HAURAKI
DISTRICT COUNCIL

Hauraki District Council are appreciative of the work that the Productivity Commission have put into its review of local government funding and financing, and the opportunity to input into the report findings.

It is clear that considerable effort has been expended in the collation and production of the report.

Council appreciates the wide ranging nature of the commission's recommendations.

Hauraki agree with the majority of the commission's findings and recommendations. Our response to the commission's questions, and our comments on certain specific findings and recommendations, are attached.

We would like to convey our thanks to the commissioners, and to the staff at the commission, for the time they have put into this review, and for the professional manner in which the commission has undertaken the consultation process.

If you have any questions about any of response, please contact Duncan Peddie in the first instance.

Toby Adams
Deputy Mayor

Summary of questions

Chapter 3 –Trends in local government revenue, expenditure, prices and debt

Q3.1 Is the current methodology for preparing the Local Government Cost Index sufficient for forecasting the prices that local authorities are likely to face? If not, should the methodology be improved, such as by one or more of:

- carrying out more frequent reweighting;
- including output indices; and
- disaggregating by council type?

Council considers the current methodology is adequate.

Chapter 4 – Pressures on funding and financing

Q 4.1 To what extent are the Treaty-related costs associated with fulfilling the obligations and requirements under local government statutes "business as usual" for councils? And to what extent should they be considered costs incurred to fulfil obligations on behalf of the Crown under the Treaty of Waitangi?

Hauraki District Council believes that it has considerable room to improve in ensuring local iwi input across the whole range of council decision-making.
It is hard to quantify the potential cost to do this well, especially the level of funding for iwi groups that would be needed to enable good participation.
Council believes that council costs should be generally borne by local government, but that iwi funding may need a level of central government input?

Chapter 5 – Improving decision making

Q 5.1 The Commission is seeking more information on the advantages and disadvantages of reducing the frequency of Long-Term Plan (LTP) reviews, while retaining the requirement for annual plans. What would be the benefits, costs and risks of reducing the frequency of LTPs, from every three years to every five? What if five years were a minimum, and local authorities were free to prepare LTPs more frequently if they wished?

Hauraki recommend remaining with the current frequency and timing which is well matched to electoral cycle. The current timing is ideal as new elected members get to spend some time gaining an understanding of the issues and constraints facing their authority before they are required to create their plan. The plan sets the direction for the remainder of their term, and the start of the next term. If the planning frequency was longer then the next council may find it difficult to change the direction set by previous elected members.

Q 5.2 Is it appropriate for local authorities to include an adjustment for anticipated price inflation when they set rates each year? If not, what disciplines could be applied to the rate-setting process, to encourage local authorities to seek to manage cost and price pressures through productivity improvements? What would be the benefits and drawbacks of such an approach?

When planning over longer timeframes it is critical to recognise the effect of inflation.

Councils are continually endeavouring to drive increased efficiency through process improvements and taking advantage of technological change.

In most council activities, increasing levels of service driven by ratepayer expectations, and central and regional government regulation, are the major driver of cost increases. Inflation is also a reality that councils have to deal with. In the Annual Plan budget setting process at Hauraki, staff are required to justify the need for any inflation uplift. The inflation increment is not given as of right.

Q 5.3 Would establishing a capital charge for local authorities be an effective way of incentivising good asset management? What would be the advantages and disadvantages? Are there other, more effective ways of encouraging better asset management practices in local government?

Hauraki does not believe an overall capital charge would be a useful tool.
Unlike most businesses, and many government departments, the majority of council assets are not able to be traded in an open market. For most infrastructure assets there is limited opportunity to lease assets so the only choice is to own them.
A cost of capital calculation is a useful tool in the selection of asset solutions to decide between different alternatives.
A capital charge is already recognised to some extent in interest charged on that activity's debt balance
Hauraki believes there is limited usefulness in a Capital charge where no real choice

Chapter 6 – Future funding and financing arrangements

Q 6.1 How desirable and useful would a tax on vacant residential land be as a mechanism to improve the supply of housing for New Zealanders? How would such a tax measure up against the principles of a good system of local government funding and financing?

This is not currently an issue for Hauraki, but Council feels it is a tool worth investigating for other authorities.
In areas where there is limited land available it feels like it could be a useful tool.
There is anecdotal evidence of developer land banking
This is especially difficult for councils where they have supplied infrastructure to an area, and then a developer land banks this land for an extended period.
Such a tool could create difficulty for those who don't want to develop, e.g. a farmer on historic family farm on the edge of a city – but the local council is generally the best placed to evaluate the trade-off between the rights of current user and the needs of the urban community to expand.

Q 6.2 What would be the advantages and disadvantages of a system of payments to territorial authorities based on new building work put in place in each territorial local authority?
What would be the best design for such a mechanism? Would it be effective in incentivising councils to keep the supply of consented land (greenfield and brownfield) and local infrastructure responsive to growth pressures?

If the purpose of this tool is to incentivise councils to allow for growth then funding provided should be targeted, and not allocated on the basis of new building work in each authority.
Allocating on the basis of new building work would likely reward those councils where growth is happening anyway, whether the council is trying to encourage growth, or to curb it.
Using the fund for targeted grants for infrastructure required from growth would be better help councils struggling to provide for growth, esp. in those with currently low income communities.
The amount allocated to an authority would have to be significant to have any significant impact on council decision-making.

Infrastructure costs from growth pressure are lumpy and different from place to place. Targeted grants would better address these cost pressures.

Chapter 8 – Adapting to climate change

Q 8.1 What legal options exist for placing a condition on land-use consents that would make a voluntary assumption of risk by a current owner (and any person or entity who later becomes the owner) enforceable in all future circumstances?

Council is only aware of s72 of the Building Act 2004, which allows councils to issue a building consent despite a hazard being on the property. This allows a hazard notice to be attached to the land title.

Findings and recommendations

The full set of findings and recommendations from the report are below.

Chapter 3 – Trends in local government, expenditure, prices and debt

Findings

F 3.1 Over long periods of time, and with some variation, increases in local government revenue and rates have roughly matched increases in national and household income.

F 3.2 Local governments face higher price inflation than general consumers largely because of the specialised inputs councils use to construct and operate infrastructure. Councils have little direct influence on the prices of many of these inputs, but can adjust their demand and mix of inputs, in response to changes in prices.

Council has some ability to adjust its mix of inputs, but generally this is quite limited.

F 3.3 Modelling of price inflation in local government goods and services using an index that reflects yearly changes in the composition of expenditure produces a slightly lower measure of inflation than the Local Government Cost Index currently used by councils. This suggests that councils do adjust their mix of inputs in response to prices, to some extent.

F 3.4 After adjusting for price inflation using the Commission's preferred price index, local government operating expenditure (opex) per capita (excluding depreciation and interest) grew at an average of 1.2% a year between 2007 and 2017. The opex per capita of regional and rural councils grew faster than that of metropolitan and provincial councils.

One possible reason for the higher increase in rural councils, is being required to meet the same Three Waters environmental and quality standards as larger authorities, from a generally lower starting point

Chapter 4 – Pressures on funding and financing

Findings

F4.1 New Zealand's population has grown by about 30% in the last twenty years, but this growth has not been evenly distributed. Councils in high-growth areas are facing pressure from the costs of funding growth infrastructure, while some councils in small districts or districts with declining populations face pressure from high fixed costs distributed between a relatively small number of ratepayers. These challenges are likely to increase as New Zealand's population becomes increasingly concentrated in the future.

F4.2 All districts across New Zealand are ageing, and this is happening much more rapidly in some districts. An ageing population creates additional costs for councils as elderly residents require a different mix of accessible infrastructure and services.

F4.3 If some councils are not able to comply with all the responsibilities and functions being passed to them, then the objectives of central government legislation will ultimately not be achieved.

F4.4 When central government passes new responsibilities to local government, without providing adequate funding, this creates cost pressure for councils. Unfunded mandates fall broadly into four categories:

- new or stronger standards that councils must meet – without commensurate funding;
- new responsibilities, functions or processes that councils must undertake – without commensurate funding;
- reduction, cessation or removal of central government funding, or of government funded programmes and services within the community; and
- restrictions on the ability of councils to set cost-recovery fees for services or functions.

F4.5 Central government's passing of new responsibilities and functions on to local government is not new. However, this process has continued, and some councils are finding the cumulative impact increasingly difficult to manage.

F4.6 Central government is sometimes passing new responsibilities to local government without adequate analysis, including consideration of the range of council circumstances. This can result in regulation that is "one size fits all", making it unfit for purpose, or particularly costly to implement, in some localities.

F4.7 To date there has been no comprehensive and independent in-depth analysis of costs associated with implementing Treaty settlement arrangements – either to councils or iwi. Such analysis would be valuable to clearly identify the additional resources councils must deploy to carry out this role.

F4.8 Co-governance and co-management arrangements established through Treaty settlement agreements between the Crown and Māori can impose considerable costs on local authorities. So far, central government support has been ad hoc, and fallen short of covering the initial and ongoing costs to councils.

F4.9 Some councils are struggling to meet the costs of implementing Treaty settlement arrangements. The durability and effectiveness of some Treaty settlement arrangements may be at risk if funding issues remain unresolved.

F4.10 Evidence reveals no major shifts over the last several decades in the range of services that local government generally provides. The Local Government Act 2002 defines the purpose of local government as "to enable democratic local decision-making and action by, and on behalf of, communities". The nature, quality and extent of services provided by councils is reliant on the quality of their democratic decision-making.

F4.11 Community expectations for levels of service from local (and central) government are rising over time in response to factors such as:
- changing perceptions of risk from climate change;
- drinking water quality and impacts of discharges into waterways;
- changes in the age mix of local populations; and
- rising incomes (which make it easier for people to meet the cost of better quality and additional services).

F4.12 Tourists use the same local infrastructure as residents. The seasonal nature of tourism in New Zealand creates the need for this local mixed-use infrastructure to be able to accommodate peak visitor numbers, even if that peak only lasts for a few weeks or months. Some communities have a high visitor-to-resident ratio during peak tourist season, which can create significant pressure.

F4.13 Local authorities have access to a range of tools to address pressure from tourism.
Councils appear to under-use some of these tools, including user charges and targeted rates. Yet, even with more effective use of existing tools, a funding gap remains because tourists do not fully pay for the costs of the local mixed-use infrastructure and services they use.

F4.14 Rates of afforestation will increase as New Zealand transitions to a low-emissions economy. This increase in forested land will result in considerable new pressure on many local roads, particularly at harvest time. This will, in turn, lead to a need for more frequent maintenance and replacement of roads, resulting in increased costs. The cost pressure this creates for some councils may indicate a need to re-examine how funds from Road User Charges are distributed.

Chapter 5 – Improving decision making

Findings

F5.1 The elected member governance model does not consistently deliver a mix of councillors that collectively possesses the full range of skills required for effective governance, and evidence shows that many councils lack the necessary expertise for effective decision making. A lack of skilled councillors can be ameliorated by having a well-qualified and suitably experienced Chief Executive.

F5.2 A wide range of training, resources and supports are available for elected members.
However, the uptake of these is patchy. Reported barriers include reluctance to travel, public scrutiny of travel and training expenses, dissatisfaction with training provided, and lack of personal awareness of the need for capability development.

F5.3 The accountability of local government to local communities is highly reliant on the transparency of its processes, decision making, and performance.

F5.4 The current performance reporting requirements on local authorities, including the financial and non-financial information disclosures, are excessively detailed, inappropriately focused and not fit-for-purpose.

F5.5 Successive legislative reforms aimed at increasing the transparency of council performance through prescriptive reporting requirements have been counterproductive. The local government performance reporting framework requires fundamental review, with a mind to significantly simplifying the required disclosures,

and improving their overall coherence and fitness-for-purpose.
Agreed
This review should have a focus on plain English and readability. There is a need to reduce the overall quantity of disclosure with better targeting of disclosure to those decisions where councils need community input.
There is currently a lot of compliance disclosure that is not approachable to the general reader

F5.6 While the purpose and content of Long-Term Plan consultation documents are prescribed in legislation, the form and manner of engagement are not. Councils are free to undertake early engagement to ask open-ended questions, and use a wide range of techniques tailored to their local communities. Some are doing this effectively.

F5.7 There is scope for greater transparency across councils, in how they have considered and balanced the range of community views in their decision making.
Hauraki believe this is a work in progress and has improved considerably over the last few LTP's. Councils often incorporate the best examples of presentation from other authorities in future LTP's.

F5.8 Long-Term Plans (LTPs) are long, complex and contain duplication. This is partly a function of the legislative requirements, which are disjointed and require an unnecessary level of detail. This works against the strategic intent of LTPs.

F5.9 The benefits associated with auditing Long-Term Plans and their consultation documents currently exceed the costs. These benefits include assurance and transparency for the general public, as well as recommendations and advice for councils about good practice.

F5.10 A clear strategic framework is an important mechanism for guiding councils' prioritisation and resource-allocation decisions. While the current legislative requirements impose parameters around the content of Long-Term Plans (LTPs), they do not preclude the preparation of a strategic framework, and alignment of the LTPs and other accountability and planning documents within this. A number of councils have done this successfully; others lack a coherent framework to guide their strategic planning.

F5.11 Undertaking long-term planning within a spatial planning approach promotes a more coordinated and integrated approach to strategic planning as well as investment decision making.

F5.12 The effectiveness of the decision-making procedures by local government depends on the public understanding, and taking part in, local democratic processes – both of which are notoriously deficient. This weakens the incentives that those processes provide for local governments to be accountable for the quality of their decisions.

Recommendations

R5.1 The Department of Internal Affairs, Local Government New Zealand (LGNZ) and the New Zealand Society of Local Government Managers should work together to improve basic governance, including financial governance, skills and knowledge across elected members. In undertaking this work, they should consider:

- a range of mechanisms, such as formal training; peer support, mentoring (eg, via "sister council" links), and networking; and sharing of resources and best practice; and
- a variety of delivery platforms, including online media and collaboration tools.

LGNZ should ensure that resources and initiatives are well evaluated.

R5.2 Local Government New Zealand should work to achieve greater participation in ongoing professional development by elected members, including new and existing members, to ensure skills and knowledge are built and periodically refreshed.

R5.3 The Local Government Act 2002 should be amended to require all local authorities to have an Audit and Risk Committee (or equivalent assurance committee).

- Audit and Risk Committees should have an independent Chair, and ideally include at least one other external expert, to ensure they span the full range of necessary skills and experience.
- Independent members should be appropriately skilled and qualified.
- Councils should draw on the good practice guidance and resources that are
- available to develop and run their committees.

Hauraki agree that having an Audit & Risk Committee is an important tool in council accountability and decision making.
Council is concerned that the importance of this may change over time and a different tool may be of more benefit in the future. In light of this, perhaps the requirement for an Audit & Risk Committee could be by way of regulation rather than legislation.
Council also agrees that it is best practice to have an independent chair, and currently does have an independent chair, but believes this should not be a requirement. One concern is that the Committee may not be able to act when no appropriate qualified independent chair has been able to be appointed.
Council agrees that it is ideal to have at least one other external expert member however this should not be a requirement.

R5.4 The local government reporting framework (including the financial disclosures, Funding Impact Statement and performance measures for service delivery) should be subject to a fundamental, first principles review. This review would:

- identify financial disclosures of low value to users of financial statements;
- examine the mix of financial and non-financial disclosures, and recommend a revised framework that provides the most efficient, coherent and accessible way of reporting the range of information sought by both types of users;
- consider the potential for new forms of external reporting, including integrated reporting, to shape changes in the reporting framework; and
- be undertaken by a working group comprising the Department of Internal Affairs, the External Reporting Board and representatives of the local government sector and information users. The Office of the Auditor-General would be consulted.

R5.5 The Department of Internal Affairs, Local Government New Zealand and the New Zealand Society of Local Government Managers should continue to work together to promote and encourage councils' participation in existing performance review and improvement initiatives, such as CouncilMARK™ and the Australasian Local Government Performance Excellence Program. The emphasis should be on learning for continuous improvement, rather than a one-off exercise. This work should include efforts to boost public awareness of initiatives such as CouncilMARK™ to increase demand for their use.

Council has participated in both the CouncilMARK and Australian LG Excellence program. Council found the CouncilMARK program to be a very helpful process. Council do not believe that in its current form that the Australasian Local Government Performance Excellence Program provided sufficient benefit to justify the effort and cost involved.

R5.6 The legislated information requirements for the consultation processes of local authorities should be amended to:

- make the terminology around the required analysis of alternative options consistent across relevant sections of the Local Government Act 2002;

- clarify that Long-Term Plan (LTP) consultation documents must describe the reasonably practicable alternative options for addressing each identified issue; and
- explicitly require that LTP consultation documents include high-level information on the implications for rates and future service levels associated with each of the identified options.

R5.7 The Local Government Act 2002 should be revised to clarify and streamline the required content of Long-Term Plans so as to reduce duplication, ease the compliance costs on councils, and help make them more accessible documents.

R5.8 The scrutiny on long-term planning provided by the audit requirements should not be considered a substitute for internal quality assurance processes. Councils should have robust quality assurance procedures across their Long-Term Plan process, including the use of expert review where appropriate (such as for significant decisions).

Chapter 6 – Future funding and financing arrangements

Findings

F6.1 The roles and funding tools of local government do not impinge on the prime responsibilities of central government to stabilise the macro economy and redistribute income and the cost of services from those well-off to those in need. The responsibilities for making choices about public goods and infrastructure are mostly coherent across the two levels of government.
Some areas of difficulty and tension between central and local government have emerged. These tend to be where the benefits or costs of local government infrastructure and services cross local-authority boundaries, yet current funding arrangements do not consider this.

F6.2 The rating tools of New Zealand local governments have low compliance and administration costs. The complexity of development contributions (DCs) causes them to have higher administration and compliance costs.
Rates based on (unimproved) land values cause little or no economic distortion and therefore are a highly efficient way to raise revenue.
Rates on capital value are relatively less efficient because they can disincentivise land and building development. Rates on the capital value of businesses can, in addition, cause unnecessary productive inefficiency.

Hauraki disagrees with the finding that capital value rates are a disincentive to development. The dollar value of the difference in the rates on an undeveloped property vs. a developed property rating is insignificant compared to the capital costs of development. Council is aware of examples where developers have expressed concern about the value of development contributions, but is not aware of any examples where developers have been put off development because of rates.

Capital value has a two significant benefits:

- Capital value reduces the impact of differential valuation swings between different sectors. Valuation swings change the proportion of rates paid by the properties in each sector.
  For example, Council's two largest property sectors are Residential and Dairying. In Council's 2018 revaluation, residential properties increased, while dairying properties decreased in value. As is usually the case, the land value movements were greater than the capital value.

	Land Value	**Capital Value**
Residential	57%	66%

Dairying	-4%	-8%
Net value swing	**61%**	**74%**

- Capital value better reflects the 'beneficiary should pay' principal. Developed land typically places more demands on council services and receives more benefit

Even so, when rates, user charges, DCs and connection charges reflect benefits received and the marginal cost to the council of providing services, these are efficient ways to raise revenue.

F6.3 The fiscal adequacy of the local government funding system is under strain in the areas of tourism, adaptation to climate change, growth infrastructure and unfunded mandates from central government. Pressures in these areas are mostly uneven across councils, and in the first two areas are set to continue rising.
Since the early 1990s, rates revenue per person, council expenditure per person and income per person have grown at similar rates. While this suggests that the current funding system has proved adequate and sustainable in the past, the new and growing pressures may require new funding tools for the future.

F6.4 The current main funding tools of local government in New Zealand measure up well against the principles of appropriateness for local government use, coherence within national policies and institutions, efficiency, enforceability, and the stability and predictability of revenue. Yet scope exists for many councils to make better use of their funding tools and this would help relieve funding pressures.

F6.5 Development contribution (DC) policy and implementation are inherently complex.
Good examples exist of council DC policies. Councils appear to have been refining and improving them over time. Yet the DC policies of some councils still fall considerably short of best practice. The good policies provide a transparent and reliable platform for setting DC charges in line with the purpose and principles of DCs in the Local Government Act 2002.

F6.6 Councils have a portfolio of charging and rating tools to recover the costs of their growth-related infrastructure investments. Yet cost recovery may take many years, councils face investment risks (eg, over-investment or investing in the wrong location) and some councils face debt limits. Councils also face political pressure to not support growth. The result is that some councils in fast-growing cities are either not willing, or not able to, invest in growth-related infrastructure at levels that match demand.

F6.7 Giving councils powers to levy a value-capture rate, congestion charges and volumetric wastewater charges would give them additional means to recover the costs of growth without burdening existing residents. Yet some councils and their residents may still not be willing to accommodate growth to the extent needed for supply to match demand.

F6.8 Many councils and ratepayers still perceive that council revenue from local growth does not fully cover costs that councils incur from growth and that therefore growth is financially disadvantageous. This perception is exacerbated by the:

- highly visible way that property owners are billed for and pay rates;
- much less visible way that most people pay income tax and GST; and
- the automatic link between economic activity and revenue from income tax and GST which does not exist for rates.

F6.9 While local property taxes are in widespread use in other parts of the world such as the United States, they are not a panacea for aligning the incentives of existing voters and property owners with socially desirable growth rates in dwellings. Given that property prices in New Zealand have been neither stable nor predictable, property tax revenues would not be either, and this would be undesirable. The highly transparent system of rating in New Zealand provides a fiscal discipline on councils and should be retained.

F6.10 None of the options of a local property tax, a local income or sales tax, or a portion of national GST or income tax is a fully satisfactory solution to the problem of councils and existing property owners and voters failing to embrace growth, because no direct and transparent link exists between growth and council revenue.
Each option does not meet at least one important criterion for a good local tax. The revenue from local property tax would be neither stable nor predictable, local income and sales taxes would be complex and likely to have high administrative and compliance costs, and a portion of national GST or income tax would be likely to undermine local autonomy and accountability.

Agreed
Local Income/Sales Taxes can produce economically inefficient outcomes such as businesses locating where taxes are lowest rather than the most economically efficient location.

F6.11 A system of payments from central government to councils based on new building work in territorial local authorities could offer local government a practical additional funding source. The system would substantially preserve local autonomy and provide a direct link between council revenue and a council's effectiveness in keeping land supply and infrastructure responsive to demand. This could be effective in incentivising councils and their existing ratepayers to support growth.

F6.12 While councils vary widely in their use of debt, they should use it to spread the cost of long-lived infrastructure assets fairly over the people and properties that benefit from these assets. Most councils have adequate capacity on their balance sheets to finance their infrastructure development. A few high-growth councils face debt-limit barriers that have the potential to cause serious social harm by preventing council infrastructure investment keeping pace with demand for new development.

F6.13 Special Purpose Vehicles (SPVs) can be an effective way to reduce the barrier caused by council debt limits where these limits constrain a council's ability to invest in infrastructure to serve new greenfield developments. The SPVs raise finance for infrastructure investment in a way that puts debt on the balance sheets of new property owners who benefit from the infrastructure, rather than on the balance sheet of their council or the Crown.

F6.14 The Government and officials are working on ways to expand the use of Special Purpose Vehicles (SPVs) to finance large brownfield infrastructure investments that will benefit both new and existing residents. While more challenging to design, and requiring legislation, these expanded SPVs promise to deliver a further valuable means to reduce the barrier of debt limits for fast-growth councils.

F6.15 The factors driving population decline in rural districts and small centres are often difficult to counter and may result in funding shortfalls that affect a council's ability to supply basic infrastructure services.

F6.16 Tourists pay for many of the costs they create, either directly through a user-pays system, or indirectly by paying for services they buy from businesses. Yet, because tourists do not pay any equivalent of residential rates, tourists do not fully pay for the costs of local infrastructure and services that they consume directly. The payment shortfall is exacerbated by the strong seasonality of tourism that creates the need for infrastructure that can cater for peak loads.

F6.17 Greater user pays and accommodation levies are the two best options for recovering from tourists their share of the cost of facilities provided by local government for which it cannot otherwise charge. These are the only options that target the right group, are practical, do not involve an industry subsidy, promote economic efficiency, are consistent with local autonomy, and have reasonably modest compliance and administration costs.

Recommendations

R6.1 The Government, Local Government New Zealand and the New Zealand Society of Local Government Managers should work together to develop standardised templates both for the development contribution (DC) policies of councils and council assessments of DC charges for individual property developments. Councils should be required to use the standardised templates.
The development and use of required templates has been problematic in the past, e.g. the Funding Impact Statement template developed by DIA still causes some issues for Council.
Council would be concerned if use of such a template was made compulsory.
Council are very supportive of a template being developed that would be available for use.

R6.2 While local authorities' general approach to depreciating their infrastructure assets is satisfactory, three issues are of concern and may require action:

- councils' decisions about the best use of the large amounts of cash that depreciation funding can give rise to should be part of formulating their wider financial and infrastructure strategies;
  There are not likely to be large cash surpluses in the infrastructure activities of many councils for a long time. Most council are facing large replacement programs in the near future, which will result in debt rather than cash, for the foreseeable future. Typically councils only build up infrastructure cash reserves where they have recently built assets that were built without debt.

- councils should prioritise improving their knowledge of the condition and performance of their assets to, among other benefits, avoid the risk of underestimating asset lives and overestimating depreciation expense;
  Councils do need to balance the benefit from this with the cost of obtaining this information. Condition knowledge can be particularly expensive to gain for underground assets. While having a certain level of asset knowledge is critical for future planning, beyond this level the benefit begins to be outweighed by the cost.
- the Essential Services Benchmark should be reviewed as part of the wider review of the local-government performance reporting framework referred to in Recommendation 5.4. Any reframing should avoid the implication that individual councils must invest in as much asset renewal each year as their depreciation expense.
  Agree. 10 year timeframe is too short when dealing with 100 year life assets.

R6.3 In choosing among funding tools, rating bases and whether to charge rates as a percentage of property values or as uniform charges or some other targeted feature, councils should emphasise the benefit principle and efficiency in the first instance. They should also balance greater economic efficiency against lower compliance and administration costs.
Councils should factor in any significant concerns about ability to pay at a second stage in their decision making.

This two-step process is currently followed by Council. However, Council do not believe we present the impact of 'ability to pay' adjustments in a transparent manner. This presentation is something Council intends to put further effort into in the next review of the Revenue and Financing Policy.

R6.4 The Government should consider implementing a system of payments to territorial authorities, based on new building work put in place in each territorial local authority, to incentivise councils to increase the supply of infrastructure-serviced land to match growth in demand.
This funding should be targeted rather than being allocated based on the value of new build work – see earlier comments in response to Question 6.2.

R6.5 The Government should direct officials to continue work on how to expand the use of Special Purpose Vehicles to finance investment in growth infrastructure in fast-growth
local authorities that face debt limits. If needed, the Government should promote legislation in Parliament to enable the placement of debt-servicing obligations on existing residents who will benefit from the infrastructure.

R6.6 In its review to improve the service delivery of the three waters, the Government should favour models capable of applying efficient scale and specialisation to help small communities meet the challenges of maintaining and upgrading their water, wastewater and stormwater infrastructures.

The major benefits of scale are achieved where multiple small water/wastewater supplies are able to be amalgamated. In Hauraki this has already been done, and seven water supplies have been amalgamated to form three supplies. This is only economically efficient where the supplies are geographically close.

With the exception of the amalgamation of separate water supplies, Council does not believe there is strong evidence that scale necessarily results in cheaper three waters outcomes. Hauraki supplies water that is compliant with drinking water standards at a lower cost per unit than Watercare. Hauraki also treats wastewater to a high quality at a lower cost per residential ratepayer compared to Watercare. Hauraki's water and wastewater activities are fully funded from water by meter charges and wastewater targeted rates.

R6.7 The Government should legislate to enable councils in tourist centres to choose to implement accommodation levies to recover the tourism-induced costs of providing local mixed-use facilities not otherwise charged for.
Councils in tourist centres should make greater use where possible of user pays for mixed-use facilities.
Accommodation levies should be made available to all councils. Hauraki District Council has partnered with central government to create the Hauraki Rail Trail and this has resulted in a large increase in the use of some other Council facilities. Local accommodation providers have had tremendous benefit from the new tourism attraction and it would seem appropriate that they should make some contribution to the additional costs incurred by Council.

R6.8 The Government should provide funding from the international visitor levy for councils responsible for small tourist hotspots which cannot reasonably recover all their operating costs of providing mixed-use facilities from tourists through user pays or accommodation levies.

R6.9 The benefit principle and maintaining the integrity of local government autonomy, responsibility and accountability should guide central government funding of local government activities. This implies that central government should generally limit its funding to where there are national benefits. Central government should not expect local government to act simply as its regulatory agent. Rather, the two levels of government should seek a regulatory partnership based on mutual respect and an agreed protocol.

R6.10 Central and local government should strive to achieve a more constructive relationship and effective interface through:

- central and local government providing input (formally or informally) into each other's relevant policymaking processes, under an agreed set of principles or a protocol;
- central government engaging in a meaningful dialogue with local government early in the process of developing relevant new regulations;
- cooperative approaches to tackling problems with implementing relevant new legislation, regulations or environmental standards;
- the creation of formal and informal feedback loops to identify problems with delegated regulations when they first appear; and
- the spread of information through the system and the sharing of expertise and knowledge.

Chapter 7 – Equity and affordability

Findings

F7.1 Councils often make rating decisions in a non-transparent manner that follows a confused consideration of benefits, affordability and local politics.

F7.2 Local government legislation currently provides only weak support for allocating rates primarily according to who benefits from council services.

F7.3 Differentials and the uniform annual general charge are not transparent in allocating the burden of rates to those who benefit from council services. Targeted rates provide a more direct connection between the funding and the beneficiaries of services; and therefore are a much more transparent way of giving effect to the benefit principle.

F7.4 The statutory 30% cap on uniform charges (covering Uniform Annual General Charges and uniform targeted rates applying across the district, but excluding uniform water and wastewater rates) has no clear rationale and unnecessarily restricts the discretion of councils to use rates to reflect the benefit of services and amenities. Currently, few councils are close to the cap.
The cap is not effective in its current form. It should apply to all Annual Charges whether uniform or not and include water and wastewater.
Sends a signal though about central government's expectations.

F7.5 There is little or no evidence that rates generally have become less affordable over time.
Much concern focuses on affordability for low-income (particularly elderly) households who own their own homes. Yet such households generally have much lower housing costs than other low-income New Zealand households.

F7.6 Recipients of New Zealand Super are the main beneficiaries of the Rates Rebate Scheme. Most recipients are not eligible for the Government's Accommodation Supplement because their accommodation costs are below the threshold to qualify, unless they have a mortgage or substantial essential repairs.

F7.7 The Rates Rebate Scheme (RRS) is administratively inefficient and satisfies neither the horizontal equity principle nor the vertical equity principle. The level of assistance currently offered by the RRS is just over $12 a week at most. Low-income homeowners can, as an alternative, access equity in their properties to help meet living costs including rates.

F7.8 The Accommodation Supplement is a well-tested major government programme that, compared to the Rates Rebate Scheme, efficiently and equitably provides support to eligible low-income households to meet housing costs, in a range of circumstances across New Zealand.

Recommendations

R7.1 The Local Government (Rating) Act 2002 should be amended to remove rates differentials and uniform annual general charges. Councils should have five years to implement their removal.

Not agreed.
Differentials and UAGCs are valuable rating tools for addressing beneficiary pays and ability to pay issues.

Anecdotally it appears that differentials are sometimes used in a non-transparent way to address ability to pay. Council believes this could be addressed through councils doing a better job of presenting the rating shifts used to address ability to pay.

R7.2 Local government legislation should be amended to require councils to:

- match the burden of rates to the benefits of council services, as a first step in setting rates;
- consider ability to pay as a second step;
- set out the reasons for their rating decisions in each step in a clear and transparent manner; and
- (in applying the ability-to-pay principle) consider coherence and consistency with the income-redistribution policies of central government.

Councils should continue to have the power to determine, on reasonable grounds, the appropriate allocation of rates within their district or region.

This is Hauraki's current practice, however Council are working on presenting the ability to pay shift in a more transparent manner.
Any revised process needs to continue to include the current rating act requirements for transparency and administrative simplicity.

R7.3 Local Government New Zealand and the New Zealand Society of Local Government Managers should develop advice for councils on how to apply the benefit principle (the burden of rates should reflect the benefits received) in their rating decisions.

R7.4 The Local Government (Rating) Act 2002 should be amended to remove the statutory cap on uniform charges.

Council believes the cap sends a message from central government that rates should not be completely based on Annual Charges and that higher value properties should contribute more to the cost of council services.
Currently all Council's 'annual charge' type rates contribute approximately 53% of overall rates.
The current cap test should be revised to include all rates, and should include all 'annual charges' and not just 'uniform annual charges' as this is too easy to structure rates to avoid the cap. The cap would need to be increased to account for all 'annual charge' type rates.

R7.5 The Government should work with local government and suitable financial providers to develop and implement a national rates postponement scheme. The scheme should:

- have a single set of clear and generous eligibility rules;
- be accessible and have provisions that are easy to understand and work with;
- have moderate and transparent fees; and
- be nationally promoted.

Council supports this initiative but points out that a rates postponement scheme would need to take into account the developing reverse mortgage market. The security for postponed rates ranks higher than mortgages, so ratepayers may find it difficult to borrow under a reverse mortgage for other living costs, where they are postponing rates.
Rates postponement is a valid tool for older ratepayers but is less useful for younger ratepayers on low incomes.

R7.6 The Government should phase out the Rates Rebate Scheme (RRS) over a defined period, such as five years, from when an effective national Rates Postponement

Scheme is in place. In the meantime, the current income abatement thresholds and maximum payments should be maintained.

Disagree

Council's two largest towns are in the 10% most deprived NZ communities. 28% of households have rates that are unaffordable, based on the Shand test of rates becoming unaffordable when they are greater than 5% of total household income.
1,700 of Council's 10,000 ratepayers received a Rates Rebate in 2018/19, and this has had a significant impact on ratepayers' ability to pay their rates and the level of overdue rates. While many ratepayers are asset rich, many are also cash poor.

Chapter 8 – Adapting to climate change

Findings

F8.1 Considerable guidance for councils on climate-change adaptation already exists. But more is needed, and providing it through central, specialised sources of knowledge will be more cost-effective than each council inventing its own solution. Most councils will welcome guidance and find it helpful not only as advice but as backing for taking the difficult and unpopular decisions that will sometimes be necessary.

F8.2 New Zealand's laws and institutions acknowledge the risks from climate change and require local governments to plan for the approaching and rising hazards it will cause. Yet much thinking and practice is still dominated by assumptions that risk profiles are static, like earthquake risk.
A systematic shift to a dynamic risk paradigm is needed to deal with the increasing and cumulative nature of climate-change risk. Such a shift will support decisions that:

- lean against the tendency to continue along current courses (with hard forms of protection for new and existing land use);
- encourage the use of anticipatory and flexible decision tools; and
- reduce risks and costs over the long term.

F8.3 Formulating a set of principles about funding the costs of adaptation to climate change is a helpful place to start. Persuasive, high-level principles include:

- decisions about whether, when and how to defend/protect, adapt, or retreat in the face of hazards related to climate change should aim to minimise long-run costs;
- the way costs of adaptation are shared should be fair and just across communities and generations; and
- active engagement with, and empowerment of, affected communities in developing adaptation pathways is vital.

The first two principles imply placing a high priority on avoiding behaviour that leads to increased risk exposure for private gain at others' expense ("moral-hazard" behaviour).

F8.4 Properties at growing risk from sea-level rise, river-plain flooding or other types of climate-change hazard will become increasingly uninsurable. This is because the nature of climate-change risk lacks two essential characteristics for insurability:

- it is not possible to calculate the chance of loss either mathematically or through experience due to the novel, uncertain and dynamic character of climate-change risk; and
- losses are not unforeseen – climate damage is foreseeable (even though its precise form, magnitude and location are uncertain).

F8.5 New Zealand has a strong tradition of social insurance in which society at large helps those in need who suffer hardship or loss through no fault of their own and where these losses may be uninsurable. This tradition provides a possible basis for some form and amount of central-government assistance to councils seriously threatened by losses due to climate change. Any such assistance will need careful design to incentivise risk reduction and avoid moral hazard.

F8.6 The New Zealand Transport Agency model of co-funding local roads could be extended to provide central-government assistance to relocate local roads and bridges that will be non-viable because of climate-change-induced sea-level rise, flooding and/or storms. This approach has potential benefits to:

- incentivise councils to anticipate climate risks to local roads, and encourage community engagement and buy in;
- prioritise spending in line with net social, economic and environmental benefits while taking account of equity across regions;
- counter optimism bias by requiring that the discipline of a strong business case and engineering and environmental quality standards are met; and
- make specialist knowledge and skills available to councils and help spread best practice and successful innovations around the country.

F8.7 The past approach of containing many New Zealand rivers within relatively narrow stopbanks for flood protection and to maximise the area of productive land for agriculture and other uses will become less viable as climate change increases the risk of more frequent and more intense rainstorms.
Best practice is now to allow wider river corridors that give rivers room and make space to more safely manage flood risk. But making this change faces barriers of existing property rights, expectations of continued protection, and high costs.

F8.8 Credible arguments exist both for leaving private owners to use current arrangements to find ways to adapt to climate change, and for public funding to support private owners to undertake cost-effective risk reduction up to and including managed retreat.
The decision whether to provide additional dedicated funding is for central government to make. Yet the existence or not of a scheme will impact local authorities' responsibilities for leading and implementing managed retreat or other forms of adaptation.

Recommendations

R8.1 The Government and local government should work together to establish centres of knowledge and guidance about climate-change adaptation for councils. One centre should be an authoritative and up-to-date source of advice on science and data while another should be a source of specialist advice on policy, planning, risk management, legal issues and community engagement.

R8.2 The Government should implement a review of existing legislation and policy to ensure that considerations about climate-change adaptation are integrated and aligned within that legislation and policy where relevant.

R8.3 National and local authorities should adopt anticipatory and flexible approaches to climate-change adaptation, in line with recognising the constantly changing nature of the risks. Any additional funding for climate-change adaptation should be conditional on the use of such approaches.

R8.4 The Government should provide legal frameworks that give councils more backing and knowledge to make land-use planning and infrastructure investment decisions that are appropriate in the face of constantly changing climate risks.

R8.5 The Government should extend the New Zealand Transport Agency's role in co-funding local roads to include assistance to councils facing significant threats to the viability of local land-transport infrastructure from sea-level rise and more intense storms and flooding due to climate change. The amount of assistance should reflect the size of the threat facing each council and its rating capacity.
Assistance should be conditional on a strong business case and meeting engineering and environmental quality standards. It should only be available to defend existing infrastructure when business cases indicate that this option is superior to other options by a significant margin.

R8.6 The Government should create a new agency and a Local Government Resilience Fund. The new agency should work with at-risk councils and co-fund the redesign and possible relocation and rebuilding of wastewater and stormwater infrastructure when it becomes no longer viable because of sea-level rise and more intense flooding due to climate change.
The new agency should also assist regional councils and communities to work out the best way to lessen future flood risks from rivers. This could include moving to a new, more sustainable and best-practice paradigm of giving rivers room and developing multiple innovative uses of the wider river corridors.

Chapter 9 – Case study: Three waters

Findings

F9.1 Considerable evidence is available that shows poor performance of the three waters sector in many parts of New Zealand, in terms of their impact on human health, the natural environment, productivity and costs to consumers and ratepayers. However, some councils and providers are taking the tough decisions needed to improve their performance, including Auckland's Watercare, Tauranga City Council, Kāpiti Coast District Council and the five councils involved in Wellington Water.

F9.2 The inherent economic features of three waters makes it a natural monopoly in many cases, and poor-quality water treatment can impose large negative externalities on communities. These natural monopoly and externality features are not the reason for the poor performance of councils. Even so, they do make it very important that councils have effective decision-making, governance, accountability, funding and delivery arrangements in place.

F9.3 The poor performance of the three waters sector in New Zealand can be attributed to the following factors in some cases.

- Inadequate supplier expertise and capabilities, resulting from some local councils prioritising local control of their three waters activities rather than increasing their operational scale through shared services, joint ventures or mergers.
- Poor governance capabilities and incentives, due to lack of independent directors and insufficient use of company-type structures when they are likely to be beneficial.
- Poor financing, funding and pricing arrangements, due to under-recovery of costs and funding from council rates rather than water service charges and development fees.
- Weak safety, environmental and economic regulation, due to poorly designed regulations, weak enforcement and lack of regulatory expertise.

F9.4 The performance of the three waters sector would substantially improve by using an approach that (1) rigorously enforces minimum performance standards; and (2) is permissive about how councils meet these minimum performance levels. This approach would have the following features.

- The new regulatory regime is administered by an existing, credible and independent regulator such as the Commerce Commission, which already regulates similar activities, has a credible "industry watchdog" reputation and has significant experience applying light-handed regulation to some suppliers and stronger forms of control to other suppliers.
- The performance regime would be permissive and flexible, leaving it to councils to decide how to achieve the regulatory standards. However, a backstop arrangement would need to be put in place for those councils that fail to lift performance sufficiently to meet minimum health, environmental and economic-performance standards.
- While significant cost efficiencies should be possible for most council-led water services, some communities will require financial assistance from government to help them make the transition to achieving minimum performance standards for drinking, wastewater and stormwater services.

Council agrees with most of this finding, however Council does not believe that significant cost efficiencies will be possible for most council-led water services. Most larger water supplies do have the benefit of scale but the majority of those benefits cannot practically be achieved for councils that have a number of small geographically separate supplies.

Council believes that water standards should be risk based and that the cost of upgrading and monitoring small supplies to the same standard as large supplies is not an effective use of New Zealand's economic resources. There is some general public benefit in having all water supplies meet a minimum level of service. Council believe this could be best met by providing some central government funding through an organisation similar to the manner that NZTA provides funding for roading.

These comments are from the perspective of a rural authority that has water supplies that exceed the latest drinking water standards (the last small supply will be compliant in the next few months). This was achieved with some assistance from central government grants.