

**LOCAL GOVERNMENT FORUM**

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**SUBMISSION ON THE  
LOCAL GOVERNMENT BILL**

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## TABLE OF CONTENTS

Executive summary	i
1 Overview	1
2 The role of government	5
3 The purpose and powers of local authorities	9
4 The power of general competence	12
5 Financial management	15
6 Non-resident ratepayer franchise	18
7 Treaty of Waitangi	20
8 Conclusion	21
Appendices	23
I Elaboration of selected issues	23
II The Local Government Forum	29



## **EXECUTIVE SUMMARY**

- A thorough revision of the Local Government Act 1974 (the Act) is warranted. The new act must, however, be based on sound principles.
- Unless the government strengthens New Zealand's institutional and policy framework and implements a proven growth strategy there is no prospect that a sustainable improvement in economic growth and social indicators, relative to those of other OECD countries, will be realised.
- By broadening the mandate for local government and by seeking to overturn longstanding constitutional and legal constraints on the activities of councils, the Bill would weaken rather than strengthen the existing framework for local government.
- The best possible contribution that local government can make to the advancement of the overall well-being of communities and thus to the achievement of the government's broad goals is to confine its activities to local protective and public good roles and undertake them as efficiently as possible.
- New Zealand's constitutional arrangements do not envisage local democracy limited only by popular vote. Limited government and proper checks and balances are required to protect liberty and promote prosperity.
- The proposals contained in the Bill place unwarranted faith in the efficacy of democratic processes at the local level.
- The activities that councils may engage in should be tightly circumscribed and enumerated in the new act. The deliberate specification of limited powers is a vital constraint on local government.
- A power of general competence is inconsistent with New Zealand's longstanding constitutional arrangements and the common law, and is a threat to personal and economic freedom.

- An integrated approach to the activities, funding and rating of local authorities is needed. The Rating Bill and the Bill should be examined together.
- The financial management provisions contained in the Bill should be re-examined to reduce the discretion of councils and to accord primacy to the concept of economic efficiency as originally intended.
- The non-resident ratepayer franchise should be retained.
- The proposed recognition of the Treaty of Waitangi is a significant constitutional issue that should be the subject of a referendum; otherwise it has the potential to be very divisive.
- The Bill reflects unsound principles and should be re-examined afresh.

# **SUBMISSION ON THE LOCAL GOVERNMENT BILL**

## **1. Overview**

- 1.1 This submission on the Local Government Bill (the Bill) is made by the Local Government Forum (the Forum). The Forum comprises mainly business organisations that have a vital interest in local government (see Appendix II). The members of those organisations are among the largest ratepayers in the country and they are affected directly by the activities of local government. Businesses pay about half of all rates raised by local authorities.
- 1.2 This submission focuses on the broad principles that are reflected in the Bill. The Forum also endorses the detailed comments on the Bill that are made in a separate submission by Business New Zealand, a member of the Forum.
- 1.3 The serious deficiencies of the Local Government Act 1974 (the Act) are widely recognised.<sup>1</sup> The Act is complex and in many places it is excessively detailed and poorly drafted. A thorough revision of the Act is warranted. It does not follow, however, that the only or best solution to the problems is to empower councils to engage in any lawful activities that they choose to undertake and to rely upon consultative processes and triennial voting to focus local authorities on the advancement of overall community welfare. More effective checks and balances are required.
- 1.4 The new act must be based on sound principles. The Forum's submission on *Reviewing the Local Government Act 1974: Have Your Say* (the Consultation Document that preceded the Bill) observed that:

One of the most disturbing features of *Reviewing the Local Government Act 1974: Have Your Say ...* is the absence of principled argument and analysis. Fundamental issues such as the nature of constitutional democracy at the local government level, the protection of the freedoms of citizens and the rights of minorities, and the proper role of local government are at stake. It

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<sup>1</sup> Local Government Forum (1999), *Refocusing the Role of Local Government*, Local Government Forum, Wellington

is incumbent on the government to apply a contemporary public policy analysis to such issues.

1.5 In line with the Forum's view, the Ministerial Panel on Business Compliance

Costs recommended that the government "Treat with urgency the review of the role and regulatory powers of local government from a first principles perspective."<sup>2</sup> The Panel apparently understood that a principled examination was being undertaken as part of the review of the Act. No such analysis was included in the Consultation Document and, as far as the Forum can tell, none has been undertaken following its publication. The perfunctory regulatory impact and compliance cost statement included with the Bill (pages 21-25) makes no reference to such issues.

- 1.6 It is vital that a proper analysis of the role of local government and its place in our democratic arrangements be undertaken. ***The Bill should not proceed until such an analysis has been prepared and all interested parties, including ratepayers and citizens and not just central and local government representatives, are properly consulted.*** As noted in Appendix I, section 2, the Forum is exceedingly disappointed with the level of consultation afforded the Forum and the business sector in general.
- 1.7 Unless New Zealand's institutional and policy framework is strengthened, the government has little hope of achieving the ambitious economic and social goals that it has set, namely of restoring New Zealand to the top half of the OECD rankings. The proposals contained in the Bill would weaken that framework by:
- seeking to overturn longstanding constitutional constraints on the scope of council activities;
  - broadening substantially the mandate for local government;
  - weakening the principles of financial management; and
  - according preferential treatment to Maori.
- 1.8 The overwhelming direction of government policy in developed and developing countries is toward a more tightly focused government sector and

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<sup>2</sup> Ministerial Panel on Business Compliance Costs (2001), *Finding the Balance: Maximum Compliance at Minimum Cost*, Ministry of Economic Development, Wellington, p 24.

the removal of obstacles to wealth creation by the private sector. The trend is not based on ideology – centre-left governments and centre-right governments have been moving in the same direction. The broad direction of policy reflects the weight of analysis and evidence.<sup>3</sup> The Bill is out of step with policy in other countries and is inconsistent with the policies that are required if the government's economic and social objectives are to be achieved.

1.9 Local government has a vital role in advancing the overall well-being of all New Zealanders. However, its role is not all-encompassing. It needs to be established on a principled basis and properly circumscribed. Local government has a role in establishing and maintaining the general social framework that protects lives, liberties and properties. However, the core business of local authorities should be the funding and – in justifiable circumstances – the provision of local public goods and services that cannot be better provided by firms, households and non-profit organisations, and the administration of appropriate regulations.

1.10 ***The powers of local authorities should be tightly defined and explicitly enumerated in the new act. Councils should be prohibited from engaging in other activities. The proposition reflected in the Bill, that territorial authorities should largely be able to do as they please, subject only to various forms of consultation, is inconsistent with New Zealand's longstanding constitutional arrangements.***

1.11 The Local Government (Rating) Bill (the Rating Bill) is before parliament. It would authorise local authorities to impose rates and substantially expands the scope to impose selective (targeted and differential) rates. The Rating Bill does not provide any criteria to guide councils in choosing among the ways in which rates may be levied.<sup>4</sup> Moreover, the Bill would essentially gut the structured framework and transparent process for funding council activities established by the Local Government Amendment Act (No 3) 1996. ***An integrated approach to***

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<sup>3</sup> Barry, Phil (2001), *How Do We Compare? New Zealand Public Policy Directions in an International Context*, New Zealand Business Roundtable, Wellington.

<sup>4</sup> See Local Government Forum (2001), *Submission on the Local Government (Rating) Bill*, Local Government Forum, Wellington.

***the activities, funding and rating of local authorities is needed. The Rating Bill and the Bill should be examined together. They should preferably be merged into a single bill. Furthermore, local authorities should be required to accord primacy to the concept of economic efficiency as originally intended.***

- 1.12 The activities of local government will be affected by separate reviews on transport, waste management and issues that relate to Auckland. There is also a bill before parliament that would amend the Resource Management Act. A review of the water industry was initiated some years ago and handed over to Local Government New Zealand. There has been no discernible progress. High quality outcomes in all areas and in respect of rating are essential. These exercises should be coordinated and based on sound and widely agreed principles.
- 1.13 The balance of this submission is presented in 7 sections. The next section (section 2) discusses the role of government. Section 3 comments on the purposes and powers of local authorities. Section 4 examines the proposal to confer a power of general competence on local authorities. Section 5 discusses the financial management provisions of the Bill while section 6 comments on the intention to abolish the ratepayer franchise. Section 7 discusses the proposal to recognise the Treaty of Waitangi in the Bill. Section 8 presents our main conclusions. We elaborate on certain of our views in Appendix I.

## **2. The role of government**

- 2.1 The role of government at any level needs to be established on the basis of a proper public policy analysis. The demand for public services will generally be excessive from the perspective of the level and growth of national income because people and groups that lobby for particular services do not face the marginal social costs of the services that they demand. Tightly focused groups are able to obtain services that they value by imposing costs thinly over the majority of ratepayers who face excessive costs in representing their views. The absence of information on the real value to ratepayers of particular services makes it impossible for councils to accurately assess the preferences of

ratepayers. Furthermore, ratepayers are compelled to bear the costs that are imposed on them. Their opportunities to move to a more fiscally attractive territory are constrained.

- 2.2 There are two primary functions of government at any level. They are to maintain order and to provide public goods and services. They have been called the protective and productive states. The former refers to the establishment and the maintenance of a general framework within which all social interactions take place. This protective state entails the enforcement of rules against theft, fraud and the like, and the monopoly use of force to protect citizens from each other and from outsiders. Crucial elements also include the enforcement of contracts and the avoidance of regulations, restrictions and excessive taxation that would unjustifiably restrain voluntary exchange.
- 2.3 When the government performs its protective function well, individuals can have a high level of confidence that they will not be cheated and that the wealth they create will not be taken from them by intruders, or by the government through high taxes or inflation. On the other hand, if private property rights are not clearly defined and enforced, people will be encouraged to engage in harmful activities toward others. Resources will be used inefficiently, such as the excessive exploitation of fish in international waters and the under-utilisation of resources owned in common.
- 2.4 Beyond the maintenance of order, the government might be able to enhance the wealth of its citizens by undertaking or funding productive activities that cannot be organised efficiently through voluntary exchange. Such activities involve the production of public goods and services. A 'pure' public good has both of the following characteristics:
- Non-rivalry in consumption. A good is 'non-rival' when an individual can consume a unit of it without detracting from the consumption opportunities available to other people. Examples of non-rival goods are atmospheric quality and disease eradication programmes.

- Non-excludability of benefits. Goods or services generate non-excludable benefits if it is too costly to prevent access to their benefits by people who do not pay. Examples are defence, flood control and cleaner air arising from pollution control devices.

Very few goods or services exhibit both characteristics.

- 2.5 Public goods and services can often be produced privately. Private firms may produce what at first sight appear to be public goods by charging for them with complementary products. An example commonly cited in the economic literature is that of lighthouses. The benefits of lighthouses are non-rival and non-excludable. It is, however, possible to charge for their services along with port dues. A more relevant example is the provision of lighting in shopping malls. The cost involved is recovered from shoppers through the rents charged to traders.
- 2.6 The non-rival property does not automatically mean that government action is necessary. Many services traded in markets are non-rival in that extra users could be accommodated at little or no additional cost. Surplus capacities at concerts, sporting events and on airlines are possible examples. Firms use a number of techniques to use the capacity available. In particular, they often differentiate levels of associated services and set different prices for each market segment.
- 2.7 The technical definition of public goods is essential to a proper analysis of the role of government. The term 'public good' is commonly used very loosely, for example to imply that a service is of general value to a community. Often local government services are described as public goods or a widespread pattern of benefits is alleged when a careful analysis would reveal that the services have few or no public good characteristics. Used loosely, the term public good becomes no more than an assertion that a particular function should be publicly provided, funded, or both.
- 2.8 The discussion to this point has not distinguished between the functions of central and local government. There are circumstances where the role of the

protective and productive states can most efficiently be undertaken by central government rather than local government, and *vice versa*. Probably the most common circumstances where local government is likely to be more efficient than central government are where local knowledge is required, where the costs and benefits of government action accrue locally, and where appropriate incentives apply at the local level.

- 2.9 Most activities that fall within the protective state are properly undertaken by central government in New Zealand. It has responsibility for defence, police, the criminal and commercial laws, and the courts. Local government has some responsibilities in respect of law and order (eg public nuisances) and its regulatory and taxing activities affect private property rights.
- 2.10 The core function of local government, however, relates to the funding or provision of local public goods. These comprise activities related to such things as democratic, governance and representative processes, civil defence, street lighting and footpaths, open-access parks and reserves, and public health.
- 2.11 On this criterion, the range of council activities is already excessive. The vast majority relate to the provision of private goods and services. Private goods are the polar opposite of public goods. They include the supply of water; refuse, sewerage and waste water collection, treatment and disposal from private properties; libraries; art galleries; museums; recreational facilities where access can be restricted such as swimming pools and halls; and car parking facilities.
- 2.12 The best possible contribution that local government can make to the advancement of the overall well-being of ratepayers and thus to the achievement of the government's broad goals is to undertake its protective and public good roles as efficiently as possible. Any role beyond those will impair overall welfare by reducing individual autonomy and choice and discouraging wealth creation and other activities that are undertaken by individuals, private firms and voluntary organisations. The government's goal of improving the performance of the economy would be put at risk.

- 2.13 ***Local authorities should only be permitted to engage in those activities that fall within the protective and productive states discussed above (and other activities that are incidental to them) and that should be the responsibility of local rather than central government. Such activities should be enumerated in the legislation consistent with New Zealand's constitutional arrangements and the common law.***

### **3. The purpose and powers of local authorities**

- 3.1 The explanatory note to the Bill (at page 1) states:

In the future, local authorities will be clearly expected to be the mechanism by which New Zealanders in their local communities will promote, in a sustainable way, their social, economic, environmental and cultural well-being."

The related clause 8 states:

The purpose of local authorities is to enable local decision-making, by, and on behalf of, individuals in their communities, to democratically promote and action their social, economic, environmental, and cultural well-being in the present and for the future.

The explanatory statement and the related clause, together with the general scheme of the Bill, envisage an extraordinary encroachment of the state on civil society. The scope of local authorities is to be substantially extended in the areas of social, economic, environmental and cultural areas. What classes of activities could possibly fall outside one or more of these headings? According to an article in the *New Zealand Herald*, "The doyen of local government law, Professor Ken Palmer, has joked that the bill is broad enough to allow local authorities to enter the used car business should they wish."<sup>5</sup> Furthermore, we are told that local government "*will be the mechanism*" by which New Zealanders will promote their social, economic, environmental and cultural well-being. As in the Bill, there is little recognition of the roles of individuals, firms and voluntary organisations in promoting social, economic environmental and cultural well-being. Instead a collectivist and statist framework that is the

antithesis of individual freedom, voluntary cooperation and social cohesion is proposed.

3.2 The Bill places undue faith in the capacity of democratic and consultative processes to control the activities of local government. The underlying notion is that democratically elected representatives can be expected to act in the interests of ratepayers and citizens and, if they fail to do so, they will be replaced at the next election. This is a naïve view of political decision making. It fails, for instance, to recognise the vast literature and experience that establishes the need to restrict the activities of government because governments frequently act in the interests of particular constituencies rather than the general public interest.

3.3 Democratic processes at the local government level are weak:

- There is a low turnout at elections.
- An electoral mandate does not necessarily mean that most voters support the particular policies that are promoted by elected representatives or the governing parties.
- Voters have little information about who, or what, they are voting for.
- Mayors and chairpersons may be unable to implement their election commitments.
- Governance and management roles of councils are confused.
- Media coverage of local government activities, elected representatives and candidates is more limited and less questioning than comparable reporting of central government.
- The costs borne by individuals in monitoring the activities of local government (for instance the opportunity cost of their time) are large relative to the expected benefits.

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<sup>5</sup> Julie Chambers and Chris Diack, 'Historic legislation extends grasp of local body octopus', *New Zealand Herald*, 21 February 2001.

- Differential and targeted rating (which would be extended by the Rating Bill) enables councils to impose the costs of their spending programmes on selected classes of ratepayers such as businesses that are entitled to fewer votes than if voting rights reflected the amount of rates paid.
- There are few grounds on which ratepayers can mount a legal challenge to council decisions and the test that must be met for a successful judicial review is demanding.

The weaknesses of democratic processes are discussed further in Appendix I, section 3.

- 3.4 By allowing councils to operate beyond their regions and territories, subject to the weak conditions noted in clause 9(3), the Bill departs from the stated purpose of local authorities. Where a local authority operates beyond its territory or region "democratic decision-making" is not by, and on behalf of, individuals in their local communities but by and on behalf of individuals in another community. The individuals involved could be as far apart as Cape Reinga and the Bluff, and the communities affected could be as different as those of the Auckland central business district and the Chatham Islands.
- 3.5 There is minimal public participation in consultative exercises such as those related to draft annual plans. Moreover, public submissions seem to make little difference to many plans. The Controller and Auditor-General reported that there is a perception that the consultative process is a sham.<sup>6</sup> The Forum's experience suggests that such perceptions are justified.
- 3.6 The Bill extends the range of matters on which the public would be consulted, but it does not address the problem caused by councils consulting on a policy that has been predetermined. Furthermore, some of "the principles relating to local authorities" seem to change fundamentally the focus of local authorities from an obligation *to act in the interests of their residents and ratepayers* (section 122G(a) of the Act) to *the advancement of their priorities and the achievement of their*

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<sup>6</sup> Controller and Auditor-General (1988), *Public Consultation and Decision-Making in Local Government*, Office of the Controller and Auditor-General, Wellington, p 9.

*desired outcomes* (clause 12(a)). Consultation is no substitute for imposing principled limits on the activities of local authorities.

3.7 While the Bill is predicated on the assumption that democratic and consultative processes are sufficient to control councils, the government clearly does not have full confidence in the outcome of such processes. If it did, it would not seek to prohibit the following:

- the transfer of the ownership or control of a local authority water supply or wastewater services to a person other than a council-controlled organisation (clause 129);
- the Auckland Regional Council from selling 15 named parks (clause 127);  
or
- a territorial authority from charging its residents to join its public library (clause 130).

These provisions are unjustified and they are also inconsistent with the claimed move away from prescriptive legislation.

#### **4. The power of general competence**

4.1 The Bill proposes to confer on territorial authorities a power of general competence. This is a key proposal in the Bill which is examined in more detail in Appendix I, section 4. The Bill states (clause 9(2)) that "For the purposes of performing its purpose, a local authority has –:

- (a) full capacity to carry on or undertake any activity or business, do any act, or enter into any transaction; and
- (b) for the purposes of paragraph (a), full rights, powers and privileges."

4.2 The proposed power is intended to diminish or remove the impact on councils of the *ultra vires* doctrine. The effect of the doctrine is to make unlawful the

expenditure of money by a local authority on any object or purpose other than those that are expressly or impliedly authorised by statute.

4.3 The explanatory notes to the Bill (page 2) state that local authorities "will have the same rights and freedom of action, consistent with the general law, as individuals and corporations." The implication that the introduction of a power of general competence is consistent with the power conferred on companies by section 16 of the Companies Act 1993 is misleading for the following reasons:

- No company has the power to impose a tax on its shareholders or the general public. The fundamental issue concerning the powers of local authorities is their right to engage in activities that are funded by taxation.
- A person may choose whether to become a member (shareholder) of a company and can cease to be a member by selling or transferring a shareholding. Every citizen is bound by the lawful decisions of his or her territorial local authority and regional council, and bears rates levied by them either directly as a property owner or indirectly as a renter, consumer, employee or investor.
- A shareholder is protected by a range of specific measures that constrain the actions of companies (for example the interests of minority shareholders are protected by certain provisions) and provide for the monitoring of company management. Those mechanisms are vastly more elaborate and sophisticated than any comparable provisions that would apply to local authorities. The "capacity, rights, powers, or privileges" of a company can, for instance, be restricted through its constitution (section 16(2) of the Companies Act 1993). Notwithstanding any provision in a company's constitution, some proposals, such as a major transaction or an amalgamation, are required to be approved by a special resolution (section 106 of the Companies Act 1993). The democratic equivalent of a special resolution would be a referendum that is supported by 75 percent of electors who are entitled to vote and vote on the resolution (see section 2 of the Companies Act 1993).

- 4.4 The proposal to confer on councils a power of general competence would change a longstanding constraint on local government in New Zealand and would be a threat to liberty and efficiency. The grounds advanced for the proposal in the Consultation Document reflected the lower order argument of providing greater flexibility without any consideration of the constitutional and legal issues involved. What is more, there was no proper discussion of the implications of the proposal. For example, if regional councils are given an effective power of general competence, what is to stop them and territorial authorities from owning bakeries, banks and breweries and subsidising those businesses from rates? No effective provisions are proposed in the Bill that would prevent councils from owning such businesses in the regions or territories of other councils or overseas.
- 4.5 The paramount issue is the extent of statutory powers and privileges that are conferred on local authorities. The protection of liberty and the promotion of efficiency require that councils undertake only those public order, public good and regulatory activities that should be properly performed by government at the local level. The Bill should make that restriction unequivocal by enumerating the public goods that councils may fund or provide. It is appropriate to require additional activities to be added by amending legislation. A power of general competence is inconsistent with the suggested approach.
- 4.6 Regardless of how the courts may interpret an expansion of the powers of councils (see Appendix I), there are no sound public policy reasons for introducing uncertainty, by attempting to change the *ultra vires* doctrine that has applied for over a century, for no demonstrated benefit. Furthermore, the change is being proposed without examining what other changes to governance arrangements might be necessary to compensate for any relaxation in controls over council activities. ***For these reasons, the Forum is opposed to the introduction of a power of general competence.***

## 5. Financial management

5.1 Part VIIA of the Act contains the financial management provisions inserted by the Local Government Amendment Act (No 3) 1996. Those provisions were intended to apply the principles of the Fiscal Responsibility Act 1994 to the local government sector.

5.2 The present financial management provisions reflect compromises that followed from an unsatisfactory debate on the initial proposals. While the adopted provisions recognised the principle of economic efficiency and provide for transparency, the practical outcome has been disappointing. Their deficiencies include the following:

- The thrust of the provisions was to encourage councils to focus on their core (public good) activities and to exit from other activities. The provisions have not achieved that objective. Councils, particularly in the larger centres, have continued to engage in an extensive range of private good activities. The arguments advanced for such activities often reflect a low quality analysis.
- The provisions were intended to raise the efficiency of council operations. Councils have generally been slow to corporatise their business operations and reluctant to contract out services except where they are required to do so, for instance to qualify for funding from Transfund. Councils are required to assess the costs and benefits of significant proposals. An Audit New Zealand director recently reported that very few councils have prepared cost benefit studies.<sup>7</sup> When cost benefit studies are prepared they may have little impact on decision making or consultative processes. The Waitemata waterfront interchange project, better known as Britomart, is an example.
- The provisions were intended to encourage councils to apply more efficient methods of funding. Owing to weaknesses in the legislation,

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<sup>7</sup>

Brian Smith, personal communication, 11 June 2001.

councils have unduly focused on equity issues (the benefit principle) rather than efficiency. Too many councils have sought to justify their existing funding policies in terms of the legislation instead of conducting a first principles examination of such funding.

- 5.3 The Consultation Document stated that the financial management provisions contained in the Act would be retained. It proposed several additional principles. The Bill, however, reflects a different stance. The financial management provisions (Part 5 Subpart 3) have been substantially watered down, thereby reducing transparency and providing councils with greater scope to take decisions that are poorly conceived.
- 5.4 When detailed controls on the level of borrowing were lifted, local authorities were broadly required to budget for sufficient operating revenue to cover projected operating expenses and thereby avoid a projected operating deficit (section 122C(1)(f)). They are permitted to deviate from such policy in a small number of specified ways "from time to time" and "where it is considered on reasonable grounds" prudent to do so after having regard to the principles contained in section 122C(1) and to any other relevant provisions of the Act.
- 5.5 These provisions are to be replaced by clause 81 which, like the present provision, requires a balanced budget in the first instance. However, any local authority would be permitted to resolve, having regard to the matters covered in Part 5 of the Bill, that it is financially prudent to set projected revenues at a different level. Further, such a resolution must not result in a local authority deciding to cease an activity on the sole basis that insufficient cash is available to fund the asset management requirement of that activity.
- 5.6 The thrust of the proposed provision is to make it easier for territorial authorities to forecast operating deficits and thus borrow to fund current operating expenditure. The recent experience of district health boards illustrates how quickly debt can build up if operating expenditure is not funded from operating revenue. No public company could continue to budget for operating deficits and expect to remain in business for long.

5.7 The extraordinary provision in relation to asset management invites councils to plan for continuing deficits by not raising revenue to cover depreciation and maintenance. It reflects a step back to cash accounting and away from accrual accounting. The issue primarily relates to the matching of operating costs with operating revenue and thus the proper reporting of an authority's operating performance. It is only indirectly related to the funding of assets or their replacement.

5.8 The principles contained in clause 82 are substantially weaker than those contained in section 122C(1) of the Act as the following demonstrates:

- Principle (a) in section 122C(1) requires revenues, expenses, assets, liabilities and investments to be managed *prudently in the interests of the district of the local authority or its inhabitants and ratepayers* and only for lawful purposes. This principle is omitted from clause 82 of the Bill. However, under clause 12(h) a local authority "must endeavour" to "ensure prudent stewardship and the efficient and effective use of its resources in the interests of the district or region." This obligation on authorities is far less demanding than principle (a).
- Principle (c) in section 122C(1) requires the costs and benefits of different options to be assessed in determining any long-term financial strategy, funding policy, investment policy or borrowing management policy and in making any decision with significant financial consequences. This principle was intended to require a formal assessment of the costs and benefits of policy and spending proposals. While the principle is to be retained in respect of any long-term plan and in making "any decision with significant financial consequences", costs and benefits are to be "assessed by the local authority" (clause 82(b)). Thus it appears that the discipline of a professional cost benefit assessment is to be dropped by a subtle change in drafting. This would substantially reduce the quality of information available to ratepayers and remove the discipline on councils that comes from the knowledge that a cost and benefit study will be

available to the public under the Local Government Official Information and Meetings Act 1987.

- The present Act provides a structured framework for funding decisions that are guided by the application of principles. Principle (d) in section 122C(1) and related sections lay out the framework and principles. The principle is to be replaced by a looser requirement that six general factors be taken into account (clause 82 (c)). The three-step process that structured funding decisions and made them transparent is to be dumped. The principle of economic efficiency is also to be dropped. As a consequence of what is effectively a 'do you as you please' approach, councils will have vast discretion over funding, transparency will be much reduced and ratepayers will have very limited opportunity to challenge decisions that are doubtful. These changes are to accompany the introduction of a much wider range of rating mechanisms contained in the Rating Bill. The outcome would be an increase in the use of discriminatory rating policies that are politically motivated, a decline in the quality of funding decisions and greater inefficiency.

5.9 ***The Forum submits that the financial management provisions contained in the Bill need to be re-examined to reduce the discretion of councils and to accord primacy to economic efficiency.***

## **6. Non-resident ratepayer franchise**

6.1 The Bill proposes that the non-resident ratepayer franchise be abolished (clause 280). The Forum submits that the non-resident ratepayer franchise should be retained for the following reasons:

- There is a long-established democratic principle that there should be no taxation without representation. This principle is aimed at providing some protection for the minority from the tyranny of the majority. The property owned by non-residents is subject to rates and thus such ratepayers should be entitled to vote, if they so wish. (The situation

might be different if councils were not funded primarily by rates.) What is more, present funding arrangements include discriminatory taxes such as universal charges and differential rates that may bear no relation to the level of public goods provided to the ratepayer or a particular class of ratepayers. This is a further ground for allowing all ratepayers to vote since it may be possible for councils to impose, directly or indirectly, discriminatory taxes on non-resident property if such ratepayers are disenfranchised.

As no person can exercise two votes, the proposal would disenfranchise incorporated businesses. Such businesses pay about half of local authority rates.

- The fact that most non-resident electors have not exercised their right to enrol and vote is not a sufficient reason to withdraw the franchise. It would be regarded as highly undemocratic if residents were denied the right to vote in future on the grounds that they had not voted in the past couple of elections. Given the low turnout in local body elections, many residents would be disenfranchised by such a rule (other things being equal). The right to vote should an issue of sufficient importance to the ratepayer arise is a democratic constraint on the behaviour of councillors (albeit a limited one) whether it is exercised or not. There are few constitutional checks on the powers of local government and to weaken them further would be a step in the wrong direction.
- While non-resident property owners may account for a relatively small proportion of property owners and residents in many local authorities, that is not necessarily true for all authorities (for example the Thames-Coromandel District Council).

## **7. Treaty of Waitangi**

7.1 The Consultation Document indicated that the government had yet to decide whether and, if so, how the Treaty of Waitangi may affect the new act. Thus there was no substantive consultation on the proposals included in the Bill.

7.2 Clause 4 of the Bill states:

To recognise and respect the principles of the Treaty of Waitangi with a view to maintaining and improving opportunities for Maori to contribute to local government decision-making processes, Parts 2 and 5 provide principles and mechanisms to facilitate participation by Maori in local authority decision-making.

A number of clauses make special provision for Maori. Maori would also be preferentially treated in the Rating Bill.

7.3 Local authorities are not directly involved in the settlement process. The parties are the Crown (represented by central government) and Maori. Indeed any obligations that arise under the Treaty rest with central government, at least in the first instance. Central government can request the involvement of local government or it can pass legislation requiring it to take certain actions.

7.4 Provision was made in the Local Electorate Act 2001 for separate representation for Maori. That Act allows local authorities to decide whether to establish separate Maori wards. The Bill amends it. Separate Maori wards and other special provisions for Maori in the Bill and the Rating Bill are undemocratic, divisive, or both. There should be one rule for all citizens. Representative and other arrangements must be fair to all persons.

7.5 The implications of the Treaty of Waitangi for local government are a significant constitutional issue. Any proposal to treat Maori or any other group on a preferential basis should be the subject of a referendum; otherwise it has the potential to be very divisive.

7.6 Although the Bill seeks to "recognise and respect the principles of the Treaty of Waitangi" those principles are not specified in the Bill or elsewhere. Nor is

there any certainty that the courts will interpret clause 4 in the limited context that appears to be intended. Ill-defined references to the Treaty are undesirable.

## **8. Conclusion**

8.1 The Forum's main conclusions are noted below:

- The local government sector is large and its effects are pervasive.
- The sector is massively under-performing. The achievement of the ambitious goals for improving economic growth rates and social indicators set by the government will be impeded unless the performance of the sector is substantially improved.
- The institutional and policy framework within which local government operates is the primary influence on its performance. The overriding objective of the Bill should be to strengthen that framework.
- The concept of limited government is fundamental to the constitutional and legal principles that New Zealand was fortunate to inherit from Britain. An all-inclusive mandate for councils and a power of general competence are inconsistent with those principles.
- The activities that councils may engage in should be tightly circumscribed and enumerated. The deliberate specification of limited powers should be seen as a vital constraint on local government. It would prevent local government from expanding into activities that are not enumerated and thus help protect liberty and promote economic efficiency and growth.
- The best possible contribution that local government can make to the advancement of the overall well-being of the community and thus to the achievement of the government's broad goals is to undertake its protective and public good roles as efficiently as possible.
- Any role beyond those will impair overall welfare by reducing individual autonomy and choice and discouraging wealth creation and other

activities that are undertaken by individuals, private firms and voluntary organisations.

- The Bill reflects unsound principles and should be re-examined afresh.

## **Elaboration of Selected Issues**

### **1 Introduction**

1.1 In this Appendix, the Forum elaborates on selected aspects of its submission. In section 2 the absence of genuine consultation is noted. Sections 3 and 4 expand upon the weaknesses of democratic processes and the power of general competence.

### **2 Consultative process**

2.1 The Forum is exceedingly disappointed at the level of consultation on the review of the Act. The proposals contained in the Consultative Document were "developed in a collaborative way by officials of the Department of Internal Affairs working closely with other Departments and people from the local government sector." The prime minister reported that every cabinet paper relating to the present review was commented on by Local Government New Zealand before the cabinet considered it.<sup>8</sup> In marked contrast, the views of users and ratepayers – the parties most directly affected by local government – have been largely ignored.

2.2 The Forum noted in its submission on the Consultative Document that it expected full and genuine consultation at all further stages of the review, consistent with the prime minister's undertaking that the government would do more to listen to business concerns. Genuine consultation means a process that involves the following steps:

- the gathering of information to test policy proposals;
- presenting proposals for discussion that are not predetermined;

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<sup>8</sup> Clark, Helen (2001a), 'Conference of Local Government New Zealand: Address by Rt Hon Helen Clark, Prime Minister', press release by New Zealand government, 16 July, [www.newsroom.co.nz](http://www.newsroom.co.nz).

- informing interested parties of all relevant information on which the proposals are based;
- seeking analysis and opinion on the proposals;
- examining with an open mind the views of interested parties and being prepared to alter the original proposal in the light of information and argument advanced; and
- providing feedback to interested parties both during the consultation process and after the decisions have been taken.

Several of these steps have not been satisfied. The government clearly had a predetermined view on the Act. It also failed to provide feedback on the outcome of the Forum's submission.

### **3 Democratic processes**

- 3.1 The proposals contained in the Bill place unwarranted faith in the efficacy of democratic processes at the local level. They assume that local collective decision making over a vast range of activities relating to social, economic, cultural and environmental matters is desirable. The proposals are intended to restore "localness" to local government and to enhance its ability to recognise and respond to community aspirations. They are also intended to encourage increased participation of citizens and communities in local government.
- 3.2 The underlying notion is that democratically elected representatives can be expected to act in the interests of ratepayers and citizens and, if they fail to do so, they will be replaced at the next election. This is a naïve view of political decision making as the quotation at the start of this submission implies. It fails, for instance, to recognise the vast literature on the need to restrict the activities of government to preserve liberty and to increase prosperity. James Madison, one of the principal architects of the constitution of the United States, argued that:

... a pure democracy, by which I mean a society consisting of a small number of citizens, who assemble and administer the government in person, can admit of no cure for the mischiefs of faction.<sup>9</sup>

How much worse is that problem when government is larger and citizens are represented by elected councillors?

### 3.3 Democratic processes at the local government level are weak:

- There is a low turnout at elections, despite postal voting which was introduced in 1989 to increase participation. The turnout at the 2001 election was reported to be the lowest in 15 years at about 50 percent.<sup>10</sup> This contrasts with many countries in the European Union where between 60 and 93 percent of electors vote in sub-national elections and with New Zealand's 1999 parliamentary elections where the turnout was 84.7 percent.<sup>11</sup>
- An electoral mandate does not necessarily mean that most voters support the particular policies that are promoted by elected representatives or the governing parties. In exercising their right to vote, electors are required to choose between candidates (or parties) offering a package of policies which may well include some policies that they support and some that they do not.
- Voters have little information about who, or what, they are voting for. In part this reflects the limited role of party affiliations.
- Mayors and chairpersons may be unable to implement their election commitments. They do not necessarily lead the political party or parties with a majority on council or command the support of the majority of councillors.

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<sup>9</sup> Madison, James (1961), 'No 10: Madison' in Rossiter, Clinton (ed), *The Federalist Papers: Alexander Hamilton, James Madison, John Jay*, Penguin, New York, p 81.

<sup>10</sup> Lee, Sandra, reported by Newsroom.co.nz (2001), 'Low Voter Turnout Disappoints', 15 October, [www.newsroom.co.nz](http://www.newsroom.co.nz).

<sup>11</sup> Stewart, John (1996), 'Democracy and Local Government', in Hirst, Paul and Khilnani, Sunil (eds), *Reinventing Democracy*, Blackwell Publishers, Oxford, pp 41-42 and information supplied by the Electoral Office.

- Governance and management roles are confused. Cabinet ministers are advised by a largely independent public service that is expected to provide frank advice. There is no similar tradition in local government, where there is insufficient separation between the governance function of elected representatives and the operational responsibilities of local government officials.
- Media coverage of local government activities, elected representatives and candidates is more limited and less questioning than comparable reporting of central government.
- The costs borne by individuals in monitoring the activities of local government (for instance the opportunity cost of their time) are large relative to the expected benefits. There is minimal public participation in consultative exercises such as those related to draft annual plans. Moreover, public submissions seem to make little difference to many plans. The Controller and Auditor-General reported that there is a perception that the consultative process is a sham.<sup>12</sup>
- The adoption of differential rating has enabled councils to impose the costs of their spending programmes on certain classes of ratepayers such as businesses that are entitled to fewer votes than if voting rights reflected the amount of rates paid.

3.4 Many people are disillusioned with politics at all levels, and want to have as little as possible to do with the political process. As a result activists and special interest groups unduly influence council policies. A 1998 opinion poll that included questions supplied by Local Government New Zealand found that only 17 percent of people agreed that the average person has a great deal of influence on local government decisions whereas 76 percent disagreed with the statement. Moreover, 69 percent agreed that the public has little control over

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<sup>12</sup> Controller and Auditor-General (1988), *Public Consultation and Decision-Making in Local Government*, Office of the Controller and Auditor-General, Wellington, p 9.

what politicians do in office compared with 25 percent who disagreed.<sup>13</sup> There are no proposals in the Bill that give confidence that the widespread disillusionment with politics will reduce. Yet the thrust of the Bill is to extend the mandate of councils.

- 3.5 The reality is that most of the goals and preferences of citizens are best achieved by private means – not by political means as the explanatory note to the Bill seems to imply. The individual who chooses between candidate A and B in the polling booth is the same as the individual who chooses between apples and oranges. However, voluntary exchange provides a better indication of people's true preferences than voting because individuals are required to trade one thing (for instance a sum of money) for another (apples). The relevant difference between political and voluntary exchange decision mechanisms does not lie in the kinds of values and interests that people pursue, but in the means by which they are able to pursue their various interests.

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<sup>13</sup> Local Government New Zealand (1999), 'New Zealand Values Survey', 8 March, [www.localgovt.co.nz](http://www.localgovt.co.nz).

- 3.6 The challenge is to establish an institutional framework that enables government at any level to operate efficiently where it is necessary to advance overall welfare but beyond that to maintain the maximum possible opportunity for individuals to pursue their interests. Reliance on majority rule is not sufficient.
- 3.7 Central government is responsible for setting and evaluating the framework within which local government operates. The framework should be improved in the new act. More effective checks and balances are required.
- 3.8 New Zealand's constitutional arrangements do not envisage local democracy limited only by popular vote. Local authorities in New Zealand have never been empowered to undertake whatever activities a majority of voters or elected representatives might like councils to do. Councils may only exercise the powers that are conferred by parliament. Moreover, those powers are limited further by common law (see below). For instance, no council (or individual) can impose taxes or unilaterally alter private property rights without statutory authority to do so.
- 3.9 Limited government is required to protect liberty. For the good of society individuals cede some of their rights to the government. It is not for the government to take whatever rights it might like and leave the rest to individuals as the democratic theory advanced by some seems to imply.
- 3.10 The powers of local authorities must be conferred by statute or be incidental to such powers. Consistent with this approach the activities that councils may engage in should be enumerated and tightly circumscribed as suggested above. The deliberate specification of such limited powers is a vital constraint on local government just as the enumerated powers in the constitution of the United States limit the powers of the federal government.
- 3.11 The key solution to the shortcomings of local democracy is to depoliticise activities that do not need to be undertaken collectively. This would enable the number of local authorities to be reduced and for those that remain to be tightly

focused on valid public good and regulatory activities. Beyond this, robust checks and balances on the activities of councils are required.

## 4 Power of general competence

4.1 The prevalence of the power of general competence in countries of the European Union reflects sub-national levels of government that were created by constitutions rather than statute.<sup>14</sup> In contrast, local authorities in New Zealand, like those in Britain, are creatures of statute and are subordinate to central government.<sup>15</sup>

4.2 The proposed power appears to be an attempt to change the existing law by diminishing the impact on councils of the *ultra vires* doctrine. That doctrine arose from mid nineteenth century decisions of the courts concerning the scope of the powers of new joint stock railway companies. It was apparently applied to local authorities because they happened to be incorporated bodies operating under statute.<sup>16</sup>

4.3 The effect of the doctrine is to make unlawful the expenditure of money by a local authority on any object or purpose other than those that are expressly or impliedly authorised by statute. As Palmer observed:

Understandably the courts were concerned to safeguard commercial and private property rights, and to curb an over-zealous exercise of powers. The courts assumed that Parliament did not intend subordinate bodies or authorities to possess plenary powers or unlimited discretions as to activities, where affecting the rights of other persons and property.<sup>17</sup>

4.4 Commenting in the context of the Britain, Loughlin wrote:

The *ultra vires* doctrine, which provides the cornerstone of our modern local government law, is now under threat. Many have come to view the doctrine as expressive of the restrictive nature of contemporary

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<sup>14</sup> Stewart (1996), *op cit*, pp 41-42.

<sup>15</sup> Historically, corporations created by royal charter were assumed to have general powers of competence. However, no charter corporations of local authorities exist in New Zealand.

<sup>16</sup> Loughlin, Martin (1997), 'Ultra Vires: Hail and Farewell', in Kitchin, Hillary (ed), *A Framework for the Future: An Agenda for Councils in a Changing World*, Local Government Information Unit, London.

<sup>17</sup> Palmer (1993), *op cit*, p 46.

arrangements of local government and have indicated that its removal and replacement with a power of general competence provides the key to the rejuvenation of local government.<sup>18</sup>

A commission for local democracy, the Labour Party and a House of Lords committee on the relationship between central and local government were reported to have come to this conclusion. Although the concept of general competence seemed to have acquired the "symbolic status of a universal, principled, cost-free, progressive policy stance", Loughlin warned that it must not be assumed that those who embrace the reform have a clear grasp of its nature and significance.<sup>19</sup>

- 4.5 Loughlin's warning is relevant to New Zealand. Despite the proposed removal of the doctrine, which is also the cornerstone of New Zealand's local government law, the Consultation Document contained no substantive analysis of the reasons for the change or its likely effects. It did not identify a solitary product, service or activity that one of the 86 regional, territorial or unitary councils or 148 community boards would like to supply or undertake, and is a valid activity for local government, but is prohibited from doing so by the present law.
- 4.6 Stewart's conclusion, that the view that statutory restrictions were constraining local authorities in Britain was a myth, may also hold for New Zealand.<sup>20</sup> However, unlike New Zealand, local government spending in Britain is subject to an expenditure cap.<sup>21</sup>
- 4.7 Loughlin notes that that English boroughs created under charter were "persons" at common law. Yet in interpreting the Municipal Corporations Act 1882, the courts held that boroughs could exercise the powers of an ordinary person only in so far as expenditure from the borough fund was not involved. Moreover,

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<sup>18</sup> Loughlin (1997), *op cit*, p 1.

<sup>19</sup> *Ibid*, pp 1-2.

<sup>20</sup> Stewart, J D (1983), *Local Government: The Conditions of Local Choice*, London, cited by Loughlin (1997), *op cit*, p 8.

<sup>21</sup> In terms of the Rating Powers Act 1988 a territorial council may not levy a general rate in excess of 1.25 cents in the dollar of capital value (or the equivalent level in the case of land value) or 18 cents in the dollar of annual value. The limit on the maximum rate has been omitted from the Rating Bill. Controls on the activities of councils should focus on their functions and spending rather than the level of rates.

nothing in their status as persons authorised them to interfere with private property rights.

- 4.8 Even if the *ultra vires* doctrine had not been devised, the intrinsic powers of local government would still be limited because such limits are a consequence of Britain's basic constitutional arrangements. According to Loughlin, this is highlighted by distinguishing between *powers* and *privileges*:

... no person – whether an incorporated body or an ordinary person has any privileges other than those which are accorded by the operation of the law.<sup>22</sup>

Jennings, a distinguished British constitutional lawyer, is reported to have made the point in 1931 in the following terms:

Neither a railway company nor I may commit nuisances without express statutory authority. Neither a local authority nor I may tax inhabitants of a given area except with the consent of Parliament, even though our object be to bring untold benefits to those inhabitants. A local authority has no right to use rates to start a new service unless it can show statutory sanction. And this rule is not a nineteenth century innovation. It is almost as old as Parliament.<sup>23</sup>

- 4.9 This vital principle seems to have been overlooked in the debate in New Zealand.<sup>24</sup> However, the guidelines on legislation produced by the Legislative Advisory Committee acknowledge the role of the common law and the courts in protecting individual freedom and property rights.<sup>25</sup>
- 4.10 The power of councils under section 37L(4) of the Act appears to reflect many of the aims of the power of general competence proposed in the Consultation Document:

Every council and every territorial authority shall be a body corporate with perpetual succession and a common seal, and, subject to this and any other

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<sup>22</sup> Loughlin (1997), *op cit*, p 5.

<sup>23</sup> Jennings, W I (1931), *Local Government in the Modern Constitution*, London, cited by Loughlin (1997), *op cit*, p 5.

<sup>24</sup> See Jansen, Ross (2000), 'Local Government and the Power of General Competence', paper presented at the Building the Constitution conference, 7-8 April, Institute of Policy Studies, Wellington and Hewison, Grant (forthcoming), *A Power of General Competence – Should it be Granted to Local Government in New Zealand?*, TNT Publications, Oneroa.

<sup>25</sup> Legislative Advisory Committee (2001), 'Guidelines on Process and Content of Legislation', 2001 edition, Ministry of Justice, Wellington, [www.justice.govt.nz/lac/index.html](http://www.justice.govt.nz/lac/index.html).

Act, shall be capable of acquiring, holding, and disposing of real and personal property, of entering into contracts, of suing and being sued, and of doing and suffering all such other things as bodies corporate may do and suffer.

The empowering words of the subsection are qualified by the clause "subject to this and any other Act" which is similar to that proposed in clause 9(4). As Palmer notes:

... the preferred conventional legal view is that the section is enabling only. Accordingly, the substantive powers of a local authority to carry out works and engage in functions and activities should be found in other provisions. The ultra vires doctrine remains applicable.<sup>26</sup>

- 4.11 Crawford concluded that if the power of general competence were conferred on local authorities:

The most that would change is the presumption of legality, and it is not a fundamentally different concept. Indeed, ... in relation to Scandinavian jurisdictions, while operating within the principle of the power of general competence it is possible to have very tight restrictions.<sup>27</sup>

The courts could also be expected to circumscribe a power of general competence. Councils would be required to act in good faith and reasonably in exercising their discretionary powers as they are required to act today. These requirements arise from the common law.

- 4.12 Despite the apparent support of the Labour Party and some official commissions for the introduction of a power of general competence, no such power has been adopted in Britain.<sup>28</sup>
- 4.13 The activities of the London Borough of Hammersmith and Fulham provide a stark example of the potential cost to ratepayers if the government were successful in conferring the full powers and privileges of a natural person on local authorities. From December 1983 the Borough entered into numerous interest rate swap contracts with banks. It subsequently lost about £200 million (or about NZ\$650 million at today's exchange rate). Not surprisingly, legal

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<sup>26</sup> Palmer (1993), *op cit*, p 18.

<sup>27</sup> Crawford, C (1992), 'European Influence on Local Self-Government, LGS, vol 18 (1), cited by Loughlin (1997), *op cit*, p 6.

action involving the Borough, its auditor and the banks followed to determine which entity should bear the losses. The House of Lords held that the local authority had no power to speculate with the public's money and it could not therefore lawfully trade in interest rate swaps, whether for speculative or debt management purposes. As a result of its decision, the ratepayers of the Borough escaped liability for a loss that amounted to over NZ\$4,000 a head.<sup>29 30</sup>

- 4.14 Elected representatives are responsible for liquor licensing trusts although they are not local authorities. Those trusts have broad powers and are subject to weak accountability arrangements. Liquor licensing trusts have a history of poor earnings and financial difficulties. Subject to the objects specified, such trusts have all the rights, powers and privileges of natural persons. Some licensing trusts have engaged in activities other than their core business of the

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<sup>28</sup> Martin Loughlin, professor of public law, London School of Economics, personal communication, 21 July 2001.

<sup>29</sup> Davies, Rachel (1991), 'Council's Swaps are Unlawful', FT Law Reports, *Financial Times*, 29 January, and Loughlin (1997), *op cit*, p 11.

<sup>30</sup> Local authorities in New Zealand are permitted by section 122ZB of the Act to enter into an "incidental arrangement" in New Zealand currency to manage, reduce, share, limit, assume, offset or hedge financial risks and liabilities in relation to any investment (or investments) or loan (or loans). However, an authority could not lawfully engage in transactions similar to those undertaken by the Borough of Hammersmith and Fulham.

sale and supply of liquor and related activities like the provision of accommodation, food and refreshments. Their non-core businesses include travel services, tourism promotion, redevelopment of property (providing a service station, video outlet, retail shops and car parks) and investment in breweries. Particularly unsuccessful ventures funded wholly or partly by licensing trusts are understood to include attempts to obtain radio, television and casino licences.

- 4.15 The paramount issue is the extent of statutory powers and privileges that are conferred on local authorities. As argued above, the protection of liberty and the promotion of efficiency require that councils undertake only those public order, public good and regulatory activities that should be properly performed by government at the local level. The Bill should make that restriction unequivocal by enumerating the public goods that they may fund or provide. Councils should be required to identify spending on each public good activity in their reports to ratepayers. A power of general competence is inconsistent with the suggested approach.
- 4.16 There are no sound public policy reasons for introducing uncertainty, by attempting to change the *ultra vires* doctrine that has applied for over a century, for no demonstrated benefit. Furthermore, the change is being proposed without examining what other changes to governance arrangements might be necessary to compensate for any relaxation in controls over council activities. For these reasons, the Forum is opposed to the introduction of a power of general competence.

## **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 mainly business organisations that have a vital interest in the activities of local government. The following organisations are members of the Forum:

- Business New Zealand
- Federated Farmers of NZ (Inc.)
- New Zealand Business Roundtable
- New Zealand Forest Owners' Association Inc.
- Property Council of New Zealand Inc.