

IMPROVING LOCAL GOVERNMENT TRANSPARENCY, ACCOUNTABILITY AND FINANCIAL MANAGEMENT – REGULATORY IMPACT STATEMENT

EXECUTIVE SUMMARY

1. This regulatory impact statement (RIS) has been prepared to support a suite of papers, which have been developed following a review of the planning, decision-making and accountability aspects of the Local Government Act 2002 (the Act). Due to the large amount of material covered, proposals have been split into three Cabinet papers.
 - Paper 1: improving transparency, accountability and financial management;
 - Paper 2: long-term planning and community outcomes; and
 - Paper 3: referendums.
2. Overall, the proposals in these papers are intended to improve the mechanisms ratepayers can use to ensure council decisions reflect their views and priorities. Many of the proposals also seek to remove unnecessary compliance costs and other regulatory barriers and burdens that increase rates and impede council decision-making.

ADEQUACY STATEMENT

3. The Department of Internal Affairs has reviewed this Regulatory Impact Statement and considered it to be adequate according to the adequacy criteria.

STATUS QUO AND PROBLEM

4. The Act sought to promote transparency and accountability in local government, but in practice few new mechanisms were introduced to apply those principles. Accountability mechanisms do not provide citizens and ratepayers with direct control over council activity since they are retrospective. The transparency provisions have resulted in a lot of information being made available, but have not necessarily focused on providing useful information for ratepayers. At the same time the compliance costs in meeting the transparency requirements, especially in the preparation of the long-term council community plan (LTCCP), have been very large.
5. For several years local authority rates have been rising faster than consumer price inflation. Between 2001 and 2009, for example, residential rates grew by 63.1 per cent, while the Consumers Price Index (CPI) grew by 23.7 per cent.¹ Infrastructure costs have been a major cause of rate increases, rising at a rate more than consumer price inflation. Councils have also needed to upgrade the quality of infrastructure, especially for water and wastewater treatment plants, and invest in more infrastructure to meet growth demands.

¹ Data sourced from Statistics New Zealand consumers price index between March 2001 and March 2009.

6. These trends are expected to continue. Department of Internal Affairs (the Department) analysis of 2009 LTCCPs shows that between 2009 and 2019 rates are forecast to rise by 58.3 per cent. This is more than double probable consumer price inflation for the decade. It is driven predominantly by projected cost increases, rather than by increases in the range and quality of services provided.
7. Local government provides some services that are critical to New Zealand's economy. These include water services infrastructure (water supply, sewage treatment and disposal, and stormwater drainage), flood protection and roads. Local government also carries out regulatory functions that are critical to the economy, notably the control of land development through the Resource Management Act 1991 and the administration of building consents through the Building Act 2004.
8. In the Speech from the Throne, the Government outlined its three priority areas as:
 - growing the economy;
 - a reduction in government bureaucracy and a focus on investing in frontline services; and
 - reducing regulatory and compliance demands that get in the way of productivity growth.

Work is required to apply these priorities to local government.

9. On 20 April 2009, Cabinet invited the Minister of Local Government to report to the Cabinet Economic Growth and Infrastructure Committee with specific proposals to improve local authority transparency, accountability and financial management, and any other proposed minor amendments to the Act [Cab Min (09) 13/6 and EGI Min (09) 6/10 refer].
10. It was proposed to review certain aspects of the Act. There would be a particular focus on Part 6, which covers planning, decision-making and accountability.

OBJECTIVES

11. The proposals in these papers have been developed to address the points outlined above, by applying the following principles to local government:
 - local government should operate within a defined fiscal envelope;
 - councils should focus on core activities; and
 - council decision-making should be clear, transparent and accountable.²
12. In particular, the proposals focus on improving the operation of the third principle – the transparency and accountability mechanisms that aid ratepayers and help to ensure that council decisions reflect their preferences. It is thought that making these improvements will help to bring about the other two principles.

² These principles were set out in a Cabinet paper [EGI (09) 44], and agreed by Cabinet in April 2009.

13. In addition, some of the proposals seek to reduce unwarranted compliance costs imposed on the local government sector, advance the Government's policy agenda, and make other minor amendments to the Act.

ALTERNATIVE OPTIONS

14. This review looked at a range of possible ways of achieving the stated objectives. The following proposals were considered and discounted.

A local government cost index

15. It is difficult for ratepayers to assess how much price inflation has affected the costs for their council to deliver services to them. The news media focus on consumer price inflation as a measure of all price inflation in the economy. However, the CPI is heavily weighted to items such as food and alcoholic beverages that form a significant part of the household budget but have little impact on the cost of delivering local authority services. Conversely, significant expenditure items for local government, such as the price of road building materials, are absent from the CPI.
16. For several years price indices published by Statistics New Zealand that are specifically relevant to local government, for example the Producers Price Index (Local Government Inputs) and sub groups of the Capital Goods Index for pipelines and transport ways, have increased at rates significantly greater than the CPI. Therefore, an expectation that councils can deliver the same level of service and keep rates increases to the level of the CPI may not be achievable.
17. A single local government cost index could represent a more realistic benchmark against which to assess proposed rates increases. However, developing such an index would be expensive. An alternative approach would be to create an indicative index based upon a weighted combination of existing indices.
18. Apart from issues of reliability and comprehensiveness, this approach assumes that the mix of services provided by individual councils is roughly the same. In practice, this is not the case. Regional councils have little involvement in the provision of infrastructural services and therefore have much lower capital expenditure programmes than territorial authorities. Rural councils have considerably larger roading networks than urban councils and tend to spend proportionately lesser sums on services such as libraries and parks. It is not practical to reflect these differences in an overall index.
19. While the creation of such an index might make a small contribution to improving the transparency of local government finances, overall it is unlikely that the costs would outweigh the benefits of doing that. Hence this option is not a preferred option.

Changing the timing of the LTCCP

20. Changing the timing of the LTCCP, so that it is produced in the first year of a council's term, rather than in the middle year as currently occurs,

was also considered. The arguments in support of such a change are that it would:

- flow naturally from a pre-election report that created an election debate about the future direction of a district;
- link to any referendum decision made at the election;
- clearly unshackle the council from commitments made by the previous council; and
- make the new council squarely accountable for what happened during its term of office.

21. The arguments against the proposal are:

- councils are not bound by the decisions of previous councils. If a newly elected council does not want to proceed with a project the previous council included in its LTCCP it does not have to;
- local government elections are less driven by values than national elections; therefore, there is rarely a need for major shifts in direction when a new council is elected. Issues tend to be more about the levels of service delivered and when or if new capital projects should be undertaken;
- councils are rarely elected on the basis of parties; therefore, time is needed for a newly elected council to build consensus and understanding of issues among councillors before decision-making can proceed. Preparing the LTCCP too soon after an election could disempower newly-elected councillors as they will not have adequate time to gain an effective understanding of the issues facing their council and the LTCCP process before decisions are made. This could weaken member input into the plan and render it more prone to staff control; and
- the best LTCCP processes are those where the bulk of the public consultation takes place before the draft plan is published. This is the time when there is the most room for dialogue with ratepayers and citizens. Preparing an LTCCP in the first year after an election would severely limit the time for such consultation.

22. Overall, the difficulties in bringing the LTCCP forward outweigh the benefits, even if the content of the LTCCP is streamlined. In particular, the difficulty for new-elected councillors to fully participate in the process, and the limitations that would be imposed on effective consultation with ratepayers, outweigh the benefits in bringing the process forward. Therefore, this is not a preferred option.

Changing or removing audit requirements for LTCCPs

23. The Act introduced a requirement to audit LTCCPs and amendments to LTCCPs. This requirement is unique to New Zealand. In almost all cases where audit opinions are issued, the opinion is retrospective and provides assurance about the reporting of past events and performance. Auditing prospective financial information is rare.

24. Some councils, especially smaller ones, have challenged the relative costs and benefits of auditing an LTCCP. The total cost for the 2009 audits is expected to be about \$6.3 million, with an estimated median cost of \$66,000. This excludes the time spent by council staff in dialogue with auditors.
25. The purpose of the audit is to provide a benefit to ratepayers and citizens, not the council. In evaluating the benefit/cost of the audit requirement, it is the view of ratepayers and citizens that is most important.
26. There are three main ways to reduce the cost of an audit – by reducing the breadth of the audit (how much is audited), the depth of the audit (what level of assurance is offered), and the frequency of the audit (whether any assurance is offered).
27. The present requirement is for the auditor to provide an opinion on:
 - (a) *the extent to which the local authority has complied with the requirements of this Act in respect of the plan;*
 - (b) *the quality of the information and assumptions underlying the forecast information provided in the plan; and*
 - (c) *the extent to which the forecast information and performance measures provide an appropriate framework for the meaningful assessment of the actual levels of service provision. (Section 94 of the Act.)*
28. If proposals about service performance reporting are adopted, then item (c) will be deleted from the audit mandate. This, along with the omission of some of the financial policies from the plan, would make a small reduction in the breadth of the audit.
29. In terms of the depth of an audit, the accounting profession recognises two types of approach.³ An audit is designed to provide a high level of assurance about the accuracy of the information on which the audit opinion is given. It is a positive assurance – the auditor is confident that the statements audited are correct and reliable. (In the case of the LTCCP, that the document is ‘fit for purpose’ while recognising the prospective nature of the information.) In contrast, a review is designed to give a moderate level of assurance. Effectively, it is a negative assurance – a statement that the reviewer has found nothing to make them doubt the accuracy of the statements reviewed.
30. In many ways an audit of prospective financial information is inherently a review engagement anyway in that it is primarily an analytical process designed to test the reasonableness of a council’s forecasts. An audit of historic accounting information, such as an annual report, will place a high emphasis on obtaining positive evidence that the reported results are correct. This is not possible in the audit of forecast information.
31. The Auditor-General has estimated that shifting to a review basis might reduce audit costs by a small amount. However, each council is unique and the actual savings would vary from council to council. If this option

³ *Statement of Review Engagement Standards*, NZ Institute of Chartered Accountants, 2003

were adopted, ratepayers would need to understand the lower level of assurance obtained from a review engagement compared with an audit.

32. The third option is to lower the frequency of an audit based upon a risk assessment. With this approach, the Auditor-General would have discretion to exempt a council from having its LTCCP audited based on an assessment that it posed little risk of being qualified.
33. The assessment of risk needs to be judged against the value the audit opinion offers. Essentially, where audits are qualified, two types of qualification emerge. The first type is that the plan is in part defectively prepared (for example, the underlying information on which the plan is based is unsound). The second type is a qualification that, although properly prepared, the auditor has concerns about the financial prudence of the council's plans that should be drawn to the attention of the public.
34. Both types of qualification are important and, therefore, the risk assessment would have to address both types of risk. Importantly, a significant degree of audit work would have to be done before the risk could be assessed. It would be difficult to assess the likelihood of the second type of qualification arising until well into LTCCP development.
35. For there to be a significant impact on council budgets, whether to exempt a council from audit would need to be decided at least 15 months before the LTCCP adoption. Many events could occur in the interim period that might make an audit desirable.
36. There is also a concern that the exemption from the audit requirement could be seen as a higher degree of approval for those councils, compared to say an audited council that obtained an unqualified opinion.
37. A variation on this approach would be to audit every second LTCCP. However, simply auditing every second LTCCP seems arbitrary. Part of this approach could be to audit plans if the council received a non-standard audit opinion in the previous cycle. This would provide an incentive to councils to provide an adequate LTCCP. With this approach, though, situations where standards have fallen since the previous LTCCP, or instances of financial imprudence, would not be revealed.
38. Finally, it seems probable that those councils most concerned about the costs of audits, typically the small and rural councils, are inherently more risky. This is because of their limited resources and dependence, amongst other things, on a few key staff. Hence the result of this approach may perversely benefit those that are less concerned about audit costs.
39. It appears that the only way to significantly lower the costs associated with auditing LTCCPs is to abandon the audit altogether. However, the performance of the sector is still not at a level where the costs of the audit process outweigh the benefits. (In 2009, for example, 13 out of 85 draft LTCCPs received a non-standard audit opinion, and some other councils amended their original plans prior to publication to achieve an unqualified opinion.)

40. Having considered all of these options, we have concluded that the requirement to audit all LTCCPs should remain, unchanged.

Referendums (non-preferred options)

41. Local government legislation primarily provides for a system of representative democracy. Communities elect individuals to make decisions on their behalf, and in their best interests, though not necessarily in accordance with their wishes.
42. According to the Act, the purpose of local government is to enable democratic local decision-making and action *by*, as well as *on behalf of*, communities (section 10(a)). The use of referendums is already provided for in legislation, but could play a bigger part in council decision-making.⁴ This could help councils to improve awareness about the views of local people, and allow voters to feel more engaged in decisions.
43. A range of options relating to referendums were considered. Many of these are not preferred options, for a variety of effectiveness and/or drafting issues and concerns. A brief outline of each of the options that were discounted is provided below.

Referendum to exceed specified expenditure limits

44. This would control growth in council expenditure by ensuring ratepayers sanction growth beyond a specified limit. The limit would be defined as the previous year's expenditure, plus an allowance for inflation and community growth.
45. There are a number of potential difficulties associated with implementing this option; for example:
- measuring growth in an objective and relevant way is problematic;
 - measuring inflation is problematic, particularly as CPI is not a good representation of local authority input costs;
 - limiting operating expenditure may create perverse incentives;
 - defining expenditure is problematic (especially if this was to be put into legislation) and there would need to be exemptions (for example, for disaster recovery); and
 - there are timing difficulties with measuring actual expenditure under accrual accounting.

Referendum to exceed specified rates limits

46. This would control growth in council taxation by ensuring ratepayers sanction growth in rates beyond a specified limit. The limit would be

⁴ There are three circumstances in which voters can require referendums: to initiate or approve a reorganisation proposal; to establish whether a council should have Maori wards or constituencies; and to decide whether the single transferable vote or first past the post voting system should be used for local elections. Councils are also required to hold a binding referendum if they wish to close or transfer a water service for fewer than 200 people. The Local Electoral Act 2001 enables councils to hold referendums on most matters, but electors cannot require these.

defined as the previous year's rates, plus an allowance for inflation and community growth.

47. Many of the difficulties associated with this option are the same as those noted above, particularly in relation to measuring growth and inflation. Having a rates limit without a debt limit might mean councils borrow excessively rather than control costs.

Referendum to engage in 'new, non-core activities'

48. This is intended to help ratepayers control the range of council activities. However, there are difficulties associated with this option, particularly when attempting to define 'new', 'core' and 'activity'. In addition, current spending on what might be considered 'non-core' activities, in relation to overall spending, does not appear to be significant.⁵

Referendum to proceed with major projects

49. The concept of representative democracy relies on the ability of voters to alter council policy by changing its membership. However, major investments, such as sports stadiums and new roads, are irreversible. This option would aim to ensure that irreversible investments are consistent with ratepayers' aspirations.

50. Difficulties associated with this option include:

- producing a definition of 'project', against which costs can be measured;
- establishing whether the cost is the council's contribution or the total cost of the project, where more than one party funds the project;
- deciding which projects (or other decisions) would be sufficiently 'major' to trigger a referendum and what the cost threshold might be; and
- establishing what would happen if a project that was expected to cost less than the referendum threshold went over budget.

51. In addition, there is a risk that councils might change their behaviour to circumvent referendum requirements. They might, for example, shift project funding to developers and enter into build-own-transfer schemes, or break large projects into smaller ones. This could be more costly and less efficient.

Project ranking referendums

52. This would be held in the lead up to the LTCCP and provide councils with information on ratepayers' preferences and priorities. It could allow yes/no preferences, and for comparative rankings of major projects and proposals. Again there is a difficulty in defining 'major' projects and proposals.

⁵ The 2007/08 Local Authority Census shows that 97 per cent of operating expenditure was spent on what are described later in this paper as 'core' services. (Of this, 74 per cent was spent on roading, transport, water service, waste services, governance, regulatory planning, and emergency management; 18 per cent on culture, recreation and sport; and five per cent on environmental protection.) The remaining three per cent was spent on property, forestry, agriculture, and 'other'.

Require councils to consider using referendums in their decision-making

53. This would strengthen the current situation, by amending the Act to *require* councils to consider whether a referendum should be used for a decision.
54. This option could raise awareness, amongst councillors and the public, of the availability of referendums. However, it may have little impact on council behaviour and be ineffective in substantially increasing the use of referendums.

Alternatives to referendums

55. Additionally, alternative ways for councils to establish public preferences, through opinion polling and citizen panels, were also examined. However, opinion polling does not include a way to inform ratepayers of the issues involved before preferences are formed, which is important for them to make a considered decision. There are also difficulties associated with citizen panels. For example, this method involves using the internet to establish large representative panels and obtaining views about a range of issues. It relies, therefore, on participants being computer literate and having access to the internet. This would immediately exclude a proportion of the population. Both methods rely on sampling the population, whereas the entire electorate can participate in a referendum, giving the results greater legitimacy.

Recording contracts with the private sector in annual reports

56. On 27 March 2009, the Local Government and Environment Committee (the Committee) tabled in the House its report on petition 2008/2. This petition asked that:

*... the House of Representatives urgently amend the Local Government Act 2002 to make it a mandatory requirement to ensure councils and council-controlled organisations are open to public scrutiny by using annual reports to record contracts issued to the private sector for goods, services and people as a means of providing openness and accountability in council operations, and to help ensure prudent stewardship of citizen and ratepayer resources.*⁶
57. The issues raised in this petition were considered as part of work to improve the transparency, accountability and financial management of local government, as per the Committee's recommendation.⁷
58. The Department acknowledges that information on contracts issued to the private sector might be beneficial to some individuals and organisations, as it is not routinely available. It might also help to educate the public about council finances.
59. However, the benefits of this proposal to the average ratepayer are uncertain. Ratepayers are likely to be more interested in the overall costs of major projects and services, and how these costs might be

⁶ Petition 2008/2, of Penelope Mary Bright and 189 others, was presented on 16 December 2008.

⁷ The Government's response to the Committee's report was presented to the House on 16 June 2009. The Government accepted the Committee's recommendation that the issues raised by the petition would be considered by the Minister of Local Government in the context of this review.

controlled, than in retrospective details about every contract their council has issued. Other proposals in this paper are intended to address the first two elements here. The aim is to strengthen transparency and accountability tools and provide ratepayers with useful, prospective information at relevant times in the decision-making cycle. The annual report is backward-looking and is not a tool that helps ratepayers to influence council decisions.

60. The Act is already underpinned by principles requiring councils to conduct their business in an open, transparent, financially prudent and accountable manner. Other legislation, and financial reporting standards, augment these principles and govern contracts between councils or council controlled organisations (CCOs) and the private sector. For example, the Local Authorities (Members' Interests) Act 1968 restricts the involvement of elected members in both contracting and voting. Anyone seeking additional information about contracts can request this under the Local Government Official Information and Meetings Act 1987. Additionally, the Auditor-General provides an independent assurance of local government and, under the Public Audit Act 2001, can inquire into any matter concerning financial, accountability, or governance issues.⁸
61. It is understood that the concept behind the petition was to summarise contract details – contractor's name, contract length, value, and general scope – rather than exhaustive information. Nevertheless, work to develop systems that record and report on contracts, and to routinely collate and audit this information, could be significant and costly.
62. Practical issues, and concerns about commercial sensitivity, might also be difficult to overcome. For example, requirements to publish contract terms, scope and values, could raise concerns over the release of potentially commercially sensitive information, and may contradict existing legal provisions that enable information to be withheld. In addition, some contracts do not provide a final cost – the figures may be subject to change (being finalised on delivery, for example), or are based on unit costs without identifying the number of units. Other contracts run for several years and may not specify the annual costs. This can further complicate the recording of details in annual reports.
63. The Department is not aware of any strong evidence of inappropriate contracting by councils or CCOs that would justify a significant, and potentially costly, move away from current law and practice. The benefits of implementing this proposal do not appear to outweigh the costs. Therefore, this is not a preferred option.

⁸ Other safeguards are provided in the Financial Reporting Act 1993 and the Public Records Act 2005.

Service performance auditing

Background

64. The Royal Commission on Auckland Governance (the Royal Commission) recommended creation of a statutory position of Auckland service performance auditor (ASPA),⁹ with responsibility to:
- review the adequacy and relevance of CCO performance targets;
 - protect and advocate for consumer interests in respect of the reliability and affordability of council services; and
 - undertake three-yearly efficiency and effectiveness reviews of Watercare Services Ltd.
65. The Royal Commission's report proposed the ASPA would be appointed by the Auckland Council on the recommendation of the Chair of the Commerce Commission and the Auditor-General. It suggested that the ASPA be located in the offices of a regulatory body such as the Commerce Commission.
66. The Royal Commission saw the ASPA having a role that extended further than the Auditor-General's. The Commission considered the Auditor-General was limited to system issues; for example, the adequacy and relevance of reported performance measures. The Royal Commission proposed that the ASPA would focus on the level of performance itself with particular attention to CCOs that are monopoly service providers.
67. On 27 April 2009, Cabinet noted the Commission's recommendation about establishing the ASPA, and noted that this should be considered in light of work to improve the transparency, accountability and financial management of local government in a New Zealand-wide context. It invited the Minister of Local Government to report back to the Economic Growth and Infrastructure Committee on this recommendation [CAB Min (09) 14/2 refers].
68. In considering this recommendation, three primary issues need to be addressed.
- Is the situation in Auckland unique, or do the same issues apply to local government nationally?
 - Does the degree of oversight proposed undermine local democracy and accountability?
 - Are there other methods by which this oversight can be achieved?

These are discussed below.

Is the situation in Auckland unique?

69. Clearly the Auckland Council will be large but proportionately its role in the Auckland community will not be substantially greater than the role of other councils in their respective communities. There are two bases that

⁹ Royal Commission on Auckland Governance (2009), *Auckland Governance Report*, recommendation 32G pages 40-41.

may distinguish Auckland from the remainder of New Zealand. The first is that the performance of Auckland is so important to the national economy that further oversight is warranted. However, that would imply some accountability of the Auckland Council to central government, while the ASPA is designed to enhance accountability to the Auckland public.

70. The second basis is that the Auckland Council will be unique in that at least two of its major expenditure areas – water and transport – will be delivered by CCOs. The decisions of these two Auckland CCOs will help shape Auckland. In addition they have natural monopoly characteristics and it is likely Watercare will be charging users. The Royal Commission’s concerns about Watercare’s monopoly risks led it to recommend specific responsibilities for the ASPA to have regulatory oversight of Watercare, including the power to require information disclosure.

Does the degree of oversight proposed undermine local democracy and accountability?

71. The Act rests on the principle that councils are democratically accountable to their communities. Limitations on the roles of regulatory agents such as the Ombudsman and the Auditor-General exist so that they do not undermine that accountability. The proposed responsibilities of the ASPA are reporting responsibilities only – the Commission explicitly rules out the ASPA having a role in dealing with individual complaints and grievances. However, to form judgements on *whether the Auckland Council is performing adequately in providing high-quality services in a cost effective way* involves a significant risk that the ASPA will end up judging political decisions of the Auckland Council. This is because questions of service quality and cost-effectiveness are at the heart of local authority political decision-making.

Are there other methods by which this oversight can be achieved?

72. The Auckland Council will be of a size that it can implement a range of monitoring and performance evaluation arrangements. For local services, local boards will have a responsibility to monitor delivery of services to their communities. In addition, an organisation of the size of the Auckland Council will necessarily need to establish formal responsibilities for reviewing its effectiveness and efficiency.
73. Also, the Royal Commission may have under-estimated the potential for the Auditor-General to investigate the performance of the Auckland Council. Section 16(1)(a) of the Public Audit Act 2001 explicitly authorises the Auditor-General to examine at any time *the extent to which a public entity is carrying out its activities effectively and efficiently*. The main issue here relates to the priority the Auditor-General assigns to reviewing the Auckland Council compared to other public sector entities given the resources she has available.
74. The scale of the Auckland Council may warrant the creation of mechanisms to act as a check on the council in the same way that some of the Parliamentary offices act as a check on executive government.

Reliance on systems operating within the Auckland Council may not provide the degree of independence necessary to give the public sufficient assurance as to the efficiency and effectiveness of the council's operation. This could involve, for example, a statutory authority for the council to appoint an internal auditor independently of the chief executive and mayoral office and reporting directly to the council.

Conclusion

75. In the context of local government transparency, accountability and financial management, a service performance auditor is not warranted for the whole local government sector. However, CCOs will play a greater role in service delivery for the Auckland Council than for any other council in the country. The Department of Internal Affairs is undertaking further work on whether the CCO monitoring framework for the Auckland Council needs to be strengthened. The results of this work will be included in a later paper to the Auckland Governance Reforms Committee.

PREFERRED OPTIONS

76. Described below are the preferred options for addressing the principles and objectives outlined earlier. Although each can be considered on its own merits, many of the options would, if implemented, reinforce each other and form a collective package. Some options also have variations that respond to the objectives differently.

'Plain English' financial reporting

77. Most ratepayers do not understand the principles of accrual accounting and therefore find council accounts incomprehensible. From the ratepayer's viewpoint, the most useful way to think about council finances is to focus on funding, using a stocks and flows approach. The stock of funds is the amount of funds a council has invested or borrowed, and the flow is those transactions that either result in funds being provided to or expended by the council.
78. Two variations for how to provide this information were considered. The first was to refine the cash flow statements that councils have to provide under current generally accepted accounting practice (GAAP); the second was to develop a funding impact statement uniquely specified for local government.
79. A refined cash flow statement was rejected for three reasons. Firstly, the cash flow statement is designed to help users assess the liquidity risk of the reporting entity. This is not the same purpose as a stocks and flows statement and results in information being presented in a way that would not meet users' needs. Secondly, some transactions in a cash flow statement are classified in ways that would not meet users' needs for local government accounts. Thirdly, there are major technical difficulties in presenting a cash flow statement for individual council activities.
80. The preferred approach is to develop a purpose driven Funding Impact Statement for local government. This could explain both overall council

funding and the funding of individual activities. This approach builds on existing good practice within the sector.

81. The benefit of the approach is that it will generate information that is targeted to users' needs. This will enhance council transparency and accountability. The cost of this approach is that it will require subsidiary regulation to be prepared and implemented. This cost can be minimised by working with relevant stakeholders to achieve a partially self-regulatory approach.
82. A further part of the preferred approach is to develop and apply rules about the disclosure of reserve funds (funds set aside for particular purposes) and internal borrowing. Internal borrowing is the practice of councils utilising reserve funds temporarily for another purpose, rather than borrowing from external sources. These types of transactions and funding practices are not common in the private sector and therefore GAAP does not contain disclosure rules applicable to them. The Act could be amended to require councils to disclose additional information about reserve funds and internal loans. This would enable the public to see what funds their council is holding, and for what purpose, and where internal loans have been applied to particular activities.

Inter-council comparisons

Consistent financial information

83. Organisations operating in non-competitive environments face lower pressures to be efficient than those that must compete to survive. In the absence of competitive pressure, the ability to compare councils is important for ratepayers to ask intelligent questions about their council's performance. At present, meaningful financial comparisons between councils are very difficult. This is because there is no standard presentation of the financial information councils must report. For example, councils present rates income in at least three different ways – general rates only; general rates plus targeted rates; and general rates and targeted rates excluding metered water charges.
84. The same problem exists to some degree in the private sector. In that context, financial analysts act to solve the problem by providing information that meets the needs of potential investors or lenders to companies. However, there is a limited market for such financial analysis of local authority accounts.
85. At a whole of council level, financial disclosure would be improved if rules were applied that regulated the presentation of accounting information. These rules would have to be consistent with GAAP.
86. The benefits of such rules would be enhanced transparency of local government finances. In turn, this would allow ratepayers to ask better questions, which would enhance council accountability.
87. The cost of this approach is the need for further regulation to develop disclosure rules. This cost can be minimised by combining the rule-making process for this purpose with other rule-making processes

required to implement these proposals, as well as by allowing adequate lead-in times.

88. Achieving improvements through good practice alone was also considered. However, these reporting practices have been in existence since 1990 and, despite efforts to provide good practice and encourage consistency, there is still variation across the sector. Therefore, it is considered unlikely that non-regulatory approaches will achieve the level of consistency aspired to.

Standardised non-financial performance measurement information for major council services

89. A related proposal is to further enhance transparency with comparative non-financial data on levels of service. Providing this kind of standardised data, often referred to as benchmarking, could help to inform ratepayers about what they are getting for their money.
90. It is proposed that the Act provide for the development of a system of performance measurement for council services. This would be mandatory for the essential infrastructure services that have the greatest impact on councils' finances – roading, water supply, sewage treatment and disposal, storm water drainage, and flood protection. Performance targets for the mandatory measures would be included in councils' long-term council community plans, annual plans, and annual reports. Specific targets would be set by each council. No targets would be specified in the measurement system. Quality assurance would be achieved through auditing annual reports.
91. Responsibility for developing the measurement systems will lie with the Secretary for Local Government. The Secretary will be required to consult with relevant stakeholders in preparing the systems. This approach is similar to the approach for developing rating valuation rules contained in the Rating Valuations Act 1988. In practice it is likely that the Secretary would contract a third party to prepare the systems.
92. Allocating this responsibility to the Secretary recognises that the task of preparing measurement systems is quite technical in nature. It is also intended to minimise concerns that the systems could become an indirect method for government to dictate performance targets to local government.
93. Alternative system preparers to the Secretary were considered. These were Standards New Zealand (SNZ), the Minister of Local Government, and the Local Government Commission.
94. SNZ is a user-funded autonomous Crown entity that specialises in developing standards for a variety of purposes, using a consensus-based approach. It is required by the Standards Act 1988 to ensure that decisions are supported by those with an interest in the standard; therefore, local government and other interested agencies would be heavily involved in this process. However, situations in which Crown entities are delegated regulation-making powers are quite rare as the accountability to Parliament is weaker than that of the Executive. Crown entities with significant regulatory roles usually enforce regulations set by

the Executive or Parliament. Nor would allocating this function to SNZ achieve independence from the Executive in practice. This is because SNZ may not amend, revise, revoke or replace any standard cited in a regulation without the approval of the Minister responsible for that regulation.

95. Having the Minister prepare the measurement systems is likely to arouse strong fears within local government of the Government decreasing local autonomy through the system setting process.
96. The Local Government Commission's role has been to deal with local authority structures and representation, although section 30 of the Act authorises the Commission to promote good practice relating to local government. Giving this role to the Commission would require consideration of the skills needed by Commissioners and could create a conflict in workload in preparing the first measurement systems and in carrying out representation reviews for the 2013 local authority elections.
97. DIA has estimated the total cost of preparing five standards in the order of \$1.26 million. This includes the cost of contracting an entity (or entities) to prepare the standards, costs of procurement and contract supervision, independent peer review of the contractor's work and consultation with interested parties. Divided among 78 councils, this amounts to less than \$3,500 per council per system on average. Some councils may also be required to gather data they have not previously collected, which could have additional costs for those councils.
98. It is suggested that there be a longer lead time for implementing this proposal, to allow standards to be developed and give councils time to set up suitable data collection systems.

Improving disclosure of asset management information

99. Councils are major providers of infrastructure services. In 2008, for example, expenditure on roading, water supply, and wastewater treatment and disposal accounted for 38 per cent of council operating expenditure. Infrastructure costs have risen at a rate more than consumer price inflation and have been a major cause of rate increases.
100. Despite this, the quality of publicly available information about infrastructure services is variable and may not meet ratepayers' needs. Current provisions in the Act are not helpful in this respect. Many of the requirements to disclose asset information in LTCCPs are process based, relating to *how* things will be done, rather than *what* needs to be done and how much this will cost.
101. Providing good information about these services and investment needed to maintain or improve the standard of their delivery is important. Good information will help focus debate on these core services, and will improve transparency and accountability for service delivery.
102. It is proposed, therefore, to introduce requirements for LTCCPs, annual plans, and annual reports to clearly disclose planned and actual capital investment in infrastructure assets. This would be broken down to show investment to meet additional demand for services, investment to

improve service standards, and investment to replace existing assets. The Act will also be amended to require the Auditor-General to report separately on compliance with asset management disclosure rules.

103. In addition, it is proposed to standardise some of the groups of activities used and reported by councils, so that these are disclosed separately in plans and reports. The activities would be those with high costs and high asset bases – water supply, sewerage treatment and disposal, stormwater drainage, flood protection and roading.
104. The benefits of these proposals are that they will ensure clear and consistent information is presented to the public about both the financial and non-financial issues facing the council in respect of these services. This should help to focus debate on the standards of core services being provided. This is information that councils should hold already so there should not be additional costs in collecting it. The cost of the proposal lies in preparing the information for publication and any subsequent reporting that is required.

Pre-election report

105. A pre-election report (PER) would bring together information about a council's past financial and asset management and information about issues the council will confront in future years.
106. Information about past management would consolidate, in one place, details that are scattered throughout a number of council reports. This would make the information more accessible to potential voters, thus improving the accountability of the council for the decisions made over its term.
107. The PER would include unaudited financial information for the financial year completed immediately prior to the election. It would not be practical to include audited information because of the short period between the close of the financial year and the publication of the PER. (For example, nominations for 2010 local elections close on 20 August 2010, but the cut off for auditing the previous year's annual report is 31 October 2010, after the election.)
108. Information about future decisions the council has to make would help provide a context for local elections. It would encourage candidates to express views about those issues, thereby allowing voters to elect representatives that best reflect their preferences.
109. The benefits of a PER lie in a better informed election with greater focus on issues and council performance. It is difficult to assess how readily voters, candidates and the media would respond to the publication of such a report.
110. To minimise compliance costs, all the information in the PER will be drawn from existing reports. As councils will be preparing their annual report at the same time, collating best estimate unaudited information for the year just closed should not be difficult.
111. Whether or not the costs outweigh the benefits depends on the value placed on a better informed election debate. That also turns, to a

significant degree, on how useful the voters and candidates find the information that has been generated.

Directing a focus on core services

112. Although many of the other proposals provide indirect incentives for councils to focus on core services, a more direct approach to this issue has also been considered.
113. Decisions about the role of councils within their general empowerment should continue to be made locally. However, there are services that members of the public generally accept as being a core role of local government, and which should be provided in a satisfactory manner before a council considers funding other activities. This broad agreement derives from the role local government has historically played in our society. These functions typically include provision of public goods, public transport services, public health and environmental services, culture, recreation and heritage, and regulatory responsibilities.
114. A focus on these services could be achieved by amending section 12 of the Act, which sets out councils' status and powers. It is proposed that a clause is added, requiring councils to have particular regard to the contribution to community well-being made by specific services, such as:
 - infrastructure (transport networks, water supply, sewage treatment and disposal, stormwater drainage, and flood protection works) and the purchase of public transport services;
 - solid waste collection and disposal services;
 - the mitigation of risk and protection of communities from natural hazards and disasters;
 - libraries, reserves and recreational activities;
 - the preservation/development of culture and heritage; and
 - the performance of regulatory responsibilities and other statutory duties.
115. There is a risk with this approach that description of core services does not keep up with the changing role of local government as society evolves. Some people may try to interpret the list literally, when it is meant to be indicative, which could result in litigation. Additionally, describing core services could restrain debate on future proposals to move particular local government functions to central government or the private sector.
116. In addition, section 14 of the Act sets out principles that guide local authority actions. It includes general principles of prudence and adoption of sound business practice but gives little guidance on management of council investments. This section could be enhanced with a principle requiring councils to consider risks and returns from investments. This would encourage councils to periodically reassess their equity investments.

Community outcomes process

117. Sections 91 and 92 of the Act require each council to facilitate a process for identifying community outcomes for the immediate and long-term future of their district/region, and to monitor and report on progress in achieving these outcomes. Although the outcomes are owned by communities, they are imported into council planning and decision-making processes and are intended to guide local priority-setting and resource allocation. Other organisations that are capable of influencing community outcomes should be identified, and agree to the process, if practicable.
118. While some councils and government agencies have found their involvement in community outcomes processes to be beneficial, others have expressed concerns about the costs and challenges associated with complying with the Act.¹⁰ Councils have noted, for example, that they (and their ratepayers) are expected to pay for the process, and monitor and report on outcomes that go beyond their service delivery roles. They have also reported that the engagement of government agencies in formulating and achieving outcomes has been inconsistent.
119. Several options for the future of the community outcomes process were considered, to address concerns and in the context that 'councils should focus on core services'. The preferred option is to put the focus on the outcomes that *councils* are aiming to achieve for the well-being of their communities. This can be achieved by amending the definition of community outcomes in the Act.
120. With this option, councils that want to coordinate community debates about, and solutions to, particular issues can continue to do so. However, they will not be directed to do this by central government, using a separate process. Instead, it is proposed that the processes set out in sections 91 and 92 will be removed and the LTCCP will become the main vehicle for debating outcomes.
121. The benefit of this option is that it should reduce compliance costs as councils will no longer be required to run a major community consultation exercise every six years, or to produce three-yearly monitoring reports. Moreover, by aligning community debates, discussions about local priorities and the affordability of proposals can be held in the context of council planning and resource allocation. This should enable participants to consider the costs and trade-offs involved in achieving outcomes and delivering council services.
122. This option may have a negative impact on those councils that use the legislative mandate provided by sections 91 and 92 to persuade other agencies to work in partnership to address local issues. However, the intention is not to preclude councils from working with other organisations to address particular issues and achieve wider outcomes, if they find value in this.

¹⁰ Information on concerns about, and benefits of, community outcomes processes was gathered from local government case studies and other research. This included interviews with 14 councils carried out as part of the Local Government Commission's review of the Act, and nine case studies prepared for the Department's Local Government Information Series.

123. Other options that were considered involved maintaining or modifying the status quo. These are not preferred options because they are inconsistent with Government goals and with the objectives of this review. Councils would still be required to pay for identification, monitoring and reporting processes on outcomes that go beyond their service delivery roles. This would also mean that discussions about community priorities are being held separately from the normal planning and decision-making vehicle, the LTCCP.
124. Repealing the Act's community outcomes provisions without merging the process into the LTCCP was also considered. However, this would not encourage councils to engage in debates about outcomes with their communities, or explain links between the outcomes being sought and proposals to achieve them.

Requiring councils to include a financial strategy in their LTCCP

125. Although the Act requires councils to have a number of funding and financing policies, it does not require councils to synthesize these into an overall financial strategy. The Auditor-General was critical of councils' 2006 LTCCPs for failing to clearly articulate their financial strategies. Good practice guidance to the sector has encouraged councils to include such strategies in their 2009 LTCCPs, but the quality of the response has been variable.
126. A high level financial strategy would encourage a strategic approach, and help each council and its ratepayers to debate and resolve the key financial and service delivery trade-offs the council must make. It would need to be informed by the council's overall strategy for its district; otherwise, there is a risk of the financial strategy being formulated without a wider sense of purpose or direction.
127. Specifically, a financial strategy would identify factors expected to have significant financial impacts on the council. It would contain a statement of the council's quantified limits for rates, rate increases and debt, as well as an assessment of its ability to provide adequate levels of service for the present and foreseeable future within those limits. It would also state the objectives for holding council investments and the quantified targets for returns on material investments.
128. The benefits of the proposal are that it would help councils to prioritise expenditure, and make them more accountable and transparent to ratepayers and citizens. This would be achieved, firstly, by stating explicitly what may be already implicit in councils' plans. Secondly, explicit targets would provide a clear measure for ratepayers to subsequently measure councils' performance. It would be a tool to implement the objective that councils operate within a defined fiscal envelope.
129. The costs of the proposal are relatively low. The information required to prepare a strategy is already gathered by councils when preparing their LTCCP. Preparing the strategy itself should be within the capability of each council and its advisors.

Removal of descriptive and operational material from the LTCCP

130. According to section 93(6) of the Act, the purpose of the LTCCP is to:
- (a) describe the activities of the local authority; and*
 - (b) describe the community outcomes of the local authority's district or region; and*
 - (c) provide integrated decision-making and co-ordination of the resources of the local authority; and*
 - (d) provide a long-term focus for the decisions and activities of the local authority; and*
 - (e) provide a basis for accountability of the local authority to the community; and*
 - (f) provide an opportunity for participation by the public in decision-making processes on activities to be undertaken by the local authority.*
131. LTCCPs are usually large, multi-volume publications that are expensive and time consuming to prepare. In addition to fulfilling the purpose outlined above, they are required to include summaries of other plans and policies, many of which are descriptive or operational in nature.
132. To make LTCCPs more accessible to the public, councils must prepare a summary of the major matters contained in the plan and use this document as the basis for consultation. This raises questions about whether the other material needs to be included at all, and if it diverts attention away from the more strategic purpose of the LTCCP.
133. With this option, the Act would be amended to remove the following descriptive and operational material from the LTCCP:
- waste management and minimisation plans, or summaries, as the case may be (as these are already made available to the public);
 - rates remission and postponement policies;
 - development contribution and financial contribution policies; and
 - investment policies and liability management policies (though some of the elements in them will be included in the proposed financial strategy described above).
134. Removing this material should help to make the LTCCP a shorter, more strategically focused document. It should also help to reduce preparation and auditing costs, particularly in relation to policies that can only be amended as part of an amendment to the LTCCP.
135. It would be beneficial, though, if the public is still given the opportunity to comment on some of these policies. It is suggested, therefore, that councils are required to carry out periodic reviews of rates remission and postponement policies, and development and financial contribution policies. This would be done using the special consultative procedure.

Non-financial performance reporting

136. The Act requires LTCCPs to contain statements of the intended level of service provision for each group of activities, including *the performance*

*targets and other measures by which actual levels of service provision may meaningfully be assessed.*¹¹ The auditor's report on the LTCCP must contain an opinion of the extent to which these measures provide an appropriate framework for assessment. In annual reports, councils must include an audited statement setting out *a comparison between the actual levels of service provision ... and the intended levels of service provision for each group of activities.*¹²

137. Although considerable attention is currently given by councils to the measurement and reporting of service performance information, it is not clear that this provides value for money to ratepayers. Public submissions on LTCCPs rarely make reference to specific performance measures,¹³ and there appears to be little interest in council annual reports.¹⁴
138. With this option, the system would be streamlined and focused on: major issues; changes to levels of service provision; changes to the cost of services, and the reasons for this; mandatory benchmark performance measures/targets; and other significant performance measures/targets. Councils will be able to determine for themselves if additional performance information is required.
139. There are several potential benefits associated with making these changes. They will help to focus councils' LTCCPs and annual reports on strategic issues and matters of concern to ratepayers (such as proposed changes in service levels and increased costs). There should also be a reduction in the costs associated with preparing LTCCPs and annual reports, and with monitoring performance.

Referendums

140. As noted earlier, a wide range of possible options for increasing the use of referendums were considered. The preferred option is to amend the Act to require councils to hold non-binding referendums outlining three scenarios for their rates and debt levels over the coming years. These referendums could occur during local elections (with a three year forecast), with the LTCCP (with a 10 year forecast), or at both times. They would cover each council's preferred scenario, plus a 'higher' and a 'lower' scenario. Voters would be asked which scenario they prefer.
141. With this option, voters will be invited to trade off different levels of service and funding mechanisms. It is important, therefore, that they

¹¹ Part 1 of Schedule 10, clause 2(2)(a)

¹² Part 3 of Schedule 10, clause 15(e)(i)

¹³ Research and analysis undertaken by the Department of 2009/19 LTCCP submissions from five councils showed there were very few references to performance management information or levels of services as specified in the LTCCP. For the five councils studied, the number of points raised on performance measures varied from 3 to 9, which equated to less than 0.5% of all submission points received. These findings are supported by an informal survey of councils undertaken by SOLGM. This showed that while many submissions deal with levels of service, few are about specific performance measures (for example, only 3 of the 4,634 submissions to Tasman District Council, and 2 of 1,395 to Tauranga City Council).

¹⁴ For example, in 2005 Invercargill City Council was unable to produce an audited annual report for 2004/5 until February 2008 – over two years after the statutory deadlines. Only one ratepayer wrote to the then Minister of Local Government to express concern about this situation.

have sufficient information to make a considered choice and are aware of the potential implications. It is proposed that councils be required to send voters the following details for each scenario:

- forecasts of rates and debt levels;
- a comparison of the changes in service that would occur; and
- comment on the adequacy of infrastructure asset renewal.

142. This option allows referendums to play a bigger part in council decision-making, by providing ratepayers with a means to influence decisions about the overall size of their council’s budget and future rates and debt increases. This supplements their ability to vote for particular people, with an opportunity to vote for a policy programme. It may also increase interest and engagement in council business and the political process.

143. Although the Act already contains consultation provisions, these do not necessarily enable councils to obtain a representative picture of community views. The special consultative procedure, for example, is only feasible if a relatively small percentage of the local population takes part; otherwise, the submission process would be impracticable.¹⁵ Referendums provide a mechanism for councils to make themselves aware of the views of entire communities.

144. There are costs associated with referendums. Firstly, there are administrative costs of preparing, posting, and processing voting papers. These are likely to be lower for referendums held as part of local elections as the processes could be combined. Secondly, there will be costs involved in developing the options on which the referendum will be based and in presenting this in an easily understood format to voters. Doing this could be challenging for many councils, particularly when referendums fall outside of the long-term planning cycle.

145. The table below sets out indicative costs for a one-off referendum.¹⁶ These are administrative and postal expenses, as it is difficult to predict how much the information packs will cost.

Electors	Costs per Elector	Total Cost
10,000	\$3.00	\$30,000
100,000	\$1.75	\$175,000
300,000	\$1.15	\$345,000

Nationally, the cost to councils is estimated to be in the range of \$4.5 and \$5.5 million. This excludes the cost of developing the options to be considered.

146. An additional concern is that this system might encourage perverse behaviour as councils try to minimise the impact of the referendums. They could, for example, present three scenarios with little variation.

¹⁵ This process requires councils to hear public submissions. If, for example, 10 per cent of a district of 40,000 wanted to take part, at 10 minutes per person the public hearings would last over 13 weeks.

¹⁶ Estimate of costs from a provider of election services to local authorities.

Alternatively, two of the scenarios could be so extreme that they are effectively meaningless. Furthermore, the fact that the referendums are non-binding could mean councils ignore the results.¹⁷ However, the public nature of the referendums should, in itself, be sufficient to ensure that councils provide realistic scenarios and adhere to the results. Not doing so would create a negative impression of the council, which might become the focus of local debate and jeopardise the position of elected members.

147. A further debate is about when these referendums will be held – during local authority elections (with a three year forecast), with the LTCCP (with a 10 year forecast), or at both times. There are pros and cons associated with all three options.
148. Referendums with the election may have lower administrative costs and help to promote election debate, but they would fall outside of the planning and budgeting cycle. Effectively, this could mean there is a significant time period between individuals casting their vote for a referendum scenario and them seeing the consequences, which could result in disenchantment with the process and the council. (For example, it would take approximately eight months before the council could set new rates, and nine to ten months before this affected rates bills.)
149. Conversely, referendums with the LTCCP are closer to budget setting and likely to be more influential on actual decision-making. While the cost of developing the scenarios is likely to be lower, there would be extra costs of holding a separate ballot.
150. Having a referendum at both times has the benefits associated with each option, but would obviously cost more. In addition, having a referendum every 18 months could mean there is a risk of voter fatigue. It is possible that, over time, this could result in decreasing turnout and the public feeling less compelled to take an interest in the referendum. (This might be a particular risk if the electorate does not see a direct relationship between their vote and council actions.)
151. Ideally the first referendum would be held with the 2010 local authority elections, but this could be difficult as the timeframes are tight. If, for example, the first referendum was to be held with the elections in October 2010, and the Bill was passed in April 2010, councils would have a short transition time. In practical terms, this would give them about two months to introduce the new system. (The deadline for public notice of this election is 23 July 2010 and the referendum would have to be included with this.) Preparing the information packs, with sufficient time for voters to receive and digest their contents, could be difficult, especially for smaller councils. There could be capacity/resourcing issues and other priorities, such as preparing annual plans. There is a risk that councils will not be able to develop reasonable options for voter consideration at this time.

¹⁷ Binding referendums are impracticable because there may be circumstances under which previous plans need to be reconsidered and the result cannot be implemented (such as natural disasters and significant changes to the economy).

152. It is proposed, therefore, that the first referendum be held in conjunction with the 2012 LTCCP and the first election referendum be held with the 2013 local authority elections.
153. In addition, the need to pass a third Bill to implement the Auckland Council provides an opportunity to legislate for a pilot referendum in Auckland in 2010. This would require the Auckland Transition Agency (ATA) to prepare the referendum and supporting material.
154. Apart from the general considerations set out previously, the following advantages and disadvantages arise from this proposal. Advantages are that:
- in the absence of any specific effort to the contrary, the first Auckland election will probably be conducted without authoritative information about the overall financial position of the Auckland Council and the issues it faces. Having a referendum will fill this gap;
 - a referendum will give the incoming Auckland Council a guide to Auckland ratepayers' expectations of the new council; and
 - conducting a referendum in Auckland will provide an opportunity for councils conducting their first referendum in 2012 to learn from the Auckland experience.

Disadvantages are:

- preparing a referendum may distract the ATA from its core responsibilities of establishing organisational structures and capabilities;
- with the time and resources available, the ATA may not be able to carry out sufficient investigation to prepare robust alternatives for consideration;
- the effects of developing a unified rating system for Auckland are likely to be as significant for many Auckland ratepayers as the absolute rating levels required to run the council. Holding a referendum may create misleading expectations for some ratepayers as to the effect of the reorganisation on their rates; and
- the fact that an unelected body is making political judgements about possible future scenarios for Auckland may detract from the legitimacy of the proposals in the eyes of some voters.

Minor amendments to the Act

155. It is proposed that several minor changes are made to the Act. These are primarily aimed at reducing regulatory burdens and compliance costs, and allowing resources to be used more productively. There should be few financial costs associated with making these changes. Safeguards contained elsewhere in the Act should prevent there being negative side effects.

Policies on partnerships with the private sector – repeal provisions

156. Section 107 of the Act requires councils to have a policy on partnerships with the private sector. This applies where the council proposes to

provide funding or other resources to any form of public-private partnership. In addition, the Act requires councils to have a policy on investments. Many public-private partnerships also fall within the scope of this policy.

157. As public-private partnerships are rare, for many councils preparing these policies is an unnecessary compliance exercise. It may also be difficult to develop an effective policy because they have little or no experience to guide them. It is proposed, therefore, to repeal these provisions.

Conditions applying to the sale or exchange of endowment land

158. Endowment land is land that has been donated to a council by the Crown or a private individual. Section 141(1)(b) of the Act requires councils to include proposals for the sale or exchange of endowment land in LTCCPs. If an unforeseen situation arises, a council must complete an audited amendment to its LTCCP to allow a sale or exchange to proceed.

159. It is proposed to repeal this requirement as it adds compliance costs for councils and is inconsistent with the strategic nature of the LTCCP. It is also largely unnecessary as there are other legislative duties that are likely to ensure formal consultation occurs on major proposals.

160. The other requirements in section 141 will remain, including notifying the donor of the land and allowing them to comment on the proposed sale or exchange.

Auditing LTCCP amendments

161. Under section 97 of the Act, certain decisions can only be taken if provided for in an LTCCP (or done through an audited LTCCP amendment). This applies to decisions about:

- significant alterations to the level of service of a significant activity (s.97(1)(a));
- transferring ownership or control of a strategic asset to or from the council (s.97(1)(b));
- the construction, replacement, or abandonment of a strategic asset (s.97(1)(c)); and
- a decision that will, directly or indirectly, significantly affect the capacity of the council, or the cost to the council, in relation to any activity identified in the LTCCP (s.97(1)(d)).

162. It is proposed to amend the Act so that sections 97(1)(c) and 97(1)(d) are removed. The former is, effectively, already covered by the provisions in 97(1)(a); the latter is vague and hard to comprehend.

163. A further requirement is that *any* amendment to a council's funding and financial policies must proceed through an audited LTCCP amendment. It is suggested that the Act is changed so that only a *significant* alteration would require an audited amendment.

164. These changes, along with removal of other descriptive and operational material (described earlier), will reduce the number of audited amendments made to LTCCPs. This will lower compliance costs for councils and allow more productive use of audit resources.

Decision-making requirements

165. Section 78(1) of the Act requires a local authority, when making a decision, to *give consideration to the views and preferences of persons likely to be affected by, or to have an interest in, the matter*. Section 78(2) specifies four distinct stages in the decision-making process where this must be done.

166. This provision has been identified by the Society of Local Government Managers (SOLGM) as creating confusion and encouraging risk averse councils to consult with the public on multiple occasions on the same issue. It has given rise to two High Court cases.¹⁸ These produced conflicting judgements, with one judge openly disagreeing with the decision of another.

167. It is proposed to repeal section 78(2), as this is an unnecessary addition to the principle already covered in section 78(1). This would leave the general duty on councils to consider the views of interested parties in decisions, but with discretion to decide how to do this, according to the circumstances.

168. This option reduces the risks to councils of legal challenges and the potentially high costs associated with these. It also removes an incentive to carry out repetitious and costly consultation exercises.

Consultation on change of mode of service delivery

169. Section 88 of the Act requires a local authority to carry out formal consultation if it wishes to transfer delivery of a significant activity from:

- the council to a CCO;
- the council to a not-for-profit organisation or private contractor; or
- a CCO to a not-for-profit organisation or private contractor.

170. This section is biased against using the private sector to deliver council services. If a council wishes to contract out a service, it may have to consult the public, but bringing services 'in-house' does not require consultation. Levelling the playing field between public and private delivery of council services could be achieved by requiring consultation on transfers to councils, but this is likely to increase compliance costs. Therefore, it is proposed to repeal this section.

Assessments of water and sanitary services

171. Section 125 of the Act requires territorial authorities to assess, from time to time, the provision of water and other sanitary services in their districts. Sections 126 to 129 prescribe the process to be used and information required in these assessments. Subclause 3(1)(a) of

¹⁸ Christchurch City Council v. Council of Social Services and Whakatane District Council v. Bay of Plenty Regional Council.

Schedule 10 requires that a summary of the most recent assessment must be included in the LTCCP.

172. These were new provisions in the 2002 Act. Water services include reticulated drinking water supplies, sewage treatment and disposal systems, and stormwater drainage systems.¹⁹ Other sanitary services are the provision of public conveniences, cemeteries and crematoriums.
173. It is proposed to remove sections 126 to 129, and subclause 3(1)(a) from the Act. Removing specific requirements relating to the process will provide flexibility by allowing councils to decide for themselves how to carry out the assessments. Removing summaries of the assessments from LTCCPs will help to make the LTCCP a more strategic document.

Funding of community boards

174. It is proposed to amend provisions in the Act relating to funding of community boards. Clause 39(1) of Schedule 7 states that community board expenses are to be met *out of the general revenues of the district*. The use of the term 'general revenues' has led to confusion, which needs to be resolved.
175. Some organisations have taken this term to mean general rates, and argue that a targeted rate cannot be used to meet community board costs. However, the Local Government Act 1974 defined 'general revenues' more broadly, as *all the funds received or receivable by a local authority, excluding loan money*. This definition was not carried forward into the 2002 Act, but may offer guidance on how to interpret this term.
176. The 2002 Act enables councils to make their own funding decisions, providing these are specified in Funding Impact Statements and then consulted on in their LTCCPs. The Local Government (Rating) Act 2002 empowers councils to set targeted rates.
177. In its review of the operation of the 2002 Act, the Local Government Commission recommended an amendment to *expressly preclude the levying of targeted rates for the purpose of funding community boards*.²⁰ However, the Department views this as impracticable because not all councils assess a general rate. Even if they did, it might be difficult to amend the Act to ensure that only general rates, levied across an entire district, fund community boards. Implementing this recommendation would also impede councils' ability to make their own funding decisions, in consultation with their ratepayers.
178. To resolve this matter, it is proposed that the words *out of the general revenue of the district* be omitted from clause 39(1) of Schedule 7 of the Act. This should not result in any additional compliance costs,

¹⁹ In its *Annual Review of Drinking-water Quality in New Zealand 2006/07*, the Ministry of Health recorded 700 separate local authority water supply schemes, 607 school supplies and 996 other supplies. The other supplies served 141,000 people (3.4 per cent of the population) and are unevenly distributed (for example, 118 are located in the Far North District Council). There is no central information source that allows private sewerage or stormwater schemes to be identified.

²⁰ Local Government Commission: *Review of the Local Government Act 2002 and the Local Electoral Act 2001*, page 119.

particularly as many councils already apply a targeted rate and will not be required to stop. It will also remove the need for councils to obtain legal advice on the legitimacy of this practice.

IMPLEMENTATION AND REVIEW

179. To remove compliance costs, it is suggested that the following proposals are addressed immediately:

- repeal of the community outcomes provisions;
- policy on partnerships with the private sector;
- sale or exchange of endowment land;
- auditing LTCCP amendments;
- decision-making requirements;
- consultation on changing mode of service delivery;
- community board funding; and
- remove rates remission and postponement policies and development contribution policies from the LTCCP.

180. Many of the proposals are linked to the LTCCP cycle. The next LTCCPs will be adopted no later than 30 June 2012. To allow councils time to put in place the necessary information systems and other changes, requirements for the form and content of LTCCPs should be in place by March 2011.

181. It is proposed that implementation of the matters listed below should occur through the 2012 LTCCPs:

- funding Impact Statements;
- disclosure of reserve funds;
- disclosure of internal loans;
- prescription of the form and definition of accounting disclosures in financial statements;
- disclosure of infrastructure activities as separate groups of activities;
- disclosure of planned and actual investment in infrastructure assets;
- standard groups of activities; and
- consistently classified financial information.

182. As noted earlier, the creation of a measurement system for non-financial performance information is complex and requires a longer lead time. A deadline of 30 June 2014 for implementing this system is proposed.

183. Other implementation details are proposed below.

- Revised audit reporting requirements on asset management disclosure – June 2011 (to take effect for the 1 June 2010 to 30 June 2011 financial year).

- Referendum outlining three scenarios for rates and debt – the first referendum will be held in conjunction with the 2012 LTCCP and the first election referendum be held with the 2013 local authority elections. There will be a pilot referendum in 2010 for the Auckland Council.
- Plain English financials – July 2012. (This proposal has three components: a balanced funding impact statement (FIS), and disclosure requirements for reserves and internal loans. The FIS should be integrated with the 2012 LTCCP to reduce compliance costs. The other two elements could occur from 1 July 2011, but there is merit in these changes occurring at the same time.)
- Pre-election reports – to start with the 2013 local authority elections.

CONSULTATION

184. Three discussion documents were prepared, covering the main elements of the review:

- improving the overall financial management system used by local government, and the role and content of the LTCCP;
- the future of the community outcomes process; and
- the use of polls and referendums in financial decision-making.

185. These papers were circulated, for comment, to the following government departments and other organisations:

Ministry of Social Development (MSD); Ministry of Health; Ministry of Justice; Te Puni Kōkiri; Ministry of Agriculture and Forestry; the Treasury; Ministry of Transport; Department of Building and Housing; Ministry for the Environment; Ministry for Culture and Heritage; Ministry of Education; Ministry of Economic Development; Inland Revenue Department; Statistics New Zealand; Ministry of Youth Development; National Library of New Zealand; Ministry of Pacific Island Affairs; Department of the Prime Minister and Cabinet; Sport and Recreation New Zealand; Corrections Department; New Zealand Police; Ministry of Women's Affairs; Office of the Auditor-General (OAG); Society of Local Government Managers (SOLGM); Local Government New Zealand (LGNZ); Auckland Chamber of Commerce; Local Government Forum; and Grey Power.

186. Detailed responses were received from: Ministry of Justice; MSD; Te Puni Kōkiri (TPK); Department of Building and Housing (DBH); Ministry of Education; OAG; SOLGM; LGNZ; Local Government Forum; and Grey Power.

187. In addition, discussions were held with Treasury, Ministry of Health, Sport and Recreation New Zealand, and Statistics New Zealand. The Ministry of Economic Development facilitated a presentation to the Small Business Advisory Group. Several other government departments did not comment on the documents, but expressed an interest in receiving future papers.

188. Proposals relating to other minor changes to the Act were not included in these discussion papers. These are relatively small amendments,

primarily designed to advance the Government's goals of reducing regulatory and compliance demands, or to resolve interpretation issues. Some of these points were discussed in meetings with the OAG, LGNZ and SOLGM. Other organisations were able to comment when the draft Cabinet papers were circulated.

Feedback on improving financial management discussion document

189. This paper covered the majority of the options considered in the review. Detailed, often technical, feedback was received from the OAG, SOLGM, and the Local Government Forum. Government departments, however, made few comments and did not raise any significant concerns.
190. OAG saw merit in a number of the suggestions in this paper, such as Plain English financials and improved use of funding impact statements. However, it suggested a reconsideration of proposals relating to LTCCP audits and the possible modifications of the nature of the audit. For example, it was not thought to be feasible to shift the timing of LTCCP preparation to the first year of a council's triennium. These proposals were changed or discounted in response to this feedback.
191. SOLGM welcomed the intent of the review – a more strategic LTCCP and reduced compliance costs – but was uncertain whether all of the proposals in the discussion paper would deliver either of these. For example, it was unconvinced by the Prefu (now PER) and mandatory statements of funding flows, and thought that Plain English financials could be achieved through additional good practice guidance to the sector. It suggested that there should be a risk-based approach to auditing LTCCPs.
192. The Local Government Forum and Grey Power were generally supportive of many of the suggestions in the paper, such as fiscal strategies, Plain English financials, and a tool for inter-council comparisons. They agreed that many of the policies currently included in LTCCPs could be removed. The Forum thought it was important for LTCCPs to be audited, but Grey Power supported lowering audit standards and having reviews instead.

Feedback on community outcomes discussion document

193. The responses from government departments tended to focus on this paper. However, of all the departments contacted, only two – MSD and Justice – expressed a strong preference for retaining mandatory requirements relating to community outcomes.
194. Both MSD and Justice favoured retaining the community outcomes process, largely because they have worked with councils to address issues arising from this process and found this to be beneficial. Community outcomes are viewed as an important vehicle for local collaboration to resolve complex issues. MSD warned that removing the requirement for councils to facilitate the identification and monitoring processes will reduce other organisations' commitment to these outcomes.

195. However, MSD and Justice acknowledged the procedural and capability issues raised by local authorities. They supported further consideration of ways to improve the efficiency and effectiveness of the community outcomes process, without removing it from the Act entirely.
196. LGNZ's feedback was also broadly along these lines, suggesting that improvements might be made through further good practice, efforts to incentivise the engagement of other organisations, and removing the requirement for councils to produce three-yearly monitoring reports.
197. SOLGM contended that central government participation in the community outcomes process has been mixed. Although there have been some frequent and useful contributors (such as MSD), assistance with the delivery of outcomes has been limited and there has been relatively little new funding.
198. SOLGM also noted that there is little evidence that councils' roles have expanded through their involvement in community outcomes processes. Nevertheless, it supported removal of the mandatory requirements relating to this process, with the introduction of council outcomes instead.
199. The Local Government Forum and Grey Power both supported the repeal of the community outcomes requirements in the Act. Grey Power favoured the option that includes council outcomes, but noted that this will only work if councils are required to focus on core services and activities.
200. Concerns and suggestions were taken into account when arriving at the preferred option. However, it was considered unlikely that there would be a significant reduction in compliance costs if councils were still expected to lead community outcomes processes. Those organisations that find value in using community outcomes as a vehicle for joint working should not need a legislative mandate to carry on as these relationships have already been established.
201. The preferred option encourages councils to continue to focus on achieving outcomes, but those that they have the ability and resources to influence. This is intended to ensure that councils consider how well their services meet community needs and align with local priorities, in the context of their LTCCPs.

Feedback on referendums discussion document

202. This paper considered six options, ranging from the status quo to councils holding a binding referendum on rates increases or spending increases above a certain level. It also discussed the advantages and disadvantages of binding and non-binding referendums.
203. There were fewer comments on this paper than the other two, and only SOLGM, Grey Power and the Local Government Forum had particularly strong views.
204. Both Grey Power and the Local Government Forum expressed a preference for options involving binding referendums on significant proposals and/or on rates or spending increases.

205. SOLGM was not averse to changes that encourage councils to make more use of referendums, but on a voluntary basis. It strongly opposed any attempt to widen the scope of decisions where referendums are mandatory, on grounds of: cost; potential impact on sustainable delivery of service and consistency of policy direction; and impact on representative democracy.
206. Te Puni Kōkiri was concerned about how referendums can be structured to avoid the 'tyranny of the majority', and who should frame the questions asked in referendums. It noted that Māori are generally the minority population in council districts and their views may be marginalised in referendums. It also suggests that referendum questions can be worded to misrepresent issues or lead to inappropriate responses.
207. Department of Building and Housing suggested that non-binding referendums better reflect the representative role of elected members and this is a realistic option for ascertaining the community's voice under section 78 of the Act. It warned that binding referendums could significantly compromise long-term funding and growth management, unless contained within a statutory framework requiring maintenance of the service potential of existing assets.

Consultation on draft Cabinet papers

208. Four draft papers were circulated, for comment, to the following government departments and other organisations:

Ministry of Social Development; Ministry of Health; Ministry of Justice; Te Puni Kōkiri; Ministry of Agriculture and Forestry; the Treasury; Ministry of Transport; Department of Building and Housing; Ministry for the Environment; Ministry for Culture and Heritage; Ministry of Education; Ministry of Economic Development; Inland Revenue Department; Statistics New Zealand; Ministry of Youth Development; National Library of New Zealand; Ministry of Pacific Island Affairs; Department of the Prime Minister and Cabinet; Sport and Recreation New Zealand (SPARC); Corrections Department; New Zealand Police; Ministry of Women's Affairs; Office of the Auditor-General; Society of Local Government Managers; Local Government New Zealand; and the Auckland Transition Agency.
209. Comments were received from Ministries of Social Development (MSD), Culture and Heritage, Health, Transport, Economic Development (MED), and Justice, Department of Building and Housing, Ministry for the Environment, and Te Puni Kōkiri (TPK). LGNZ, SOLGM and OAG provided detailed feedback. Ministry of Education, SPARC, Inland Revenue, Corrections and National Library responded with no comment.
210. LGNZ and SOLGM consider that many of the proposals are matters of good practice, which should be addressed that way rather than through regulation. They oppose mandatory referendums and any attempt to define core services. They also have concerns about the practicality and

effectiveness of the pre-election report, and about auditing costs. They supported the minor changes proposed in the papers.

211. There were considerable discussions with the OAG about many of the proposals. Their primary concern is the policy objective of changing the scope of the LTCCP audit relating to service performance measurement and the impact on the audit scope in reality. They believe it is important to retain the audit function over the whole LTCCP.
212. The comments from MSD focus on proposals relating to community outcomes. Although they support proposals to incorporate community outcomes into LTCCPs, they are concerned that the proposed definition change could potentially lead to councils working in isolation, rather than with key partners. This could undermine stakeholder engagement and joint progress to achieve outcomes.
213. MED considers that the status quo could be improved by non-legislative means such as best practice. They do not support proposed mandatory referendums, suggesting that current electoral and consultation processes are sufficient to ensure community preferences are reflected. Referendums could overload voters with information, overly complicate and obscure elections, and have a negative impact on turnout rates.
214. TPK does not support the use of referendums unless specific programmes designed to give effect to Treaty of Waitangi obligations are protected.