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**REPORT 1**  
*(1215/52/IM)*

## **RATES INQUIRY SUBMISSION**

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### **1. Purpose of Report**

To present a draft submission (attached as Appendix 1) for Committee approval, before it is forwarded to the Rates Inquiry being undertaken by an independent Panel on behalf of Government. Submissions are due on 30 April 2007.

The draft submission sets out the Council position on key policy matters raised by the Inquiry. The paper chronicles the large body of work that has preceded this Inquiry process, including analysis of local government finances and funding by a Local Government Funding Project Team and other papers.

There are strong links between these issues and Wellington City Council strategies that aim to ensure the future prosperity and success of the city. This paper therefore considers the future funding sustainability of Council activities in the face of increasing costs and community expectations.

### **2. Executive Summary**

A Rates Inquiry was announced in November last year with a reporting date to Government of 31 July 2007 and submissions due on 30 April 2007. The Inquiry was a response to widespread public disquiet about rates increases promulgated in councils' 2006-2016 Long Term Council Community Plans (LTCCPs), and addresses the overall sustainability of local government funding.

The Inquiry is effectively a continuation of a long-running process to look at the future sustainability of local government funding. Under its Terms of Reference (attached as Appendix 2) it is not a review of the system or structure of local government per se, but it is difficult to disentangle this from the basis of funding. Some reports have been developed by the local government sector specifically to inform the Inquiry, notably an LGNZ-commissioned think piece from McKinlay Douglas Ltd. and an issues and options paper prepared by LGNZ and SOLGM<sup>1</sup>.

A number of New Zealand studies over many years have looked at the funding sustainability of local government. For most developed world democracies, the balance of funding and accountability between different layers of government is a vexed area. Prior to the Inquiry process, a Local Government Funding Project Team led by the Department of Internal Affairs (DIA) has produced two reports examining the state of local government finances and drivers of expenditure.

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<sup>1</sup> Local Government New Zealand, and the Society of Local Government Managers.

The Project Team's key finding was that there did not appear to be, on its analysis, a generic funding problem - although there did appear to be significant issues in some parts of the local government sector. Essentially this related to specific councils where their options to use existing funding tools were exhausted or would be over the life of their LTCCPs. There was little sympathy in the report for specific councils who claimed they had problems - when their finances showed relatively little debt or relatively low rates<sup>2</sup>. The second stage report was accompanied by a paper on alternative tax bases for local government which concluded that despite the limitations of rates they were a relatively effective option as a core revenue raising tool.

**This work clearly showed that the overwhelming driver putting pressure on local government finances was infrastructure investment need - at a time when costs have skyrocketed. Increased expectations of communities for better services and lifestyle enhancement also play a major part.**

**At the heart of the funding question is a disconnect between the clear and demonstrable need for investment by councils, and the community's willingness to pay. This attitude is influenced by poor understanding of funding drivers and need for investment, and perceptions that some spending is unnecessary or inappropriate.**

**The intensifying pressure on funding comes at a time when cities like Wellington see a need to remain competitive in an increasingly dynamic world. The lack of financial 'headroom', and cumbersome decision-making processes, run counter to the need for flexibility and speed in this environment.**

The WCC submission outlines key principles that the Council would like to see manifested in any future changes to local government funding, namely maintenance of local government autonomy and accountability; development of stronger community support; adherence to sound taxation and revenue raising principles, particularly buoyancy or linkage to growth in the economy; and developing pragmatic options for real change.

The Inquiry has highlighted issues in the form of 35 questions as a suggested prompt for submissions. These are summarised under four key headings that are discussed specifically: drivers of expenditure; demonstrating that planned expenditure is necessary, appropriate, and supported by the community; use of existing options; and the need for changes to the funding system or additional funding options.

The Council's submission is linked to those from related parties, particularly an LGNZ/SOLGM submission, and one prepared for a consortium of councils and other stakeholders.

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<sup>2</sup> "relatively" in this context relates to other New Zealand councils, and in the case of debt, conservative assumptions of appropriate gearing for local government – that recognises the lack of liquidity of many assets.

Overall the submission notes that discussion of local government funding has effectively moved beyond acknowledging that there are significant upward drivers, that planned expenditure is necessary and appropriate, and that existing tools are largely exhausted. The focus is now on real options that might improve the situation through stronger community support and supplementary sources of funding.

Community support could be enhanced through better promotion of the value for money that LTCCP spending represents, and developing a wider understanding of the need to undertake this spending to ensure international competitiveness. This could reduce the risk of sub-optimal investment decisions that will fail to deliver the type of city that Wellingtonians desire.

The WCC submission works through the issues above and presents a position on possible options being considered. The areas supported in particular are promotion of best practice; more flexibility or enhanced use of some funding tools; investigation of transport funding tools; establishing the basis of funding devolved functions and current exemptions; enhancing the rates rebate scheme; developing a community infrastructure fund; and investigation of rating as a fixed percentage.

### **3. Recommendations**

It is recommended that the Committee:

- 1. Receive the information.*
- 2. Approve the draft submission attached as Appendix 1 to the Rates Inquiry being conducted by an Inquiry Panel on behalf of central government.*
- 3. Agree to delegate to the Mayor and Chief Executive the authority to make any drafting changes before forwarding the submission.*

### **4. Background**

#### **4.1 Rates Inquiry**

On 1st November 2006 the Minister of Local Government, Hon Mark Burton, announced an independent inquiry into local government rates. The members of the Inquiry Panel are David Shand (Chair), Graeme Horsley and Christine Cheyne. The task of the Inquiry is to make recommendations to government by 31st July 2007 about the means of enhancing rating and other funding mechanisms for local government.

The Terms of Reference are attached as Appendix 2, and it has been made clear that the Inquiry is expressly not “a review of the system of local government per se, and in particular of the purpose, autonomy, or structure of local government; or the principles of democracy, transparency, equity and accountability that local government operates under”. The WCC submission comments on this somewhat artificial distinction.

This Inquiry is effectively a continuation of a long-running process to look at the future sustainability of local government funding (see Previous Work below). However it differs significantly from recent efforts in that it is independent, high profile and appears to be taking an approach of trying to develop real solutions.

The Panel's comments at public meeting have outlined how submitters might structure their input:

- Offering solutions rather than just criticisms
- Opinions need to be backed up by data where appropriate
- A view on issues and problems with rates and other tools currently used would be valuable, and then some position or view on solutions (using existing or completely new tools).

The Inquiry has established its own website at [www.ratesinquiry.govt.nz](http://www.ratesinquiry.govt.nz) and has issued a Background Paper available on that website. The Paper outlines key issues that the Panel feels it needs to address but (as appropriate at that stage) it consciously avoids proposing solutions. It uses a framework of 35 questions for submitters to respond to if they wish.

#### ***4.2 Supporting information for the Inquiry***

To inform the debate an initial report was commissioned in late 2006 by LGNZ and a consortium of Councils from McKinlay Douglas Ltd. This has been widely circulated in the sector. This paper examines in some detail the fundamental issues and funding drivers affecting local government.

An issues and options paper has also been prepared by a joint LGNZ/SOLGM working party and this is available on the LGNZ website ([www.lgnz.co.nz](http://www.lgnz.co.nz) under Current Projects – Rates Inquiry). The intent of this paper was to engage the Inquiry Panel in discussion before the point where the local government sector puts in formal submissions. It is also an opportunity to frame the debate and develop a consensus on the issues among stakeholders. Although the paper discusses the issues surrounding specific options to improve the current funding sustainability issues it does not take a position on options.

#### ***4.3 Previous work***

A DIA-led Local Government Funding Project Team has been working on this issue since December 2003, at the behest of the Central-Local Government Forum which meets six-monthly to discuss major issues of common interest between these two spheres of government. There have been a number of New Zealand studies over many years looking at the funding sustainability of local government, and the balance of funding and accountability between different layers of government is a vexed area for most developed world democracies.

For the Funding Project team the approach throughout was to first consider whether there was a funding problem for local government that needed addressing at a central government level, and if this was demonstrated to develop specific options.

The Stage 1 Report of the Project Team was released in mid-2005 and this is available on the LGNZ website ([www.lgnz.co.nz](http://www.lgnz.co.nz) under Current Projects – Funding Project). The key finding was that there did not appear to be, on this analysis, a generic funding problem - although there did appear to be significant issues in some parts of the local government sector. Essentially this related to specific councils where their options to use funding tools were exhausted or would be over the life of their LTCCPs. There was little sympathy in the report for councils who claimed they had problems - when their finances showed relatively little debt or relatively low rates.

A second phase then looked at the state of the sector in more detail, and importantly was able to utilise the first 'full' round of 2006-2016 LTCCPs that complied with all requirements of the Local Government Act 2002. They included a significant amount of infrastructure spending that, for various reasons, was not included in the first iterations of LTCCPs. These 2006-2016 LTCCPs presented the best picture ever of the state of local government finances and future investment needs – they had the most community consultation, the best asset information, and the most auditing of any planning to date.

The stage 2 process also utilised a number of case studies of specific councils<sup>3</sup> and specific functions<sup>4</sup> to tease out funding issues. These highlighted the complex and unique circumstances of individual councils - the high level of diversity across the sector - and also the real pressures faced by councils in meeting the needs of their communities using current funding tools. Drivers for increased rates noted by the Funding Project were:

- population growth and other demographic factors
- the age and state of infrastructure (e.g. roading, water, stormwater and wastewater)
- the need to account for the depreciation of infrastructure and other capital assets
- high community expectations of facilities and services provided by local authorities
- the requirements of higher standards (e.g. for water quality)
- other demands on infrastructure capital, and operating and maintenance expenditure.

The Stage 2 Report was released in December 2006 (available on the LGNZ website [www.lgnz.co.nz](http://www.lgnz.co.nz) under Current Projects – Funding Project), and although it contained a more nuanced view of issues in the sector, it reached the same overall conclusion. That is, that although there were undoubtedly significant pressures on local government funding, and there may be some specific cases where a community appeared to have 'run out of options', in general there appeared to be sufficient tools available to the sector to address these issues.

**This work clearly showed that the overwhelming driver putting pressure on local government finances was infrastructure**

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<sup>3</sup> Dunedin City, Manukau City, Opotiki District, Stratford District, Tasman District, Tauranga City, and Waitomo District.

<sup>4</sup> Libraries, drinking water.

**investment need - at a time when costs have skyrocketed. Increased expectations of communities for better services and lifestyle enhancement also play a major part.**

The second stage report was accompanied by a paper on alternative tax bases for local government (also available on the LGNZ website [www.lgnz.co.nz](http://www.lgnz.co.nz) under Current Projects – Funding Project), although this was influenced by Treasury and somewhat purist. In the paper rates, along with other options, were assessed against a number of criteria. Despite the limitations of rates the conclusion was that they were a relatively effective option as a core revenue raising tool.

#### ***4.4 Associated projects***

The Local Government Funding Project has continued work on some associated projects, which have also been picked up as options by the Inquiry. These are:

- **Crown contributions in lieu of rates:** a project has been established to look at how a contributions regime would work and the budgetary implications<sup>5</sup>. It is likely that any Crown contribution would be discounted from a maximum theoretical figure<sup>6</sup>.
- **Petroleum tax:** this is looking at the rationale for the current very small tax that comes to local government and the need for it in future.
- **Financial governance:** a working group is developing a programme to promote best practice financial governance in the sector.

#### ***4.5 Other parties' submissions***

In a general sense, the position of Wellington City Council may differ from a sector position because our spending plans are more achievable, i.e. meeting the needs of communities within constraints on additional spending. That doesn't necessarily mean they are sustainable, and WCC would share the concerns of the sector that scope to use the existing set of tools is rapidly being exhausted.

As is usual practice, individual councils including the large metropolitan councils will be putting in submissions. LGNZ will be putting in a full submission in conjunction with SOLGM and so will a stakeholder group comprising a consortium of councils and a number of advocacy groups including Grey Power, Chamber of Commerce, and Federated Farmers. Drafts of these have been circulated to Councillors.

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<sup>5</sup> The project focuses on exempt land owned by the Crown. Currently exempt under the Local Government Rating Act 2002: land for schools, universities and hospitals; the foreshore and seabed; beds of rivers and lakes where owned by the Crown; the conservation estate; airport land (Milford is the only example where this is owned by the Crown); land for the State Highway network and rail corridor; Parliament Buildings and Government House. Defence land is only rateable at land value. Land and buildings owned by the Crown and housing government departments is rateable (although many of these are owned by the private sector in any case). Non-Crown land that is exempt includes the operational areas of ports and airports, and places of religious worship.

<sup>6</sup> This is because of government views that some local benefit accrues from these activities, and this should be taken into account, and also that the rating system may not be entirely appropriate for some assets such as national parks.

The LGNZ view has to take into account a wide range of financial circumstances and future funding requirements across councils. For example the issues around road funding dominate the thinking of some rural councils because this is such a large component of their spending. The larger city councils face infrastructure investment demands much greater in scale, and a more complex set of community desires to have 'big city' amenities, services and events.

The LGNZ submission emphasises the need to have a comprehensive programme to promote value for money in council spending, better ways of ensuring best practice in councils, and the need to have supplementary income to relieve the pressures on local government funding. More resources could be made available through options like an increase on the transport Financial Assistance Rate, regional petrol tax, and Crown contributions in lieu of rates. This sector wide position does not support more direct Crown funding such as a share of GST, since the maintenance of strong local accountability and flexibility is a bottom line.

The stakeholder group submission goes further on this key issue, and also suggests a range of other changes including road pricing, partial removal of GST on rates, auditing the fairness and objectivity of the way LTCCP information is presented, use of referenda and recall, and a revamp of the rates rebate scheme.

The relationship of these submissions to the Council's is dealt with in the draft WCC submission itself. Support for the LGNZ/SOLGM submission is recommended. The submission prepared by McKinlay Douglas for the consortium noted above is addressed on a point by point basis, and there are a number of options or suggestions where support is not recommended.

#### **4.6 Summary of material**

The background material noted above is therefore:

1. Rates Inquiry Background Paper (February 2007).
2. Local Government Funding, a report prepared for Local Government New Zealand and a Consortium of Councils by McKinlay Douglas Ltd. (November 2006).
3. LGNZ/SOLGM Issues and Options paper (January 2007).
4. Report 1 of Local Government Funding Project Team (July 2005).
5. Report 2 of Local Government Funding Project Team (December 2006).
6. Report 3 of Local Government Funding Project Team - Alternative Tax Bases Paper (December 2006).
7. Draft LGNZ/SOLGM Rates Inquiry Submission (April 2007).
8. Draft Submission prepared for a Consortium of Stakeholders by McKinlay Douglas Ltd. (November 2006) in the form of a submission and resource paper.

This information has been circulated direct to Councillors.

## 5. Discussion

### 5.1 Linkage to WCC strategic objectives

The debate around funding pressures on councils raises critical issues about the way WCC intends to deliver on community expectations and ensure the city remains internationally competitive. It is not realistic to artificially separate funding from the latter two, as the Inquiry attempts to do by excluding accountability considerations in its Terms of Reference.

As a first principle, local government must be accountable to its electorate. This is achieved through local decision-making using the LTCCP process, and also a number of other networks, surveys and monitoring. Decision-making transparency is reinforced through use of rates as the primary funding mechanism, which places intense year-by-year scrutiny on spending

Developing an internationally competitive city is a core WCC goal, and the strategic framework for the city recognises the importance of foundation infrastructure and promoting a high quality of life. A range of services and activities are needed to achieve this. At the base level, all successful cities have to provide core infrastructure. For WCC this is reflected in 67% of capital expenditure being on network infrastructure and an additional 21% on community infrastructure (libraries, pools, sports fields etc).

As noted by the Local Government Funding Project, the cost of this foundation infrastructure is escalating rapidly, because of:

- Higher technical standards - such as nil overflows for sewerage and higher drinking water standards
- Construction cost inflation - up to 20% per annum in recent years
- Public demand for higher service standards - and zero tolerance for failure.

Quality of life areas sit alongside this infrastructure spending. They have the ability to differentiate the city, through things like urban development, attractions and activities. The Council has identified the need to provide these elements to achieve international competitiveness. A key objective is to deliver the quality of jobs and the quality of life that are needed to attract and retain the people that drive the economy.

**Through the LTCCP process and asset management planning, the council has a robust basis for the current mix of services and activities seen as necessary and appropriate if the city is to be successful and internationally competitive. However the cost of these plans is being driven up by higher infrastructure costs and community expectations.**

These increasing costs are expected to be about 30% over the life of the Council's LTCCP (including inflation<sup>7</sup>, i.e. there is a smaller real increase). Some

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<sup>7</sup> The level of inflation that affects councils has been significantly higher than the Consumer Price Index (CPI) because of the larger increases in construction costs. This is expected to continue.

in the community consider any increase as unpalatable, but even if the benchmark is CPI inflation then clearly there is a major difference.

In many cases there is also a poor understanding of the need to invest in quality of life areas and this expenditure is seen as non-essential. Moreover, the explicit mandating of a wider role for councils to promote community wellbeing is seen by some as leading to more expenditure, even though there is little evidence of this.

**At the heart of the funding question is a disconnect between the clear and demonstrable need for investment by councils, and the community's willingness to pay. This attitude is influenced by poor understanding of funding drivers and need for investment, and perceptions that some spending is unnecessary or inappropriate.**

**The intensifying pressure on funding comes at a time when cities like Wellington see a need to remain competitive in an increasingly dynamic world. The lack of financial 'headroom', and cumbersome decision-making processes, run counter to the need for flexibility and speed in this environment.**

The challenge is to take advantage of opportunities as they arise, through adaptation and innovation. The statutory operating framework, dictated largely through the Local Government Act, is unwieldy, and compromises the ability of the Council to respond to the changing environment.

The Council therefore has to increase revenues or to reduce costs if it wants to continue delivering agreed service levels and maintain financial sustainability. A focus of the Inquiry is more effective use or fine tuning of existing tools. However WCC Officers feel that this Council already uses most of the current tools effectively. Emphasis on this area risks merely redistributing taxation over the existing taxpayer base, rather than a genuine search for a wider tax base.

An initial option would be finding ways for non-ratepayers to pay for services they consume within the city. This is, for the most part, achieved directly through user charges, and indirectly through targeted rates such as our downtown levy (which contribute to tourism and business development activity). WCC does not believe that significant new revenue options can be identified at this time, from this area.

Less conservative revenue generating options would involve the council moving into increasingly commercial activities. Around the country this occurs to varying degrees, such as through shareholding in utilities, airports, transport etc., and with returns through dividends. Most councils are reluctant to actively move further down this path.

This leaves options that would channel some community funding through the wider central government tax base. Direct, untagged funding through methods like local GST is not supported in the submission because of its potential impact on local autonomy and accountability, lack of workability (and central government is unlikely to allow it). However some targeted funding is

supported, that recognises factors such as the national good of activities and issues that individual communities cannot cope with. The rationale for this is expanded in the submission itself.

Reducing costs is achieved through either reducing the cost of delivering a service or by reducing the level of service. As seen above, it is not agreed that a reduction in the level of service would be acceptable.

These factors are driving organisational work on the need to fundamentally change the WCC business model, to encourage greater flexibility and adaptability, but without compromising accountability. The nature of changes is not yet defined, but the Council will need to move from an 'asset-centric' model to a 'customer-centric' focus.

As noted above, the need for accountability remains. The checks and balances will continue to be provided through the governance structure, primarily through elected members, and through enhanced engagement with residents and ratepayers. This could mean stewardship and delivery of an agreed strategic plan without constant formal reference to the community, using a range of tools like surveys, monitoring and networks to confirm alignment with community wishes.

Finally, the disconnect noted above implies that there is scope to better promote the value for money that LTCCP spending represents, and develop a wider understanding of the need to undertake this spending to ensure international competitiveness. The 'value' of services that rates represent is not associated with the expense because it is not immediately linked in the way that, say, power or telephone is. There is scope to develop a different appreciation of rates that recognises the diversity and quality of services being provided. This could reduce the risk of sub-optimal investment decisions that will fail to deliver the type of city that Wellingtonians desire.

## ***5.2 Inquiry submission framework***

The following issues are highlighted by the Inquiry's Terms of Reference as being the focus of their investigation:

- the current level of rates and the level of rates increases
- the drivers for increased local authority expenditure
- the trends in the use of rating tools nationally to fund services
- other sources of revenue currently available to local authorities
- the sustainability of rates
- the Rates Rebate Scheme (and other government assistance packages for families), and local authority rates remission and postponement policies
- the impact of rates on land covered by the Te Ture Whenua Maori Act 1993
- exemptions from liability for rates, including Crown exemptions
- other revenue-raising mechanisms.

To address these issues the Inquiry has posed the following questions as a suggested prompt for submissions:

<b>The current level of rates and rates increases over the next 10 years</b>
1. How adequate is the value for money of the services provided by local authority rates?
2. What information is provided by councils about how rates are used and the value for money of the services provided from rates? Is the information adequate?
3. Do people have a good understanding of their opportunities to make an input to their council's long-term plans and rating policies?
4. How widely are these opportunities used by the public?
<b>Drivers for increased local authority expenditure</b>
5. Are there drivers of increased rates, other than those mentioned by the Funding Project, the Inquiry should explore?
6. What are the most significant drivers of local government expenditure?
7. Is asset management planning providing full and accurate information about projected capital expenditure?
<b>Trends in the use of rating tools to fund services</b>
8. To what extent could greater use of the available rating tools assist local government to address equity issues for particular groups of ratepayers?
9. What are the barriers to the optimal use of the range of tools?
10. How can these barriers be addressed?
11. Does the rating system need to be changed to address any continuing anomalies or inequities?
<b>Other sources of revenue currently available to local authorities</b>
12. Should greater use be made of currently available funding mechanisms, other than rates? If so, which ones?
13. Are alternative forms of revenue, such as development contributions and user fees, established through a transparent process? Are they equitable?
14. Is there a case for an increased use of borrowing by local authorities to address inter-generational equity or other issues, such as accelerating infrastructure investment?
<b>Sustainability of rates</b>
15. How should the affordability of rates for communities and individual ratepayers be assessed? What factors are relevant?
16. Which groups of people do you consider are most affected by the affordability of rates? What data is available to determine this?
17. Is the affordability of rates only an income issue, or does it also involve assets held or other factors?

18. To what extent can affordability problems be addressed through greater use of rates rebates and rates remission and postponement policies, or by reverse mortgages and similar mechanisms from private sector sources?

**Rates Rebate Scheme, other government assistance packages, and local authority rates remission and postponement policies**

19. How effective is the Rates Rebate Scheme in addressing affordability problems for ratepayers?

20. How effective are the rates remission and postponement policies in addressing affordability problems for ratepayers?

21. What, if any, barriers are there to the use of these schemes, and what measures might be taken to enhance the use of these schemes?

22. What is the current and likely future impact of these schemes on the revenue policies of local authorities?

23. Are there other ways of addressing issues of hardship caused by rates (for example, the use of reverse mortgages or other financial schemes which might be provided by the private sector)?

**The impact of rates on land covered by the Te Ture Whenua Maori Act 1993**

24. What are the major issues involving the rating of land covered by the Te Ture Whenua Maori Act 1993, and how can these best be managed?

25. Is the existing basis of the valuation of Maori land appropriate? If not, what alternative approaches could be considered?

26. Do policies aimed at improving the affordability of rates fully recognise affordability issues facing Maori landowners?

27. Are there grounds for providing rates exemptions for categories of Maori land other than those in Schedule 1 of the Local Government (Rating) Act 2002?

**Exemptions from liability for rates, including Crown exemptions**

28. Is the rationale for exemptions on Crown and non-Crown land still valid?

29. Are the current statutory provisions for exempted land reasonable and appropriate?

30. Are there other categories of land that should be recognised for the purposes of exemptions?

31. What would be the impact of reducing or removing exemptions?

**Other revenue-raising mechanisms**

32. What principles should guide the use of revenue sources to fund local government expenditure (including rates)?

33. What practical new revenue sources could, in full or part, be alternatives to rates? What are the comparative advantages and disadvantages of these alternatives?

34. What criteria should be used in assessing the desirability of any alternative revenues to the property tax (rates) system?

35. Are there funding sources that major tourist destinations should have in order to meet the cost of

council services used by these tourists?
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These questions are assembled into four areas that are discussed in the draft Wellington City Council submission (attached as Appendix 1):

- what are the major drivers of expenditure?
- is planned future expenditure, set out in the first instance in the 2006-2016 LTCCP, necessary and appropriate?
- what scope is there for better use of existing funding options?
- is there a need for changes to the funding system or additional funding options and if so what should they be and why?

This is the approach taken in the submission to avoid traversing the large amount of background material and discussion outlined above. These papers have provided an in-depth understanding of issues, funding drivers, and possible options.

### **5.3 Principles for a WCC submission**

A set of key principles has been developed on the submission to provide framework for consideration of proposed changes to local government funding. These are:

- Maintenance of local government autonomy and accountability;
- Development of stronger community support;
- Adherence to sound taxation principles, particularly buoyancy or linkage to growth in the economy; and
- Development of pragmatic options for real change.

A description of them is included in the draft submission and possible options are rated against them.

### **5.4 Specific options**

A number of options have been raised (and there are no doubt variations). The following options are discussed specifically:

#### CATEGORY A: NEW/ALTERNATIVE REVENUE MECHANISMS

1. Local Income Tax
2. Local Goods and Services Tax
3. Remove Requirement for Councils to pay part/all GST
4. 24/7 Road Pricing
5. Regional Petrol Tax
6. Regional Payroll Tax for Public Transport
7. Full Environmental Cost Pricing for Water Services
8. Green Taxes
9. Bed Taxes

10. Poll Tax
11. Government Funding of Devolved Functions
12. Removal of rating exemptions for (Churches), Schools, Hospitals etc
13. Government Grants in Lieu of Rates
14. Exemption of Maori Land not in Economic Use or Housing
CATEGORY B: MORE FLEXIBLE USE OF CURRENT REVENUE MECHANISMS
15. Lift Cap on Uniform Annual General Charge
16. Increased Use of Development Contributions
17. Choice of Alternative Rating Base
18. Balance Sheet Management
19. Greater Use of Targeted Rates
20. Increased Government Funding for Roothing or Other Infrastructure
21. Best Practice and Consistency
22. Role of the Auditor-General in respect of the LTCCP
CATEGORY C: REDUCING IMPACTS OF CURRENT REVENUE MECHANISMS
23. Differential to Smooth Impact of High-value Residential Properties
24. Valuation Averaging
25. Enhance Take up of Rates Rebates
26. Rates Postponement
CATEGORY D: COST CONTAINMENT
27. Performance Improvement/Measurement
28. Amalgamation
29. Review of Requirement to Fund Depreciation
OTHER
30. Rating Capability
31. Referenda and Recall
32. Community Infrastructure Fund
33. Rating at a fixed percentage

### ***5.5 Key areas supported***

The areas that are supported by WCC are in particular:

- a) promotion of best practice (21, 27)
- b) more flexibility or enhanced use of some tools (8, 15, 16, 17, 19, 24, 29)
- c) investigation of transport funding tools (4, 5, 6, 20)
- d) establish basis of funding devolved functions and current exemptions (11, 12, 13)
- e) enhanced rates rebate scheme (25)
- f) community infrastructure fund (32)
- g) investigate rating as a fixed percentage (33).

The rationale for these is provided in the submission itself.

### **5.6 Linkage to other submissions**

A specific Council position is taken in the draft submission in relation to the LGNZ/SOLGM submission, and a submission from a consortium of councils and other stakeholders prepared by McKinlay Douglas Ltd.

## **6. Conclusion**

The issues of local government funding sustainability being tackled by the Inquiry are long standing and intractable. They have however been brought into sharp focus by significant funding pressures on councils and the resulting LTCCPs.

Detailed analysis has shown that the cost drivers facing local government are real and not easily mitigated against. There is good evidence in the planning processes of local government that LTCCP expenditure is necessary and appropriate, with the direct result that substantially more funding will be needed.

The use current of current funding tools by local government is reasonably sophisticated and although there is some scope to use them better, this is unlikely to fully resolve funding sustainability issues.

Part of the solution will need to be new or supplementary funding tools and a concerted campaign to build community support for spending plans. The WCC submission works through the issues above and presents a position on possible options being considered. The areas that are supported are in particular promotion of best practice; more flexibility or enhanced use of some funding tools; investigation of transport funding tools; establishing the basis of funding devolved functions and current exemptions; enhancing the rates rebate scheme; developing a community infrastructure fund; and investigate rating as a fixed percentage.

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## **Supporting Information**

### **1) Strategic Fit / Strategic Outcome**

*The paper presents a draft submission on local government funding principles that support all Council outcomes and activities, with particular relevance to governance matters. This is because community support for the Long Term Council Community Plan is essential if the wellbeing of the community is to be promoted and enhanced.*

### **2) LTCCP/Annual Plan reference and long term financial impact**

*None. Funding sustainability for local government will naturally have a significant financial impact at the macro level.*

### **3) Treaty of Waitangi considerations**

*The paper contains some reference to rating of Maori land covered by the Te Ture Whenua Maori Act 1993.*

### **4) Decision-Making**

*This paper does not deal with significant decisions in terms of the Local Government Act 2002 because it is a policy input to central government.*

### **5) Consultation**

#### **a) General Consultation**

*The paper is a response to a wide-ranging public consultation being carried out by the Rates Inquiry. At a national level there has been some interaction with key stakeholders.*

#### **b) Consultation with Maori**

*None specifically on this paper.*

### **6) Legal Implications**

*None as this is a policy development project.*

### **7) Consistency with existing policy**

*This report is consistent with Council policy. For some specific questions a policy position is sought, for determination by the Committee, most notably on support for revenue sharing or direct funding from central government.*

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## RATES INQUIRY SUBMISSION WELLINGTON CITY COUNCIL

30 April 2007

The Council welcomes the opportunity to make a submission to the Inquiry. It would appreciate the opportunity to remain involved in current and future policy development in this area, and would be happy for a representative of the Council to discuss any aspect of this submission.

### 1. Structure of this submission

The submission opens with some context in terms of its relationship to other key submissions which link to this one. It then outlines key principles that the Council would like to see manifested in any future changes to local government funding. The 35 question framework in the Inquiry's Background Paper is assembled into four key areas that are addressed in subsequent sections. These are a Wellington City Council (WCC) view on drivers of expenditure; demonstrating that planned expenditure is necessary, appropriate, and supported by the community; use of existing options; and the need for changes to the funding system or additional funding options.

### 2. Context

The Inquiry's Terms of Reference state that the Inquiry is expressly not "a review of the system of local government per se, and in particular of the purpose, autonomy, or structure of local government; or the principles of democracy, transparency, equity and accountability that local government operates under". The Council believes that the funding system of local government is inextricably linked to these issues and principles, and it is not possible to artificially partition them. It may be that some of the more fundamental possible changes, such as amalgamation, are less likely to eventuate. However all options should be considered and debated.

The Council recognises that the views of stakeholders will be framed from a number of different perspectives in their submissions and these will emphasise different issues. The ones from associated groups where the Council has had a linkage to their development are:

- A Local Government New Zealand submission on behalf of the entire sector. This submission is supported while recognising it is a sector-wide view that necessarily contains some compromise across the very wide range of circumstances affecting individual councils. These reflect history, happenstance, and prior decisions of communities, so it can be risky to generalise or to formulate generic solutions.

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- A submission prepared for a consortium of councils and other stakeholders by McKinlay Douglas Ltd. Only parts of this submission are supported by Wellington City Council as some areas are at variance with the position set out in this submission. However the process for preparing this submission is regarded as very valuable as it has provided a forum to work through issues of common concern to all stakeholders, including councils. The options listed by the stakeholder group have been used as a framework for responses to specific options below (with addition of two further options by WCC).

## 3. Key principles

The key principles that the Council would like to see manifested in any future changes to local government funding are:

- Maintenance of local government autonomy and accountability;
- Development of stronger community support;
- Adherence to sound taxation and revenue raising principles, particularly buoyancy or linkage to growth in the economy; and
- Development of pragmatic options for real change.

### 3.1 Autonomy and accountability

This is seen as a principal strength of the current system, where local solutions can be developed for local problems and there is genuine ownership of both. Options that weaken this linkage are not favoured.

### 3.2 Community support

The need for an increased level of spending to meet the needs of communities, especially in the infrastructure area, will test their resolve to commit to higher levels of rates and other revenue generation. This principle seeks better ways to improve understanding and support of council's plans and associated spending.

### 3.3 Sound taxation and revenue raising principles

These are generally accepted as including principles such as: providing sufficient yield, equity and fairness, economic efficiency, administrative simplicity and ease of collection, neutrality in terms of not distorting investment decisions, and buoyancy or linkage to growth in the economy. Of these, buoyancy is one where there appears to be failure in current options.

### 3.4 Pragmatic options for real change

Some of the options under consideration consist of fine tuning and making better use of tools that are already available to councils. Others are unlikely to raise significant additional revenue. This may not be sufficient to ensure future funding sustainability and breakthrough changes are sought.

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## 4. Key issues

The questions in the Background Paper above lead to four major areas that are addressed in turn:

- what are the major drivers of expenditure?
- is planned future expenditure, set out in the first instance in the 2006-2016 LTCCP, necessary and appropriate?
- what scope is there for better use of existing funding options?
- is there a need for changes to the funding system or additional funding options and if so what should they be and why?

The analysis to date means that it is possible to move confidently through the first three of these before analysing specific options. The Council believes that the focus of the Inquiry should be on new options rather than establishing the nature of the problem, funding shortfall, or 'fine tuning' existing options.

### 4.1 Drivers of expenditure

The work of the Local Authority Funding Project Team and others has unambiguously demonstrated the nature and magnitude of key cost drivers. They are producing significant pressure on councils, as agents for their communities, to deliver services that will cost more overall. Their summary is fair, particularly the overwhelming dominance of infrastructure investment. The figures arrived at of 73% of capital spending on network infrastructure and an additional 18% on community infrastructure are similar at Wellington City Council, where they are 67% and 21% respectively.

The nature of infrastructure assets makes this type of expenditure difficult to reduce or even contain if sound management practices are followed – i.e. if service levels are maintained, risk is managed and massive catch-ups of deferred maintenance avoided. A significant risk factor is the long life cycles of different asset groupings, where the need for significant renewals across groupings can fall due over a relatively short period. The age and size of the asset base means that renewal of assets can use up most if not all of depreciation budgeted.

Clearly there has been significant cost escalation in construction and maintenance costs for infrastructure, far higher than the Consumer Price Index. This is driven by international trends and is largely out of councils' control. It is expected to continue at a higher rate than the CPI.

Councils may also be facing a sharply increased role in the provision of broadband infrastructure, to break the existing deadlock where multiple privately-owned networks are not providing sufficient incentive to invest. This is happening in many parts of the world and local government is clearly a key participant given its role in other local network infrastructure.

As a further driver, the need for cities to remain competitive internationally is not highlighted. This does put additional pressure on a range of areas that

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enhance the 'quality of life' for existing and potential residents. The competition for skilled and talented people worldwide is strong and expected to remain so.

From research we know that these people (and our existing residents) have high expectations of their living and working environment, and a low tolerance for poor quality services or service failure. The higher expectations of communities for quality services, amenities and attractions is also a significant driver of expenditure.

Other demands on expenditure include the operational expenses necessary to maintain a high-performing organisation, such as personnel costs and communication technologies.

It should be noted that there are few if any trends in funding pressures that are giving relief to councils, particularly where there is no 'buoyancy' in rates i.e. a linkage to growth in the economy. It may be that over time the rate of cost inflation for infrastructure will reduce, although it appears that many countries have significant further investment planned and there is a worldwide catch-up related to ageing infrastructure in older cities.

## **4.2 Necessary and appropriate expenditure**

Secondly there is the question of whether expenditure is necessary and appropriate. The evidence sits mostly in asset management planning and the LTCCP process. Both are extensive and robust, and although not perfect they are rapidly approaching the point where further gains the accuracy of predicted expenditure will be incremental. Asset management planning for example is very dependent on the quality of the information used, which is expensive to generate.

### **Asset management planning**

The sophistication of asset management planning varies across councils, but is generally good and for WCC we now have a very detailed picture of infrastructure investment needs over the 10-year life of the LTCCP. It can be difficult to accurately predict beyond that. For all councils there is a diminishing return on better and better asset information, and we are close to achieving that balance in Wellington City. The very significant improvement in asset management planning over the last ten years is a feature of management practice in New Zealand local government.

### **LTCCP and other processes**

Then there is the complex LTCCP planning process, which can tend to favour compliance over effectiveness as a consultation tool. Certainly for WCC the LTCCP consultation processes are only part of a 'system' of formal written input, statistically valid surveys, monitoring, use of advisory groups and networks, and other methods of maintaining consistency with the wishes of the community. Of course in this situation with relatively low levels of formal written submissions, maintaining the option of making your views known becomes very important.

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Communities have a good understanding of their opportunities to provide input to plans and policies – the LTCCP process is now firmly established as the major opportunity for the community to shape future spending plans. Although some of the policies are set in place every three years, the discussion of future spending plans is effectively an annual event. This is entirely consistent with the Local Government Act, where decisions on all plans and financial policies have to be linked back to the LTCCP. There is a high level of awareness of the LTCCP process and a steady level of submissions and participation in this and other processes.

The information provided on how rates are used is extensive. There is a high degree of disclosure and a high level of detail provided – perhaps to the point of excess (feedback that information is too detailed has increased). Speaking for the Wellington city situation, a great deal of effort goes into presenting this information in a way which is easy to follow and assimilate. And of course this information is audited.

However the statutory decision-making framework is cumbersome, and can be a significant constraint on councils which need to react in an increasingly dynamic world. Even with the extensive process above, it could not be said that Local Government Act objectives of greater transparency and understanding have been achieved, because the large amount of information is hard to navigate.

Since it is a fundamental principle of democratic systems that people are involved and participate in strategic direction-setting for their communities, the overall level of participation is probably not as high as councils would like.

This can mean that the Council is effectively a steward of that direction, built up over time and with a range of ways of ensuring consistency with community wishes. The engagement process can then be used to develop and refine ideas and make them more robust, rather than to regularly go back to the community and ask “what do you want your future community to look like?”. This can result in ‘consultation fatigue’.

## **Demonstrating value for money**

For most services delivered by councils, there are not direct substitutes provided by the private sector. However there are a range of ways in which value for money is ensured and demonstrated.

Firstly, the constraint on any increases in rates or other charges, no matter how solid the justification, produces a strong incentive for councils to look for efficiencies.

Most councils including Wellington City Council have outsourced activities where this is appropriate, and in this situation they are typically provided under competitive processes like tenders. For example in the water, wastewater, stormwater and roading areas approximately 90% of expenditure would be in this category. For some specific activities WCC has carried out very thorough analysis of in-house versus outsourced options (swimming pools, facilities

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management) to ensure value for money and achievement of objectives. There are often wider objectives than just providing a low cost service, but these comparisons have demonstrated closely comparable value for money in these areas.

There has been some work in benchmarking across councils, but this is difficult because of differing service levels, asset ages and circumstances (such as extent of investment assets, topography for building roads, etc.). Many councils including WCC are involved in business excellence programmes that run in both the private and public sector, and regularly participate in and are successful in award competitions.

WCC and most others undertake regular satisfaction surveys of residents to determine whether Council services are meeting their needs. The results of these surveys are healthy. There is also a complete system of performance measurement that tracks achievement of community objectives and the internal performance metrics that support this activity. This includes things like response times to resolve issues, energy efficiency, human resources practices, and many other measures that are all comparable to or better than the private sector.

So in summary the difficulty with direct demonstration of value for money is recognised, but there are a range of useful proxies. Overall however, there does appear to be scope to provide better information to ratepayers of the value for money delivered through council services.

## **4.3 Better use of existing options**

There are a very wide range of tools available to local government, and although some suggestions are made for greater flexibility (i.e. in the LGNZ/SOLGM submission), the overall level of flexibility is high.

### **Rates**

There is a fundamental issue that more refined use of rating tools may just shift around the incidence of rates between various groups. This is worthwhile to promote fairness and equity but doesn't actually produce more revenue. Moreover, the existing rating policies of councils have usually been fine tuned over many years to alleviate 'pressure points', and changes aren't necessarily easy to implement when there are 'winners and losers' (and the 'winners' remain quiet while the 'losers' make their feelings known with great fervour!).

Overall WCC feels that it is already using a range of rating tools appropriately and while further improvement is an objective, significant change is not contemplated and this is not seen as a way of resolving current local government funding issues.

### **Affordability of rates**

Rates are a significant expense but they are mainly used to fund local services that enable the community to function effectively and successfully. If these are

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necessary and appropriate then the rates are affordable by definition or the community is non-viable. At an individual scale clearly income levels are the major determinant of affordability, but there is also a strong linkage to assets (for the purposes of this discussion, rateable property assets).

Accessing the equity that individuals have in their homes (or farmers in their farms) is not always easy or appropriate. However it is disingenuous to maintain that the community has no claim on this property equity to fund community assets and services, when its value is largely supported by the network of infrastructure, property and residents that form the same community. In most cases the amount levied is small in percentage terms, and when the absolute level of rates is higher that only corresponds with a higher than average property value.

### **Rates rebates, remission and postponement policies**

Rates are a sound funding tool for local authorities, because they adhere to good taxation principles. However one of their significant drawbacks is the impact they have on individuals who are asset rich but have low incomes. The Rates Rebate Scheme addresses this issue directly for those on low incomes, so is therefore very effective in a technical sense.

In operation the Scheme does not appear to be getting the uptake it should considering the significant affordability issues that are raised by communities. The coverage should be increased to people who are currently ineligible, such as property owners in rest homes, and consideration given to transferring management to Work and Income. The overall quantum of the Scheme should also be reviewed at some point because even at full uptake, it would only represent a relatively small percentage of rates levied.

Rates remission and postponement policies have not been a particularly useful tool for councils, including WCC, to date because they involve judgements about affordability and income levels that councils are not in a good position to make. In this situation it can be difficult for councils to give effect to well-intended policies.

As a tool to address affordability they come second to a well designed primary rating system, and are used by WCC more as a refining or specific issue tool (for example remission of rates to recognise heritage work on buildings).

There has also been an underlying consideration that conceding significant revenue in these areas would only increase the need to raise additional revenue from other groups in the community.

As noted above, hardship can be difficult for councils to assess. Equity release schemes have their place but are not likely to be an ideal option in all cases where they may be applicable. Equity release assumes extremes in terms of income levels and the amount of equity available, and is also less appropriate where a person or their partner living in the same house expects to be around for a while.

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## **Rates exemptions**

In terms of changes to the rating system, the removal of exemptions is the most obvious example. These could be removed, with care to ensure that other legislative provisions would enable community choice for all such options. The alternative approach, to target some of the 'side effects' of the rating system with specific measures, could be applicable in the case of rates rebates as well as the exemptions area.

Current exemptions do appear to be largely the result of historical accident or circumstances that no longer apply. For a Crown-owned property sitting in the middle of a city and supported by all the infrastructure and services of a city to be rated differently than the building next door is artificial.

The argument that these facilities produce local benefits that balance off rates is weak where these are nationally administered and funded functions. Many functions produce both local and national goods and these can only be identified at a broad brush level. If exceptions were generated on this basis then councils would qualify for exemption from GST for swimming pools and libraries, to the extent that GST funding contributes to health and educational outcomes and so do these local government activities.

The local good of community facilities such as churches may be less clear cut and communities would need to retain the discretion to grant these exemptions where appropriate.

## **Other existing options**

There is scope to make more use of other funding mechanisms, but in the case of WCC, the scope is not great. Development contributions, for example, have recently been significantly strengthened and enhanced. Higher revenues from this source have already been budgeted for and are included in the current LTCCP.

It also needs to be recognised that changes in the use of tools will evolve over time and there are clear indications that this is happening across the sector – an example is the growing use of development contributions noted in the report of the Local Government Funding Project.

There is a case for an increased use of borrowing and particularly for councils where the use of this tool is minimal or non-existent. In the case of Wellington City Council, the appropriate level of borrowing in relation to the total capital expenditure programme has recently been considered, and a cap put in place to ensure that we don't constrain future generations in their decision-making.

There are few technical barriers to the use of tools, although changes are recommended to resolve some anomalies and inconsistencies. These include removing the constraints on modern financing options, fee setting, and determining reserve contributions.

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For debt and other tools community education and a better understanding of how the rating system works are probably the key. The attractiveness of “low rates” or “no debt” political platforms will however is likely to remain an issue. Legislative change would be needed for technical barriers.

In summary the Council believes that discussion of local government funding has largely moved beyond acknowledging that there are significant upward drivers, that planned expenditure is necessary and appropriate, and that existing tools are largely exhausted. The focus is now on real options that might improve the situation through stronger community support and supplementary sources of funding. Without these, the level of rates rises will remain the focus of debate.

## **Other revenue-raising mechanisms**

In terms of principles that should guide the use of revenue sources, firstly they need to follow sound taxation or revenue raising principles such as: providing sufficient yield, equity and fairness, economic efficiency, administrative simplicity and ease of collection, neutrality in terms of not distorting investment decisions, and buoyancy or linkage to growth in the economy. The final point is critical because rating only to cover funding needed is one of the major weaknesses of the current system. It focuses attention on increases rather than working on the principle that a tax based on a percentage of property value is a fair way of supporting the many services needed by communities.

The maintenance of the autonomy of local communities to make funding decisions, and the associated accountability relationship between councils and their communities, is highly desirable. Despite the many issues that reliance on community support raises, the pressure involved should drive sound decision-making and a sense of involvement and self-reliance in communities. The risk is that if the pressure becomes too great, then investment that is necessary and appropriate will not be made.

Related to this, revenue options should promote clarity, equity and transparency in the funding choices available to communities, and through this develop stronger support of council spending plans.

Finally, changes to revenue sources or the system of funding are needed that significantly advance and improve the sustainability of local government funding. Given the nature of the issues, refining existing tools in an incremental way is unlikely to produce the improvement needed.

Specific options are dealt with in more detail below, but some general comments are warranted here. There may be an expectation that rates could be reduced significantly if new revenue sources could be found. The scale of the issues makes this unlikely without a wide-reaching overhaul of the taxation system, and in any case, significantly reduced reliance on rates could be a poor trade-off if the drawbacks of other options are similar or worse.

The concept that some options, such as road pricing, could serve a dual purpose of raising revenue and supporting policy objectives is valid. However this is not

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included as a criterion as its application is likely to be limited – for most rating the revenue raising does not have that type of effect.

There may be a tendency to focus on obvious anomalies or on extreme impacts on individual (usually small and rural) councils, possibly because we instinctively have sympathy for these smaller communities. This may gloss over the less extreme but more significant dollar impacts of infrastructure deficit in the cities.

## 5. Specific Options

The pros and cons of many possible options have been extensively discussed in other material and reports. Possible candidates raised by this process are assessed below against the principles established earlier, and a brief discussion follows of a couple of options that may be more specific to this submission.

Note that the framework of options listed by the stakeholder group (consortium of councils and other stakeholders with submission prepared by McKinlay Douglas Ltd.) has been used, with addition of two further options by WCC at the bottom of the list below.

Option	Autonomy and accountability	Building Community support	Sound taxation and revenue raising principles	Pragmatic options for real change	WCC support
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### CATEGORY A: NEW/ALTERNATIVE REVENUE MECHANISMS

<b>1. Local Income Tax</b>	<b>x</b>	<b>x</b>	<b>x</b>	<b>x</b>	<b>No</b>
Description: A tax set locally on income.					
Position: This option is not supported because direct funding is not supported – it would inevitably compromise the local accountability that is a core strength of the current system. It is also likely to be very difficult to implement without distortions and would suffer from high transaction costs.					
<b>2. Local Goods and Services Tax</b>	<b>x</b>	<b>✓</b>	<b>x</b>	<b>✓</b>	<b>No</b>
Description: Direct funding from local government by way of a share of current GST (suggested at 1%) funded either by reducing government's share to 11.5% or by increasing GST.					
Position: This is not supported for similar reasons to option 1.					
<b>3. Remove Requirement for Councils to pay part/all GST</b>	<b>✓</b>	<b>✓</b>	<b>x</b>	<b>x</b>	<b>No</b>
Description: Local government expenditure on activities which are primarily of a public good character should be zero rated for GST purposes.					
Position: This option is not supported because it is likely to be unworkable. It will not be possible to easily distinguish these activities and the amount of GST would create perverse incentives to categorise activities as zero rated (i.e. moving funding to the general rate).					

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Option	Autonomy and accountability	Building Community support	Sound taxation and revenue raising principles	Pragmatic options for real change	WCC support
<b>4. 24/7 Road Pricing</b>	✓	✓	✓	✓	<b>Yes*</b>
Description: Investigation of 24/7 road pricing (at variable rates to reduce congestion) for all road usage by powered vehicles, either replacing existing road related taxes or supplementing them.					
Position: Investigation of this option is supported, noting that establishing the objective out of revenue raising, congestion reduction, or some combination would have a significant impact on the actual pricing regime. In addition this would need to be under a national framework.					
<b>5. Regional Petrol Tax</b>	✓	✓	✓	✓	<b>Yes*</b>
Description: Regional petrol tax particularly for funding regional transport options.					
Position: Investigation of this option is supported, noting that although it would be relatively simple to implement, it would be a less desirable option than road pricing for demand management.					
<b>6. Regional Payroll Tax for Public Transport</b>	✗	?	?	✓	<b>Yes*</b>
Description: A regional payroll tax as a significant funding contributor to urban public transport.					
Position: Investigation of this option is supported; noting that community acceptance of it would need to be carefully managed. There seems to be a developing trend in the transport area of demands for action coupled with unwillingness to accept direct means of payment.					
<b>7. Full Environmental Cost Pricing for Water Services</b>	✓	?	✓	✓	<b>Yes*</b>
Description: Reticulated water services (including sewerage) would be charged for at full economic cost plus the cost of the impact on the environment. The short-term cost impact of installing water meters is expected to be offset by reduced capital expenditure on new infrastructure in the medium to long term as pricing moderates demand.					
Position: Investigation of this option, including financial modelling and attribution of costs, is supported. Previously, the cost of installing measuring equipment has been a major barrier to implementation, but analysis is warranted that takes into account the long-run costs, including establishment of new water sources and the impact on the environment.					
<b>8. Green Taxes</b>	✓	✓	✓	✗	<b>Yes*</b>
Description: Specific levies on environmentally detrimental products.					
Position: This is supported for investigation but a more general approach, using levies at landfills, is preferred. The legislation for this is already well advanced and this option has the potential to produce significant revenue for advancing projects in the environmental area.					
<b>9. Bed Taxes</b>	✓	✓	✓	✓	<b>Yes</b>
Description: A per night tax on beds available in commercial accommodation.					
Position: This option is supported as it would achieve similar benefits to a targeted rate.					
<b>10. Poll Tax</b>	✗	✗	✓	✗	<b>No</b>
Description: A charge linked to individuals to recognise the services they consume.					

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Option	Autonomy and accountability	Building Community support	Sound taxation and revenue raising principles	Pragmatic options for real change	WCC support
Position: This option is not supported because it would have a disproportionate impact on the less well off.					
<b>11. Government Funding of Devolved Functions</b>	<b>x</b>	<b>x</b>	<b>✓</b>	<b>✓</b>	<b>Yes</b>
Description: The government in consultation with local government adopt a set of principles to apply when it seeks to impose a new function on local government, and that it accompany any new function with adequate funding.					
Position: This option is supported because it recognises the potential additional cost of new functions transferred from central government to local government.					
<b>12. Removal of rating exemptions for (Churches), Schools, Hospitals etc</b>	<b>✓</b>	<b>✓</b>	<b>✓</b>	<b>✓</b>	<b>Yes</b>
<b>13. Government Grants in Lieu of Rates</b>	<b>✓</b>	<b>✓</b>	<b>✓</b>	<b>✓</b>	<b>Yes</b>
Description: The Crown accept an obligation to make adequate grants in lieu in respect of Crown property currently exempt from rating such as Department of Conservation and national park land. Exemptions from rating should only be provided for land which supports activities that are local public goods, and that this should be subject to the discretion of the local community expressed through the LTCCP/annual plan process.					
Position: This option is supported because it applies rating principles to all properties that benefit from rates funding. As well as the conservation estate, Crown property in urban areas is also significant and similar principles should apply. In these cases the rating valuation methods used for similar properties may be more appropriate than possibly arbitrary valuations used because of the difficulties of valuing, for example, conservation land.					
<b>14. Exemption of Maori Land not in Economic Use or Housing</b>	<b>✓</b>	<b>✓</b>	<b>✓</b>	<b>✓</b>	<b>Yes</b>
Description: In keeping with a basic objective to protect Maori land against alienation, and that being a Crown objective consistent with its obligations under the Treaty of Waitangi, the rates levied should be taxpayer funded. The principle that this is a special type of land where the rating system does not work effectively is supported. On this basis recognition of this status via some Crown funding is considered appropriate.					
Position: This option is supported.					
<b>CATEGORY B: MORE FLEXIBLE USE OF CURRENT REVENUE MECHANISMS</b>					
<b>15. Lift Cap on Uniform Annual General Charge</b>	<b>✓</b>	<b>?</b>	<b>✓</b>	<b>x</b>	<b>Yes</b>
Description: This to be done in conjunction with the introduction through legislation of additional funding tools so that its relative significance, and regressivity, is markedly reduced.					
Position: This option is supported because it provides further flexibility for councils.					

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<b>16. Increased Use of Development Contributions</b>	✓	✓	✓	x	<b>Yes*</b>
Description: Development contributions should be available to regional councils and the Crown should not be exempt.					
Position: This option is supported in principle to recognise the regional-level impact of development and to directly attribute some of the costs of additional infrastructure. The cost of new infrastructure to accommodate growth is significantly higher than the sunk cost of existing infrastructure. There is however a limit to the usefulness of this tool – it is only suitable as a partial funding mechanism.					
<b>17. Choice of Alternative Rating Base</b>	✓	?	✓	x	<b>Yes</b>
Description: Consider whether the actual choice of rating base itself is something councils should consider in the context of promoting community well-being. There is evidence that capital value and, to a lesser extent, annual value is regressive in its impact on low income households and land value rating results in a less affordable outcome for land intensive uses such as farming.					
Position: This option is supported as a clear understanding of these impacts is desirable.					
<b>18. Balance Sheet Management</b>	✓	?	✓	✓	<b>Yes</b>
Description: An in-depth analysis of balance sheet management issues similar to the recent New South Wales Inquiry, and a recommended a set of financial key performance indicators.					
Position: This option is supported as it has the potential to bring greater consistency in the appropriate use of debt. Where there are clear requirements for community investment, the managed use of a sensible level of debt recognises the desirability of spreading the cost over time.					
<b>19. Greater Use of Targeted Rates</b>	✓	✓	✓	x	<b>Yes</b>
Description: Highlight the potential of targeted rates and the desirability of making greater use of them.					
Position: This option is supported as it has the potential to more closely align costs and beneficiaries.					
<b>20. Increased Government Funding for Roothing or Other Infrastructure</b>	?	✓	?	✓	<b>Yes</b>
Description: Increase in the average FAR from 50% to 75% by increasing the funding pool, and affirm the principle that all tax derived by government from road related activity should be applied to roading.					
Position: This option is supported as it recognises the nature of roads as a national network infrastructure. To further widen the range of FARs within a static funding pool is not supported, because this represents a greater shift from urban to rural.					
<b>21. Best Practice and Consistency</b>	?	✓	-	✓	<b>Yes</b>
Description: A good practice guide on the use of local government funding tools to provide a common starting point for decision-making on how to fund any particular service or activity, and a set of agreed rationales, to assist councils achieve consistency where that is desirable, or explain departures when they decide to take a different approach. The statutory requirement for local authorities to adopt the funding and financial policies set out in section 102 of the Local Government Act 2002 be extended to include the council's policy on affordability with specific reference to the impact on the bottom decile and quartile household incomes.					
Position: This option is supported. The flexibility of legislation is a strength but it does appear to					

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have led to approaches that are not logically sound or consistent across the sector. Improvement in the overall standard of financial management can only be positive for the sector and the level of confidence in local government. The explicit consideration of lower income households would be useful, noting that existing rating systems inherently contain decisions about the distribution of rates across groups in the community.

<b>22. Role of the Auditor-General in respect of the LTCCP</b>	✓	✓	-	✗	Yes
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Description: The Auditor-General to report on the fairness and objectivity of the presentation of the material in the LTCCP (but not on the fairness and objectivity of the policies and objectives themselves as that would take the Auditor-General into the political realm).

Position: Options that widen the role of the Auditor General to provide greater assurance to communities are supported, noting that the definition of “fairness” may need some work to ensure it is measurable. .

## CATEGORY C: REDUCING IMPACTS OF CURRENT REVENUE MECHANISMS

<b>23. Differential to Smooth Impact of High-value Residential Properties</b>	✓	✓	?	✗	No
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Description: A more regressive tax for high value properties.

Position: This option is not supported as it is already factored into and recognised in current rating systems.

<b>24. Valuation Averaging</b>	✓	✓	✓	✗	Yes*
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Description: Smoothing the impact of changes by implementing a rolling average system.

Position: This option is supported for investigation. It may be possible to achieve similar objectives using annual revaluation, and in any case it would be likely to work more effectively if this was used. Any system that lessened the impact on particular properties would need to be carefully analysed because it is in effect redistributing that impact.

<b>25. Enhance Take up of Rates Rebates</b>	✓	✓	✓	✓	Yes
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Description: The maximum rebate and the abatement threshold for the scheme should be indexed to the consumer price index. The eligibility rules should be reviewed so that low income people who are de facto ratepayers, such as residents in retirement villages, and in homes owned by family trusts, also qualify. Administration of the rates rebate scheme should be transferred from the Department of Internal Affairs (the currently responsible department) and local government to Work and Income New Zealand.

Position: This option is supported. The rates rebate scheme has excellent potential to ameliorate one of the major flaws in the rating system – its impact on low-income people/households. Councils are not in a good position to make these income-related decisions so that the assistance reaches those people who need it most.

<b>26. Rates Postponement</b>	✓	✓	✗	✗	Yes
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Description: Ensure older people are aware of the potential of rates postponement and understand how to access it, and support measures to encourage more local authorities to offer rates postponement.

Position: This option is supported and should be promoted as a useful tool, where appropriate for the circumstances.

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## CATEGORY D: COST CONTAINMENT

<b>27. Performance Improvement/Measurement</b>	✓	✓	-	✓	<b>Yes</b>
Description: The voluntary development of a comprehensive performance management/benchmarking system.					
Position: This option is supported. As above, improvement in the overall standard of financial management can only be positive for the sector and the level of confidence in local government. It is important however that such a system be voluntary, because measures imposed from the top down could result in a 'compliance mentality'.					
<b>28. Amalgamation</b>	x	x	?	x	<b>No</b>
Description: Merger of councils.					
Position: This option is not supported as a cost saving measure because it has not been demonstrated that major savings are accessible. Individual councils may however wish to pursue this voluntarily.					
<b>29. Review of Requirement to Fund Depreciation</b>	x	?	?	x	<b>Yes*</b>
Description: Development a set of principles to be applied by all local authorities for this purpose.					
Position: This option is supported as it has the potential to bring greater consistency in this area. The principle of fully funding depreciation, unless there are clear and justifiable reasons for not doing so for specific assets, is a fundamental financial management principle.					

## OTHER

<b>30. Rating Capability</b>	x	?	?	x	<b>No</b>
Description: Endorse the principle that, under specific conditions, the Crown should be the ultimate risk bearer if communities become non-viable financially.					
Position: This option is not supported as it undermines local accountability. Clearly in some circumstances the Crown is the ultimate risk bearer, but to make this explicit could allow communities to escape their responsibilities to be self-supporting where possible.					
<b>31. Referenda and Recall</b>	✓	✓	-	x	<b>No</b>
Description: Submitters are agreed there is a problem with public perception of the credibility of local government consultation but are not agreed on a solution. Two alternatives are proposed:  Referenda (supported by Grey Power, Federated Farmers, and the Federation of Maori Authorities) - there be a requirement for any non-core expenditure exceeding defined amounts to be put to a referendum of <b>ratepayers</b> with information provided on the cost and proposed means of funding of the intended expenditure. Councils should be required to take note of the resultant expression of willingness to pay in making their final decision.  Recall (supported by other stakeholder group members) - communities dissatisfied with their councils' major spending proposals should have the right to seek recall - a poll of <b>voters</b> which, if carried by a simple majority, would result in a fresh election for the entire Council (including the Mayor). Recall would be triggered by a petition of not less than 10% of voters on the Council's electoral roll.					
Position: Referenda are not supported there are already adequate mechanisms for determining a community view on specific funding proposals, and they set up new democratic dynamics that run counter to the planning framework embodied in the Local Government Act 2002.  Recalls are not supported because they could encourage single issue elections and be used to stymie new proposals.					

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<b>32. Community Infrastructure Fund</b>	?	✓	✓	✓	<b>Yes*</b>
<p>Description: A community infrastructure fund would aggregate most of the current central government targeted funds, with the exception of transport-related funds, which have their own conditions, criteria and agencies.</p> <p>The fund would be administered under a policy framework that recognised the need to centrally fund some activities. The fund would be a contestable pool and likely to be a matching funding arrangement for successful bids. Criteria for applications would include national good elements similar to those that exist for broadband infrastructure and water quality funding. Careful consideration would be needed of the ability of local communities to be self-reliant to avoid councils abdicating their responsibilities to make hard choices. And the fund would need to be of sufficient size to allow both small and large councils to access it.</p>					
<p>Position: Investigation of this option is supported because it could rationalise and improve the current recognition of national good in targeted central government funding, without moving to 'direct funding'.</p>					
<b>33. Rating at a fixed percentage</b>	?	?	✓	✓	<b>Yes*</b>
<p>Description: Rating at a fixed percentage, probably for at least the three years of a triennium. It would be based on the principle that a tax based on a percentage of property value is a fair way of supporting the many services needed by communities.</p>					
<p>Position: Investigation of this option is supported because it could move the focus of communities from annual increases to long term planning for infrastructure needs. Such a tax would have some bouyancy as it would fluctuate with the ups and downs of property capital values, and would require councils to plan for accumulation of or running down reserves. The recent increases in value of the property market should not be taken as a long-term trend, and naturally buoyancy works both ways.</p>					

\* support for investigation of this option

## 5. Conclusion

The issues of local government funding sustainability being tackled by the Inquiry are long standing and intractable. They have however been brought into sharp focus by significant funding pressures on councils and the resulting LTCCPs.

Detailed analysis has shown that the cost drivers facing local government are real and not easily mitigated against. There is good evidence in the planning processes of local government that LTCCP expenditure is necessary and appropriate, with the direct result that substantially more funding will be needed.

The use current of current funding tools by local government is reasonably sophisticated and although there is some scope to use them better, this is unlikely to fully resolve funding sustainability issues.

Part of the solution will need to be new or supplementary funding tools and a concerted campaign to build community support for spending plans. The role of councils to develop stronger community support and understanding of spending plans is acknowledged. This may be under the umbrella of national programmes. The areas that are supported are in particular:

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- a) promotion of best practice (21, 27)
- b) more flexibility or enhanced use of some tools (8, 15, 16, 17, 19, 24, 29)
- c) investigation of transport funding tools (4, 5, 6, 20)
- d) establish basis of funding devolved functions and current exemptions (11, 12, 13)
- e) enhanced rates rebate scheme (25)
- f) community infrastructure fund (32)
- g) investigate rating as a fixed percentage (33).

And finally it is noted that pressures on funding and the cumbersome planning processes of councils can be counterproductive in a global environment that requires flexibility and speed of action on the part of councils. The challenge in this situation is to maintain democratic accountability while enabling councils like WCC to continue evolving as organisations that serve their communities effectively and maintain the international competitiveness of their cities.

## APPENDIX 2

### Terms of Reference of the Independent Inquiry into Local Government Rates

#### Purpose

1. To provide an independent assessment of New Zealand's local government rating system and identify options to enhance rates as a funding tool for local authorities.

#### Context

2. The Inquiry has arisen as a consequence of public concern in light of financial and rates projections outlined in Long-term Council Community Plans and confirmed in local authority rating decisions during the June-August 2006 period.

3. The Government has announced the establishment of an independent inquiry to provide the public, key stakeholders and the local government sector with a mechanism to outline issues relating to the local government rating system and suggest options to address these issues.

#### Objective

4. To consider issues relating to current local government rating, and to other revenue raising mechanisms, and provide recommendations to the Government for enhancing rating and other funding mechanisms for local authorities.

#### Tasks

5. The tasks associated with the inquiry will include:

(a) Examine the level of rates, level of rates increases and trends in the use of rating tools nationally to fund services, as well as other sources of revenue currently available to local authorities;

(b) Consider the phase one and phase two reports of the Local Authority Funding Project, their recommendations and implications for the future of rates;

(c) Develop an understanding of the drivers for local authority expenditure, including, growth, the age and state of infrastructure (e.g. public transport, roading, water and wastewater), requirements of 'higher standards' (e.g. water quality) and other infrastructural demands on both capital and operating expenditure needs;

(d) Examine the sustainability of rates as the major revenue raising tool, having regard to affordability issues for communities, groups within communities, and individuals, particularly those on fixed incomes;

(e) Examine the impact of rates on land covered by the Te Ture Whenua Maori Act 1993;

(f) Examine the impact of the new Rates Rebate Scheme (and other government assistance packages for families) and local authority rates remission and postponement policies;

(g) Examine the impact and ongoing need for existing exemptions from liability for rates, including Crown exemptions from liability for rates; and

(h) Provide a report by 31 July 2007 on (a)-(g) above along with recommendations to enhance rating and funding mechanisms for local authorities.

#### Submissions

6. It is expected that the inquiry will invite written submissions on an open basis and hear oral submissions from key sector groups identified by the inquiry.

#### Assumptions

7. The inquiry is not a review of the system of local government per se, and in particular of:

- the purpose, autonomy, or structure of local government; or
- the principles of democracy, transparency, equity and accountability that local government operates under.