Three Waters Reform
Detailed information pack to support submissions on the Water Services Entities Bill

Department of Internal Affairs
June 2022

Find out more at www.dia.govt.nz/Three-Waters-Reform-Programme
This pack provides detailed information on the following elements of the Three Waters reforms.

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Overview of Reform
Why are ‘three waters’ important

- Every New Zealander has a right to safe drinking water no matter where they live. We also expect strong and resilient stormwater and sewage services that enable communities to prosper and grow, while protecting the environment.

- Drinking water, wastewater and stormwater services make up the ‘three waters’. This three waters system is critical for the health and wellbeing of all New Zealanders.

- The performance of the three waters system is significant for upholding Te Mana o te Wai, the health of the environment, and the performance of the economy, building resilience to climate change and natural hazards, and unlocking housing and growth.

What is the current performance of three waters services?

- Every year, some 35,000 New Zealanders get sick from tap water that does not meet the international benchmark for clean drinking water.

- It is estimated that nationally an average of 20% of drinking water is lost on the way to households. This is more than the volume of water supplied by Hamilton, Rotorua, Dunedin and Christchurch City combined.

- Of the 321 wastewater treatment plants in the country, more than 100 are breaching consents and 60 require upgrades to meet minimum standards under the National Policy Statement for Freshwater Management.

- In 2021 there were 2,754 dry-weather wastewater overflows (i.e. blockages or system failures) and 1,159 wet-weather (i.e. rainfall events) overflows, and a further 355 from combined wastewater and stormwater networks. Out of 37 councils reviewed, there were 648 reported consent non-conformances in wastewater treatment plants.
What are the objectives of reform

The Government’s reforms aim to significantly improve the safety, quality, resilience, accessibility, and performance of three waters services, in a way that is affordable for New Zealanders now and into the future.

The purpose of the entities will be to provide safe, reliable and efficient water services. With high-level objectives including:

- Giving effect to Te Mana o Te Wai
- Delivering efficient and financially sustainable services
- Protecting and promoting public health and the environment
- Supporting and enabling housing and urban development
- Acting in the best interests of consumers and communities
- Managing water services in a sustainable and resilient manner

The Government also wants to ensure it delivers on Treaty-related obligations, including by improving outcomes for iwi/Māori in relation to three waters service delivery and upholding Te Mana o Te Wai. Integral to this is effective infrastructure delivery, underpinned by an efficient, high-performing, financially-sustainable, and transparent three waters system.
Why is the Government reforming three waters

• The Government’s reform proposals follow the Havelock North Drinking Water Inquiry, and many years of discussion with local government and iwi about the outcomes we expect of our three waters services and the challenges facing the provision of these services into the future.

• The future of water service delivery is changing regardless of the Government’s reforms. These are expensive services to provide. Upgrading our services to maintain infrastructure, meet health, community and environmental expectations and combat future challenges will see the costs of delivering these services increasing across the country.

• These future challenges include:
  o Adapting to climate change and building resilience to natural hazards
  o Lifting the standard of service delivery to meet health, environmental and cultural bottom lines
  o Responding to growth, housing and urban development needs
  o Maintaining and upgrading aging infrastructure
  o Operating within a constrained budget and workforce

• The national evidence base show that across New Zealand communities face an estimate cost of $120bn-$185bn over the next 30 to 40 years for investment in three waters infrastructure.

• Research shows that without reform, meeting community expectations to provide safe, reliable and clean water services will become increasingly unaffordable for some communities. Doing nothing will lead to further deterioration of services and be more costly for future generations to fix.
What has the Government proposed

• The three waters services in the ‘Three Waters Reforms’ are the council-owned infrastructure network and processes used to treat, transport, and discharge drinking water, wastewater and stormwater.

• The Government’s Three Waters Reforms are proposing to shift the current 67 council-owned and operated three waters services into four new publicly-owned entities to manage the future delivery of these services.

• These new entities will:
  o be publicly-owned by councils as the sole shareholders on behalf of communities, with strong protections against any future privatisation
  o have joint strategic direction and oversight through Regional Representative Groups (and sub-committees) made up of local government and mana whenua to ensure the entities are driven by community expectations and priorities
  o be financially separate from councils with a greater ability to borrow to fund long-term infrastructure
  o have independent competency-based boards that will run the day-to-day management of the entities and oversee the maintenance and renewal of this infrastructure.

• The Government has also proposed a new economic regulatory regime to protect consumer interests and drive efficient investment and performance.
Entity Structure

The entity structure is designed to have:

- Direct input from consumers and communities.
- Council ownership of the entities via shareholding.
- Joint strategic oversight by local government and mana whenua.
- A trio of regulators to ensure the right services are delivered to meet community needs and expectations.
- The right skillset to deliver water infrastructure and services.
What underlying problems do the reforms solve

- The Department’s analysis identified four root causes that contribute to persistent and systemic problems in the provision of three waters services.*

1. **Limited opportunities to achieve benefits of scale** – with most councils currently supplying services to less than 100,000 customers.

2. **Significant affordability challenges** – New Zealand’s three waters services are estimated to need investment of between $120bn to $185bn over the next 30+ years. Meeting these costs without reform will be challenging for most local authorities, with average household bills needing to increase significantly.

3. **Poor incentives for critical water infrastructure decisions** – Councils have a constrained ability to borrow to spread the high up-front costs of infrastructure over the lifetime of the service. Local authorities water infrastructure investment decisions must be considered against other council services.

4. **Lack of effective oversight and stewardship for the three waters sector** – There is a lack of transparency about the state of assets and performance of the three waters system that make it difficult for customers and communities to hold water services providers to account. This has enabled the current challenges to slowly accumulate over time.

- The Government considers that **comprehensive system-wide reform** is required to address these root causes **together**. Simply addressing one cause alone, such as changing funding arrangements or introducing stronger regulation, will add pressure on the system in different places. This is likely to exacerbate inequities, and will not achieve long-term outcomes for all New Zealanders.

*Discussed further in Options Analysis section of this pack.
Addressing the underlying problems

• The Government’s reforms proposals would create multi-regional entities with a singular focus on delivering safe, reliable and affordable water services to communities.

• These new entities will be able to achieve greater efficiencies than councils and will have greater ability to build capability to respond to future needs.

• This is achieved through a combination of factors including highly competent boards, strong management capability, greater workforce specialisation, greater capacity to invest in innovation/technology and modern systems and economies of scale in procurement.

• Local government and mana whenua will provide joint oversight and strategic direction which will set priorities for these entities and keep them to account.

• Communities and consumers will have existing and new mechanisms to engage directly with the entities.

• In addition, a stronger regulatory environment from Taumata Arowai, Regional Councils and the proposed economic regulator will drive efficiencies and transparency of performance and ensure these entities deliver the right services for the right price. National-level direction may also be set through the introduction of a Government Policy Statement.
What is outside the scope of the Government’s Three Waters Reforms

- **This is not about taking over operation of privately-owned supplies.** The Rural Supplies Technical Working Group released its report to Government which made 30 recommendations on ensuring rural communities’ unique drinking water needs are recognised in the Three Waters model and to understand how the proposed entities may support private supplies that currently receive assistance from councils to run their services. A link to the full report can be found here: [Rural Supplies Technical Working Group Report](#).

- The proposed entities will continue to operate within the resource management system – **the Three Waters Reforms will not alter the system for gaining resource consents, water allocations, or ownership and management of freshwater.** This is subject to work of the Ministry for the Environment you can read more about this work here: [Resource management system reform | Ministry for the Environment](#).

- **The Three Waters Reforms are not reforming the flood protection system** implemented mostly by Regional Councils. However, in taking a catchment-based approach, the reforms are considering the interplay of stormwater in this system.
A guide to co-governance in Three Waters

What is the governance structure for the new water services entities and how does co-governance fit into this?

- The Water Services Entities will have a two-tier governance structure comprising:
  - A regional representative group, and
  - A corporate skills-based board.

- The role of the regional representative group is to appoint the board, set performance expectations, sign-off on the entity’s strategic direction, and to monitor and hold the board to account. It’s an oversight role, to ensure the board understands and delivers on community expectations.

- To represent community expectations, the regional representative group will be made up of equal representatives of the local authority owners and mana whenua with interests in water services in the area.

- The board, on the other hand, develops the strategy, appoints the chief executive, monitors execution of strategy by the senior management, and is answerable to the regional representative group. It is independent and makes decisions about what investments to make to meet regulatory requirements and provide for growth in the network, what services standards are appropriate, and how services will be funded and charged for.

- There is no requirement for co-governance at the level of the board, nor any requirement for representation by local authorities or mana whenua. Members of the board would be appointed for their knowledge, skill and experience.
A guide to co-governance in Three Waters – cont’d

What are the reasons for including co-governance in the model?

- The Government believes it’s appropriate that there be involvement of both local authority owners and mana whenua at the strategic oversight level of the governance structure.
- Local authorities represent the broad interests of the communities they represent, and they should be involved in the setting of aspirations and expectations for water services entities on behalf of their communities. Local Authorities will also be the owners of the new entities as shareholders on behalf of their communities.
- Water services entities will be required to give effect to the principles of te Tiriti and must give effect to Te Mana o te Wai. They also have responsibilities to uphold existing Treaty Settlements that relate to water services provision. So it is appropriate that mana whenua are at the table setting expectations for the entities in relation to these matters.
- Under the Articles of Te Tiriti, mana whenua have the right to participate in decisions that relate to water services. They also have responsibilities as kaitiaki to protect Te Mana o te Wai, the health and mauri of our water.
- This is consistent with the approach across all legislation relating to water services, including the Taumata Arowai – Water Services Regulator Act 2020 and the Water Services Act 2021, which together provide key parts of the regulatory system water services entities need to operate within.
Water Services Entities Bill
Water Services Entities Bill - Overview

The Government has introduced the Water Services Entities Bill to implement its decisions to establish four public entities to take on the delivery of drinking water, wastewater and stormwater services across New Zealand. This reform is intended to ensure all New Zealanders have safe, clean and affordable water services.

You can read the full Bill here. But in short, the Bill:

- provides the legislative basis to establish the four new publicly-owned water services entities, and sets out the ownership, governance, and accountability arrangements relating to these entities – find out more here: Water Services Entities Bill fact sheet - Governance and accountability
- sets out the boundaries, objectives and functions of the new entities
- includes essential provisions for ongoing public ownership of the new entities, including safeguards against future privatisation, and sets out the framework for community and consumer engagement - find out more here: Water Services Entities Bill factsheet - Public ownership and consumer engagement
- provides for transitional arrangements relating to the establishment of the new entities – find out more here: Water Services Entities Bill factsheet - Transitional arrangements
Water Services Entities Bill - Objectives

The Bill sets out the objectives and functions of the water services entities and establishes the boundaries of the four entities. Under this legislation the entities will:

- Deliver water services and infrastructure in an efficient and financially sustainable manner;
- Protect and promote public health and the environment;
- Support and enable housing and urban development;
- Operate in accordance with best commercial and business practices;
- Act in the best interests of present and future consumers and communities; and
- Deliver water services in a sustainable and resilient manner that seeks to mitigate the effects of climate change and natural hazards.
Water Services Entities Bill – Operating principles

In delivering these services, the entities will have operating principles which include:

• Developing and sharing capability and technical expertise throughout the water services sector;

• Being innovative in the design and delivery of water services and water services infrastructure;

• Being open and transparent in the calculation and setting of prices and levels of service delivery to communities and consumers;

• Partnering and engaging early and meaningfully with Māori/iwi, including to inform how to give effect to Te Mana o te Wai and Treaty settlement obligations;

• Partnering and engaging early and meaningfully with councils and their communities; and co-operating with, and supporting, other water services entities, infrastructure providers, local authorities, and the transport sector.
What the Water Services Entities Bill does NOT do

• **The Bill does not** transfer assets and liabilities from local authorities to water services entities or establish powers and functions for the entities in relation to managing the provision of water services. These matters will be addressed through further legislation. This will also integrate the entities into other regulatory systems, such as resource management.

• **The Bill does not** establish economic regulation for the water services entities. Decisions on the details of this regulation are expected to be taken to Cabinet in the coming weeks with an aim to introduce further legislation in the latter half of 2022.

• The Three Waters Reforms will **NOT** transfer privately-owned water supplies to the new entities.
Making your Submission to the Select Committee

The Finance and Expenditure Select Committee are now accepting submissions until 22 July 2022. We encourage you to read the detail of the Bill and make a submission.

The Select Committee is expected to report back to the House by 11 November 2022 with the intention of completing the remaining legislative stages shortly thereafter.

You can follow the Bill’s progress on the parliament website [here](https://www.parliament.nz).

The following link will give you guidance on how to make a submission to Select Committee. [Click Here](https://www.parliament.nz).

You may also wish to make an oral submission which means presenting your views to committee members. For more information about appearing before the Select Committee, please read the Submission help pages – This can be [Found Here](https://www.parliament.nz).
Further legislation to come

• The Water Services Entities Bill will be followed by further legislation to provide for specific powers, functions, and responsibilities of the new water service entities, and pricing and charging arrangements. This will:
  ○ create mechanisms to guide the transfer of the three water assets, interests, and liabilities from territorial authorities to the new water services entities;
  ○ transfer across, and amend where appropriate, the current legislative provisions relating to local authorities as three waters services providers;
  ○ create legal obligations and relationships between the water services entities and their customers, including for drinking water and wastewater provision, stormwater services, and businesses disposing of trade water;
  ○ creating a compliance, monitoring and enforcement regime; and
  ○ establish various mechanisms to replace the current regulatory role served by bylaws.

• Legislation will also be required to establish the economic regulation and consumer protection regime framework.

• Together this suite of legislation will implement the Three Waters Reforms.
Working with local government to refine the reform proposals

Overview
A five year conversation

• In mid-2017, following the Inquiry into Havelock North Drinking Water, the Government established the Three Waters Review to look at how to improve the regulation and service delivery arrangements of drinking water, wastewater and stormwater.

• The findings of the Review raised system-wide questions about the effectiveness of the regulatory regime for the three waters, and the capability and sustainability of water service providers.

• The Three Waters Review led to three key pou, or pillars, of reform:
  o Establishment of a dedicated water service regulator, Taumata Arowai;
  o Regulatory reforms outlined in the Water Services Bill; and
  o Reforms to water delivery services – what is now known as “The Three Waters Reform”

• At the May 2020 Central/Local Government Forum, central and local government leadership discussed challenges facing New Zealand’s water service delivery and infrastructure, and committed to working jointly on reform – establishing the Joint Three Waters Steering Committee

• The Joint Three Waters Steering Committee was established to provide oversight and guidance to support progress towards reform, and to assist in engaging with local government, iwi/Māori and other water sector stakeholders on options and proposals.
Engagement on the Three Waters Reforms

• The Department of Internal Affairs have held a series engagements with local government, iwi/Māori, and the water industry throughout the Three Waters Review and Reforms to better understand the case for change and test developing reform proposals.

• This includes:
  o The joint Central/Local Government Steering Committee oversight of the Reforms;
  o Three national roadshows in July/August 2020; August/September 2020 and March 2021;
  o Regular webinars, sector/zone meetings, and one-on one hui;
  o A Stormwater Technical Working Group, established to identity future arrangements for the planning and management of stormwater services;
  o A te ao Māori Technical Working Group, to test, provide constructive feedback and offer advice, from a te ao Māori perspective to officials;
  o The Request for Information and supporting engagements (October 2020-February 2021).

• In June 2021, the Government released it’s reform proposals informed by this earlier engagement. At the request of LGNZ, the Government then set aside a period from 1 August 2021 to 1 October 2021 for local authorities to consider the impact of the reform proposals on them and their communities, and to provide feedback on the proposed model. You can read more about this feedback [here](#).

• Following this late-2021 feedback, three further working groups were established – discussed on the following slides.
Representation Governance & Accountability Working Group
About the Working Group on Representation, Governance, and Accountability

• The Working Group was established with an equal number of representatives from local government and iwi/Māori to consider feedback and make recommendations about the representation, governance and accountability arrangements in the Government’s reform proposals.

• The Group was led by an independent chair and included a balance of membership from across all four entity boundaries and a mix of rural, provincial and metropolitan leadership.

• The Working Group followed an inclusive process, with consensus-based decision making to develop its recommendations. The final report reflects this constructive approach.

• Through their process, the Working Group considered potential alternative models including: a cooperative ownership model; the Wellington Water model; the council-controlled organisation (Watercare) model; the Hawke’s Bay regional model; a Ngāi Tahu model; the ‘Communities 4 Local Democracy’ alternatives; and a shareholding model.

• They also considered: core concepts of accountability, oversight, control and decision making; financial capacity and separation; other governance models that were considered during the development of the Government’s reform proposals; Te Mana o te Wai and co-governance considerations; community ombudsman schemes; and stormwater considerations.
The Working Group on Representation, Governance, and Accountability developed a set of 47 recommendations to enhance the reform proposals. These recommendations cover the following main areas:

- A public shareholding structure that makes community ownership clear, with shares held by councils on behalf of their communities – to provide a tangible expression of ownership that is recognisable by communities and territorial authorities;

- Ensuring mana whenua have input in the delivery of water services through equal representation on the regional representative group, while maintaining a merit-based approach to board appointments;

- Recognising and embracing Te Mana o te Wai as a korowai that applies across the water services framework;

- Tighter accountability from each water services entity board to the community, through new and stronger mechanisms, including strengthening and clarifying the role of the Regional Representative Group; and

- Strengthened connections to local communities, including sub-committees feeding into the regional representative group to ensure local voice is considered as part of investment prioritisation.

This Working Group released its report on 9 March 2022
The Government's bottom lines

• The Working Group considered a range of reform options, analysis, and considerations both within their Terms of Reference. This included consideration of wider context as reflected in their recommendations.

• The Government considers the **recommendations fall within its bottom lines**, which represent important elements of the design of the future system.
  
  o **Good governance** will ensure competency-based boards govern the entities with the right combination skills, expertise and capabilities in delivering large infrastructure within the New Zealand context;
  
  o **Public ownership** through collective council ownership, among other protections, will safeguard these services for future generations to come and ensure they continue to deliver services to those communities that have invested in them;
  
  o **Balance sheet separation** will ensure the entities are not constrained in their ability to invest in infrastructure needed to meet future needs and expectations. This will in turn ensure councils are freed up to focus their investment on things that matter to local place-making and community wellbeing; and
  
  o **Upholding the Treaty partnership**, through the joint strategic direction and oversight of these entities, will ensure these new entities benefit from the intergenerational knowledge and experience of mana whenua alongside local government leadership in setting local priorities for these services.

• The Government has accepted the majority of the Working Group recommendations and included them in the Bill.
Rural Supplies Technical Advisory Group
The Rural Supplies Technical Working Group was established to provide advice to the Department of Internal Affairs and Taumata Arowai to support policy development related to rural drinking water supplies and rural communities in the context of the new drinking water regulatory and service delivery regime.

The purpose of the Rural Supplies Technical Working Group was to inform:
- The proposed legislation to implement the Water Services Entities through Bill 2
- Wider policy development related to rural supplies within the Department and Taumata Arowai
- The approach to implementation of water services regulation by Taumata Arowai
- Areas of support required for rural communities.

This Working Group comprised of members drawn from across rural New Zealand. The membership of the group has a wide range of rural expertise, experience and perspectives, acknowledging the complexity and breadth of issues the group needed to consider. The Group presented its report in May 2022. Making 30 recommendations to ensure rural communities’ unique drinking water needs are recognised in the Government’s Three Waters model.

The full report can be found here: Rural Supplies Technical Working Group Report which was released on 31 May 2022.

The report notes that private rural supplies will be unaffected by Government’s service delivery reforms, which only apply to supplies that are council-owned.
Planning Technical Advisory Group
The Planning Technical Working Group was established to provide advice to the Department and Ministry for the Environment to support policy development related to the intersection between the role and functions of the new water service entities and the resource management system.

The purpose of the Planning Technical Working Group is:
• To inform the policy work for Bill 2 where policies relate to the interaction of the new water service entities and the resource management/planning system;
• To inform the three waters policy team’s secondary advice and engagement with resource management system reform; and
• To advise on the implications of the resource management system reform on three waters legislation.

This working group includes technical experts from across local government and iwi. The Department, in consultation with LGNZ and Taituarā, invited those with a strong technical understanding of the planning system to become members of the group. This includes those with subject matter expertise in te ao Māori and iwi/Māori engagement with the planning system.

You can read the Term of Reference and papers for this group here: Planning Technical Working Group
Iwi/Māori engagement on Rights and Interests in service delivery

A fuller discussion of these matters can be found in Cabinet Paper Three.
Continuous and ongoing engagement

• Engagement with iwi/Māori on the three waters service delivery reforms is a continuation and extension of a multi-year programme of engagement undertaken through the Three Waters Review, which included the establishment of Taumata Arowai and a suite of regulatory reforms.

• In addition open engagement with iwi alongside local government, the Minister of Local Government has worked to ensure that the groups targeted for engagement included a range of perspectives, to help understand Māori interests in the three waters. Groups included Kāhui Wai Māori, the Māori freshwater forum, and a group of iwi representatives from key regions. Case studies of rural communities with a high Māori population that face three waters issues have also contributed to this understanding.

• Te Mana o te Wai has been an important vehicle for the Government to engage with Māori during the creation of Taumata Arowai and development of the Water Services Bill. Māori have consistently identified improving water quality and ecosystem health as a priority, and their feedback on the three waters regulatory reform proposals reflected these concerns.
System Connections

Where does reform to three waters service delivery sit in the context of iwi/Maori rights and interests in Wai?

Anything we create in the three waters reforms will need to uphold Te Mana o Te Wai.
Objectives for the Crown/Māori relationship within the service delivery reforms

The following objectives have guided the Government’s consideration of iwi/Māori rights and interests within the Three Waters Service Delivery Reforms, and informed the development of specific mechanisms for addressing them:

- **Enabling greater strategic influence**: Enable iwi/Māori to have greater strategic influence to exercise their rangatiratanga over water services delivery, including through enhanced capacity and capability.

- **Integration within a wider system**: Ensure that the rights and interests of iwi/Māori are analysed within a wider system, including issues related to allocation and the future of the Resource Management Act 1991, but specifically focussing on issues that relate to the establishment of water services entities and delivery of water services.

- **Reflection of a Te Ao Māori perspective**: Recognise the holistic manner (environmental, cultural, spiritual, economic) in which water is viewed using te ao Māori perspectives and Te Mana o te Wai including ki uta ki tai or a catchment-based approach, consistent with rohe/takiwā or whakapapa links.

- **Supporting clear accountabilities**: Ensure roles, responsibilities, and accountability for the relationship with the Treaty partner is clear throughout the wider system, and that capacity and capability is available to honour the Crown’s Treaty obligations.

- **Improving outcomes at a local level**: Provide a step change improvement in delivery of water services for iwi/Māori at a local level, including through enhanced capacity and capability and improved wellbeing.
Mechanisms for addressing rights and interests

- The reforms are intended to achieve a step change in the way Iwi/Māori rights and interests are recognised in three waters service delivery.
- These rights and interests are woven into the new service delivery system via a number of mechanisms:
  - statutory recognition of the Treaty of Waitangi and Te Mana o te Wai
  - creating a mana whenua group in the oversight and strategic direction of each entity, with equal rights to local government (with a kaupapa Maori selection method for this group with transitional provisions to enable this to occur)
  - requirements for the entity boards to have:
    - Treaty of Waitangi, mātauranga Māori, tikanga Māori, and Te Ao Māori competencies
    - specific expertise in kaitiakitanga, tikanga and mātauranga Māori in delivering water services
  - provision for the mana whenua group to issue Te Mana o te Wai statements to the entity, and requirements on the entity to respond
  - requirements for the entities to fund and support capability and capacity of mana whenua to participate in the new governance and accountability system
- Future three waters service delivery operators will be required to uphold Treaty Settlement legislation.
The Water Services Entities Bill upholding Iwi/Māori rights and interests

• This Bill contains robust mechanisms to provide for, and promote, iwi/Māori rights and interests. The board of an entity must have expertise in the Treaty of Waitangi and te ao Māori, and must ensure that the entity has the capability and capacity to give effect to the principles of the Treaty of Waitangi.

• Entities are also required to give effect to Te Mana o te Wai, and mana whenua whose rohe or takiwā is in the entity’s area can make a Te Mana o te Wai statement setting out their expectations in relation to particular water catchments.

• The Bill also provides strong protections for Treaty settlements to ensure they are enduring, these provisions will be further advanced by the second Bill. The Bill provides that, where there is any inconsistency with a Treaty settlement obligation, the Treaty settlement prevails. Alongside that, entities must give effect to Treaty settlements.

• Councils and mana whenua have also entered into detailed arrangements relating to three waters services, and engagement is underway to identify these arrangements and ensure they are safeguarded.
Understanding the challenges
1. Limited opportunities for benefits of scale

- Most local authorities in New Zealand currently serve 100,000 or fewer connected ratepayers, and this creates significant inefficiencies within the system for delivering three waters, including:
  - lack of strategic and co-ordinated asset planning across district boundaries
  - limited opportunities to consider catchment-level outcomes
  - lack of funding and pipeline certainty to create competitive pressures in the supply chain
  - lack of specialist management capacity and capability
  - a lack of innovation
  - lack of career pathways and opportunities for the workforce to specialise; and
  - wide variation in water charges and service standards, particularly for vulnerable communities.

- International experience shows that greater scale enables improved governance, management and financial strength, enabling services to be delivered more effectively and efficiently. Scale also enables costs to be shared across larger customer bases, addressing affordability issues in smaller communities.

- Evidence indicates each entity would need to serve a connected population of at least 600,000 to 800,000 to fully realise the potential for efficiency gains.
2. Affordability challenges

- To achieve the quality outcomes across New Zealand’s three waters services, an investment requirement of between $120bn - $185bn will be required over the next 30+ years.

- Meeting these costs will be challenging for most local authorities, with average household bills needing to increase significantly.

- Without reform, the costs of accessing safe, clean and environmentally friendly three waters services are projected to increase significantly and would have an impact on the cost of living for New Zealanders, especially lower income households.

- The expected increases do not only impact on rural and provincial areas and include significant increases for metros (including Auckland).

![Average household bills in 2051 with and without reform](source: Water Industry Commission for Scotland, 2021)
3. Incentives for critical infrastructure decisions

- Local authorities operate in a political environment, in which infrastructure investment decisions must be taken against broader community interests and investments.

- This is also a constrained financial environment, in which the main funding and financing mechanisms are via ratepayers and council borrowing.

- **These factors combine to limit the level of three waters investment due to:**
  - covenants imposed by lenders which limit the debt to revenue ratios that councils can maintain while achieving a good credit rating and cost-effective financing
  - varying attitudes to debt and rates increases across communities
  - financially constrained households (such as ratepayers on low incomes), especially in areas with higher levels of deprivation
  - misaligned incentives, and a lack of management focus, connected with an operating environment in which three waters is just one aspect of the broader responsibilities that councils have and services.

- Independent reviews into the delivery of three waters infrastructure in Wellington, the West Coast, Otago/Southland, and Hawkes’ Bay have arrived at similar conclusions regarding the challenges associated with three waters service delivery and infrastructure provision in the current local government operating environment.
4. Lack of effective oversight and stewardship

- At the time of the review, New Zealand had 67 local authority (or CCO) suppliers, 20 district health boards (noting the major reform in this area), 16 regional councils, and seven government ministries that have a role in relation to the supply of safe drinking water.

- The dispersed nature of the roles and responsibilities within the system means no one is responsible for monitoring or overseeing the performance of the whole system.

- While the Government has taken steps to strengthen the regulatory environment – with the creation of Taumata Arowai and the Water Services Bill – this focuses on improving quality of services.

- Gaps remain around how the performance of the system and its outcomes for customers are regulated
  - existing water service providers are not subject to even a basic form of economic regulation, such as information disclosure
  - This has impacted the quality of information about the condition of three waters assets and the performance of water network.

- This lack of effective oversight and stewardship arrangements compound the challenges with how the system is currently designed.

- Without good quality information, there is a lack of transparency about fundamental elements of the three waters system for customers and communities to hold water services providers to account.
Options Analysis undertaken by DIA
Options to resolve these challenges assessed by the Government

- Alternative options that were considered by the Government include the following, **none of these options address all four of the underlying problems**:

  1. Sector-led reform (*political and legislative barriers mean this will have a piecemeal and slow change*)
  2. A national three waters fund (*increased operational burden with no clear revenue source*)
  3. Central government funding to close the infrastructure deficit (*taxpayer funding to an inefficient system is unsustainable*)
  4. Regulatory reform only (*unlikely to be affordable for some communities which will incentivise piecemeal change as communities struggle*)

- An overview of these alternatives is included in this pack. Comprehensive analysis can be found in the Department’s Regulatory Impact Analysis online here: [RIA](#)
1. Sector-led reform

- While some regions have undertaken investigations of local service delivery reform options such as the Hawke’s Bay, limited progress has been made with these sector-led reforms.
- There are also statutory barriers to aggregation of service delivery that are likely to limit the potential benefits of these reforms.
- Continuing with a sector-led approach would require a significant, coordinated approach to reform, of a scale and extent not previously seen. There are no guarantees that reforms would be delivered consistently across the country.
- Evidence suggests that political and economic barriers to sector-led reforms are high.
- Proceeding with a sector-led approach to service delivery reform, or unconditional investment, would not guarantee that reform will occur or be achieved in a way that meets the objectives of reform or addresses root causes.
- Without asset ownership, investment decisions will still be made by individual local authorities and subject to revenue and debt constraints and in the longer-term, inefficiencies will still be likely due to limits on scale.
1. Sector-led reform cont’d

- It is likely that councils would need to establish multi-regional providers as council-controlled organisations (CCOs) as provided for through the Local Government Act 2002 (LGA).

- This approach would have some limitations, including:
  - current provisions in the LGA are not fit for this purpose, and present barriers to reform
    - It is likely to take as long to redesign and amend the existing legislative provisions, as it would to create bespoke provisions in new legislation (including some form of economic regulation)
  - establishing CCOs requires the agreement of all councils, each of which would need to undertake public consultation. This would take time and creates uncertainty about the outcome
  - if the new entities were CCOs, this is likely to have implications for council financing arrangements
    - For example, they may not be sufficiently separate from local government to borrow at similar rates as other utilities.

- Shared service models, which do not involve asset ownership, have a number of shortcomings. Wellington Water, for example, is still subject to decisions of council owners who retain asset ownership and have different views on relative priorities and charging which limit Wellington Water’s ability to plan and invest strategically in its network. The impact of this is evident in this week’s media coverage.
2. National three waters fund

• Officials have considered the option of establishing a national three waters fund, similar to the National Land Transport Fund (NLTF) that the New Zealand Transport Agency administers.

• There are fundamental challenges with establishing a national three waters fund including:
  o this approach would not deliver the benefits of scale
  o The NLTF is sourced from road users through various charges, with local government co-investment in addition to this (sourced largely from rates). However, there is no consistent user charge regime in place that would be amenable to a centralised collection of revenue without operational inefficiencies
  o A newly created national fund would also require machinery to administer it, either through the creation of a separate function within an existing entity or a completely new entity altogether. This adds to the costs and complexity associated with the fund.

• More importantly, even if the operational and administrative challenges noted above were addressed, a national fund would fail to address the other root causes we have identified, and any lift in investment levels would occur within a system that will continue to struggle from a lack of scale, capability, accountability and operational independence.
3. Central Government funding

- Councils often call for more central government funding to help councils get on top of the $120bn - $185bn infrastructure deficit.

- This would accelerate a closing of the infrastructure gap, however it has a reliance on taxpayers (many of whom are also ratepayers) to continue to fund a system that has systemic failings and inefficiencies.

- This would not result in fundamental changes to how this critical infrastructure is procured, assets are managed, and services are operated and therefore would be unlikely to realise significant operating, capital and financial efficiencies.

- This is not a sustainable long-term solution.
4. Regulatory reforms only

• Officials have also examined the extent to which outcomes, objectives, and ‘strategic shifts’ can be achieved through regulatory reform alone
  o This would require a coordinated change in the regulatory system to strengthen the consideration of environmental impacts alongside the increased focus on public health that Taumata Arowai brings
  o It would also require the introduction of economic regulation of local authority service provision, including much more stringent performance measurement, information disclosure, and protections for consumers than is currently the case.

• This approach, on its own, will not achieve benefits of scale, greater flexibility to borrow, greater access to capital, long-term funding certainty, and greater capability and capacity.

• It may encourage some sector-led service delivery reforms, but this is unlikely to be on the widespread scale that would be required to meet the added pressures introduced on the system.

• While regulatory reform alone would not be sufficient to achieve the outcomes Ministers are seeking, it will form an important part of the overall reform pathway.
Was a CCO model considered?

Instead of the bespoke governance model, the Government considered whether an entity design could be adopted that:

- Broadly mirrors the existing Council Controlled Organisation model.
- Retains levers for councillors to set local priorities and influence key decisions.
- Provides for co-governance through some mana whenua representation (i.e. less than 50%).
- Could cover multiple councils - though some models provide some councils with greater control than others (i.e. Auckland proposal).
- An option identified has been to underpin this model with a Crown guarantee/indemnity to assist balance sheet separation.
CCO model analysis

Limitations

• CCOs are unlikely to be viewed as sufficiently separate from local government to borrow at similar rates as other utilities.

• Establishing CCOs requires the agreement of all councils with each required to engage separately with its constituents - this would take time and creates uncertainty about the outcome.

• Addressing the above limitations would require legislative amendment to Local Government Act (likely to take just as long as creating new legislation).

• Does not materially improve governance oversight or the incentives on council decision-making in relation to water infrastructure and services (Wellington Water has been highlighted as an example of how different council views on priorities and charging has limited its ability to plan and invest strategically in its network)

• Crown indemnity is unlikely to meet bottom lines.
What about consideration of a regional option?

Instead of the proposed 4-entity model, adopt a regional-council based model using existing regional council boundaries (with some consolidation for unitary councils) to identify each entity’s catchment.

The Government modelled 30 different amalgamation scenarios ranging from 2 to 13 entities and concluded that four entities achieved the balance of efficiencies of scale and communities of interest.

You can read more about these here: WICS final report - economic analysis of water services aggregation (dia.govt.nz).

Limitations of a regional model

• Would prevent scale benefits to sparsely populated areas.

• Likely to result in greater regional price and quality variations.

• Could allow mergers over time, however is a slower more costly route to achieve reform benefits.

• Is inconsistent with some of the sectors own analysis including Tonkin and Taylor supporting the West Coast and Morrison Low supporting Otago/Southland.
Regional model considerations

Benefits

- More identifiable communities of interest.
- Aligns with regional council catchments.
- Potentially more manageable number of representative interests for both Councils and mana whenua.

Limitations

- Would prevent scale benefits to sparsely populated areas.
- Likely to result in greater regional price and quality variations.
- Could allow mergers over time, however is a slower more costly route to achieve reform benefits.
- Is inconsistent with some of the sectors own analysis including Tonkin and Taylor supporting the West Coast and Morrison Low supporting Otago/Southland.
You can click here for Frequently asked Questions

Find out more at
www.dia.govt.nz/Three-Waters-Reform-Programme