

LOCAL GOVERNMENT FORUM

**SUBMISSION ON THE WELLINGTON
CITY COUNCIL'S DRAFT ANNUAL
PLAN 2002/03**

MAY 2002

WELLINGTON CITY COUNCIL'S DRAFT ANNUAL PLAN 2002/2003

1 Introduction

- 1.1 This submission on the Wellington City Council's draft annual plan 2002/2003 (the Plan) is made by the Local Government Forum (the Forum). The Forum comprises business organisations listed at the back of this submission that have a vital interest in local government. Its members are among the Wellington City Council's largest ratepayers.
- 1.2 In submissions over the past few years, we have called on the Wellington City Council (the Council) to focus on its core business, exit from other activities and implement more efficient funding arrangements. By focusing on its core activities the Council could cut expenditure and rates, which we believe is an essential step towards making Wellington an attractive place for business. In turn, only a vibrant business sector can underpin and sustain the general welfare of the community.
- 1.3 It is clear from a reading of the latest annual plan that there remains a large gulf between the views of the business sector and the Council. The Council has not moved to restrict its activities over the past five years, and no further progress is made in the current plan.
- 1.4 Last year we conveyed to the Council our belief that past consultations had not been meaningful and that business sector views had not been given significant weight. We therefore chose not to prepare a submission on last year's annual plan.
- 1.5 This year in response to the Council's stated commitment to carefully consider our views, the Forum has decided to participate in the annual planning process. The responsiveness of the Council to our submission will determine whether we participate in future.

2 Local government's comparative advantage

- 2.1 Essential to the objective of reducing expenditure and rates is confining the Council to activities where it has a comparative advantage. Defining the role of the Council involves determining which activities are best undertaken by households, firms and voluntary organisations and which are best funded or undertaken by the Council. For most goods and services, private production is the most efficient option.
- 2.2 The prime justification for government involvement at any level is that public goods might be under-provided by the private sector, or that the existence of significant externalities might lead to under- or over-provision. Governments have a role regulating private activity when this can improve economic outcomes.
- 2.3 The focus of local as opposed to central government should be on the performance of the regulatory functions conferred on it by central government and the provision of local public goods – public goods which provide benefits to residents of a particular territory or region. Before local government funds or provides local public goods it should demonstrate that the benefits of supply exceed the costs, and that the Council is the best party to provide or fund such outputs.

- 2.4 Governments are legitimately concerned with fairness (equity) issues. In our view, central rather than local government is generally best placed to address equity issues – local government has little information on the income and/or wealth of ratepayers.

3 Funding the Council's activities

- 5.3 The overall level of Wellington City Council spending and its rates burden are far too high. The following table compares total expenditure by 10 of the largest councils in New Zealand.

Total Expenditure	1995/96	1996/97	1997/98	1998/99	1999/00
Auckland City	348,008	576,388	317,149	335,220	343,108
Christchurch City	192,823	205,257	224,030	218,225	231,169
Dunedin City	105,081	192,499	122,430	105,596	110,684
Hamilton City	87,054	88,295	80,994	88,884	100,837
Hutt City	70,876	82,771	77,458	75,955	75,469
Manukau City	156,361	153,411	176,833	194,726	199,755
North Shore City	98,613	115,553	119,497	127,966	137,640
Tauranga District	52,270	57,383	64,568	67,966	69,501
Waitakere City	97,951	113,153	109,725	142,748	133,879
Wellington City	225,093	224,503	261,907	214,652	226,195

Source: Statistics New Zealand

Wellington City and Waitakere City have similar populations yet total expenditure in Wellington was \$226 million in 1999/00 compared with \$134 million in Waitakere. Wellington City's expenditure is similar to that of Christchurch yet Christchurch has nearly twice the population. This expenditure pattern is reflected in rates. Waitakere and Christchurch are often regarded as big spending 'people's republics' yet Wellington's ratepayers are hardest hit of all. We are well aware that a range of factors needs to be taken into account in drawing conclusions from such comparisons but Wellington's status as a high spending, high rating council is clear-cut.

- 5.3 In this year's plan, net operating expenditure is forecast to increase by around 11 percent. The proposed rates rise is 4 percent despite the Council using surplus funds from previous years and under-funding depreciation (ie running down the Council's equity). Without these actions the rates rise would be over 6 percent. The local economy is not growing at this rate so the council is accounting for an ever-growing share of it, squeezing the private sector. Far from congratulating itself, the Council should acknowledge its abysmal failure to control expenditure.
- 3.3 The excuse that some expenditure is out of the Council's control is not acceptable. We are aware that the current budgetary difficulties stem in part from dubious past commitments. Like a firm or a household in the same situation, however, the Council must reduce spending in other parts of the budget in response. There should also be a vigorous effort to get costs down. Employment expenses should be one focus of attention. While comparisons can be distorted because of a differing mix of services, the

figures contained in Annex I suggest that the Council's average staff costs are well above those of other major local authorities.

- 3.4 There are many other ways in which spending could be cut and/or rates reduced. The Council should not provide private goods, but if it does it should fully fund them from user charges. User charges help ensure that the Council only provides goods to the extent that users value them by as much as or more than the cost of production. Charging can therefore help ensure the Council provides the optimal level of service.
- 3.5 Where an identifiable group benefits from particular Council services, levying charges on those beneficiaries may be efficient if it helps ensure that the appropriate level of service is provided.
- 3.6 Where it is not economic to fully recoup the costs of a service from user charges and use-related fees and levies, and the benefits from a service exceed its costs, rate-based funding should apply. In levying general rates, there is no justification for differentiating between residential and commercial ratepayers.
- 3.7 The Council's decision to reduce the differential between commercial and residential ratepayers over a 10-year period is positive for business and the local economy. However, the Forum believes that the Council should reduce the differential to zero over a three-year period. Implementation of our other recommendations should allow this to be achieved without imposing an undue burden on residential ratepayers.
- 3.8 We note that a number of other councils have no differentials for their general rates and that others are moving to eliminate them. The long adjustment period proposed by the Council means that commercial businesses will continue to pay millions of dollars in excessive rates. In effect, business owners who are poorly represented at the ballot box are being forced to continue to subsidise services demanded by residential voters. This is neither fair nor efficient. The owners of commercial property range from self-employed people struggling to earn an adequate income to large companies whose shareholders include many, such as retired people, with limited income. Firms exposed to international competition cannot pass on the cost of rates in higher prices but must absorb such costs or relocate or close their businesses.
- 3.9 We do not favour discriminatory treatment of different categories of business and support the Council's decision to include utility rates in the total rates raised from the commercial sector. From a business perspective the focus should be on the total level of business rates.
- 3.10 The Forum is opposed to any increase in the level of rates. Polling by the *Evening Post* prior to the local government elections last year indicated that rates and Council spending were among the issues considered most important by Wellington residents. Residents clearly indicated that they wanted rates increases to stop and better management of Council finances.¹ Both commercial and residential ratepayers are in agreement on this matter. The Council should undertake a zero-based review of its spending programmes, if necessary using outside consultants as Auckland City did recently.

¹ *Evening Post*, 25 March 2002.

4 Business and the community

- 4.1 The Council will be well aware of the trend for many Wellington businesses to move their head offices to Auckland or offshore. Other businesses are reducing costs (including employment) in order to survive. The downsizing of business activity represents a major risk for the Wellington community. Although some changes are driven by external considerations, for others the cost of doing business in Wellington is an important factor.
- 4.2 Council policies which adversely affect businesses also negatively affect the community. As businesses move from Wellington, jobs are lost and families are forced to shift out of the area. The local economy is weakened, opportunities for Wellington people shrink and the best and brightest seek better job and earning prospects elsewhere.
- 4.3 Wellington has been one of the worst performing regions over the past five years in terms of GDP per head.² A study commissioned by the Wellington Regional Council indicated that growth in the region over the past year had been 0.5 percent, down from almost 4 percent 18 months ago.³ Over the year to March 2002 the unemployment rate in Wellington has gone up from 4.5 percent to 5.8 percent. The Council's operations affect economic activity in the region and these figures should be of concern to it. In turn, underperformance by a major region will be a drag on New Zealand's prospects of regaining its former position in the OECD income rankings.
- 4.4 Our strong and consistent contention is that the best way the Council can improve the business environment and retain and attract businesses is to focus only on core public good activities, cut its spending and rates, minimise regulatory burdens and ensure the provision of efficient infrastructure.
- 4.5 Taxing all ratepayers to selectively benefit some businesses does not increase economic activity in Wellington. Nor do we believe that the Council can pick winners ('business clusters') that are particularly worthy of ratepayer funding. We therefore urge the Council to scrap the proposed allocations to the economic development agency (\$2 million) and Totally Wellington (\$3.1 million). Business rate reductions are preferred to selective hand-outs.
- 4.6 We believe that businesses can organise and fund such activity themselves if they believe they will benefit from them. An example of such an approach is the Priorityone initiative in the Western Bay of Plenty. Priorityone is an incorporated society established by the Western Bay of Plenty business community to encourage economic development in the region. Although the local council supports the initiative, it is largely funded and run privately.

5 Exiting from non-core activities

- 5.1 We continue to strongly believe that Council should exit from commercial activities. These include:

² *Evening Post*, 11 February 2002. Ganesh Nana of BERL is quoted as saying that Wellington and the Hutt performed so poorly that he was hesitant to divulge their exact ranking.

³ *The Dominion*, 27 February 2002.

- the Council's shareholding in Wellington's airport. The Auckland City Council is selling its airport shareholding. A competent scoping study should be undertaken as a first step;
 - its ground leases;
 - the Evans Bay marina and the Clyde Quay boat harbour;
 - the Wellington Festival and Convention Centre;
 - off-street parking facilities; and
- 5 waste disposal facilities.

Such asset sales would be financially beneficial for the Council. Sales at prices reflecting the capitalised value of the assets would allow reductions in debt servicing costs that exceed current revenue streams and contribute to rate reductions.

- 5.2 The Council should divest the bulk of its rental housing stock. The private market is able to supply accommodation for most people, including those on low incomes. The problem of income inadequacy, which is a responsibility of central government, is better addressed through income supplements than the provision of subsidised housing.
- 5.3 The Council should divest its interest in the CitiOperations unit. Exposure of the unit to increased competition has already provided benefits. Privatisation would cement in those benefits by ensuring a level playing field for all operators.

6 'Club' goods

- 6.1 The Council should not, in general, be involved in the provision of private or club goods. Unlike a public good, people who do not pay can be excluded from obtaining a club good. A club good shares some characteristics with a public good in that as long as there is excess capacity, the use of a club's facilities by one member does not significantly detract from its use by other members. Activities such as art galleries, museums, the zoo, swimming pools and dedicated sports facilities are examples of facilities that provide club goods.
- 6.2 The Council should look to divest services with club characteristics. Where it retains ownership, it should move to full or near full user charges since users of the services are clearly the main beneficiaries. People who use swimming pools or libraries clearly benefit from them far more than people who do not. Where users are not prepared to cover the costs through user charges, this is a clear signal that the activities should be downsized or no longer provided.
- 6.3 The subsidy from ratepayers to users of galleries and museums is equal to 100 percent of the cost. For users of swimming pools the subsidy is 53 percent, for the zoo it is 62 percent and for recreation centres it is 72 percent. These subsidies are well beyond the levels that could possibly be justified on valid public policy grounds. Subsidies should be limited to the level supported by careful policy analysis. They should be explicit and should also be offered to private providers of closely substitutable services.
- 6.4 The Council should not subsidise Te Papa (around \$2 million of funding is proposed). As a national museum Te Papa should be funded largely by central government and

(probably to an increased extent) user charges. Continued subsidisation by the Council only facilitates free riding by the users of the museum on the payments of others.

- 6.5 The suggestion that visits to the museum should be subsidised because the museum attracts visitors who spend money in Wellington (a figure of \$208 million in 1999 is quoted in the draft plan) is flawed for a number of reasons. Most of the visitors would come to Wellington without the Council contribution. Ratepayers who would be left with an extra \$2 million of money would be likely to spend much of that in the local area, providing similar 'multiplier' effects. In fact, the benefits of leaving the money with residents are likely to be greater given the distortions and costs created by rate funding. In any case, counting the entirety of spending grossly overestimates the benefits, since it is value added (the value of what is spent less the costs of producing goods and services consumed) which is relevant.
- 6.6 The Council's libraries constitute a significant activity and cost to the Council. The operating cost of the central library is forecast to be \$8.1 million (net) with the suburban libraries adding another \$4.6 million (net) in operating costs. In addition, the central and suburban libraries account for nearly \$4 million in total capital expenditure. Around 90 percent of the funding of the libraries comes from ratepayers' money. The total net expenditure on libraries constitutes almost 8 percent of the Council's total net operating expenditure for 2002/03. The Council should consider carefully whether it is funding library services efficiently and fairly and providing the right level of output. We believe moves towards a greater level of 'user pays' are justified on both equity and efficiency grounds. Further argumentation and suggestions for policy changes are contained in an annex.

7 The Council's core activities

- 7.1 Divesting its non-core activities would allow the Council to focus much greater attention on its core activities. One area that would benefit from closer Council attention is its water and wastewater distribution activities.
- 7.2 The Council has long discussed options for its water and wastewater distribution businesses but has achieved very little. Little information is provided in the plan on these activities, which constitute major businesses. It is not clear whether adequate maintenance is being carried out, or whether the Council is delivering the services preferred by consumers. We believe that a thorough review by the Council would confirm our view that the best option for the Council is to divest or franchise the operation of these activities (with or without the cooperation of other councils) to the private sector.
- 7.3 The Council should cease its domestic recycling programme (net costs of around \$1.5 million) unless these costs are less than the costs of disposing of the waste.
- 7.4 Roothing is a core Council activity. It is pleasing that the Council has not adopted the anti-car attitude displayed by the Wellington Regional Council. We support the Council's objectives of increasing the efficiency of the transport network through Wellington to reduce congestion and ensuring that existing roads are maintained in good order.
- 7.5 The provision of open spaces, parks, waterfront open spaces and enhancements to public areas (including the beach at Oriental Bay) is core Council business. However, in

providing such amenities, it is important that the Council conduct careful cost benefit analyses to ensure that ratepayers' money is wisely spent.

- 7.6 In the case of Lambton Harbour, the Council does not need to be involved in property development to achieve its public good objectives. It should be able to contract for the outputs it desires. Of course, the opportunity cost of open space in the city is very high (namely the value of the land that would otherwise be available for development) so careful consideration must be given to optimising the balance between public and private use. The fact that some of the costs of providing public spaces are covered by the return from commercial development does not change the fact that the total cost of providing public spaces in the waterfront area is very high.

8 Conclusion

Council spending and rating policies, including the commercial differential, are depressing the Wellington economy and making it an unattractive environment to do business. This is evidenced by the inferior growth and employment statistics and the out-migration of businesses. A major rethinking of policies is required. We are pleased that the Council has indicated that it wants meaningful consultations with the business community on its plans and we have responded accordingly. We seek a substantive engagement on our submissions and follow-up explanations and dialogue on points of disagreement.

Annex II

Library Services

Despite the provision of virtually 'free' services, around 35 percent of residents are not active users of the library. Nevertheless, they are forced to subsidise others who use the libraries. The case for a 90 percent subsidy of library services on public good or equity grounds is weak. Those who use the services benefit most from them. Businesses in particular should not be forced to subsidise library services.

The spillover benefits to the public from "better-informed and educated" individuals as a result of their library use is likely to be small given the availability of free education and alternative sources of information. A variety of other activities create similar benefits eg individuals reading books, newspapers or magazines they have bought, or watching informative television programmes, or accessing the Internet, yet these activities are not subsidised by local government.

Library services do not constitute a true public good because it is possible to exclude non-payers from entering the library. However, providing library services involves large fixed costs (buildings and the collections), with relatively low marginal costs of use. Arguably, there is some degree of non-rivalry in consumption (ie one person's use of the library does not detract from another's use up to a point), particularly for browsing of books although less so for borrowing books. While the Council has systems in place for controlling the issue of books, it currently does not have, and may not wish to have, arrangements that would prevent people from browsing the library collections.

This suggests that the Council could reduce ratepayer funding by moving to a fairer and more efficient charging regime as follows. Those who wish to borrow books, CDs etc, should desirably pay an annual fixed fee (this would require a change to legislation which the Council could promote) and a charge per item borrowed. This would ensure that those who make the greatest use of the library make the greatest contribution towards its costs. The willingness of individuals to pay for such library services would give the Council much better guidance as to the value placed on its use by ratepayers. Access to the library for browsing and reading books in the library could remain free, at least initially, meeting many of the Council's objectives for 'community' and education benefits.

Equity considerations might constitute another possible reason for subsidising library services. However, such considerations do not justify wholesale subsidisation but rather targeted assistance to low income individuals. Present arrangements are likely to subsidise people who are better educated and on higher incomes more than those on low incomes.

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. The following organisations are members of the Forum:

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