LOCAL GOVERNMENT FORUM

SUBMISSION ON THE AUCKLAND CITY COUNCIL'S DRAFT ANNUAL PLAN 2004

MAY 2003

AUCKLAND CITY COUNCIL
DRAFT ANNUAL PLAN 2004

1 Overview

1.1 This submission on the Auckland City Council's draft annual plan 2004 (the Plan) is made by the Local Government Forum (the Forum). The Forum comprises business organisations that have a vital interest in local government (see Appendix I). The members of those organisations are among the largest ratepayers in Auckland City.

1.2 The Auckland City Council (the Council) is to be commended for the steps that it has taken to concentrate on its core activities, reduce the rate of growth in spending and rates, and lower net debt. The thrust of the Council's policies over the last couple of years has been consistent with those advocated by the Forum in past submissions to the Council. They will help to put in place an environment that encourages the growth and development of business, and benefits the community at large.

1.3 Much work remains to be done, however, if the Council is to make the best possible contribution to the advancement of the overall welfare of the citizens of Auckland City. The main contribution that the Council can make to growth and employment prospects in Auckland is to reduce the rates and regulatory burdens it imposes on the private sector, focus on the funding of genuine public goods and services, and facilitate the provision of necessary infrastructure.

1.4 Spending and rates are still excessive. We consider that the Council should exit from private good activities such as the ownership of off-street car parking facilities rather than increase its investment in them. It should also refrain from engaging in new private good activities such as the promotion, subsidisation and/or ownership of the proposed indoor sports arena and convention centre. New proposals, including investment projects, should be rigorously scrutinised against recognised public policy criteria. The same approach should apply to regional transport projects in which the Council has a financial interest.

1.5 The Plan proposes an increase in the level of rates of 2.5 percent. In our view any rate rise is unacceptable. Moreover, the rate rise is not required to fund budgeted operating spending. The Forum opposes the proposed introduction of a new uniform annual general charge, the increase in the uniform annual charge (targeted rate) for waste collection, and the increase in differential rates. There is no economic or financial justification for imposing a disproportionate rate burden on the business sector. The Council should put in place a planned programme to phase out such differentials over 3 to 5 years.

1.6 The balance of this submission is presented in 4 sections. The next section (section 2) reviews the Council's spending and revenue. Section 3 examines the key issues that are addressed in the Plan. Other issues are discussed in section 4. The proposed rate increase is examined in section 5.

2 Forecast spending and revenue

2.1 The forecast statement of financial performance indicates that total operating spending (excluding that undertaken by LATEs such as Metro Water Limited and the ARC levy) will amount to $401 million in 2003/04, an increase of 2 percent on the forecast outturn for the current year. This probably underestimates the likely growth in spending. Over recent years actual operating expenditure has regularly exceeded budgeted spending. The budgeted operating spending for 2002/03, for instance, was $385 million whereas the present forecast outturn is $392 million. A projected increase in 2003/04 spending in the 2002/03 plan of 1.6 percent is now expected to be 3.4 percent.

2.2 The long-term forecasts contained in the policy on revenue and financing (which are not entirely consistent with those referred to above) show that total operating spending (excluding the ARC levy) is expected to increase by 8 percent between 2002/03 and 2012/13. While the Council has taken steps to slow the rate of growth in spending – the forecast growth over the next 10 years is almost 2 percentage points lower than that forecast last year – it has not arrested the persistent upward trend in spending.

2.3 There is a significant risk that new policies will add to spending levels over time. Net operating spending on some programmes, for example community facilities (21 percent) and premier parks and neighbourhood reserves (19 percent), is expected to increase substantially in 2003/04. Spending on museums is to increase by 39 percent over the next three years. The Plan provides little or no explanation or justification for those increases. They offset savings in other programmes including those that arise from the Birch review.

2.4 Much spending is undertaken through council-owned companies. There is no indication of the level of such spending in the annual plan as forecasts for the Auckland City group have been omitted from this year's plan. Moreover, certain funding transactions undertaken by the City on behalf of Metro Water Limited have been omitted from the long-term forecasts contained in the policy on revenue and financing. This seems to be inconsistent with the accounting policies and procedures adopted for the preparation of the City's forecast and actual financial statements, and may be inconsistent with sections 95(6)(a) and 111 of the Local Government Act 2002.

2.5 Auckland City businesses and residents are also exposed to substantial financial risk through the Council's 61 percent equity holding in Auckland Regional Transport Network Limited (ARTNL). Councils are investing heavily in uneconomic mass passenger transport projects through ARTNL. Despite a planned exorbitant increase in Auckland Regional Council (ARC) rates averaging 10 percent a year from 2002/03 to 2010/11, planned grants and operating revenue may prove to be insufficient to fund ARTNL's capital spending and operating costs.

2.6 The planned funding of ARTNL should be more fully disclosed and explained to ratepayers and its major projects should be thoroughly scrutinised against standard public policy criteria and be subject to public consultation. These matters may be required to be addressed by the new statutory requirement to adopt and apply a policy on significance. The Council's draft policy on significance treats its shareholding in ARTNL as a strategic asset but appears to be silent on the activities that ARTNL undertakes on behalf of the Council and other councils in the region.

2.7 Total rates revenue available to the Council in 2003/04 is budgeted to be 3.5 percent higher than the forecast outturn for 2002/03 (excluding the ARC levy). This arises from the proposed increase in the level of rates (2.5 percent) and the increase in the value of rateable property.

2.8 Total rates revenue (excluding the ARC levy) is forecast to rise by 17 percent or an average of 1.6 percent a year between 2002/03 and 2012/13. This rate of growth is 0.8 of a percentage point a year higher than the forecast growth in spending. Revenue from activities is forecast to decline through to 2012/13. The reason for placing greater reliance on rates and relatively lesser reliance on revenue from activities (user charges) does not appear to be explained in the Plan.

2.9 The long-term financial projections provide for an operating surplus of at least $22 million a year, a reduction in total liabilities from $284 million in 2002/03 to $120 million in 2012/13, and an increase in total assets from $6.1 billion to $6.6 billion over the same period. Ratepayers' equity is expected to rise from $5.9 billion to $6.5 billion. These forecasts point to an excessive expansion of the Council's balance sheet and somewhat higher surpluses (ie higher rates than otherwise) than is appropriate, given the partial sale of the City's shares in Auckland International Airport Limited. The new act generally requires councils to plan for a balanced budget (section 100 of the Local Government Act 2002). The commendable effort to lower debt by selling assets and funding most capital spending from operating cash flows may, over time, lead to a new round of debt-financed capital spending on projects that do not yield an attractive return from a community perspective. The risk is illustrated by the mayor's reported comment that the Council could have sold all of its shares in Auckland International Airport Limited but the City's debt position had improved so it did not need to do so.[1]

2.10 As in last year's submission, the Forum recommends that the Council's policy on revenue and financing (previously its long-term financial strategy) be adjusted to incorporate further reductions in spending, no increase in the level of rates payable per dollar of rateable property and lower surpluses. There is a case for going further and reducing rates. Borrowing could, if necessary, finance a higher proportion of planned capital expenditure.

1 'Auckland City Sells Airport Stake', www.onebusiness.nzoom.com/onebusiness_detail/0,1245,153664-3-166,00.html.

3 Key issues addressed in the Plan

Transport

3.1 In last year's plan the mayor stated "We are giving top priority to completing Auckland's part of the regional state highway network." In the Plan he states "Completing Auckland's Transport Infrastructure is priority number one." This seems to reflect a shift in emphasis from roading to mass public passenger transport. A change in emphasis is not warranted.

3.2 The councils in the region have devoted disproportionate attention to mass passenger transport services, most notably those related to rail. Mass passenger transport services can only make a relatively small contribution to the region's transport needs. Congestion on motorways and arterial roads is imposing massive costs on business and the wider community and, despite the mayor's leadership, insufficient progress is being made in solving the problems. While there is much that the Council can do to reduce traffic congestion within Auckland City, prime responsibility for expanding the capacity of state highways and motorways rests with other agencies. The Council can, however, exert influence on them.

3.3 Passenger transport services are a private good activity – not a public good activity.[2] Unlike public goods, for instance city parks and street lighting, public transport services such as buses, trains, ferries and taxis are provided by private operators and charged for in the normal way. There are no free-rider problems arising from the inability to exclude non-payers. In addition, the use of passenger transport services by one person detracts from their enjoyment by other people. The streetlight illuminates the footpath regardless of how many people pass by. In contrast, once a seat on the bus is taken it is not available for other commuters.

3.4 The mistaken view that the government has a significant role in funding and / or providing passenger transport operations and infrastructure is reflected in the policies and activities of the Auckland Regional Council, the region's territorial authorities and Infrastructure Auckland. Several policies and

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2 In oral hearings on our submission last year there was some misunderstanding on the part of Councillor Bruce Hucker of the distinction being drawn between public and private goods. These are technical terms. A simple description of public goods is attached as Appendix II.

comments contained in the Plan reflect such views. They include the Council's participation in ARTNL, projects aimed at providing preferences for buses (further subsidies for one class of road user) and cyclists (who make no direct contribution to the costs of cycle ways) and endorsement of urban intensification along mass passenger transport routes. The last of these policies puts the promotion of mass passenger transport ahead of the preferences of citizens. It is not surprising that affected residents are resisting it.

3.5 A more rigorous analysis of the economic merits of proposed investments in public transport infrastructure is required. The first issue to be addressed on a principled basis is whether there are valid grounds for government involvement. These are dubious at present and would certainly disappear if roads were properly priced. Undue emphasis seems to have been placed on obtaining funding for projects from Infrastructure Auckland and other agencies while too little attention has been paid to the vital question of whether the projects represent a good use of resources from an overall community perspective. It is also unclear to the Forum which agency accepts responsibility for assessing the overall economic merits of large regional transport projects, other than those relating to roading. This matter should be addressed in the current review of governance issues relating to transport. The economic merits of projects should properly be assessed and open to public scrutiny. The public should be advised of the costs and benefits of options including those intended to mitigate environmental effects, such as tunnels, and those proposed to placate public transport lobbies.

3.6 The country cannot hope to achieve the ambitious growth targets advocated by the major political parties if local government in the Auckland region spends hundreds of millions of dollars over the next few years on projects that are expected to generate low or negative net community benefits. This happened with the Britomart project and we are apprehensive that it will be repeated. We seek the Council's assurance that it will only fund public transport projects that are supported by a rigorous cost benefit analysis.

3.7 Although progress is being made with the roading network, it still falls far short of what is required. Major problems include the inadequacy of the Land Transport Management Bill currently before parliament and the Resource

Management Act. The Council should be putting more emphasis on solving these problems. We would be willing to work with the Council to promote more effective and urgent action.

Growth and economic development

3.8 The Plan states "The Council wants to encourage economic development in Auckland and takes a leading role in the Auckland Regional Economic Development Strategy." The Plan also states that major projects for 2003/04 include "getting involved in activities that support tourism and helping to establish Film Auckland to draw film-making business to Auckland. The Council also continues to be involved in major projects such as the indoor arena and the Auckland Festival."

3.9 Most of these projects entail the subsidisation of favoured private good activities and thus the taxation of other activities. Such a policy rests on the belief that governments can pick winners and that planning should augment market mechanisms in allocating resources and encouraging growth. The thrust of the policy was tried with Think Big and similar interventions in the past. New Zealand learned the hard way that such schemes can only benefit some firms at the expense of others, misallocate resources and make the overall community poorer. Industries such as tourism, film-making and entertainment should stand on their own feet. As organisations representing businesses we are not seeking Council handouts for our members.

3.10 The main contribution that the Council can make to growth and employment prospects in Auckland is to reduce its spending, rates and regulatory burdens. The Council should also carry out its public good activities as efficiently as possible. It should focus on them and disengage from other so-called economic development activities.

4 Other issues

Arena and convention centre

4.1 The claim that Auckland City is missing out on possible conferences and sporting events may well be true. But it is a pointless claim. Auckland is also missing out on a host of other activities, like the construction of jumbo jets and nuclear reactors, for the same reason, namely that it is not economic to engage in them.

4.2 The provision of an indoor sports arena and convention centre is a private activity that should be the responsibility of the private sector. The grounds for public ownership are weak. Similarly, the argument that spill-over or external benefits that accrue to the wider community justify subsidisation is dubious.[3] Promoters can capture many spill-over benefits through sponsorship arrangements. Moreover, if subsidies were justified, they should be directed at the particular events that generate the intended benefits and not at the provision of facilities that may remain under-used.

4.3 It is implausible that externality grounds could possibly justify the provision of $50 million of the $80 million cost of constructing the proposed indoor stadium, together with any subsidies related to the provision of land. If the indoor stadium is built, the Council may be exposed to risks should it encounter financial difficulties. We ask the Council to provide a rigorous economic evaluation of the project for public scrutiny.

Water

4.4 Last year's plan stated that the Council will determine, with the rest of the Auckland region, the future of water, wastewater and stormwater industries. That project is reported to have been completed but there is no discussion of the outcome in the Plan.

4.5 The ownership structure that would provide the region and Auckland City with the most efficient water and wastewater services should have been the focus of such deliberations. There is compelling evidence from New Zealand and overseas that corporatised and privatised enterprises are, on average and

3 See New Zealand Business Roundtable (1999), *Should Governments Subsidise Stadiums and Events?*, New Zealand Business Roundtable, Wellington.

over time, more efficient than businesses that are run by politicians. Various forms of privatisation of water supply and wastewater disposal, including franchising and contracting for services, have produced major benefits for consumers and the wider community in other countries. When a socialist-leaning country like France has had a predominantly private water industry for decades, it is absurd for New Zealand councils to close their minds to the idea on ideological grounds. Private sector participation in Auckland's water and wastewater industries should be introduced as soon as possible. While section 130 of the Local Government Act 2002 prohibits the sale of its water supply business (other than to a another local government organisation) it does not stop all forms of private participation.

Off-street car parking facilities

4.6 The Plan provides for an expansion of the Council's interests in off-street parking. The provision of off-street car parking is an inappropriate activity for the Council as the Birch report concluded. The establishment of a more commercial structure for the management of such facilities is not an adequate response. Such facilities should be sold.

Airport shares

4.7 The Forum supported the sale of all the Council's shares in Auckland International Airport Limited. In the event the Council sold half its holding and still holds 12.8 percent of the company's shares. The provision of airport and related services (such as the supply of property for retailing and car parks) are private good activities that should be left to the private sector. The Council has committed (subject to some exceptions) not to sell its remaining holding for two years. On the expiry of that commitment, it should sell the balance of its holding.

Significance policy

4.8 The Forum doubts that the requirement in the Local Government Act 2002 for councils to consult on matters deemed to be 'significant' will place effective constraints on their activities. However, in the absence of more effective constraints under the current legislation, we suggest that the Council's significance policy be used to help confine the Council to activities that are consistent with its core public good role. The Forum submits, therefore, that a decision should generally be considered significant if the proposal does not involve the supply and/or funding of a local public good, or the provision of regulatory services required by central government.

4.9 The Forum notes also the vulnerability of councils to special interest group lobbying where parties attempt to secure benefits to themselves that are paid for by others. It therefore suggests that a decision also be considered significant if the costs of a proposal are not borne largely by those parties who will benefit from it.

4.10 The Council's draft statement on significance helpfully summarises the relevant legislative requirements. In relation to strategic assets the Council's approach focuses on large undertakings such as the roading network as a whole. However, in relation to an activity, significance is defined as "whether or not a decision or proposal would change the nature of the reporting component by more than a 50 percent increase or decrease, or would constitute a new reporting component." Some reporting components are modest indeed, for example Hauraki Gulf islands wastewater projects at $0.3 million. This seems to encompass too many items that are arguably not at the higher level of significance envisaged by the act. Moreover, it is unclear whether the policy is to be applied on a single year basis or over the life of the project. The measure of significance for a component should arguably be set on a present cost basis.

5 Proposed rate increase

5.1 The Plan proposes a rate increase of 2.5 percent "to cover inflation". The idea that rate or price increases are justified by reference to movements in general prices is a hangover from New Zealand's high-inflation and highly regulated past. In the present environment, rate increases by councils should be justified by reference to the costs and benefits of their valid public good activities.

5.2 The Council proposes to collect part of its rates by imposing a new uniform annual charge of $150 per rateable property. The uniform annual charge redistributes part of the rating burden from high-value properties to lower-value properties, including from the business to the residential sector. (The redistribution between the business and residential sectors is, however, limited in 2003/04 by the proposal to cap the level of residential rates.) The uniform annual general charge is intended to mitigate the impact on the level of rates payable by owners of high-value property following the revaluation in 2002.

5.3 According to the Plan the uniform annual charge will "ensure that every ratepayer makes an equal minimum contribution towards council-provided services that benefit everyone, such as street lighting, sporting grounds, pools, libraries and footpaths." Some of these examples, for instance pools and libraries, are private good activities where user charges should apply. More importantly, there is no analysis in the Plan which shows that the proposed uniform annual charge has been derived from a consistent application of the three-step process outlined in the Council's policy on revenue and financing. Although that process was not carried forward in the Local Government Act 2002, the Council maintains that its continued use is consistent with the requirements of the new act.

5.4 The Council proposes that the uniform annual general charge for waste collection that was introduced in 2002/03 should be increased from $47 to $110 per rateable property. This charge does not increase economic efficiency, and hence the community's overall well-being from a better use of resources, because each residential ratepayer would pay $110 regardless of the amount of waste (if any) that is collected from his or her property. From this perspective there are no valid grounds for funding waste collection from a uniform annual general charge. The position would be different if the charge paid by each ratepayer reflected the actual volume of rubbish collected from the property. In that event the charge would affect the incentive to generate and dispose of waste.

5.5 Unlike appropriate user charges, uniform annual charges are discriminatory taxes where the affected services are mandatory, where the link between the value of the service as perceived by identified beneficiaries and the amount of the charge is tenuous, and where the beneficiaries have little influence over the spending programme and the level of spending. These circumstances apply to the proposed uniform annual general charge and the charge for waste collection. They are unlikely to enable revenue to be raised at a lower economic cost than general rates. Broad-based taxes are generally considered to be more efficient than selective taxes. The latter weaken the accountability of elected representatives because they enable excessive taxes to be imposed on minority groups that are less than proportionately represented in the political process.

5.6 The proposed general uniform annual charge and the increased waste collection charge may impact harshly on some ratepayers. The Plan does not make a case on equity grounds for imposing a higher proportion of general rates on ratepayers who own relatively low-value residential property. For these reasons, the Forum opposes the introduction of the proposed uniform annual charge and the increase in the charge for waste collection. For waste collection and other private good services (where charges can be set), we recommend a move to user charges instead.

5.7 In 1999/00 the Council adopted a policy of moving to lower rate differentials over a period of 10 years. The key non-residential and CBD non-residential differentials were to be reduced to 180 percent and 200 percent respectively of the residential rate. The following table shows the official differentials comparing rates in the dollar relative to the residential rate for 1998/99 (before the policy was implemented) and 2001/02 through to 2003/04.

5.8 If the Council's proposal is adopted the key non-residential differentials will be substantially higher in 2003/04 than in 2002/03 and even higher than in 1998/99, and a long way short of the policy objective. The implementation of the policy of reducing differentials, which was proceeding at a snail's pace, is to be reversed to mitigate the impact on residential ratepayers of the 2002 revaluation of rateable property.

Rate Differentials

Ratepayer Group	Relative Differential for the General Rate			
	1998/99	2001/02	2002/03	2003/04
	%	%	%	%
Residential	100	100	100	100
Non-residential	226	199	196	247
CBD non-residential	312	258	256	323
Rural 1 [1]		86	86	86
Rural 2 [1]		25	25	25
Rural 3 [1]		0	0	0

Great Barrier Island non-residential [1]		166	179	179

1. The ratepayer group was established after 1989/99.

5.9 The rates policy for 2002/2003 and the draft rates policy for 2003/04 reintroduce uniform annual charges into the general rate. They are not reflected in the official differentials shown in the table. Uniform annual charges are reflected in effective differentials. The Plan and the annual plan for 2002/03 do not disclose effective differentials. It is understood that effective differentials in 2003/04 would be lower than official differentials but would still be higher than if the level of non-residential rates were not capped as proposed in the Plan. The cap is understood to lower the increase in the average residential rate by about 40 percent.

5.10 There is no economic or financial justification for imposing a disproportionate rating burden on the business sector. The force of this argument was recognised when the decision was taken to reduce differentials. The inequity of the present differential has been ignored to pacify residential voters. The task of reducing differentials will be made more difficult if the proposed rating policy for 2003/04 is not changed. This is implicitly acknowledged in the suggestion that the policy goal should be reviewed.

5.11 User charges should be applied where appropriate and remaining revenue requirements should generally be met by a uniform levy on rateable property with no discrimination between residential and non-residential ratepayers. The Forum submits that differential rates should be phased out over 3 to 5 years. The impact on residential ratepayers could be moderated by reducing spending and by applying user charges were appropriate.

Appendix I

The Local Government Forum

The Local Government Forum was established in 1994 to promote greater efficiency in the local government sector and to contribute to debate on policy issues affecting the sector.

The Forum comprises business organisations that have a vital interest in the activities of local government. Member organisations include:

- Business New Zealand
- Federated Farmers of New Zealand
- New Zealand Business Roundtable
- New Zealand Forest Owners' Association
- Property Council of New Zealand
- Retail Merchants Association of New Zealand

Appendix II

A SIMPLE DESCRIPTION OF PUBLIC GOODS

There is much confusion about the term 'public goods'. Yet a clear understanding of it is important for deciding what things we need governments – central and local – to be involved in.

As the name suggests, the job of the public sector is essentially to provide public goods that people can't provide for themselves (in the case of central government, it is also to provide some level of welfare and social services). The job of the private sector is to provide private goods.

Clearly a public good is not just something that is 'good' for us. Food, gymnasiums and dental care are all 'good' for us but they don't need to be provided by the public sector.

Also many services called public are not public goods – they are simply services supplied to the public. Public transport is a case in point – bus, train and taxi services can be provided by private businesses.

A first approximation of a public good is something that can't be charged for. If private firms can sell goods and services to customers for a price, they are trading in private goods. Fares meet the cost of taxi services.

An example of a genuine public good – for which private supply is not feasible – is national defence. Individual beneficiaries can't be charged for it. Defence expenditures must be funded from taxation.

Streetlighting and stormwater are examples of local government public goods.

More rigorously, public goods have two distinct aspects. First, non-payers can't be excluded from the benefits of the good or service so there is a 'free-rider' problem (think national defence). Second, one person's use of them does not limit their availability to others (think streetlighting).

Such goods may be supplied inadequately through private initiatives – commercial or otherwise.

Markets can overcome some of these problems. Free-to-air broadcasting does not have to be financed from taxation: advertising is a source of revenue. Cable television services can exclude non-subscribers.

Also there are indirect means of covering costs: shopping malls provide lighting and parking but recover costs through rentals.

Some items are partly public and partly private goods. Patents provide private returns to inventors but on their expiry the invention becomes a public good.

With advancing technologies, what were once public goods (eg basic science) are sometimes capable of being produced privately – Celera's private human genome project is an example. Also people can come together voluntarily – eg in environmental and cultural organisations – and provide a tolerably efficient level of public goods.

The fact that market or voluntary solutions may not be perfect does not mean that government solutions will be better – inadequate information and special interest politics bedevil government solutions.

Finally, governments don't need to provide all public goods themselves. Often they can contract out their provision.

The number of genuine public goods is quite small. Governments have expanded far beyond their core roles to undertake things that would be better left to firms or the voluntary sector.