to be creative when developing incentives for mergers across the public sector. Within the private sector, financial reward is often the most effective incentive. Within the public sector, however, financial incentives need to be considered as well as political and ‘power’ incentives. Our experience shows that the strength of financial incentives, whether positive or negative, should not be underestimated across the public sector as a stimulus to drive change.

Presentation (South London Housing Association) were in significant financial difficulties and that was the central reason for the merger – you could say there were huge incentives and no opportunity to do anything else.

Kate Davies,
Chief Executive of
Notting Hill Housing

After being involved in mergers at York, Stockport and Leeds, I can say with certainty that no two mergers are the same. They all have idiosyncrasies – there’s a core activity, but the cultures and context are always different.

Peter Roberts,
Principal & Chief
Executive of Leeds
City College

Consideration will need to be given as to what the right incentives are for all those involved and affected by the merger process. For those in senior management positions tasked with implementation, what are the benefits for them to drive through a merger? For those front-line staff whose workloads may increase and undoubtedly work routines will be disrupted, what incentives will help maintain levels of customer service through the disruptive period, and what incentives will help speed up the transition to business as usual?

The different sectoral challenges

Survey respondents generally state that their own sector is most likely to experience some form of merger and consolidation activity in the next 18 months.

Overall, 47% of respondents believe that the health sector is most likely to experience merger activity in the next 18 months, closely followed by central government (including arm’s length bodies) and local authorities.

To understand the differing complexities and challenges associated with mergers within different sectors, and to provide a practical and pragmatic perspective on implementing what can be a daunting task for many, we have broken our research findings down by sector and provided the insight and experience from business leaders within those sectors.

Sector	Level of respondents believing merger activity likely in the next 18 months
NHS trusts, foundation trusts and PCTs	47%
Central government including ALBs	45%
Local authorities	40%
Charities	35%
Social housing	33%
Higher and further education	29%
Police and fire authorities	19%
Other	3%

NHS, under the surgeon's knife

With the recent publication of the NHS White Paper and the current Transforming Community Services agenda, it is clear that the NHS will experience significant levels of mergers and consolidation activity. This is supported by our research, with 98% of NHS respondents (and 47% of all respondents) expecting some form of mergers and consolidation to take place in this sector in the next 18 months. Respondents expect this increase to have a high impact on workforce numbers and service redesign.

As expected, a high proportion of respondents highlight cost reduction (61%) as a key opportunity from mergers and consolidation. However, only roughly a quarter of respondents believe savings to be likely or extremely likely to materialise and only 13% responding that mergers and consolidation will be the

greatest focus of savings and efficiencies over the next year. This highlights the fact that most NHS managers currently see that the focus of savings needs to come from within their organisations rather than concentrating on wider, pan-organisational solutions. We see this due to two main issues, the need to identify local solutions driven by commissioning arrangements that traditionally concentrate on a single organisation, and a lack of strategic clarity and direction that has the potential to increase in the short-term with the winding up of SHAs.

Improved services for beneficiaries (47%) and more strategic, smarter systems (45%) are identified as further key opportunities. These findings reflect the desire to find wider solutions that need strategic, pan-agency decisions, particularly with the potential for NHS organisations needing to work far more closely with local authorities and the third sector to find cost-effective solutions to service redesign.

A number of barriers are identified by our research including:

- lack of capacity and capability (37%)
- lack of senior management incentives (35%)

- vested board interest (32%)
- lack of direction from central government (31%)
- lack of understanding of market needs (31%).

This highlights the significant challenges that face sectors in delivering the required level of change and efficiencies. The barriers identified as cultural issues above all represent concerns over the internal market and the lack of strategic direction that has created internal barriers to change. These barriers may be broken down by the move to greater GP involvement and responsibility for commissioning, but the solutions will have again a greater local focus that may increase the risk of ignoring sound, system-wide solutions to generating efficiency and decreasing risk.

With the NHS having undergone numerous structural changes and about to embark on another round of organisational reconfigurations, it is not unexpected that there is doubt and a lack of buy-in from personnel within the sector regarding the most recent proposed reforms.



Comment

Stuart Bell,
Chief Executive of South
London and Maudsley NHS
Foundation Trust

Stuart Bell has seen far-reaching changes in the NHS since he first joined in 1982. Now the chief executive for South London and Maudsley NHS Foundation Trust, mergers have seen his role expand to provide mental health services across London and the UK. The South London and Maudsley NHS Trust was formed in April 1999 as a result of the merger of Bethlem and Maudsley NHS Trust, Lewisham and Guy's Mental Health NHS Trust and the mental health services of Lambeth Healthcare NHS Trust, and can trace its history directly back to 1247 – making it the oldest psychiatric institution in the world. The Trust now services two million patients every year with a turnover of £2 billion – what lessons can be learnt from their experience of mergers?

A healthier ten years – health sector mergers have been a great success story of the last decade

Around ten years ago, an awful lot of mental health trusts went through mergers. If you take London as an example, back then there were about 25 mental health trusts. For the last five years there have been ten or so. All over the country there were these consolidations. The reasons were that they had often tended to be relatively small organisations, combining mental health services and community health services, and these community services were being moved into specialist providers.

Interestingly, those mergers have been pretty successful. There are some obvious cases where two hospitals next to each other have been put together and it hasn't always worked, but people only seem to notice these cases that attract attention. A very significant – and in some cases complex – series of mergers have on the whole seemed to work.

You need to be clear about what it is you intend to achieve when you embark on doing it, and there were well defined objectives for the organisations that came into being. For a start, they were focused on the provision of a particular type of service, mental health services, and they were also explicitly committed to providing a networked approach to care. They were clear about the partners they needed to engage with, both the local authorities to begin with and later on the primary care trusts. Given that you knew what it was that you were trying to achieve, you had some pretty clear measures about how successful the merger was.

An important lesson was that there is a susceptibility to see a quick change in leadership as a panacea, but frequent, ill-considered changes in organisational configuration can have a disruptive effect. If one looks at many of the successful United States healthcare providers,

you will see that they have had very stable leadership for long periods of time – fifteen or twenty years. They've had stable leadership teams and develop their own talent from within. That gives a consistency and continuity to the organisational direction, and you're also able to come to terms with your own mistakes and sort them out.

The mental health trusts learnt from each other. One of the things that the mergers made possible was the operation of more effective networks: if you take London, where you originally had 25 organisations, that's quite a large group of people to bring together in a way where you can learn effectively from one another. We've had a very successful network over the last ten years where there's been around ten of us: that's a group that can really do things together.

Mergers are an essential part of business life, and the NHS has had its fair share of them over the years. The most significant issues in success that we have seen are:

- **leadership** – strong leadership is essential, along with the judgment as to how much work and effort the organisations themselves are willing to invest in the new organisation
- **creating a vision** – not all organisations can create enough of a compelling vision to energise and concentrate the legacy organisations on the future

- **good communication** – the stakeholders to any public sector merger are numerous and complex, and getting messages right, concentrating on success is essential not only for the external audience, but probably more importantly for the staff and patients of the new organisation
- **a commitment from the board to see it through** – the old adage 'failing to plan is planning to fail' is so appropriate. Boards that structure mergers properly, taking account of all

aspects of the integration and not just concentrating on the (predominantly) financial benefits of the merger, are the ones that tend to succeed the most.

The key is getting provider organisations fit for purpose and able to confidently face the future as solid, well performing foundation trusts.

Whitehall, a lean and mean centre

Central government departments have recent experience of restructuring and reorganisation. A recent National Audit Office report earlier this year noted that between May 2005 and June 2009 there were over 90 reorganisations across central government.

Despite this experience of change, our research revealed that 37% of central government respondents see a lack of capacity and capability as a key barrier to implementing a merger. As departments embark on a programme of significant public rationalisation, those driving and implementing change need to learn from this experience.

A key finding from the recent National Audit Office review is that departments fail to robustly forecast and compare the costs and benefits of alternative options to implement a reorganisation. As a consequence,

public bodies frequently run the risk of carrying out reorganisations unnecessarily, and with no certainty that the chosen approaches are the most cost effective. Departments and public bodies should assess the costs and benefits of a full range of alternative options at an early stage in identifying the best course of action.

Government bodies are weak at identifying and securing the benefits they hope to achieve from a reorganisation. There is no standard approach for preparing and assessing business cases, and robustly setting out intended benefits against expected costs.

Departments fail to demonstrate value for money of a reorganisation as most have vague objectives and have not developed a clear approach to realising benefits, a view supported by 29% of survey respondents who stated that not

validating the benefits was a barrier to a successful merger.

The ability of government to identify reorganisation costs is also poor. With no requirement to set reorganisation budgets, few departments, and only a half of public bodies, begin implementation with a sufficient budget in place. In addition, there is no requirement for bodies to disclose the costs of reorganisations after they happen – meaning the true cost of reorganisation is often hidden.

The decisions to reorganise departments and arm's length bodies are often taken at short notice and with inadequate understanding of what can go wrong. Reorganisations of departments are generally announced before appropriately detailed project plans are in place, with only a quarter of arm's length bodies having the necessary plans in place before an announcement is made. This approach often leaves management teams planning and implementing reorganisations simultaneously,



with inadequate understanding of what can go wrong, and frequently leads to poor communication with staff, and prolonged levels of uncertainty and low morale – ultimately having a detrimental impact on the quality of service provided.

There are some key learning points here for managers as they face the task of implementing Spending Review decisions over the next few years, not only in Whitehall departments where 18% of respondents expect to be directly affected but also in non-departmental public bodies (NDPBs) where, at the time of our survey, 27% believed they would be affected; as choices are made about which services continue to be delivered by the public sector, which migrate to the third and private sectors and which are stopped.

The cultural barriers to implementing a merger are ranked highly for both central government survey respondents (64%), and for NDPB respondents (57%). The complexity of the task ahead will be exacerbated by the rapid pace of change needed to generate the required cost savings. A fast pace of change will risk forcing poor decision-making with no clear understanding of costs, risks and benefits. However, the speed of change will also leave the many public servants tasked with implementation faced with a minefield of complex legal and regulatory barriers to navigate through, as was highlighted by 30% of survey respondents who stated that

regulatory inhibitors were a barrier to implementation.

Despite the challenge ahead, there is a big prize, and significant savings, to be made in reshaping the central government and public body landscape. While it will be important to maintain momentum in delivering change, the complexity of implementation and the tough decisions ahead should not be underestimated.

Reshaping and rationalising the landscape will provide not only an opportunity to reduce costs as stated by 77% of our central government survey respondents, but will also create unique opportunities to sharpen some of the complex governance and accountability arrangements that exist between departments and public bodies.

Simplifying the reporting structures and relationships will not only release cash savings, but can also leverage substantial additional benefits (perhaps 10 times the direct cash savings) through speeding up funding and reporting processes, reducing bureaucracy and simplifying delivery chains, which frees up extra resources for the frontline.

What is clear is that a reshaping of central government will change the nature of the relationship that departments have with the public bodies they fund. As the driving force behind the reforms and the decision makers, it is likely that Whitehall departments will put quangos under severe pressure to deliver the lion's share of the savings.

Local authorities, rising to the challenge

Local government will need to identify and implement radical solutions to contribute to the required scale of deficit reduction. In rising to this challenge our survey highlights that merger activity will be a focus for local authorities, with 40% of respondents believing that local authorities will experience merger activity in the next 18 months.

Our survey highlights that 46% of local authority respondents believe that local authority mergers will provide an opportunity for realising innovative approaches for improving service delivery.

Given the scale of reductions to local authority spend being forecast, it is perhaps not surprising that 67% of local authority respondents believe that local authority mergers will provide an opportunity for realising significant cost reductions. Such cost reductions will relate to the rationalisation of executive and senior management posts in the merged organisation, but also from wider economies of scale that a merger can provide.

It is clear that the reductions in expenditure required by the government will place many local authority services under threat, particularly those of a

discretionary nature, such as arts, sports and leisure services. While the government's Big Society agenda seeks to provide a solution to this problem, local authorities must now manage the expectations of the recipients of their services and engage them in the debate on the prioritisation of their spending. In addition, the focus of any major service redesign must remain on local authority customers. This customer focus was reflected in our survey which highlights that 34% of our local authority respondents believe that mergers provide an opportunity to improve services for citizens.

Strategic partnering as an alternative option for service delivery is also high on the agenda for many local authorities. Our survey findings indicate that mergers are also set to become a significant option for consideration in the short to medium-term, with 33% of local authority respondents believing that formal merger activity will provide a stronger delivery model for

local authority services, than via strategic partnerships with private sector partners.

Not unsurprisingly, cultural differences are seen as the most significant barrier to successful merger activity (61% of local authority respondents). This is in line with wider research on successful change management, which identifies behavioural change and successful organisational leadership as prerequisites for maximising and realising benefits. This understanding may have contributed to the following also being highlighted as inhibitors to effective mergers: a lack of senior management incentives (37%); a lack of political will (36%); and the benefits not being validated (34%). As with other sectors, these findings highlight the importance for local authorities in having appropriately skilled and motivated staff to lead and deliver the changes required over the short to medium-term.



Comment

George Garlick,
Chief Executive at
Durham County Council

George Garlick was appointed by Durham County Council in 2008 to lead a reorganisation of local government. Part of the 2009 structural changes to local government saw the eight existing councils in the county amalgamate into a single unitary authority. Employing 22,000 staff and spending in the region of £1bn a year, the unitary authority has been seen as a great success story of the area, at a time when efficiency and innovation have been watchwords for the public sector.

The unitary solution

The unitary movement is very much based on the idea of bringing together district council and county council functions over a coherent geographical area. It is about giving stronger political leadership and stronger economic drive to an area, freeing-up considerable resources through economies of scale and improving services by bringing things up to a best-practice level.

Previous unitary reorganisations hadn't been on the scale of this last one. In contrast, Cornwall, Durham and Shropshire are all new unitaries with populations around the half-million mark. These were a new beast and part of the experiment that was going on to see how far you could push the unitary concept. Certainly we found that it has worked very well.

The key to it for me has always been to aim for a stable platform on day one of the new authority.

Effectively, services transit into the new organisation so that the customer, the people of the area, don't notice that anything has happened. It's best not to get too hung up on some of the very high-level stuff, because you inevitably have a couple of years at least after reorganisation where you start to bed down, particularly with central support services. The key thing is to get the actual front line services running on day one and then improve the support services as you go through the process.

In terms of the former district functions that we've brought together, in virtually all cases they're operating at a much higher level than they were under the former local government set-up within Durham. A lot of that is down to what was, certainly for Durham, innovative best practice which we were able to bring in, particularly with new senior managers and directors with experience right across the board.

We were bringing in a lot of innovation, a lot of new ideas, and really refreshing and trying to bring up to best practice a lot of the stuff that hadn't been happening in Durham for a long time. I don't think that's exclusively an issue for Durham, I think it's true in any area that this kind of radical change gives you an opportunity for refreshment.

To succeed, it has to have very strong commitment from the political and managerial leadership. We've seen over the last ten years a lot of possible shared services networks, often at county district levels, which at the last moment as they've gone towards creation have fallen away. You have to say: "Right, we've chosen to do this and we're going to end up doing it." There has to be an absolute commitment.

While the government stopped the previous administration's plans for local government reorganisation, there is an emerging trend for local authorities to progress opportunities for mergers and collaborations. This has taken the form of a merged service (such as Westminster City Council and the London Borough of Hammersmith and Fulham's plans for a joint education service) or discussions on more wholesale merger activity (such as Mid Suffolk and Babergh District

Councils announcing their intention to investigate a full 'constitutional merger').

It is likely that smaller, typically neighbouring, district councils will consider merger activity, particularly where shared management arrangements already exist or are being planned – there are around 11 local authority joint chief executives in place – and this trend is likely to increase as part of local government's response to the cuts agenda.

This is supported by our survey results,

with mergers in particular being seen as a potential solution to realising significant savings, while maintaining the quality of service provision. The survey also recognises that, for mergers and consolidation to be realised, authorities will need an appropriately skilled leadership team to successfully manage the merger process, not least to ensure that behaviours and organisational cultures become aligned, and that the benefits from merging are maximised.

Charities, spare some change

The charity sector is unique in its variety. The sector has a relatively small number of large organisations and a very large number of very small entities, often relying on a significant number of volunteers and part-time employees.

While the headline mergers have resulted in the large becoming even larger, much of the focus for mergers is on the smaller charities where administration represents a significant burden, and cost and transparency and clear strategies are harder to identify and implement. This is reflected in our research finding that 57% of respondents (the highest score for that category) believed that merger would lead to smarter and more strategic systems. The sector was also ranked

as fourth most likely to experience mergers within the next 18 months, indicating that the volume of media commentary and the recent Charity Commission campaigns may have raised expectations of such activity.

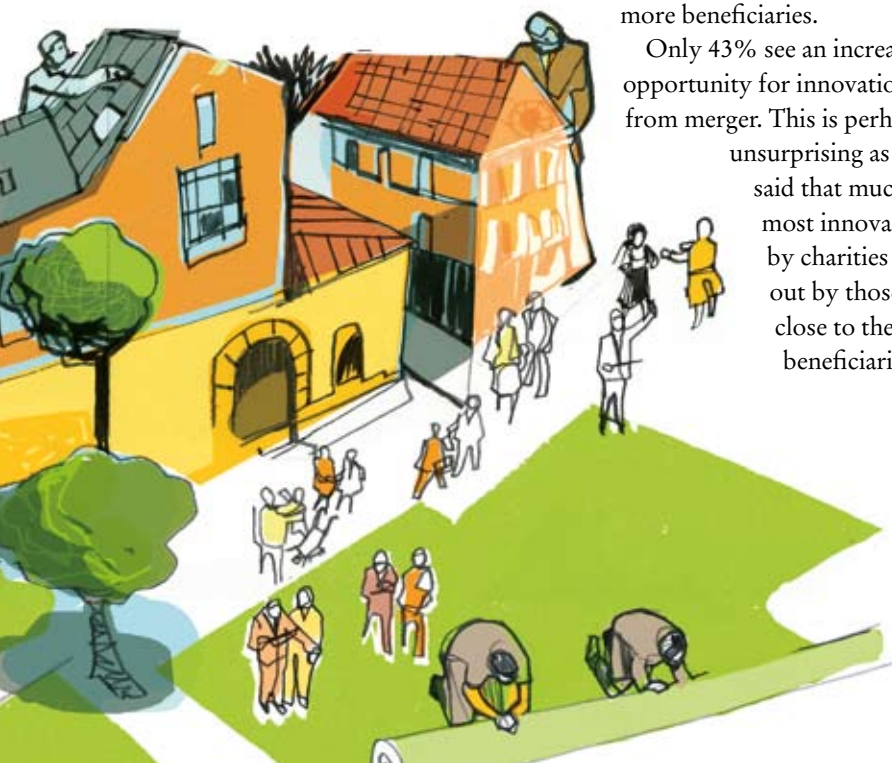
Interestingly, in a sector where the needs of beneficiaries are held above all other objectives, only 45% see merger benefits as including improved services for beneficiaries while 83% see an opportunity as being cost reduction. This perhaps reflects the impact of the conflicting demands from increasing needs for services and reductions in funding, focusing the efforts of charities on becoming as cost effective as possible in meeting the basic needs of more beneficiaries.

Only 43% see an increased opportunity for innovation resulting from merger. This is perhaps unsurprising as it is often said that much of the most innovative work by charities is carried out by those who are close to their beneficiaries, often in

smaller grass roots charities where the work is reliant on the efforts of a small number of individuals unimpeded by complex systems and processes.

The charity sector often has leaner finance teams in an effort to keep central costs lower, and this may be the reason that a high number of respondents thought that a key barrier will be lack of capacity and capability (38%). Charities are often unable to afford the fees of the professional advisers necessary to deliver a successful merger, a fact acknowledged by the Charity Commission. To address this the Charity Commission has published several guides (eg CC34 Collaborative working and mergers: an introduction), and has a specialist unit available to assess individual mergers and identify possible legal pitfalls.

Trustees generally become involved in a particular charity as a result of a strong personal belief in the objectives of the charity, as do many senior management team members. This can have serious implications for a successful merger as some board members may not find a role on the new board and senior management roles are reallocated. The research findings support this with 40% of respondents stating a vested board interest and 46% noting a lack of senior management incentive as barriers to a successful merger.



Comment

Alan How,
Finance and Resources
Director at Anthony Nolan

Alan How is Finance and Resources Director at Anthony Nolan, ensuring the charity's infrastructure operates efficiently. Previously, he worked with Age Concern England and was a key player in their 2009 merger with Help the Aged, forming the new organisation Age UK. A strong finance background and experience of private sector mergers and acquisitions contribute to his practical approach to the problems of merger in the charity sector.

Experiences of not-for-profit mergers prove it's hard work, but rewarding.

A major motive towards the merger of Help the Aged and Age Concern England was that there was confusion between the two different organisations. That overlap was the essential driver, and then when you put two organisations together you don't need two chief executives and so on, so you get resources released. If you look at the Cancer UK merger, which was done in a more benign financial climate, I believe that some of the benefits that Cancer Research UK achieved in their merger stemmed from the success of their legacy income which exceeded their predictions.

One reason why Age UK was able to merge from two charities was that their two chief executives had both decided to accept retirement. The opportunity to choose one new chief executive was easier in that scenario, and perhaps easier than it had been for twenty years.

I was working probably 90 hours a week for the last 18 months: you just can't address everything that you

could do previously. Inevitably there is a downside effect on some elements of beneficiary support. You can't focus on the external world because the internal world suddenly becomes the only thing you are worried about.

As a way to smooth the process, the merger team brought in consultants. There are some pluses and minuses to that. They are experienced and bright, but they don't know your business. They evaluate your business and join two organisations up in the way in which they have been familiar. There aren't people who are experienced in both the charity sector and mergers who you can go to. There are people who are good at charities, or people who are good at mergers, but not the two. It's a new paradigm we're still seeing unfold.

In the near future, some charities will have to merge simply because they'll fail otherwise. I suspect there will be more rescue mergers taking place of the kind that happened to ChildLine some years ago. They'll need to be combined

with somebody else to continue some level of service, but there will still be some that fail and just cease to exist, I have no doubt about it. Conversely, there will be charities that see an opportunity to expand their services, and that will also happen more and more: the main issue is if they have the resources to manage the merger.

Where things are unclear is the overlap between charity sector and public sector organisations. If a charity service and a public sector service can combine for efficiencies, there may be problems with the standard model of merger. Pensions, for instance – will the charity take on the much more generous pension packages of the transferred public sector staff, or vice versa? It will cause problems that don't exist today. It might mean that a new model needs to be developed, a model for public sector and charity mergers that's distinct from charity/charity mergers.

Although charities must identify areas of overlap in order for a merger to be of value, and many mergers involve charities with very similar objectives, cultural differences can be a significant issue as charities often have a very individually developed ethos and identity. Sixty-two per cent identify cultural differences as a barrier to merger. This is particularly an issue for smaller charities where individual trustees may have a strong influence on the overall behaviour of the charity.

The driving factor behind mergers in the charity sector is likely to continue to be cost reduction. Even without the economic downturn, the pressure from donors, other stakeholders and observers to reduce the proportion of income spent on administration and central services will always create an argument for merger and collaborative working. As mentioned in the case study, there are also instances of donor and stakeholder confusion where significant overlap exists between the objectives of two or more charities.

In addition, as opportunities increase to provide services on behalf of the public sector, charities will be expected to demonstrate increased strength, both financially and structurally. This is an issue only likely to be resolved through fewer, larger charities bidding for contracts, or charities working together in collaboration to successfully win contracts. The support from the regulator to ensure there is no detriment to beneficiaries from such mergers is essential.

Social housing, at home with a new agenda

Given the emphasis on the quality of services to tenants and other service users within the housing sector, it is perhaps unsurprising that 52% of respondents identify an opportunity from merger and collaborative working as improved services for beneficiaries, and is the highest response for this opportunity out of all the sectors.

The respondents from the housing sector are, however, least likely to identify the opportunity to innovate as a benefit from merger, with only 35% believing this to be the case. Perhaps this acknowledges that as economies of scale are implemented costs can be reduced, but at the expense of a grass roots understanding of the needs of individual tenants and the ability to respond in innovative and less formulaic ways. Any move away from the reflection of local needs is likely to result in lack of support from both tenant groups and regulators.

Of the respondents, 89% identify cost reduction as a key opportunity from mergers, one of the highest response rates across the groups surveyed (and 15 percentage points higher than the overall group result). Given the other options available within the survey this is likely to include those who see merger as an opportunity for those in financial difficulty or unable to secure funding needed for their business plans.

As would be expected given the past experience of the sector, 65% of

respondents believe cultural differences to be a significant barrier to successful merger, higher than the average score across all the sector groups. While this is a possible barrier, as previously discussed the sector already has mitigating practices in place for this obstacle, the retention of the identities of the merged entities by creating a complex group structure. This is also reflected in the fact that more respondents than in any other group (50%) believe that vested board interest is a barrier to successful merger.

Respondents state that the benefits of the merger not being validated is a significant barrier to merger (43%), compared to the overall group rate of 33%, perhaps reflecting a level of cynicism regarding the resulting benefits of past merger activity or a concern that insufficient clarity is obtained over actual benefits before negotiations are finalised.

Interestingly, our research shows that only 26% of respondents believe that a lack of capacity and capability will be a barrier, compared to 32% in the overall group. This may be an acknowledgement of the knowledge built up within the sector from previous merger activity.

Encouragingly, also based on past experience, the social housing sector reports the highest proportion of positive impact from previous merger activity and the lowest negative impact. In addition, the sector's respondents also anticipate the benefits will occur in a proportionally shorter timespan than other groups and

record the highest likelihood that the sector's desired savings can be delivered through merger.

The research appears to reflect a more mature attitude of the sector to mergers, and the recognition of the importance of beneficiary needs and cost effective delivery in any decisions taken by housing associations along with the negative effect that culture and personality can have on the success of any such activity.

Mergers will certainly remain on the agenda and we may well see the creation of groups with over 100,000 properties under management. However, there is a catch – the expectations of government and the regulator are for local service delivery, meeting local needs, engaging with tenants at a local level, and the ability of large-scale organisations to deliver on this agenda will be a massive challenge. Whether it will prove to be bigger and better will only become apparent in the longer-term.



Comment

Kate Davies,
Chief Executive of
Notting Hill Housing

Kate Davies is the Chief Executive of Notting Hill Housing, an association whose tenant base has expanded thanks to a successful growth strategy. In 2009, that strategy included a merger with Presentation, a South London housing association in financial difficulty. Before Notting Hill, she served as Chief Executive of Servite Houses and Director of Housing in Brighton and Hove.

Mergers of housing associations are a special case with distinct characteristics.

The financial situation is quite difficult for housing associations at the moment and it's about to get even worse. Some of them will be pushed over the edge. As it gets more difficult, mergers are a way of making sure the tenants will be looked after, because they'll be going to a bigger group.

Housing associations are judged in three ways: their management; their governance; and their financial standing. In our case, Presentation was in significant financial difficulties and that was the central reason for merger, but there wasn't an awful lot else that was wrong with it. There was quite a ground swell of support for merger in the end. Presentation wanted it to happen; it gave the board, the staff and tenants security – you could say there were huge incentives and no opportunity to do anything else.

The merger prevented them going bankrupt. We ensured continuity of service, protected staff and took out £2m of overheads immediately. We saved a number of developments from going toxic and built homes that wouldn't otherwise have been built. It had to come into a safe haven; and that's what we did.

You can read up on private sector mergers and all they say is true. Where housing associations differ is that no money changes hands: you get the assets and liabilities of the other association. In our case, the assets were considerable, but so too were the liabilities. They had borrowed more than they should have to finance their developments and failed to follow their accounts, so the banks increased their cost of borrowing. That's what put them in danger; the expensive loans which we had to deal with immediately by refinancing.

Until recently, the regulators in the government have taken a position that neither encourages, nor opposes mergers. I think that they should take an even more hands-off approach in future. It's quite a long task to convince the regulators that everything is under control and good for the tenants, and that the process of consent and due diligence is carried out: it may be that the government begins to simply allow you to go ahead. On the other hand, because finances are so tight, if government feels that the capacity of smaller associations is rather wasted they might encourage them to merge with the bigger associations – it could go either way.

Higher and further education, merging of minds

I know there are a large number of colleges that are wondering about how sustainable their future is. There may not be as many mergers as people think, but some colleges are saying that they don't think they can continue as they are: only the bigger colleges can ride the higher waves we may see.

Peter Roberts
Principal & Chief
Executive of Leeds
City College

It is widely recognised that the higher and further education (HE/FE) sectors have a critical role to play in contributing to economic recovery and providing the skills base that will be essential for the UK economy to remain competitive in an increasingly global knowledge economy. Our research highlights that the sector will not be immune to the tightening fiscal environment, with 29% expecting some form of merger or consolidation activity to take place in the next 18 months.

HE/FE institutions have for a number of years explored opportunities to diversify and commercialise their teaching and research strengths in collaboration with private companies and other institutions, entering new markets, providing professional training development services and exploring the

potential of business spin-offs. With 80% of HE/FE survey respondents stating that mergers and consolidations of specific services offer the greatest opportunity to assist them to achieve long-term cost savings and efficiencies, our research findings indicate that more will be done across the sector to explore innovative and collaborative offerings.

As with many sectors, 74% of survey respondents state that cost reduction presents the largest opportunity through merger and consolidation activity, perhaps recognising the significant overlap that still exists in attracting overseas students in an increasingly competitive market. With some closely geographically located institutions already exploring the opportunities of shared services, collaborative cost reduction measures can be a significant option for many institutions.

Cultural differences emerge as the strongest barrier to successful merger (61% of HE/FE respondents), perhaps recognising the challenges and clashes that research-led and teaching-led institutions will face in finding the synergies in their offerings and branding. A lack of senior management incentives (50%), and benefits of the merger not being validated (41%), also feature highly as barriers to an effective merger. These findings highlight the fact that those institutions considering a merger will need to ensure they have the right people and the right skills to facilitate and implement change effectively. The education sector generally appears to be relatively sceptical about the impact of mergers with the respondents from this group being more likely to state that any benefits from merger would take a long time to deliver, and the highest proportion of respondents stating negative impact from previous mergers, particularly on staff and governance.



Comment

Professor Cary Cooper
CBE, Lancaster University
Management School

Professor Cary Cooper CBE is in a unique position to examine the concept of mergers in higher and further education. Leaving UMIST as it began its merger with Manchester University in 2002, he moved to Lancaster University Management School, where he is now Distinguished Professor of Organisational Psychology and Health. Professor Cooper also co-edits *Advances in Mergers and Acquisitions*.

Can HE & FE learn tough lessons from the private sector?

The main research shows globally that about two out of every three mergers or acquisition fail. By failure, I don't mean the company or the organisation goes bankrupt or disappears entirely, but they don't get what they had anticipated. In other words, the anticipated two plus two should equal five – but it ends up being more like three. There are three main reasons why they fail. Firstly, the motives of senior management are often personal. Secondly, the cultures may be wholly incompatible. The third reason is because the merger or acquisition is badly managed. Uncertainty creeps in, the good people leave the organisation in droves and what you're stuck with [are] the people who couldn't get jobs outside.

We do not have as many public sector mergers as we have had in the

private sector, but we are now likely to, given the scenario with public spending cuts. Employers may find out that they end up having more costs, because the merger is badly managed, loses good people and disrupts workflow and systems. We have to be very careful in considering any M&A in the context of higher and further education. Where it is going to be problematic is that they don't have the funds to get the support they need to manage the change. A lot of organisations such as schools and universities have professional people in them, but my worry is that academics seem to think they know how to manage change.

We are also going to have trouble in higher education mergers because some universities are research led, while some are teaching led: it could dilute the quality of the merged institution.

It's unlikely to be well managed because in universities people don't have the skills of change management, and they won't have the money to buy in help to do this. They are likely to lose a lot of good people in the process who will go elsewhere, particularly abroad, because we see that in all organisations. There have only been a few mergers in higher education, and I don't think any of them have been terribly effective. I think that the people in those institutions would admit that that's the case. Now, it's going to be even worse: at least when some of the other mergers took place, there was financial support to help in the merger process and change management. Now, with 25% to 40% cuts, how is that going to happen?

There is no doubt that both higher and further education institutions need to consider mergers and collaborations in greater detail over the coming months, with a greater motivation for making such arrangements successful.

A key obstacle will be overcoming the lack of available funding for such arrangements. Past attempts have not necessarily been overwhelming successes, and with cost being the greatest driver, the factors that create

success (skills and capability) are likely to be limited. Even where one institution identifies significant benefit from merger, persuading the other party may also be a challenge, as is the case in South East Wales where the University of Glamorgan has made a number of rebuffed approaches to the University of Wales Institute, Cardiff. Therefore, without specific incentives from regulators and funders that overcome the costs, there may be insufficient

reason for institutions that are successful to put themselves forward as potential merger partners.

The benefits from taking part in shared services for both further and higher education are much more attractive as they are perceived to have fewer downsides. For those institutions that have a need to cut costs but have an otherwise reasonable financial and strategic position, such collaboration is likely to be a much more popular option.

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