**“Model report” – for chief executives to draw from when briefing their councils on the three waters service delivery reform/stimulus programme**

**[EXAMPLE] Purpose**

This report asks the [Name] Council to:

* sign a Memorandum of Understanding (MoU) with the Crown, agreeing to participate in the initial stage of a central/local government three waters service delivery reform programme (**Appendix A**); and
* authorise the Chief Executive to enter into the Funding Agreement, to accept a grant from the Crown to spend on operating and/or capital expenditure relating to three waters infrastructure and service delivery (**Appendix B**).

**[EXAMPLE] Recommendations**

* **Note** that:
	+ in July 2020, the Government announced an initial funding package of $761 million to provide a post COVID-19 stimulus to maintain and improve water networks infrastructure, and to support a three-year programme of reform of local government water services delivery arrangements; and
	+ initial funding will be made available to those councils that agree to participate in the initial stage of the reform programme, through a Memorandum of Understanding (MoU), Funding Agreement, and approved Delivery Plan.
	+ this initial funding will be provided in two parts: a direct allocation to individual territorial authorities, and a regional allocation. The participating individual authorities in each region will need to agree an approach to distributing the regional allocation
	+ the Steering Committee has recommended a preferred approach to the allocation of regional funding, being the same formula as was used to determine the direct allocations to territorial authorities
* **Agree** to sign the MoU at **Appendix A** andFunding Agreement at **Appendix B**.
* **Agree** to nominate [Name], the Chief Executive of the Council as the primary point of communication for the purposes of the MoU and reform programme – as referred to on page 6 of the MoU.
* **Agree** to delegate decisions about the allocation of regional funding to [Name], the Chief Executive of the Council, with the understanding that the minimum level of funding to the Council be based upon the formula used to calculate the direct council allocations, and noting that participation by two-thirds of territorial authorities within the [SPECIFY] region is required to access the regional allocation
* **Note** that the MoU and Funding Agreement cannot be amended or modified by either party, and doing so would void these documents.
* **Note** that participation in this initial stage is to be undertaken in good faith, but this is a non-binding approach, and the Council can opt out of the reform process at the end of the term of the agreement (as provided for on page 5 of the MoU).
* **Note** that the Council has been allocated [amount] of funding, which will be received as a grant as soon as practicable once the signed MoU and Funding Agreement are returned to the Department of Internal Affairs, and a Delivery Plan has been supplied and approved (as described on page 5 of the MoU).
* **Note** that the Delivery Plan must show that the funding is to be applied to operating and/or capital expenditure relating to three waters infrastructure and service delivery, and which:
	+ supports economic recovery through job creation; and
	+ maintains, increases, and/or accelerates investment in core water infrastructure renewal and maintenance.
* [COUNCILS COULD ALSO INCLUDE RECOMMENDATIONS RELATING TO THE DELIVERY PLAN; E.G. SEEKING AGREEMENT TO SUBMIT AN ATTACHED DRAFT DELIVERY PLAN; AUTHORISING THE CHIEF EXECUTIVE TO FINALISE THE DELIVERY PLAN TO ADDRESS FEEDBACK FROM GOVERNMENT AND OBTAIN THE APPROVAL NEEDED TO RELEASE FUNDING.]

**[EXAMPLE] Summary**

* In July 2020, the Government announced a $761 million funding package to provide post COVID-19 stimulus to maintain, improve three waters infrastructure, support a three-year programme of reform of local government water service delivery arrangements (reform programme), and support the establishment of Taumata Arowai, the new Waters Services Regulator.
* A Joint Central/Local Government Three Waters Steering Committee has been 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.
* The reform programme is designed to support economic recovery, and address persistent systemic issues facing the three waters sector, through a combination of:
	+ stimulating investment, to assist economic recovery through job creation, and maintain investment in water infrastructure renewals and maintenance; and
	+ reforming current water service delivery, into larger scale providers, to realise significant economic, public health, environmental, and other benefits over the medium to long term.
* Initial funding from the stimulus package will be made available to those councils that agree to participate in the first stage of the reform programme, through a Memorandum of Understanding (MoU), Funding Agreement, and approved Delivery Plan. The MoU must be signed by the end of August 2020, with the Funding Agreement and Delivery Plan submitted and approved by the end of September 2020.

**Background and context**

***Issues facing the three waters system, and rationale for reform***

* Over the past three years, central and local government have been considering the issues and opportunities facing the system for regulating and managing the three waters (drinking water, wastewater, and stormwater).
* The Government Inquiry into Havelock North Drinking Water – set up following the serious campylobacter outbreak in 2016 – identified widespread, systemic failure of suppliers to meet the standards required for the safe supply of drinking water to the public. It made a number of urgent and longer-term recommendations to address these significant systemic and regulatory failures.
* The Government’s Three Waters Review highlighted that, in many parts of the country, communities cannot be confident that drinking water is safe, or that good environmental outcomes are being achieved. This work also raised concerns about the regulation, sustainability, capacity and capability of a system with a large number of localised providers, many of which are funded by relatively small populations.
* The local government sector’s own work has highlighted similar issues. For example, in 2014, LGNZ identified an information gap relating to three waters infrastructure. A 2015 position paper, argued for a refresh of the regulatory framework to ensure delivery of quality drinking water and wastewater services, and outlined what stronger performance in the three waters sector would look like.
* Both central and local government acknowledge that there are many challenges facing the delivery of water services and infrastructure, and the communities that fund and rely on these services. These challenges include:
	+ Underinvestment in three waters infrastructure in parts of the country, and substantial infrastructure deficits. For example, it is estimated that between $300 to $570 million is required to upgrade networked drinking water treatment plants to meet drinking water standards; and up to $4 billion is required to upgrade wastewater plants to meet new consent requirements. These deficits are likely to be underestimates, given the variable quality of asset management data.
	+ Persistent funding and affordability challenges, particularly for communities with small rating bases, or high-growth areas that have reached their prudential borrowing limits.
	+ Additional investment required to increase public confidence in the safety of drinking water, improve freshwater outcomes, and as a critical component of a collective response to climate change and increasing resilience of local communities.
* COVID-19 has made the situation even more challenging. Prior to COVID-19, territorial authorities were planning on spending $8.3 billion in capital over the next five years on water infrastructure. However, COVID-19 is likely to cause significant decreases in revenue in the short term. As a result, borrowing will be constrained due to lower debt limits that flow from lower revenues, and opportunities to raise revenue through rates, fees and charges will be limited.

***Progress with three waters regulatory reforms***

* Good progress is already being made to address the regulatory issues that were raised by the Havelock North Inquiry and Three Waters Review. The Government is implementing a package of reforms to the three waters regulatory system, which are designed to:
	+ improve national-level leadership, oversight, and support relating to the three waters – through the creation of Taumata Arowai, a new, dedicated Water Services Regulator;
	+ significantly strengthen compliance, monitoring, and enforcement relating to drinking water regulation;
	+ manage risks to drinking water safety and ensure sources of drinking water are protected;
	+ improve the environmental performance and transparency of wastewater and stormwater networks.
* Legislation to create Taumata Arowai had its third reading on 22 July 2020 and should be enacted shortly [TO BE UPDATED ONCE BILL IS ENACTED]. This new Crown entity is currently being built, and will become responsible for drinking water regulation once a separate Water Services Bill is passed (anticipated mid 2021).
* However, both central and local government acknowledge that regulatory reforms alone will not be sufficient to address many of the persistent issues facing the three waters system. Reforms to service delivery and funding arrangements also need to be explored.

**Proposal – central/local government three waters reform programme**

***Overview of proposed approach to three waters investment and service delivery reform***

* At the recent Central/Local Government Forum, central and local government leadership discussed the challenges facing New Zealand’s water service delivery and infrastructure, and committed to working jointly on reform. A Joint Central/Local Government Three Waters Steering Committee has been established to provide oversight and guidance to support this work. [Further details are provided in Appendix E.]
* Central and local government consider it is timely to apply targeted infrastructure stimulus investment to enable improvements to water service delivery, progress service delivery reform in partnership, and ensure the period of economic recovery following COVID-19 supports a transition to a productive, sustainable economy.
* In July 2020, the Government announced an initial funding package of $761 million to provide post COVID-19 stimulus, support a three-year programme of reform of local government water service delivery arrangements, and support the establishment and operation of Taumata Arowai.
* The reform programme is designed to support economic recovery, and address persistent systemic issues facing the three waters sector, through a combination of:
	+ stimulating investment, to assist economic recovery through job creation, and maintain investment in water infrastructure renewals and maintenance; and
	+ reforming current water service delivery, into larger scale providers, to realise significant economic, public health, environmental, and other benefits over the medium to long term.
* While the Government’s starting intention is for publicly-owned multi-regional models for water service delivery (with a preference for local authority ownership), final decisions on a service delivery model will be informed by discussion with the local government sector and the work of the Joint Steering Committee.
* Further information on the reform objectives, and the core design features of any new service delivery model, are provided in pages 3 to 4 of the MoU at Appendix A.

***Reform process and indicative timetable***

* As noted above, this is a three-year programme to reform three waters service delivery arrangements, which is being delivered in conjunction with an economic stimulus package of Crown investment in water infrastructure. The reform programme will be undertaken in stages.
* The initial stage is an opt in, non-binding approach, which involves councils taking the actions and signing the documents described below (MoU, Funding Agreement, and Delivery Plan).
* Councils that agree to opt in by the end of August 2020 will receive a share of the initial funding package.
* Any further tranches of funding will be at the discretion of the Government and may depend on progress against reform objectives.
* An indicative timetable for the full reform programme is provided below. While this is subject to change as the reforms progress, and subject to future Government budget decisions, it provides an overview of the longer-term reform pathway.



**Allocation of the investment package**

* The Government has determined a notional allocation framework based on a nationally-consistent formula.
* The general approach to determining each authority's notional allocation is based on a formula that gives weight to two main factors:
	+ The population in the relevant council area, as a proxy for the number of water connections serviced by a territorial authority (75 per cent weighting)
	+ The land area covered by a local authority excluding national parks, as a proxy for the higher costs per connection of providing water services in areas with low population density (25 per cent weighting).
* The investment package is structured into two components:
	+ A direct allocation to each territorial authority, comprising 50% of that territorial authority's notional allocation; and
	+ A regional allocation, comprising the sum of the remaining 50% of the notional allocations for each territorial authority in the relevant region
* The relevant allocations for [INSERT TERRITORIAL AUTHORITY] are:
	+ $X (excluding GST) direct allocation for [INSERT TERRITORIAL AUTHORITY]
	+ $X (excluding GST) regional allocation for [INSERT REGION]
* The purpose of the Government’s regional allocation is to establish collective participation by councils in the reform programme. Each regional group of councils has until 30 September to agree on how best to apportion the regional funds to the individual territorial authorities that make up the region. Appendix F includes a hypothetical example of how a regional allocation decision-making process could work
* The Steering Committee has recommended a preferred approach to the allocation of regional funding, being the same formula that is used to determine the direct allocations to territorial authorities.
* Officers recommend delegating decisions about the allocation of regional funding to [Name], the Chief Executive of the Council, with the understanding that the minimum level of funding to the Council be based upon the formula used to calculate the direct council allocations, and noting that participation by two-thirds of territorial authorities within the [SPECIFY] region is required to access the regional allocation

**What actions are the Council being asked to take at this point?**

* The initial stage of the reform programme involves three core elements:
	+ Memorandum of Understanding (Appendix A);
	+ Funding Agreement (Appendix B);
	+ Delivery Plan (Appendix C).
* Initial funding will be made available to those councils that sign the MoU, and associated Funding Agreement, and provide a Delivery Plan.
* This initial funding will be provided in two components: a direct allocation to individual councils, and a regional allocation. The participating councils in each region are required to agree an approach to distributing the regional allocation.
* The MoU is the ‘opt in’ to the first stage of the reform and stimulus programme. The MoU needs to be signed and submitted by the end of August 2020. The Funding Agreement and Delivery Plan need to be submitted by the end of September 2020, to access the stimulus funding,
* Councils that do not opt in by the end August 2020 deadline will not receive a share of the stimulus funding.  Councils will still be able to opt in to the reform programme at a later date, but will not have access to the initial funding package, retrospectively.

***Memorandum of Understanding***

* A MoU has been developed by the Steering Group, for each council to enter into with the Crown. This is a standardised document, which cannot be amended or modified by either party.
* Signing the MoU commits councils to:
	+ engage in the first stage of the reform programme – including a willingness to accept the reform objectives and the core design features set out in the MoU;
	+ the principles of working together with central government and the Steering Committee;
	+ work with neighbouring councils to consider the creation of multi-regional entities;
	+ share information and analysis on their three waters assets and service delivery arrangements.
* At this point, this is a voluntary, non-binding commitment. It **does not** require councils to commit to future phases of the reform programme, to transfer their assets and/or liabilities, or establish new water entities.
* The MoU is effective from the date of agreement until 30 June 2021, unless terminated by agreement or by replacement with another document relating to the reform programme.
* A legal opinion by Simpson Grierson, commissioned by SOLGM on behalf of the Steering Committee, advises that the MoU **does not** contain any explicit triggers for consultation under the Local Government Act 2002. (REFER TO APPENDIX D)

***Funding Agreement***

* This Council has been allocated [INDIVIDUAL AMOUNT] by the Crown, if it opts in to the reform programme. A further [REGIONAL AMOUNT] has been allocated to the [REGION] to agree an appropriate distribution between participating Councils. This funding will be provided as a grant, which does not need to be repaid if the Council does not ultimately commit to reform at later stages of the process.
* There are several options for how the regional funding could be allocated between councils. The joint central-local government Three Waters Steering Committee preferred approach is to apply the same formula[[1]](#footnote-1) used to calculate the direct allocations. Under this approach, the Council would receive an additional [SHARE OF REGIONAL AMOUNT], contributing to a total funding allocation of [INDIVIDUAL AMOUNT + SHARE OF REGIONAL AMOUNT].
* It is recommended that the Council delegates authority to the Chief Executive to agree an appropriate allocation with other participating councils, with the understanding that the Council share of the regional allocation should be [SHARE OF REGIONAL AMOUNT] at a minimum, noting that participation by two thirds of territorial authorities within the region is to access the regional funding.The Funding Agreement is one of the mechanisms for accessing the funding package. Like the MoU, it is a standardised document, for agreement between each council and the Crown. It cannot be amended.
* The Funding Agreement guides the release and use of funding. It sets out:
	+ the funding amount allocated to the Council;
	+ funding conditions;
	+ public accountability requirements, including the Public Finance Act;
	+ reporting milestones.
* While there is some local flexibility around how the funding can be applied, the Government has indicated that this investment is intended to support economic recovery, enable improvements in water service delivery, and progress the service delivery reform programme.
* The Funding Agreement will be supplemented by a Delivery Plan, which is the document that sets out how the grant funding is to be applied by the Council.

***Delivery Plan***

* The Delivery Plan is the other mechanism for accessing the funding package.
* This Delivery Plan must show that the funding allocation is to be applied to operating and/or capital expenditure relating to three waters infrastructure and service delivery, and which:
	+ supports economic recovery through job creation; and
	+ maintains, increases, and/or accelerates investment in core water infrastructure renewal and maintenance.
* The Delivery Plan is a short-form template, which sets out:
	+ a summary of the works to be funded, including location, estimated associated costs, and expected benefits/outcomes;
	+ the number of people to be employed in these works;
	+ an assessment of how the works support the reform objectives in the MoU;
	+ reporting obligations.
* The Delivery Plan will be supplied to Crown Infrastructure Partners (and other organisations as agreed between the Council and Crown), for review and approval. Crown Infrastructure Partners will monitor progress against the Delivery Plan, to ensure spending has been undertaken with public sector financial management requirements.

[NOTE: COUNCIL COULD INCLUDE SPECIFIC DETAILS ABOUT ITS PROPOSED DELIVERY PLAN AND SEEK AGREEMENT TO THE PROJECTS TO BE INCLUDED.]

**Attachments**

* Appendix A: Memorandum of Understanding
* Appendix B: Funding Agreement
* Appendix C: Delivery Plan
* Appendix D: Legal opinion provided by Simpson Grierson relating to consultation requirements
* Appendix E: Information on Joint Three Waters Steering Committee
* Appendix F: Hypothetical example

**Appendix E – Information on Joint Three Waters Steering Committee**

* The Joint Three Waters Steering Committee has been 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.
* The Steering Committee comprises independent chair Brian Hanna, local government mayors, chairs and chief executives, representatives of Local Government New Zealand (LGNZ) and the Society of Local Government Managers (SOLGM), and officials and advisors from the Department of Internal Affairs (DIA), Taumata Arowai, and the Treasury.
* The Steering Committee will ensure that the perspectives, interests and expertise of both central and local government, and of communities throughout New Zealand are considered, while the challenges facing water services and infrastructure are addressed. This will include periods of engagement, in the first instance with the local government sector. an overview is provided below.
* The Steering Committee is supported by a secretariat made up of advisors and officials from LGNZ, SOLGM, DIA and the Treasury. This secretariat is hosted by DIA.
* The terms of reference for the Steering Committee is available on the DIA Three Waters website.

**Appendix F – Hypothetical scenario for agreeing regional funding allocation**

***The following is a hypothetical, worked example of how the funding allocation approach could work for a mythical Council and region***

This is for Monkchester City Council in the Bernicia Region of New Zealand. Monkchester is a small city with a population of 80,000 in a region of 140,000. The rest of the Region is made up by Bidchester with 30,000 residents and Smithchester with 30,000 residents.

The notional funding allocated for the Bernicia Region, based on the national formula, is set out in Table 1.

**Table 1 Funding Allocation for Bernicia Regional**

|  |  |  |
| --- | --- | --- |
| Area | Direct council allocations $ Millions | Regional allocation $ Millions |
| Monkchester | 5 | 10 (to be allocated to territorial authorities by agreement through a regional process) |
| Bidchester | 2.5 |
| Smithchester | 2.5 |
| Bernicia Region | 10 |
| Total direct and regional allocation  | 20 |

Council officers looked at a range of projects as candidates for the stimulus funding:

* An unsuccessful bid for the ‘Shovel Ready’ programme
* Projects the Long-Term Plan
* Accelerating planned maintenance, renewals and renewals upgrades
* A new project.

Projects already fully-funded in the Annual Plan were excluded for obvious reasons.

A discussion was also held at regional level to agree how to allocate the regional element of funding. Three options were considered:

* Discuss regional priorities and then allocate the monies based on the formula the Government used, as recommended by the Steering Committee.
* Discuss regional priorities and allocate the money in three equal shares.
* Allocate all the regional money to a single project of regional importance.

After two meetings the Mayors and Chief Executives agreed two regional priorities for accelerating renewals and improving resilience for earthquakes. They decided against pursuing a new regional project because it required considerable preparatory work, design work, consents and a procurement programme. This would mean in practice a 4-year timescale and high risks and this would not meet the economic stimulus objective.

They also agreed to allocate the regional fund to territorial authorities using the Government’s formula. This means Monkchester’s overall allocation is $10 Million.

The criteria used to identify the best use of the investment were – priority for water and wastewater services, speed of delivery, job creation in the City and the risk profile of the project. An analysis of the candidates is set out below in Table 2.

**Table 2 Analysis of the Project Options**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Project | Speed | Job Implications | Risk | Alignment with Regional Priorities | Overall Score |
| Shovel Ready project – new water treatment plant | Low as it requires resource and building consents and procurement. Overall a 3 year project. | Medium, creates 50 jobs directly | High, especially in an overheated construction market with extreme volatility | Low | 4 out of 10 |
| Upgrade of wastewater treatment plant from year 3 of LTP | Medium as it requires building consent and fresh procurement. Overall a 2-year project. | Medium, creates 50 jobs | Medium | High | 6 out of 10 |
| Renewal programme for the Central City’s sewer network | High as no consents or procurement required. Overall an 18-month programme. | High with 100 jobs largely from the local area | Medium as the work is underground and we will find things we did not expect to so a sensible contingency will be needed. | High | 8 out of 10 |
| Completely new project - a new reservoir | Low as is requires community consultation, consents and a fresh procurement. | Low as will take a good 18 months to be shovel ready | High due to seismic issues | Medium because improves long-term reliance  | 3 out of 10 |

Accelerating investment in the renewals and renewal upgrade programme for the Central City’s sewer network is the preferred project. It can be done speedily. No resource consent is required. No fresh procurement is required either as the City Council already has a 5-year renewals partnership with Downers. It creates 100 direct jobs for 18 months whilst the network is upgraded. Moreover, it will enable significant expansion of activity in the Northern quarter of the CBD which could lead to 20000 square meters of new development and 2000 jobs. Work will begin on the ground by February 2021. Finally, it is a low risk project being contracted to a trusted partner. An appropriate contingency budget has been established and this will be the subject to a confidential pre-committee briefing with the CFO.

Through the Mayoral Forum, councils also agreed to progress further discussions on three water service delivery reform opportunities within the region.

Mayors of participating councils wrote to the Minister to communicate their decision on the regional allocation and the steps they were proposing to take to advance the objectives of the reform programme.

1. Applying a 75% weighting for population and a 25% weighting for land area, excluding national parks. [↑](#footnote-ref-1)