

Current developments in New Zealand local government

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Peter McKinlay
AUT University

Local Government Funding and Rating

August 2007 saw the release of 'Funding Local Government', the report of the Local Government Rates Inquiry (available at www.ratesinquiry.govt.nz).

New Zealand local government has one of the world's most flexible rating (property tax) systems. Councils may choose between capital value, land value or annual (rental) value. Rates may be levied primarily as an ad valorem charge but councils may also use a variety of fixed charges. In addition they may levy a targeted rate or rates, which may be either a fixed amount or ad valorem, charged on a single property or category of properties to recover the cost of a specific service or services. Councils also have the power, in consultation with their communities, to adopt highly flexible postponement policies allowing people to defer, indefinitely, payment of rates. (Normally when this is done, councils take a first charge on the property and recover interest at their marginal cost of borrowing.)

Despite this high degree of flexibility, there is a sense that the rating system as such is reaching the limits of its potential to provide adequate funding for local government activities. The Rating Inquiry itself noted that approximately 56% of local government operating revenue came from rates but recommended that, long-term, this proportion should not exceed 50%. More generally, in respect of local government itself, the Inquiry concluded:

Local government works well in meeting the diverse needs of New Zealanders. It provides, at reasonable cost, a substantial range of basic services, which can broadly be categorised as either network infrastructure (roads and public transport, the "three waters" - water supply, waste water and stormwater - plus solid waste disposal), or community and social infrastructure (cultural and recreational

facilities), as well as a range of regulatory activities. Overall it accounts for somewhat less than 5% of national expenditure.

Ironically, some of New Zealand's difficulties result from attempts to ensure greater fairness, transparency and accountability. Councils are required to revalue properties for rating purposes at least once every three years (some do so annually). New Zealand, like much of the world, has recently come through a major property boom. This impacted differentially with residential property in premium locations (coastal, lakeside for example) rising in value much more rapidly than residential property generally. When rates are levied on an ad valorem basis, the result can be major shifts in rating burden between different homeowners even though total rate revenues for the council may not increase greatly.

This coincided with new accountability requirements, with New Zealand local authorities required to produce 10-year forecasts which are reviewed by the office of the Auditor-General to ensure their robustness. The purpose was to make sure local authorities were properly providing for maintenance, upgrading and investment in needed infrastructure. The result was a one-off step jump in projected future expenditure, and thus rating requirements, as local authorities 'came clean' about the extent of required investment.

A further factor is that New Zealand local authorities are required to report in accordance with international financial reporting requirements. Among other things this means making full provision for depreciation. For some councils this is now the single largest item in their operating expenses. Councils have a statutory obligation to operate a balanced budget but with an exception that, if they deem it prudent to do so, they may operate at a deficit. This was intended to provide some flexibility around full recovery of depreciation, especially for councils which were investing very heavily in new long-life infrastructure.

There is thus a theoretical opportunity for councils to relax the pressure of depreciation on current rating but this comes at a price – publicly revealing that they are operating at a deficit with the consequent risk of ill-informed criticism. Few councils have been prepared to take this risk, preferring instead to try and hold their total expenditure down.

The Rating Inquiry undertook a commendably thorough review of local government funding and has produced a very useful report. Some of it focuses on improving local government practice, for example, making greater use of borrowing for long-life assets. It also made some helpful recommendations on tidying up anomalies in statutory exemptions or partial exemptions from rating (a number of central government funded activities are partly or wholly exempt, effectively amounting to a subsidy from the local ratepayer to the national taxpayer).

Overall, however, the report has not produced any 'magic bullet'. It recognizes the practical reality that higher tiers of government are not falling over themselves to provide additional funding for local government. It did include a relatively modest proposal designed to provide smaller local authorities with some assistance towards the cost of necessary water and waste water infrastructure, but disappointed those advocating major increases in funding support.

Whether and to what extent any of its recommendations will be taken up is still a matter of conjecture. At least the government is giving it serious consideration, seemingly in contrast to the immediate response to the report of the UK Lyons Inquiry, and of the Scottish Rating Inquiry.

In contrast with the relative lack of progress with the Rating Inquiry, some New Zealand local authorities are demonstrating how our flexible rating powers can be used creatively to help individual ratepayers or groups of ratepayers in quite innovative ways. As examples:

- A large industrial estate was having very real difficulties with security. Break-ins and vandalism were at a relatively high level. A contributing factor was the disparate range of security arrangements in place for individual firms. The local council worked with a group of businesses in the estate to find a solution. The estate formed a business association to act as the single purchaser of security arrangements for the entire estate. The local authority agreed to facilitate funding by using a targeted rate provided it received a two-thirds majority in a vote of estate ratepayers (this was essential to overcome the free-rider and transaction costs problems which make it extremely difficult to introduce these kinds of arrangements on a purely voluntary contractual basis). The majority was forthcoming. The new security arrangements have seen a dramatic drop in break-ins and a very real improvement in response time on call outs.
- Central government's Energy Efficiency and Conservation Authority is introducing a subsidised loan scheme for home retrofit, including upgrading home heating. It recognized that many homeowners in its priority group would not be able to afford loan repayments (older people on limited incomes as an example). It has reached agreement with a group of councils that they will use a combination of a targeted rate and rates postponement to allow a very cost-effective means of home equity release ('reverse mortgage') which is also extremely safe (unlike a private provider, local government has no incentive to encourage people to borrow more than they absolutely need – and by statute is not permitted to make a profit but only to break even on the cost).

- Consideration is being given to other uses for targeted rates and rates postponement to support ageing-in-place: one possibility is a home maintenance service.

Royal Commission on Auckland Governance

In December 2007 the New Zealand government announced the establishment of a Royal Commission on Auckland Governance. The decision to establish a Royal Commission followed on from significant lobbying by interests within Auckland, especially from the business community, who believed that existing governance arrangements were hampering the region's growth. Amongst their concerns were fragmentation of a region of around 1.2 million people into seven city or district councils plus a regional council; the multiplicity of providers of bulk and retail water; and that some 15 agencies from central and local government were involved in decision-making on planning and provision of regional roading, together with what they saw as a general lack of progress in addressing Auckland's infrastructure challenges.



The terms of reference appear comprehensive. They range from the ownership, governance and institutional arrangements for public infrastructure, services and facilities, to the governance and representation arrangements which will best:

- Enable effective responses to the different communities of interest and reflect and nurture the cultural diversity within the Auckland region; and
- provide leadership for the Auckland region and its communities, while facilitating appropriate participation by citizens and other groups and stakeholders in decision-making processes.

However there are also significant exclusions. They include the purposes and principles of local government; local government arrangements in New Zealand generally; the extent to which recommendations relating to the Auckland region may also be appropriately implemented elsewhere; and central government agency and institutional arrangements dealing with expenditure of appropriated funds, provision of services and the stewardship of assets within ministerial portfolios.



The Commissioners (from left to right)
David Shand, Hon Peter Salmon,
Dame Margaret Bazley

The Commission has set a tight timetable. Submissions were required by the 22nd of April. Hearings will take place in the last three weeks of May and throughout June and early July. The final report must be delivered by December 2008. There is a very real sense that the opportunity for existing local authorities, key stakeholders, and the general public to engage effectively and on an informed basis will be prejudiced by the tightness of the timetable.

Despite this, and the extensive exclusions from the terms of reference, it is clear that the Royal Commission process is resulting in a very intense debate on possible options. One council has already suggested the creation of a single local authority for the whole of the Auckland region, to be responsible for all local government functions, ranging from metropolitan governance and regional spatial planning to economic development, and including infrastructure currently handled by arm's-length organisations. Others have reacted criticising this as a power grab that would effectively eliminate local democracy.

Alternative approaches are reflecting on how to balance factors such as:

- The need for effective, efficient and timely decision-making on major infrastructure, as compared with the demand for democratic local decision-making, which at an extreme can see NIMBYism bring decision-making almost to a halt.
- The demand for greater efficiency in service delivery, which many New Zealanders believe means larger local authorities, but also the importance of preserving local democracy. A greater emphasis on shared services, and recognition of international research on the limitations of amalgamation, and on the cost of larger authorities, are influencing this part of the debate.
- The proper role and function of local government: should modern local authorities be treated as though they are in practice publicly owned infrastructure companies, or is their overriding role the promotion and enhancement of local democracy?

Other challenges include the difference between administrative and functional boundaries. The economic impact of the Auckland region extends well beyond its formal boundaries, raising the question of how functions such as transport and economic development, including the role of export ports, can properly be managed.

Whilst it is always dangerous to make predictions with an undertaking such as this, there does seem to be a growing interest in the Greater London Authority model as an acceptable means both for managing region-wide functions, and for enabling the 'single voice for Auckland' which is seen as an essential requirement. Certainly, there is going to be a very major focus on the design of the structural arrangements, including the question of whether major regional functions can properly be placed within a single entity, or whether they require their own separate structures complete with 'fit for purpose' governance.