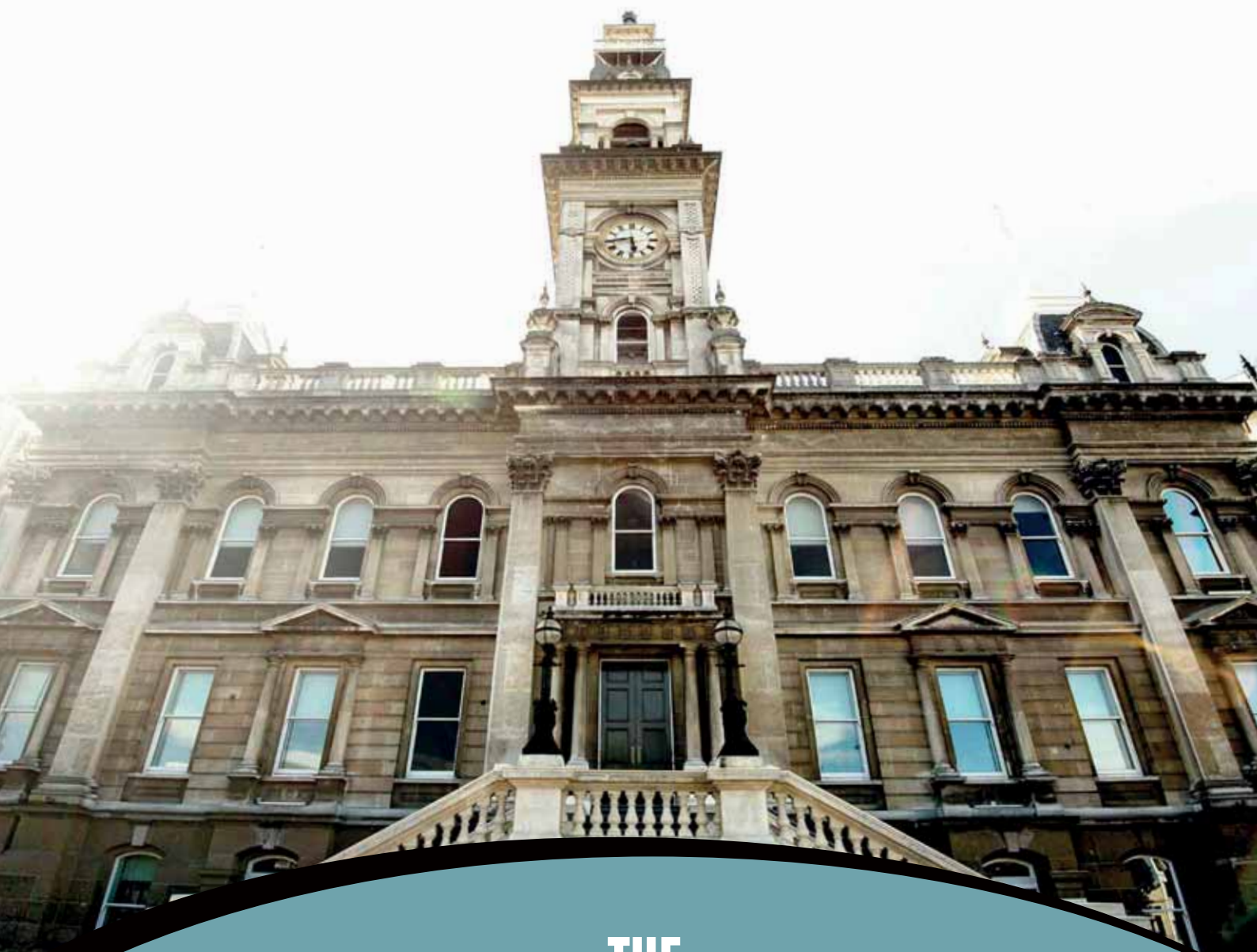


THE LOCAL MANIFESTO

RESTORING LOCAL GOVERNMENT ACCOUNTABILITY

JASON KRUPP

FOREWORD BY RODNEY HIDE



**THE
NEW ZEALAND
INITIATIVE**

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2016

The New Zealand Initiative is an independent public policy think tank supported by chief executives of major New Zealand businesses. We believe in evidence-based policy and are committed to developing policies that work for all New Zealanders.

Our mission is to help build a better, stronger New Zealand. We are taking the initiative to promote a prosperous, free and fair society with a competitive, open and dynamic economy. We develop and contribute bold ideas that will have a profound, positive, long-term impact.



ARROWTOWN

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AUCKLAND

FOREWORD

Local government for most of us is the sharp end of government. It's local government that decides where and when we can do our business and what we can and can't do in our homes.

We are also more acutely aware of what local government costs us in rates compared to central government where the much greater cost is hidden in PAYE and GST.

It's little wonder that it's local government that bears the brunt of our criticism of government. The response has been a continual attempt to reform and improve local government.

Jason Krupp challenges us in his report that the solution to the problem of local government is not the present trend of fewer councils but more, not a local government that does less but one that does more.

It's both a challenging and enticing report, especially to those of us who favour diversity, choice and competition over the rhetoric of uniformity and consistency.

The idea of local government truly responding to the needs and desires of a community is appealing, along with the prospect of readily shifting jurisdictions for both living and business purposes should a local government become excessively oppressive, inefficient or poor in providing services.

Mr Krupp shows we can have the benefits of choice and competition in government, just like with everyday goods and services.

Mr Krupp's proposal comes with an important caveat. It's essential for accountable government that the costs and benefits of decisions made on behalf of others be aligned to the jurisdiction where the decisions are made, and that the roles and responsibilities of the different tiers of government be clearly spelled out, understood and respected.

That is far from the case at present. Mr Krupp makes plain that the present lines of responsibility and accountability are hopelessly blurred. I suspect the blurred lines are favoured by politicians precisely

for the reason Mr Krupp finds them disagreeable: they enable politicians to dodge proper scrutiny and accountability. The interests of politicians and citizens seldom align, which is another reason Mr Krupp's report is so refreshing and pertinent.

Mr Krupp presents a big picture and a bigger challenge for the place of local government within New Zealand.

He also provides other telling insights to inform policymaking and improve local government.

For example, it's novel to suggest that communities be given the opportunity to 'opt out' of national standards where the communities don't believe the benefits over the costs and risks justify the standard's application to them. It's crazy that central government makes the same national standards and systems apply to Wairoa with 8,000 residents and Auckland with 1.4 million.

Mr Krupp also suggests incentivising councillors and councils with performance pay to measure and reward good performance, a concept totally foreign to the operation of our local government. If local government is important, then its performance should be measured and rewarded.

There's the big picture, the direction for local government, and wonderful policy titbits in the report.

Mr Krupp provides a challenging and excellent report on local government in New Zealand. He's not afraid to ask and answer the big questions, or to challenge the status quo. It's a report of immense value to all who have an interest in local government and in making New Zealand a better place. By its very nature, it's a report that could only ever be written outside of government and is a report well overdue. I commend Mr Krupp and The New Zealand Initiative for taking on such an ambitious project and completing it to the highest of standards.

Rodney Hide
Christchurch



QUEENSTOWN

EXECUTIVE SUMMARY

In the public discourse much of the focus falls on central government, and its policies. This is understandable, given its size and scope. Yet for all the attention on Wellington, most of our interactions with government occur at a local level. Councils are responsible for ensuring that clean water is piped to homes, roads are in good working order, and local planning is efficient. Done well, these tasks are hardly noticed. Done poorly, and the spill-over effects can have national implications.

An objective assessment of local government in New Zealand suggests we fall into the second category. Voter turnout in the most recent local elections languished at the 40% level,¹ and public polls rate council performance at 29%.² Intractable problems like declining housing affordability in Auckland and other fast growing councils show the current legislation is not working. Central government wants to amalgamate councils into bigger local authorities, but this solution is unpopular with local communities.

ACCOUNTABILITY GAP

The Initiative's research shows New Zealand's local government problem has less to do with a lack of local authority scale, and more with overlapping layers of responsibility. According to the *Local Government Act*, councils are democratically accountable to their communities, but as creatures of statute they have an obligation to take on any task central government assigns them. In theory this should provide for double oversight, but in practice it blurs the lines of accountability between those setting policy and those who bear the costs of it.

As a result of these legislative arrangements:

- Central government can pass regulatory tasks to local government without funding. These costs are ultimately borne by communities, who have limited say over the expenditures they are paying for.
- Poor lines of accountability develop between policymakers and tax or ratepayers. Councils can unfairly take the blame for centrally imposed costs, but they can also blame central government for their own poor performance.
- Communities seldom face the costs of their choices, particularly where only property owners pay local taxes directly in the form of rates.

These overlapping responsibilities and blurred lines of accountability often make it difficult for experts, let alone the average member of the public, to explain where the problems with local government structures start.

In this environment, it is hardly surprising that the relationship between central government, local government, and their respective communities is characterised by distrust and misunderstanding.

CLOSING THE GAP

The aim of this report is to restore accountability, transparency and community responsibility to local government. We propose doing this by setting clear roles for each tier of government, with limits on the ability of either party to act beyond these limits, except where agreed to beforehand or in extreme circumstances to prevent duplication of tasks. Most developed countries do this through a constitutional process, and while there is merit in pursuing this process in New Zealand, the time required to do so may not provide meaningful relief to the local government problem any time soon.

¹ Preliminary voter turnout 2016 (October 2016). <http://www.lgnz.co.nz/vote2016/preliminary-voter-turnout-2016>

² Local Government New Zealand (LGNZ), "The New Zealand Local Government Survey" (Wellington: New Zealand Government, 2015).

Instead we propose a quasi-constitutional separation of powers to achieve much the same end. This will require change on both sides. For central government, it will mean reforming the *Local Government Act* and ceding full responsibility over local matters to councils.

CENTRAL ACTION

We recommend fixing the double oversight problem by making local councils fully responsible for the local tasks they currently perform. If a council takes responsibility for a function, like roading or dog control, the buck must stop with them. This will stop regulatory duplication, blame shifting, and unfunded mandates.

- There will be times when central government policy or intervention is needed, such as to set up a nationally consistent planning framework. This should be recognised in the *Local Government Act*. But councils should be allowed to opt out of these rules to prevent central government from overstepping its mandate. A necessary check and balance on opt-outs is approval by local referendum. Councils should be liable for any expense if the opt-out imposes costs on central government (such as the public health system) to avoid a moral hazard.
- Some local authorities may be better placed to take on tasks managed by central government in their jurisdiction. Where councils are likely to achieve better outcomes, local authorities should be allowed to negotiate with central government to have these functions, including block funding, handed over to them.
- Property taxes present councils with weak incentives to promote economic growth in their region. This is particularly so for infrastructure investment, where the costs fall immediately but rates revenue is many years off. Financial incentives can circumvent this problem.

DEVOLUTION BY EXAMPLE

If councils are to be given more responsibility, they need to show they are capable of managing it. This is needed to combat the widely held (and often mistaken) view that councils are incompetent.

- Local authorities need to show they are prudent spenders of public money. Councils need to improve the quality of their cost-benefit analyses on long-term plans. Current assessments fall far short of what an economist would recognise as a cost-benefit analysis.
- According to the *Local Government Act*, the purpose of local government is to “enable democratic decision making and action by, and on behalf of, communities”. Current consultation processes are overly technocratic and complex, which disenfranchises many communities. If councils are to be allowed more autonomy, they need to show their actions are steered by local democratic preferences. Two excellent mechanisms worth considering are local referenda and citizen juries.

The policy recommendations in this report provide a practical means of making local government more accountable and transparent to communities. The aim is to make New Zealand better off. Drawing clear lines of responsibility will go a long way to fixing the relationship between local and central government. In effect, it is a framework for both parties to meet each other halfway.

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INTRODUCTION

One of the most overused quotes still making the rounds is George Santayana's quip that "those who cannot remember the past are doomed to repeat it". Its overuse is explained by its applicability to so many situations. The often forgotten history of local government in New Zealand is a case where Santayana's quote is particularly apt. The almost 160 years of that history can be neatly described as a struggle between local and central government – communities sought to create more local authorities, while central government sought to whittle them down in the name of efficiency. Further consolidations have meant New Zealanders are now governed by just 78 local authorities.

Judging by the 2010 Auckland merger, and the failed 2013 amalgamation campaigns in Hawkes Bay, Northland and Wellington, central government officials still see the local government structure as inefficient. Legislation is before Parliament that would give the Local Government Commission greater power to propose amalgamations, and also facilitate local councils to initiate their own merger proposals.³ This top-down approach to council reorganisations has the potential to set central government against local authorities and communities, who have for the most part disliked the idea. This is particularly so amid the increasing weight of evidence that shows few municipal amalgamations, if any, deliver on the operating efficiencies they promise. Montreal, which was profiled in the second report of this series on localism, showcases this phenomenon.

That report provides an insightful look into alternative local government arrangements. Switzerland is roughly the size of Canterbury with a population of about 8 million people, and yet it is governed by more than 2,000 communes, or municipalities. Further, Switzerland has 26

cantons (or provinces) and a central government. If New Zealand were to copy the Swiss structure on a per capita basis, it would have about 1,400 local authorities. The Netherlands too has a diverse local government structure, consisting of 400 municipalities and 12 provinces. To the average New Zealander, this abundance of local government would seem a formula for bureaucratic chaos. But Switzerland and the Netherlands are ranked among the most competitive countries in the world,⁴ and their local government structures are crucial to the efficiency of their economies. Even the United Kingdom is reversing its highly centralised governance arrangements and devolving power to local government to cut fiscal spending and spur economic activity.

This report suggests New Zealand should break out of its long cycle of consolidations and amalgamation. If central government wants local government to play its part in improving the prosperity of New Zealand, it needs to let councils and the communities they represent share in the benefits of this growth, not just the costs. And if officials in Wellington expect councils to be truly answerable to their communities, they themselves should not blur the lines of accountability. Equally, local authorities need to demonstrate they are responsible stewards of the local economy, they have buy-in from their community, and they are aware of the wider implications of their regulatory decisions for the country as a whole.

This last report of the series aims to foster a serious discussion about the role of central and local government. Too often, the idea of local government is locked in the service delivery model, rather than thinking of local authorities as a tool with which communities can tackle the complex issues they face – and that can only be solved if the community is involved.

³ Under the 2012 amendments to the *Local Government Act 2002*, local authority reorganisations could only be initiated by groups showing they had sufficient community support in the form of a petition.

⁴ Klaus Schwab, "The Global Competitiveness Report 2015–2016" (Geneva: World Economic Forum, 2015), 7 and 23.

The policy recommendations in this report create a framework to do just this. They are built on incentives and local responsibility to transform the relationship between central and local government from a paternalistic and adversarial one to a

partnership that makes New Zealand a more prosperous, diverse and dynamic place to live. That surely is a goal central and local government can work towards together.

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CHAPTER ONE

WHAT'S THE PROBLEM AGAIN?

What is wrong with local government in New Zealand? This may seem an odd question, especially as it may not be at the top of most people's list of pressing concerns. But local government is often a common factor among many of the issues making headlines. Local councils have a critical say in matters such as house prices, economic efficiency, cost of living, alcohol policy, environmental planning, local taxes, etc. Their efficiency and competence dramatically affects the outcome of these matters, as does the design of the overall legislative structure. Declining housing affordability in Auckland due to scarce land supply,⁵ growing complaints about the drag of local regulations on business, and the struggle to resolve tensions in resource use clearly shows something is off kilter.

So what is the problem? The answer very much depends on who you ask.

CENTRAL VIEW

To the central government, local authorities are the problem – or at least the weak link in the government's plan to encourage economic growth and improve the wellbeing of New Zealanders. Various officials have made a number of critical statements about the sector in recent years. For example, former Local Government Minister Paula Bennett established the Rules Reduction Taskforce to find out which local “loopy rules” are frustrating people's lives for little benefit.⁶ Housing Minister Nick Smith has also laid the blame for Auckland's deteriorating housing affordability firmly at the feet of the city council. Indeed, the problem is

so severe that central government has proposed forcing councils to release land for development.⁷ Central government has also introduced temporary planning legislation to sidestep consultation requirements on certain housing projects. The Department of Internal Affairs too is concerned the costs of local council services continue to grow faster than wages and consumer inflation.⁸ To fix this, central government continues to look for a legislative means to force what it sees as recalcitrant local authorities to be more efficient and effective in providing local goods and services. And if this fails, Wellington has given itself the power to place underperforming councils under the control of statutory managers.

VIEW FROM THE EDGE

Local government, of course, has a different perspective on the problem. Local authorities see central government regulation as the root cause of many of the intractable policy problems facing the country. This is lent weight by the Productivity Commission's review of local government regulation.⁹ Central government's own Loopy Rules report found that two-thirds of the local red tape problems reported to the taskforce stemmed from the *Resource Management Act 1991* and the *Building Act 2004*, legislation created and controlled by central government.¹⁰

⁵ Demographia, “12th Annual Demographia International Housing Affordability Survey: 2016,” Website.

⁶ Rules Reduction Taskforce, “The Loopy Rules Report: New Zealanders Tell Their Stories” (Wellington: Department of Internal Affairs, 2015).

⁷ Patrick Gower, “Government, Auckland Council at odds over housing,” *Newshub* (16 May 2016).

⁸ Cabinet Economic Growth and Infrastructure Committee, “Local Government – Better Local Services Reforms” (Wellington: Department of Internal Affairs, 2016), 5.

⁹ Productivity Commission, “Towards Better Local Regulation” (Wellington: Productivity Commission, 2013).

¹⁰ Rules Reduction Taskforce, “The Loopy Rules Report,” op. cit. 7.

To paraphrase, many councils would say they only feature in many of the problems discussed above because they are the tier of government that interacts with the public most frequently. Furthermore, the sector sees characterisations of it being financially unsound as overdone. This position is somewhat supported by The New Zealand Initiative's research. For example, council rates have risen by 171% in real terms over the past two decades. However, local taxes have remained largely stable since 1940 when measured against GDP (unlike central government taxes).¹¹ Rates have been driven by higher levels of spending since 1994 (191% in real terms over two decades), but has been matched by an increase in the level of services local councils provide.¹² On other financial measures, local government fares fairly well, with the sector's median long-term debt equivalent to 6% of total assets in 2014.¹³ The sector agrees on the need to improve in areas such as asset management, but there is much evidence it is doing a good job within the confines of the regulatory environment.

So whose argument is the general public to believe?

MUDDY WATERS

The first report in this series found evidence to support and contradict both sides. Council spending has indeed been raised by central government passing unfunded mandates to local government. To fulfil these mandates, councils cover their costs through user fees, rates revenue,

or a combination of both. At the same time, the share of spending by councils on non-core activities has increased or remained largely stable since 2003, even as the share of spending on core activities, such as roads and water supply, has shrunk over the same period.¹⁴ Parliament is responsible for developing the regulatory structures and frameworks that local government uses, but in many cases the true costs and benefits of these policies are under-assessed.

On the other hand, councils' decision-making within these regulatory structures is also poor, at least as judged by cost-benefit analyses (see Chapter 5). In practice, these analyses amount to little more than lists of pros and cons, where the longer list is the preferred decision.¹⁵

The result is that it is often difficult for experts, let alone the public, to explain where the problems with local government structures start. If voters cannot tell which tier of government is ultimately responsible for which service, how can they be expected to reward or punish policymakers at the national or local ballot boxes?

IN A BIND

This lack of transparency and accountability goes some way to explain the political constraint identified in the first report.¹⁶ Communities resist moves by councils to increase rates, borrow more, or sell assets to fund investments that should benefit residents in the long term by growing the ratepayer base, even where it is prudent to do so. Of course no one is eager to pay higher taxes. But this constraint seems to be particularly prevalent where there is no certainty as to who is driving costs (central or local government), or

¹¹ Jason Krupp and Bryce Wilkinson, "The Local Formula: Myths, Facts and Challenges" (Wellington: The New Zealand Initiative, 2015), 17.

¹² One of the key drivers of increased council spending has been employee costs. There has also been increasing spending on core infrastructure, especially roading and water networks. Much of this higher infrastructure spending was to be on maintenance and renewals but there will be new or upgraded capacity put in growth areas.

¹³ Jason Krupp and Bryce Wilkinson, "The Local Formula," op. cit. 53.

¹⁴ Ibid. 18.

¹⁵ Kāpiti Coast District Council, "Kāpiti Coast District Plan Review Section 32 Analysis – Summary Report Infrastructure, Services and Associated Resource Use (Part 3: Community Facilities)" (2012).

¹⁶ Jason Krupp and Bryce Wilkinson, "The Local Formula," op. cit. 29.

that the additional money will be well spent. It is not helped by the drawbacks of rates as a form of government revenue – they are highly visible (unlike sales or salary taxes) as they have to be reset each year. As one referee on this report remarked: “As a form of taxation it is almost the worst you could think of in terms of garnering public support”.

The political constraint also explains the tense relationship between central and local government and the unresolved status of the many thorny policy problems involving both tiers. This chapter opened with the question: What is wrong with local government in New Zealand? Perhaps it is better to ask: What is wrong with the division of government power in New Zealand?

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MT MAUNGANUI

CHAPTER TWO

IS POWER A PROBLEM?

In asking what is wrong with the division of power in New Zealand, it is worth examining how decision-making power is typically divided in developed countries. Broadly speaking, it can be represented by a spectrum. On one end, the role of local government is limited by central government to the provision of local public goods and specific services. At the other end, local government is a democratic entity in its own right, whose role is determined by community preference and constitutionally demarked spheres of activity. Generally speaking, the more centralised is decision-making within a country, the more likely it is for local authorities to be considered agents of central government rather than independent authorities (and vice versa).

In Montreal, a city profiled in the second report, the role of municipalities is limited to a specific set of services. Likewise in the United Kingdom, which has strictly limited the activities of local government – although this is changing under devolution in jurisdictions such as Greater Manchester. In the Netherlands and Switzerland, local authorities are far more free to undertake activities of their choice, subject to democratic mandate.

These examples neatly represent the respective ends of the local government spectrum. What they have in common is a clear delineation of responsibilities and clear lines of accountability. Residents of Westmount municipality know provincial law stipulates the City of Montreal is responsible for clearing snow from the streets. In Switzerland, officials in Wohlen can enter into whatever arrangements they want to ensure their streets are clear of snow, but are also responsible for their choices. In spite of being on opposite ends of the local government power spectrum, the lines of accountability are clear. Westmount residents are unlikely to blame the municipality if their streets are impassable in winter, just as Wohlen residents are unlikely to blame cantonal authorities.

Pinpointing New Zealand's place on this spectrum is tough as it is positioned not so much in the middle but on both sides at once. The division of power represents a scattershot rather than a distinct point on the spectrum. Legislative changes over the past three decades help explain this.

DO WHAT YOU ARE TOLD

In 1879, the *ultra vires* rule was applied to local government. Any council looking to undertake an activity had to ensure it was not acting beyond its legislative mandate, or *ultra vires*.¹⁷ Even within these confines, local government's autonomy varies greatly. For example, council revenue was, and still is, largely raised from taxes on property. Councils cannot introduce another revenue stream if it is not listed in the *Local Government Ratings Act 2002*.¹⁸ Even a bed tax on tourists is currently prohibited. As a result, local government's share of total public spending was 11% in 2012, compared to the OECD average of 25%.¹⁹ However, the level of discretion over how this money is spent is high compared to many countries, where funding is typically tied to specific expenditures, such as in the Netherlands. In addition, legislation like the *Resource Management Act 1991* give councils significant leeway to pursue their own course, while the *Building Act 2004* is highly prescriptive in the duties and powers it confers on local authorities. So in this respect, local government in New Zealand was both constrained and free under the *ultra vires* legislative regime.

¹⁷ Productivity Commission, "Towards Better Local Regulation," op. cit. 40.

¹⁸ *Local Government (Rating) Act 2002*.

¹⁹ OECD and Korea Institute of Public Finance, "Institutional and Financial Relations Across Levels of Government" (Paris and Seoul: 2012).

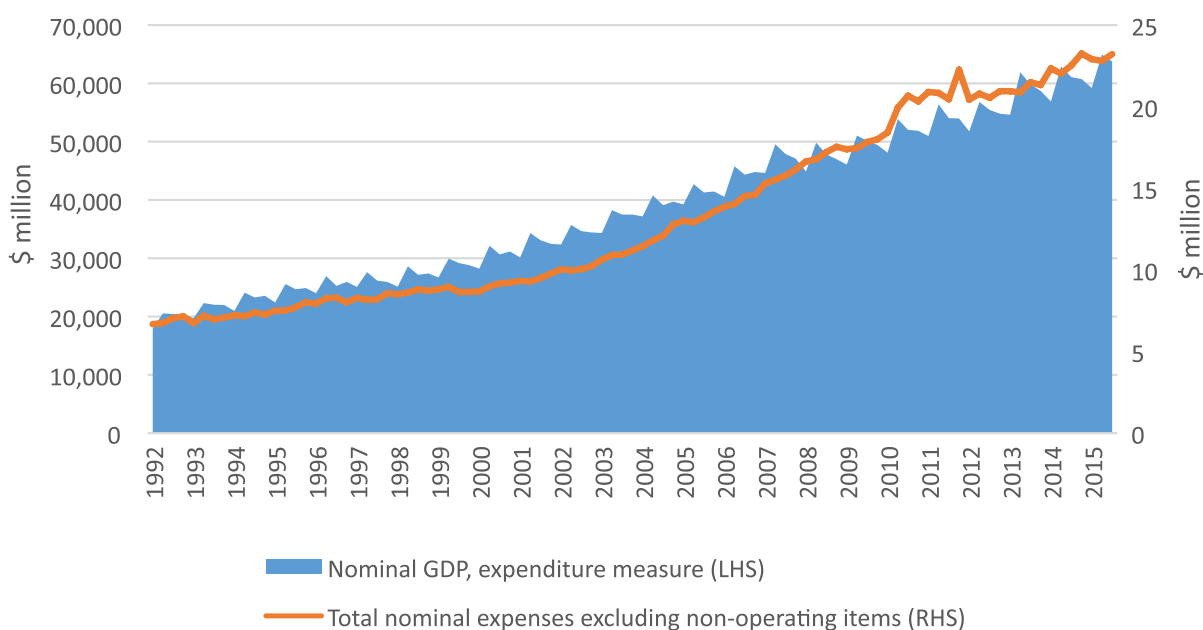
EASING THE TIES

The *ultra vires* approach to local government persisted through the major 1989 reforms of the sector and the 1990s under a National-led government, albeit with amendments to the various pieces of legislation. When the Fifth Labour Government assumed power in 1999, the *ultra vires* approach was seen as too restrictive, and prescriptive of process.

This led to the introduction of the *Local Government Act* in 2002. Local councils were given the power of general competence and an activist purpose statement to pursue the “social, economic, environmental and cultural well-being” of their communities.²⁰ The aim was to free local government from the *ultra vires* confines and

make the sector more responsive to the needs of communities (subject to prescribed consultative processes and limitations imposed by other legislation).²¹ However, many of the statutes that bound local government under the 1974 version of the *Local Government Act* (and the 1989 and 1996 amendments) were retained. One councillor was quoted as saying: “It’s nice to know that we have the power of general competence, but I haven’t yet found anything I can use it for”. This reflected the extensive list of permitted activities under the 1974 act. Local authority expenditure rose during the period when the power of general competence was introduced, but it is not clear this change in 2002 drove spending higher in particular, since the country was enjoying steady rates of economic growth during that period (see Figure 1).

Figure 1: Nominal GDP vs total nominal expenses for all territorial authorities (excl. non-operating items)



Source: Author’s calculations using data from Statistics New Zealand, “Local Authority Statistics: Total Expense Excluding Non-operating Items” and Statistics New Zealand, “National Accounts: Gross Domestic Product – Expenditure Measure”.

²⁰ *Local Government Act 2002* (pre-2012 amendments), s.

²¹ Peter McKinlay, “Better local services: Improving local government delivery through innovation and partnerships: Lessons from the New Zealand experience,” Presentation (Commonwealth Local Government Forum Asia-Pacific Regional Symposium, 2005).

THERE AND BACK AGAIN

Another wave of local government reforms was triggered in 2008 with a change of power in central government. Officials in the National-led government saw the four wellbeings as a driver of higher local government spending, and sought to rein it in. In 2012, then Local Government Minister Nick Smith replaced the four wellbeings in the *Local Government Act* with a new purpose statement.

Section 10(1)(a) of the act states the purpose of councils is to:

Enable democratic local decision-making and action by, and on behalf of, communities.

Furthermore, central government sought to focus council activities on what it saw as the core business of local government. Section 10(1)(b) states councils must:

Meet the current and future needs of communities for good-quality local infrastructure, local public services, and performance of regulatory functions in a way that is most cost-effective for households and businesses.²²

To an outside observer, these legislative changes could be seen as an oscillation between the two ends of the local government spectrum – from restrictive, to free, and then back again. However, rather than constrain council activities, these changes have further confused the role of councils. There is a palpable tension between s 10(1)(a) and s 10(1)(b). Are councils required to restrict their activities to pure local public goods and services and regulatory functions, or is their primary task to respond to the needs of their community? What if the community wanted its council to undertake an activity that strays from the cost effective provision of core goods and services? The legislation does not make this clear.

For example, Gisborne District Council read the legislation to say it should pare back its activities to those strictly laid out by law and abandon

non-core activities like economic development.²³ Auckland Council did not see the 2012 amendments as a constraint on economic development, and has nearly doubled spending in this area since 2012 (\$116 million in 2015).²⁴ And indeed, other ministries, such as the Ministry for Business, Innovation and Employment, continued to engage with economic development agencies.²⁵ Central government has only recently tried to clear up the uncertainty hanging over local economic development agencies (see Appendix 1), but has done little to stem other potential conflicts caused by the changes to the *Local Government Act* purpose statement.

SETTING THE STANDARD

Central government has also increasingly intervened at a local government level. The introduction of drinking water standards by the Ministry of Health is a clear example.²⁶ The standards set a quality benchmark for drinking water to reduce public health issues caused by contaminated drinking water. This policy forced many councils to upgrade their plants through local rates. This national policy would be justified if it generated sufficient net benefits at the national scale, and the upgrades were paid out of general taxation. However, while costs of compliance were estimated at between \$309 million and \$527 million,²⁷ central government only set aside \$150 million. The upgrades only had a small

²² *Local Government Act 2002*, s 10.

²³ Gisborne District Council, “Central Government Directions” (25 October 2012).

²⁴ Statistics New Zealand, “Local Authority Financial Statistics Income and Expenditure by Activity (Annual-Jun): Auckland Council, Economic Development 2015,” Infoshare.

²⁵ Ministry of Business, Innovation and Employment, “Regional growth programme” and “Hawke’s Bay: East Coast Regional Economic Potential Study,” Websites.

²⁶ Ministry of Health, “Drinking-water Standards for New Zealand 2005, Revised 2008” (Wellington: New Zealand Government, 2008).

²⁷ CH2M Beca Ltd, “Drinking Water Standards New Zealand Cost Benefit” (Wellington: Ministry of Health, 2010), 82.

Havelock North – localism or centralism

On 12 August 2016, Hasting District Council officials and senior health officials were alerted to a possible contamination in Havelock North town. The alert was prompted by a rising number of residents seeking help for vomiting and diarrhoea. By the time it was established that the town's water supply was at fault and emergency water supplied, almost 5,000 residents had gastric illness and one person had died.

To critics of further devolution, this proved communities and councils could not be trusted to make sound decisions on core services. If councils cannot get the basics right, how can they be trusted in other areas?

The case is, however, not as clear cut as it first seems for three reasons.

First, central government already sets minimum drinking water standards under the *Health Act 1956* and the National Environmental Standards for Sources of Human Drinking Water. The Havelock North contamination occurred despite these legislative controls. The water from the bore was not chlorinated before the incident as the aquifer's quality met minimum national standards. In 2010, the government required councils to adopt mandatory performance measures for their major infrastructure activities, including water, but this has not appeared to help, either.

Second, although an official investigation into the Havelock North case has yet to be completed, it seems the contamination was related to site specific factors: a shallow aquifer, proximity to agricultural production, and delays between water quality testing and reporting. The contamination may have been the result of factors outside of the council's control, such as flooding or well cap failure. Until that report is released it is premature to draw any firm conclusions, or indeed infer that central government intervention is needed.

Third, passing legislation requiring all drinking water be chlorinated would pose a significant cost on communities that do not chlorinate their water. Christchurch, which draws its water from multiple bores, has saved “millions, probably billions of dollars” by not chlorinating water drawn from the bores (the risk of infection is counterbalanced by a rigorous testing regime).²⁸ Indeed, Christchurch's aquifers stood up well to the 2010-11 earthquakes, and the city's water network may have even fared worse had the city processed its water centrally.

Hastings District Council should not escape scrutiny for the Havelock North water contamination. Where lapses occur or poor decisions are made, local officials (and communities) should be held accountable. More stringent controls are likely as a result of the Havelock North incident, and other councils will no doubt check their own water supplies to ensure a similar incident does not occur in their own jurisdiction.

What is debatable is whether greater central government intervention will achieve a better result. Central government can certainly pass legislation requiring chlorination of all drinking water at significant costs to local communities, particularly small, rural ones. But it is uncertain whether national wellbeing would be improved when weighing the expense against the benefit. Besides, any legislative change is likely to be slow, and the public health gains modest. Since 2011, the proportion of the population serviced by compliant water supplies has increased from 78.5% to 79.4%.²⁹ Ultimately, service standards should be left to local communities as long as they take responsibility for their decisions.

²⁸ Jamie Small, “Positive E coli tests ‘not surprising’ in Christchurch untreated water supply,” *Stuff* (19 August 2016).

²⁹ Productivity Commission, “Better Urban Planning – Draft Report,” *op. cit.* 132.

impact on residents in urban centres, whose large populations allowed significant dilution of costs on a per capita basis. But rural councils with small populations had to raise rates substantially. Water network upgrades in the townships of Renwick and Havelock (a township on the South Island, distinct from Havelock North on the North Island) cost ratepayers \$22 million and were projected to increase rates bills by an additional \$127 annually by 2021.³⁰ By setting a standard but passing on the bulk of costs, central policymakers have largely ignored the burden they were imposing on local communities. Even more problematic is that central government's intervention has not prevented the outbreak of waterborne diseases in some districts (see Havelock North case study).

Such unilateral decisions by central government impose significant cost on local authorities and communities. A 2009 study into the administrative requirements placed on councils by amendments to the *Local Government Act 2002*, the *Public Transport Management Act 2008*, the *Health (Drinking Water) Amendment Act 2007*, and the *Land Transport Management Amendment Act 2008* estimated that it would take an additional 720,000 hours of council staff time to meet them. Priced at the average hourly wage at the time, this represented \$14 million in additional salary costs,³¹ and excludes \$25 million of one-off consulting costs.³² Since then, the level of central government's legislative intervention has increased based on local council regulatory and planning expenditures. Expenditures increased by 50% to \$645 million over the 10 years to 2015.³³

These are significant costs that should have been borne to some degree by central government, but which were passed onto to local government.

Central government's power to set local services standards means it can impose costs on councils and communities. For example, amendments to the *Sale and Supply of Alcohol Act 2012*, transferred the costs of the system to those seeking an alcohol licence.³⁴ Central government collects excise taxes on alcohol at a national level, but shares none of this revenue with councils, which bear the costs associated with alcohol use (street cleaning, regulatory enforcement, etc.).

Such little visibility into who is driving costs, who benefits, and to what extent vastly reduces accountability. Ratepayers may blame the wrong tier of government. For example, the Society of Local Government Managers (SOLGM) estimated the overhaul expected under the Alcohol Reform Bill would significantly drive up licence costs. But the society said in its submission that licensees were likely to mistakenly assume that local government, as the agency overseeing the operational aspects of the bill, was the driver of higher fees, when in fact it is the Ministry of Justice.³⁵ As noted by the Productivity Commission in 2012, the "situation can arise when communities give central government the credit for introducing a new regulation to fix a 'problem', but blame councils for the financial and compliance cost of the regulation. In this case, central government has weak incentives to design the regulation carefully".³⁶ By the same token, local government could blame poor local service efficiency on central government. This role confusion allows each tier of government to blame each other, leaving long-standing problems like declining housing affordability to worsen.

³⁰ Heather Simpson, "Costs of drinking water upgrades in Marlborough to be spread across ratepayers," *The Marlborough Express* (15 June 2016).

³¹ Statistics New Zealand, "New Zealand Income Survey: June 2009 Quarter," Website.

³² PricewaterhouseCoopers, "Costs of Regulation on Local Government" (Wellington: Local Government New Zealand (LGNZ), 2009).

³³ Statistics New Zealand, "Local Authority Financial Statistics Income and Expenditure by Activity (Annual-Jun). Total (Excluding Museums), Planning and Regulation, Total Operating Expenditure 2015," Infoshare.

³⁴ Alcohol Reform Bill 236.

³⁵ Society of Local Government Managers (SOLGM), "Submission on the Productivity Commission Discussion Document 'Local Government Regulatory Performance'" (Wellington: SOLGM, 2012).

³⁶ Productivity Commission, "Towards Better Local Regulation," op. cit. 68.

MISSING THE POINT

The principle of subsidiarity, which is the belief that decision-making should be devolved to the lowest appropriate level possible (the lowest being the individual), is being misapplied in New Zealand. The principle stems from the thinking that certain decisions are better suited to central government, particularly where there are national level benefits and economies of scale.

Likewise, decision-making powers should be devolved to local government where benefits accrue exclusively to local communities, and where responsiveness and differentiation are valued. Extending this logic, the costs of national policy should be paid out of general tax revenues, while local communities should bear the costs of the local policies they choose. This arrangement clarifies the lines of accountability, unlike the ambivalent purpose statement in the *Local Government Act*.

Beyond the blurred accountability, the practical misapplications of the subsidiarity principle in the *Local Government Act* limit the efficiency of local and regional government services. For example, it is widely recognised that drinking water networks benefit from economies of scale. Yet this task has been assigned to district councils, whose responsibility ends at the district line.³⁷ This raises the costs of building a network to bigger scale. The same with roading. Of course, councils can choose to pool these assets in a regional specialist provider, or Council Controlled Organisation (CCO), but parish pump politics (or patch protection) has slowed their adoption. For this reason, central government has been trying to make it easier for the Local Government Commission to force councils to form CCOs through the Better Local Government Reforms.³⁸ These reforms are still before Parliament, so

we do not know how successful this policy will be. Most commentators remain sceptical given central government's poor relationship with local government since 2008. But even if the reforms are a success, and reshape the local government landscape under a patchwork of CCOs, they won't fix the broader issue of role confusion in the *Local Government Act*.

I CAN'T GET NO SATISFACTION

The result is deep dissatisfaction among all parties. Local government is frustrated with central government, and central government is frustrated with the perceived intransigence and profligacy of councils. But ultimately it is ratepayers who are the most frustrated. The effects are reflected at the ballot box and in opinion surveys. Voter participation rates have declined from around 57% for mayors and 56% for councillors in 1989 to 41% and 42% in 2013 respectively, a trend that has continued in the 2016 local elections.³⁹ This is compounded by the sense that local votes do not count for much. This attitude is hardly surprising given central government's intervention in the sector. A recent example is the replacement of the Environment Canterbury's elected regional council with appointed commissioners in 2010, which is being restored to partial democracy only in late 2016. If the public thought local government does not matter because central government is hovering in the wings, it is one central government has been happy to enforce with unilateral decisions.

Other measures of council performance also do not reflect well on the sector. A 2015 survey of public perceptions rated local government's overall performance as 29 out of 100, even though this is observably out of kilter with the level and quality of services most households receive.⁴⁰

³⁷ Local Government in New Zealand – Local Councils, “Regional Councils,” Website.

³⁸ Cabinet Economic Growth and Infrastructure Committee, “Local Government – Better Local Services Reforms,” op. cit. 3.

³⁹ Local Government New Zealand (LGNZ), “Voter Turnout in New Zealand Local Authority Elections – What's the Story?” (2013).

⁴⁰ Local Government New Zealand (LGNZ), “The New Zealand Local Government Survey,” op. cit.

Unless the respective roles and responsibilities of each tier of government are explicitly laid out, we can reasonably expect the current environment of poor accountability, central-local fingerpointing, and voter intransigence to fester further to the nation's detriment. Yet it is also clear that all three parties – ratepayers, central

and local government – want the best outcomes for their communities. What appears to be missing is a strategy to ensure this commonality of vision transforms into roadmap for meaningful legislative change: What is the best way to fix the problem with the local government structure in New Zealand?

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WELLINGTON

CHAPTER THREE

FIXING THE PROBLEM

Kenneth Palmer noted in the early 1990s that under the Westminster model of government, local authorities are not a constitutionally entrenched tier of government. This is a legacy that England has bestowed on many of its former colonies, including New Zealand and Australia. The role of local government in these countries is largely as an agent of central government, which assumes regulatory powers and responsibilities to its advantage.⁴¹ Unfortunately, this arrangement – characterised by role confusion and poor accountability – is detrimental to the country as a whole.

The previous chapter closed by asking: What is the best way to fix the problem with the local government structure in New Zealand? But the scope of this question is too narrow. It is more useful to expand the question: What is the best way to fix the haphazard allocation of tasks between local and central government that has reduced the ability of communities to hold decision-makers to account? What incentives are needed to encourage better local decision-making?

KEEP THEM SEPARATED

There is of course a constitutional remedy to this problem. Constitutions are a common means of separating power in most European and North American countries, some of which were profiled in *The Local Benchmark*. In Switzerland, the roles of each tier of government are clearly defined. Communes (or municipalities) are responsible for providing kindergarten and primary education, while secondary and tertiary education services are left to cantonal authorities (provinces).⁴²

Under these governance arrangements the lines of accountability are clear. Should tertiary education spending suddenly spike, cantonal residents are unlikely to blame communal authorities. An important feature of the Swiss system is the constitutionally protected division of power. Indeed, the Swiss constitution was specifically written to strictly limit the powers of central government and maintain the sovereignty of the cantons.⁴³ As such, each tier of government is pre-eminent within the sphere of its constitutionally mandated duties.⁴⁴ Should the Swiss federal government want to change the primary school curriculum, local authorities are likely ignore the changes altogether, and the federal government would probably face a backlash from local authorities and residents for overstepping its constitutional mandate.

The Netherlands employs a similarly devolved structure, where municipalities provide many social services that central government provides in New Zealand. The separation of power is also enforced by a constitution specifically designed to prevent concentrating decision-making at the central level.⁴⁵ In practice, the arrangement is more fluid than a strict reading of the constitution would suggest, and central government has more scope to dictate quality standards of publicly provided goods and services than in Switzerland. However, since the bulk of local authority funding comes from central government, the Dutch parliament

⁴¹ Kenneth Palmer, *Local Government Law in New Zealand* (2nd ed.) (Sydney: The Law Book Co. 1993), 23.

⁴² Wolf Linder and Andrea Iff, “Swiss Political System” (Bern: Federal Department of Foreign Affairs, 2010), 4.

⁴³ Thomas Fleiner, “Swiss Confederation” (International Association of Centers for Federal Studies).

⁴⁴ Under a strict interpretation of the Swiss constitution, cantons are responsible for communal activities, but in practice they are treated as an entirely independent tier of government.

⁴⁵ While these arrangements work in the Dutch context, the US federal government has been known to circumvent constitutional separation by offering funding to dictate policy at the state level.

has been reluctant to dictate high local service standards (and ultimately pay for it). In Quebec, although there is no constitution to establish the powers of local authorities, provincial authorities have achieved the same result through local regulation, which delegates full responsibility over various tasks to city or regional authorities.

But can a separation of powers be achieved in New Zealand using a constitution? Of course yes, provided there is political will. However, one major challenge with drafting a local government constitution is the document would need to encompass a far bigger range of issues than just local and central government relationships. These include the Crown's relationship with Maori, and the place and standing of the Treaty of Waitangi in a constitution. The Treaty Principles are already included in many pieces of legislation (including the *Local Government Act*). These unique conditions will add to the complexity and time taken to draft a constitution, which even without factoring Treaty issues, is an onerous process. The Initiative believes a constitutional separation of powers will solve many of local government's current problems. However, given the time and political capital needed to draw up a constitution, we need to focus on other policy means of achieving the same outcome in the meantime.

SIDESTEP

Attempts have been made to sidestep this constitutional cul-de-sac by forming a regulatory framework to assess the true costs of central legislation on local government. The most recent was the Productivity Commission's inquiry into

local regulation. The commission found that many of the assessment toolkits used by central government to determine the regulatory cost of a policy mostly failed to consider the full impact on local authorities. For example, the Treasury's Regulatory Impact Assessment Team, which assesses regulatory impact statements, requires policymakers to consider the significant impacts or risks of legislative changes. In theory, this requirement should include the cost impact and risks posed to local government, but in practice these are very often overlooked.⁴⁶

To remedy these issues, the Productivity Commission has proposed a "partners in regulation" protocol – a joint framework under which local and central government would collaboratively improve the regulatory process across the whole of government and ensure both parties are strategically better aligned.⁴⁷ Central government declined to act on the suggestion, saying the "value and effectiveness of a formal joint mechanism [was] questionable, and improvements can be achieved without one".⁴⁸ In all fairness to the government, the effectiveness is questionable, particularly as there is no mechanism to ensure local government is not sidelined in this process. Even under the Fifth Labour Government, when the central-local authority relationship was more of a partnership than it is now, legislative consultation with local government occurred at the discretion of individual ministries.⁴⁹ As Mike Reid has noted, "Without a strong constitutional reference and a constitutional court with oversight, relationships exist entirely at the discretion of the national partner which has the power and authority to write rules as it sees fit".⁵⁰

⁴⁶ Productivity Commission, "Towards Better Local Regulation," *op. cit.* 102–103.

⁴⁷ *Ibid.* 97.

⁴⁸ New Zealand Government, "Government Response to Recommendations of the Productivity Commission's report *Towards Better Local Regulation*," 1.

⁴⁹ Michael Reid, "Managing Central-Local Government Relationships: The Case of New Zealand," *Commonwealth Journals of Governance* 11 (2012), 29.

⁵⁰ *Ibid.*

ART OF THE DEAL

There is one precedent that sidesteps the constraints of both approaches. In signing the Greater Manchester ‘city deal’, the UK government devolved certain powers and responsibilities to local government using a contractual rather than a constitutional process.⁵¹ These include health and social programmes (£6 billion), housing and planning, skills and employment development, and setting and collecting business rates.⁵² This second best approach contractually assigns tasks where a full constitutional separation of powers is impractical – and has both pros and cons. Critics say the biggest weakness is the inability to prevent a future government from legislating out of the deal. This is a valid criticism in the United Kingdom, where Parliament is restricted from passing any law that would restrict a future Parliament. That weakness is likely to apply to New Zealand where Parliament is the land’s highest legislative body. (Conversely, it could be argued that contractual devolution would be more binding than a constitution, especially where local authorities enter into contracts with third parties as a devolved entity.) However, the lack of permanence has not stopped the United Kingdom from devolving some sovereign powers to Scotland and Northern Ireland. In addition, as of May 2016 more than 30 devolutionary deals had been signed in the United Kingdom (26 in England, 3 in Scotland, and 1 in Wales), and a further 3 were being negotiated.⁵³

WELL-TRODDEN TRACK

The flexible nature of contractual devolution is where much of its appeal lies. Constitutions tend to apply in perpetuity, and change very little due to the high threshold of public support required. A separation of powers could be negotiated based on the current capability of individual local authorities, and expanded as the capacity of councils increases. It would also allow central government to tailor the handover of powers according to different types of councils, as opposed to using the traditional ‘one size fits all’ approach of national legislation. It would also be flexible enough to avoid the pitfalls the Treaty Principles pose to a constitutional process, while ensuring these principles are satisfied by including them in a devolutionary deal (as happens with most modern legislation). A further advantage is the precedence in New Zealand – the *Waikato-Tainui Raupatu Claims (Waikato River) Settlement Act 2010*, a settlement under the Treaty of Waitangi. Through this settlement, the Crown handed affected iwi the power to set the vision and strategic direction to manage the Waikato River, a power previously vested in the Waikato Regional Council. Local authorities have to ensure regional, coastal and district plans align with the vision and strategy set by iwi. Notably, iwi decisions supersede national policy and coastal policy statements – two areas under central control.⁵⁴ This is a clear example of central government ceding decision-making power to local authorities.⁵⁵ If this kind of arrangement can be established with iwi, the same framework can surely be used to achieve a separation of powers between central and local government without formally drafting a constitution.

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⁵¹ Greater Manchester Combined Authority (GMCA), “Greater Manchester City Deal.”

⁵² Jason Krupp, “The Local Benchmark: When Smaller Is Better” (Wellington: The New Zealand Initiative, 2016), 15.

⁵³ Matthew Ward, “Briefing Paper: City Deals” (House of Commons Library No. 7158, 17 May 2016), 4.

⁵⁴ Local Government New Zealand (LGNZ), “Local Authorities and Māori: Case Studies of Local Arrangements” (Wellington: New Zealand Government, 2011), 19–20.

⁵⁵ Central government still retains the power to dissolve the co-management arrangement.



CHAPTER FOUR

WHY RELINQUISH POWER?

Clearly, it is possible to achieve a separation of powers without an actual constitution. But does that mean central government should do so on a wider basis? Or more specifically, why should it do so? This report argues for meaningfully improving New Zealand's governance landscape by reducing role confusion and increasing local accountability. But this will cost central government its privileged position at the top of the political hierarchy. Reasonably, a government would only proceed with a motion if the political benefits exceed the costs. The same principle applies to the separation of powers, but often it takes a catalyst to trigger devolution. In the United Kingdom, the catalyst was fiscal pressure from the global financial crisis – specifically, the failure of centrally run programmes to measurably reduce public spending and reverse the economic contraction.⁵⁶

CARROT, NOT STICK

New Zealand is not facing this kind of economic pressure, other than high house price inflation in parts of the country. Lacking a stick such as a public debt crisis, it will take a net political benefit for Wellington to constitutionally devolve power to local authorities and lose its 'free lunch': the ability to legislate without facing the true costs of policy. Instead, these costs can be passed onto local government and communities. For example, tighter building standards for earthquake prone buildings were introduced without funding in the wake of the Christchurch earthquakes.⁵⁷

The gains to the country from sound devolution can exceed the costs of giving up a free lunch for two reasons. First, policymakers need to quantify

the costs of the status quo and tally the benefits of devolution. The second is the gains from devolution itself (see case studies below).

BITING THE HAND

A clear example of central government's failure to count the costs of the status quo was the recent spate of dangerous dog attacks. The *Dog Control Act 1996* confers on local authorities the power to set their own individual dog control policies, which include the management of dangerous animals.⁵⁸ In April 2016, a series of dog attacks were reported in the media. Amid a public outcry, central government took ownership of the issue and instituted a review of dog control policy.⁵⁹ It was unclear at that stage whether the attacks represented a wider problem requiring legislative intervention, confined to a specific area, or merely coincidental – as the last Dog Safety Report was published by the Department of Internal Affairs in 2010.⁶⁰

The review was ongoing at the time of writing, but any resulting action is likely to suffer from the limitations of a 'command and control' system. First, by necessity any national policy has to be broad and affect the operations of all councils, including those that are managing their responsibilities well. Second, any tangible response from central government is likely to take a long time. It can take two years or more for legislation to go through the parliamentary process, and implementation can

⁵⁶ Jason Krupp, "The Local Benchmark," op. cit. 12.

⁵⁷ Building (Earthquake-prone Buildings) Amendment Bill.

⁵⁸ *Dog Control Act 1996*.

⁵⁹ Louise Upston, "Have your say on dog attacks," Media release (Wellington: New Zealand Government, 12 July 2016).

⁶⁰ Department of Internal Affairs, "Dog Safety and Control Report 2009/10," Local Government Information Series (Wellington: New Zealand Government, 2011).

take another 18 to 24 months.⁶¹ Third, by passing national legislation, central government officials are likely to dilute the lines of accountability for animal control. This could absolve some local councils of poor regulatory performance, such as poor resourcing. Fourth, any cost increases with animal control will be borne by law abiding animal owners, who may blame local councils for this increase, not central government. Fifth, by taking ownership of a local matter, central government is stuck with it. It is almost impossible for central government to ignore a popular call for action except where it has no jurisdiction. Had dog control activities been fully devolved to local authorities, central officials could have avoided engaging on the issue, and instead focused their limited resources elsewhere. It is too early in the review process to accurately say whether these issues will be factored into the final decision, but it is unlikely given the previous discussion about local government omissions in the Cabinet Manual and Regulatory Impact Statement toolkit. Sixth, in 2004 central government amended the legislation, requiring all dogs to be microchipped, and for all councils to participate in the national dog control database. This appears to have had little effect, judging by the current need for further central intervention, other than to increase the cost of dog ownership.⁶² A referee on this report said this highlights one of the problems with New Zealand's overly centralised governance arrangements, namely officials seldom go back to assess whether their intervention was effective.

OPTION, NOT CO-OPTION

This is not to say central government should have no role in setting policies that affect local authorities. Clearly, there are benefits from having a single set of nationally applicable standards in areas such as telecommunications. However, the

party bearing the cost should have a significant say in setting the standards. For example, it is far more expensive per person to deliver water to a required standard in a smaller community than it is to a larger community. So if residents of the small community are satisfied with trading off low quality drinking water against low rate payments, they should be allowed to opt out. Local politicians advocating an opt-out would have to defend their position, thereby increasing transparency and accountability, and confronting communities with the real costs of their decision. Appropriate checks and balances are needed, such that if contamination occurs, as in the case of Havelock North, the council has to compensate central government for the additional health costs it has imposed. Should central government still want to set a nationally applicable standard against the wishes of the community, it should fund the policy.

LUMBERING LEVIATHAN

Another rarely counted cost of the current governance structure relates to diseconomies of scale. We know how difficult it is to get departments in very large organisations to operate outside their silos. This is just as true for the private sector and government. The UK government has spent significant amounts of public money trying to shift deprivation statistics in the economically blighted cities of northern England. Yet for all the billions of pounds spent on Greater Manchester's turnaround over many decades, the city ranked as the sixth most deprived region out of 326 regions in the United Kingdom in 2015.⁶³ Manchester's officials say central government is too big to execute effectively. Sean Anstee, the leader of Trafford Council in Greater Manchester, says that with devolution:

⁶¹ Legislation can be sped through the parliamentary process, but there is no indication this will apply to the review of the *Dog Control Act 1996*.

⁶² Department of Internal Affairs, "Dog Control Amendment Act 2003," Website.

⁶³ Manchester City Council, "Public Intelligence Population Publications: Deprivation," Reports from the Indices of Deprivation 2015 for Manchester," Website.

You can start to remove a siloed mentality from Whitehall where, through no fault of its own, it is not able to connect its decisions, or look at the unintended consequences from those decisions, because it is too big ... it is just that they can't look at how well things like transport planning and skills planning could work together for a local area.⁶⁴

The limits of central government were obvious to Whitehall even before the global financial crisis, which is when the devolution process started, and picked up significant pace afterwards as officials sought new ways of cutting spending and spurring economic growth in the United Kingdom.

New Zealand's own highly centralised governance structure suffers from the same siloed limitations, and could benefit from devolving responsibility to local agencies, where appropriate. Consider the recent attempts to reduce the country's high rate of rheumatic fever infections. Rheumatic fever can lead to a medical condition that often requires heart surgery, posing significant costs to the health system. It is concentrated among lower socioeconomic groups, and is particularly prevalent among Maori and Pacific Islanders.

In 2011, the Ministry of Health launched the \$24 million Rheumatic Fever Prevention Programme, to conduct a throat swabbing campaign in schools in high risk areas.⁶⁵ Those children found positive for Group A Streptococcus, a precursor of rheumatic fever, were flagged and health authorities and parents alerted.

An independent evaluation of the programme found the intervention was generally welcomed by stakeholders but that it did not address factors (e.g. cold and damp houses) that increase the incidence of the disease.⁶⁶ Many of the cold and damp houses in areas with high rheumatic fever

rates are in fact state houses run by Housing New Zealand. Even today an internet search of 'state houses' and 'damp' results in negative news stories about poor health outcomes stemming from these buildings. The programme clearly has yet to overcome the problem. A Salvation Army report on social housing noted that the government's maintenance budget is not based on a long-term asset management plan to see all properties in the portfolio maintained to a minimum standard.⁶⁷

Of course the incidence of rheumatic fever and its causes are a significantly complex and multifactorial problem. It is plausible that channelling the programme's funding into improving state housing stock instead of school screening would have made less ground in combating the disease. This is due to the high construction costs and the condition of the state housing stock. In addition, not all the people susceptible to Group A Streptococcus infections due to cold and damp living conditions reside in state houses. Many private rental properties are affected by the same issues. This is a wickedly complex problem relating to the restrictiveness of New Zealand's planning system, and the limited means by which renters can exert pressure on landlords to lift the quality of the rental stock (either through market pressure due to lack of choice, or through the Tenancy Tribunal). Requiring the Rheumatic Fever Prevention Programme to address the problems in the private and public housing sector is clearly well beyond the scope of a Ministry of Health-led initiative.

BOOTS ON THE GROUND

The Rheumatic Fever Prevention Programme illustrates the limitations of central government. Very often the problems central government has to address are highly complex, span many policy areas, and require a multi-agency response and coordination. This means central government is

⁶⁴ Sean Anstee, Personal interview (28 October 2015).

⁶⁵ Ministry of Health, "Implementation and Formative Evaluation of the Rheumatic Fever Prevention Programme" (Wellington: New Zealand Government, 2013), 5.

⁶⁶ Ibid. 72.

⁶⁷ Alan Johnson, "Give Me Shelter: An Assessment of New Zealand's Housing Assistance Policies" (Auckland: The Salvation Army Social Policy and Parliamentary Unit, 2013).

often slow to respond to specific problems, even when they are obvious. The costs of rheumatic fever are borne by the health system, but it is futile asking district health boards to fix policy problems in the housing sector. For that matter, it can be difficult for central agencies to pick up, let alone address, specific problems in a specific area because it oversees every region in the country, not just one.

By comparison, local government has advantages that allow it to sidestep some of the limitations central government faces. It is tied to one particular place, and is generally in a better position to see links between problems than officials in Wellington and craft responses accordingly.

A good example is the Seamless Boundaries project between the Kawerau and the Matamata-Piako district councils. Kawerau had a young population struggling to find work in the traditional wood processing industry. Matamata-Piako, by comparison, had the opposite problem. The district's population is ageing, a trend accelerated by the emigration of younger people. Silver Fern Farms, the area's largest employer, was struggling to fill its recruitment needs. The respective district councils, situated about 80 km apart, partnered with Silver Fern Farms to solve their respective problems. Central agencies did provide support, but the project was initiated and led by local stakeholders.⁶⁸

This is not to say local government should be tasked with fixing New Zealand's rheumatic fever problem, nor that councils are immune to siloed thinking. But local government is often better placed to develop local solutions to local problems, such as local employment schemes, more efficiently than central government – and should be given more responsibility.

Moreover, the cost of foregone opportunities needs to be factored in when tallying the costs of New Zealand's highly centralised governance. The *ultra vires* strictures of the *Local Government Act* required councils to ensure all activities were

explicitly permitted under the law. The 2002 reforms allowed councils more scope to pursue their own policies, but since 2008 the Key Government has led a return to a legislatively constrained operating environment by portraying local government as an incompetent and profligate spender of public money.⁶⁹ This is true at the margins, as the spending blowout on a water treatment plant in Kaipara District showed. But there is no evidence the sector's spending as a whole is worse than that of central government, and on many measures (such as debt) local government's books are in better shape than the Ministry of Finance's.⁷⁰ This also holds true to a large extent for local government's ability to innovate.

STREET SMARTS

An excellent example of local government innovation is Southland District Council's Changing Direction project. The district has one of the largest road networks in the country, consisting of more than 5,000 km of roads and 1,000 bridges. These roads are used extensively by the dairy industry, but represent a significant cost to the local population of 30,600 people (0.67% of New Zealand's total population). To ensure the costs did not become too burdensome on ratepayers, the council left a significant percentage of its roading network unsealed. This was complemented by a partnership with Fonterra, which enabled live data capture of road conditions and modelling to predict which high-use unsealed roads would need maintenance. This data was also used to compile

⁶⁸ Local Government New Zealand (LGNZ), "Winners of the 2016 EXCELLENCE Awards named," Media release (25 July 2016), Website.

⁶⁹ Paula Bennett, "Speech to LGNZ Annual Conference" (Wellington: New Zealand Government, 21 July 2015).

⁷⁰ Note that debt may appear artificially low, as not all councils have fully funded depreciation of existing assets, which was estimated by the Auditor-General at \$7 billion. However, even with this factored in local government's debt-to-asset ratio is only 16% versus the 10% currently stated. Office of the Auditor-General, "Water and Roads: Funding and Management Challenges" (Wellington: New Zealand Government, 2014), 31, and Statistics New Zealand, "Local Authority Financial Statistics Financial Position (Annual-Jun) 2014," Infoshare.

the Economic Network Plan, which has allowed the council to calculate the dollar value of exports carried by different sections of the network, which in turn steered future investment decisions.⁷¹

In another example, the Canterbury Mayoral Forum's Canterbury Regional Economic Development Strategy brought together the mayors and chairs of 11 Canterbury councils to address a predicted slowdown in the regional economy once the earthquake rebuild wrapped up and also to address the challenges posed by the region's ageing population. The forum has made notable inroads within just two years. It partnered with telecommunications company Spark to roll out mobile broadband across the region (expected to be 96% complete by 2016). The network is expected to run at speeds of between 40 and 135 megabits per second, significantly in excess of central government's Rural Broadband Initiative (estimated at 5 megabits per second).⁷² The forum is acting as an intermediary between training providers and employers, and is also working with industry to remove regulatory barriers that impede value-add export industries.

By giving local authorities more autonomy, central government could increase the level of policy innovation. As the Swiss and Dutch local government case studies in the second report show, good ideas are quick to spread while bad ideas are isolated. This consideration is an important advantage of a diverse and autonomous local government sector. No agency, central or local, can be expected to get every decision right, and mistakes have costly flow-on effects. However, when local authorities get it wrong their mistake is limited to one jurisdiction. No council has sought to replicate the complicated financial arrangements that resulted in a massive cost blowout with the Kaipara District Council's water treatment plant. A referee for this report noted that Kaipara's experience could have had a stultifying effect on other local authorities, where councils defer infrastructure

investments on projects deemed 'unaffordable' under the traditional funding streams.

NATIONAL DISASTER

Unlike local policy blunders, the effects of central government's mistakes are borne by everyone. A good example is the leaky buildings crisis, when central government switched from prescriptive building codes to performance-based regulation. This introduced a sequence of new building methods, such as Mediterranean-style cladding and untreated timber framing, without assessing their collective fitness for New Zealand's climate.

The effects were worsened by government's slow response to evidence that showed the new building methods were not fit for purpose. Further compounding the problem was the liberalisation of the building inspection process. When owners of leaky buildings sought financial redress from private firms for signing off on leaky buildings, many folded, leaving councils responsible for these failures under the 'joint and several' liability provisions in New Zealand law. The total costs to remedy leaky buildings was estimated in 2008 at \$11.3 billion.⁷³ However, the true costs are likely to be much higher. That is because the regulatory response in the wake of the crisis was to set very strict building standards, which make it difficult for new building materials and techniques to enter the market, thereby stifling innovation.

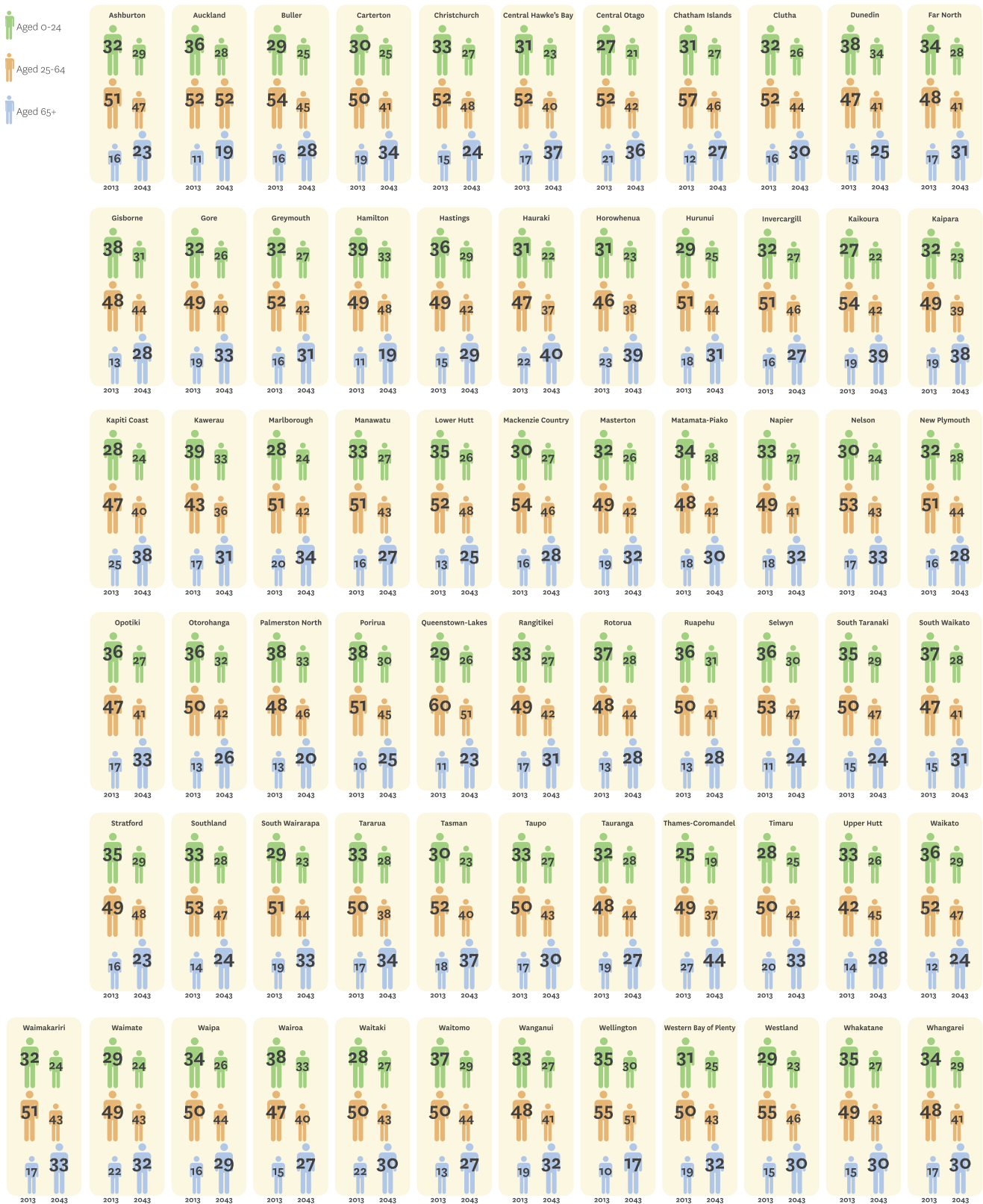
Councils too, in their capacity as building inspection authorities, have become extremely risk averse, thereby increasing both the time and expense it takes to build a house. It is a classic case of an incentive disconnect, where councils face few rewards for encouraging innovation, only increased risk. Even if they were to accept this risk, the main financial benefits from a more efficient building inspection process would flow to central government in the form of profit and sales taxes.

⁷¹ Local Government New Zealand (LGNZ), "Winners of the 2016 EXCELLENCE Awards named," *op. cit.*

⁷² Ultimate Broadband, "RBI wireless broadband," Website.

⁷³ James Zuccollo and Mike Hensen, "Weathertight buildings: What lessons can be drawn?" Paper for NZAE conference (Palmerston North: New Zealand Institute of Economic Research (NZIER), 2012).

Figure 2: Regional population by age group: projections to 2043⁷⁴



⁷⁴ Local Government New Zealand (LGNZ), “The 2050 Challenge: Future Proofing Our Communities” (Wellington: New Zealand Government, 2016).

Source: “The 2050 Challenge: Future Proofing Our Communities” (Wellington: Local Government New Zealand, 2016)

Devolving decision-making enhances local policy innovation. The ability to vary policy will become increasingly apparent as the pressures on urban, provincial and rural economies diverge. Urban New Zealand's population is ageing at a slower pace than in many rural and provincial areas, whose young people are moving to cities in large numbers. This difference also carries over to infrastructure and investment decisions. Major cities are facing the challenge of adding new infrastructure fast enough to adequately meet the rising housing supply demands. Outside of growth councils, the challenge is to wring the most use out of existing infrastructure amid a shrinking rates base whose ability to pay local taxes decreases as the population ages and retires. Even grouping New Zealand's communities into three categories oversimplifies how divergent the population challenges will be for different jurisdictions (see Figure 2). As the international research in this report series has shown, there is a growing understanding in many developed countries of the need to allow local authorities to draft bespoke solutions to local challenges. Equally clear is the understanding

that central government is poorly placed to cope with the variety and scope of these challenges – an experience central government officials in New Zealand also encounter, as the discussion in this chapter shows.

Handing over greater decision-making power to local government does not come without cost or risk. A devolutionary deal would constrain Parliament's oversight of local authorities and the ability to set nationally applicable standards where councils bear the costs thereof. However, from the discussion so far, it is equally clear it is not costless to maintain status quo. It is also reasonable to expect the costs to the country of maintaining the current governance structure will increase in the future as the population ages, cities grow, and demand for bespoke policy solutions to unique regional challenges increases. New Zealand needs to introduce a flexible, adaptive and accountable system while it still has the luxury of doing so voluntarily, rather than on the horns of a fiscal crisis (like in the United Kingdom). The only question is how should New Zealand go about this restructuring?

THE
NEW ZEALAND
INITIATIVE



CHAPTER FIVE

TOP-DOWN PLANS

Central government needs to implement reforms to repair its unsatisfactory relationship with local government. More than just repair, these structural changes should establish a robust means of engagement between the two tiers of government over the long term. These reforms can be broadly divided into two groups: top-down and bottom-up. The former refers to the reforms only central government can undertake, principally legislative changes to devolve power to local authorities. Bottom-up reforms refer to the changes local government needs to undertake to prove to central government that the sector is capable of handling additional powers (see Chapter 6).

CHANGE THEORY

As has been repeatedly highlighted in this report, as well as in the academic literature on local government in New Zealand, the mixed mandate and accountability gap problems need to be first addressed. Currently, local governments service the democratically expressed needs of their respective communities (focusing on core infrastructure and services), and perform the regulatory functions delegated by central government. Under this structure, both tiers of government are responsible for delivering services according to the wishes of the community – and cost effectively. In theory, this should provide double oversight, but has in practice blurred the lines of accountability in the eyes of ratepayers and voters alike. It has also allowed central government to enjoy a regulatory free lunch by allowing officials to sidestep the true costs of their policy decisions, while allowing councils to shift the blame for poor performance onto central government. Switzerland and the Netherlands avoid such problems by constitutionally defining the role of each tier of government; the United Kingdom does it through a contractual arrangement. These ‘separation of powers’ arrangements also ensure the respective tiers of government stick to their

mandated bailiwicks – making it substantially easier to identify success and failure and hold decision-makers to account.

DIVIDING LINE

New Zealand needs to implement a similar separation of powers if it is to improve the mixed mandate and accountability problems. The *Local Government Act* could be amended to avoid binding much needed local reforms to a broader and more complicated process, such as drafting a constitution for New Zealand. Local authorities should be given full control over and responsibility for the policy setting and regulatory powers already delegated to them under the Act, subject to democratic approval from their communities. The final say on the setting of local goods and services standards also needs to reside with the local community, subject to meeting national standards where applicable.⁷⁵

The distinction should be clear in the legislation to avoid scope and role creep later. A common observation in the countries profiled in the second report was political power tends to be centripetal and concentrates at the centre in the absence of legal limitations. The division of tasks between central and local authorities needs to be guided by the principle of subsidiarity, so local councils have final say over local tasks, regional councils over regional tasks, and central government over national issues. The quasi-constitutional separation of powers should maintain a strict distinction between the tiers of government, such that local councils cannot perform functions under central government control, such as education or welfare. This is to stop duplication of tasks and ensure voters can hold the correct agency or tier of

⁷⁵ It is assumed here that the costs of national standards are paid out of general taxation under the beneficiary pays principle since the benefits accrue at a national level.

government to account. This is a minimum form of devolution. A bespoke devolutionary structure is recommended later in this chapter.

A major advantage of this approach is that it is low risk. No material new powers or regulatory duties are conferred to local authorities. It is also low cost, limited to the costs of the legislative process. Central government would only transfer full responsibility of a range of activities to local authorities, backed by checks and balances. This will ensure clear lines of accountability, be it over dog control or releasing land for housing. Furthermore, some authorities have specialist expertise that central agencies cannot match, such as resource use expertise among councils in the mineral-rich regions of the West Coast and Taranaki.⁷⁶ This kind of devolution would allow councils to leverage this expertise further.

NO, THANKS

There will of course be instances where it is best for central government to set policy and standards nationally but which dictate outcomes at the local level. Some such areas are roads, environmental protection, telecommunication standards, and national planning frameworks, particularly where there are spill-over effects. These functions require a level of sophistication and scale that is beyond the capability and capacity of some councils. For example, under the *Resource Management Act 1991*, regional councils need to identify and protect outstanding natural landscapes (ONLs) in their regional policy statements, which district councils then approve. In practice, many district councils set the rules for ONLs. However, the Ministry for the Environment has not produced a policy toolkit on how local authorities should identify these landscapes, and many non-urban district councils have struggled with the complex process. This has resulted in a number of high profile land use disputes; in some cases, councils and anti-development activists have sought to protect outstanding national landscapes retrospectively.

⁷⁶ Jason Krupp, “From Red Tape to Green Gold” (Wellington: The New Zealand Initiative, 2015), 4.

Some of these conflicts could have been avoided had central government given councils and landowners a policy toolkit to identify possible outstanding national landscapes.⁷⁷ We would urge central government to concentrate its attention on these national policy areas instead of becoming involved in local matters.

These national matters as they exist should be listed in the *Local Government Act*, broadly stating the areas over which central government reserves the right to set policy. A mechanism whereby central government can introduce new areas should also be included. To prevent central government from expanding this list until all the devolved responsibilities are again under its control, local government should be able to opt out. This recognises that some territorial authorities are sophisticated enough to manage these functions for themselves, and that it may be desirable to let them set their own policy in these areas. In cases such as drinking water standards, communities face a trade-off between greater safety and lower service standards for a lighter tax burden. To opt out of these national standards, councils should show that their community supports this exclusion.

Referendums could test community support, ensuring sufficient discussion on the benefits and costs of accepting or rejecting centrally set standards. In some cases, central government may seek to override an opt-out decision because the benefits to the country are greater than the costs borne locally. In such cases, central government should provide the affected authority with additional funding from general taxes, consistent with the principle of ‘beneficiary pays’. However, checks and balances are needed to prevent a moral hazard, where local officials may pursue popular policies assuming central government will step in should things go wrong. The Productivity Commission has proposed charging councils for remedial actions related to releasing land for housing,⁷⁸ but this could be extended to other areas to act as a check and balance on local service standards.

⁷⁷ Ibid. 9.

⁷⁸ Productivity Commission, “Better Urban Planning – Draft Report” (Wellington: New Zealand Government, 2016), 194.

YES, PLEASE

A devolved approach tailors service delivery to unique regional characteristics. A number of functions such as education, welfare and even justice are handled by local authorities in other parts of the world. This contrasts with New Zealand, where central government provides the vast majority of public services coordinated from Wellington. However, even Wellington appreciates the limits of a ‘one size fits all’ system to some degree. For this reason, the country’s 2,500 centrally funded schools are run largely independently.⁷⁹

The district health board (DHB) structure addresses some of the shortcomings of a ‘command and control’ system. It recognises that local agents tend to have better access local information and act faster than a central ministry. This is not to endorse the DHB model of governance per se, only to highlight the flexibility of devolved structures. As Greater Manchester shows, local agencies can better see links between different types of social programmes than central government because of the siloed nature of ministries.⁸⁰ Indeed, there are moves in New Zealand to extend the role of local authorities in coordinating central government provided services, albeit at the margin. Promising examples include the Tamaki Regeneration Corporation and the Matamata-Piako and Kawerau initiative.

There is significant scope for local authorities to play a greater role in delivering services performed by central government, which needs to amend the legislation to facilitate more devolution. At the same time, it should be recognised that not all authorities will initially have the capacity and capability to take on the wide range of new tasks. Some authorities may be better equipped to perform some functions, while others will have capacity in other areas. Wellington City Council, for example, has sufficient balance sheet capacity to manage a large social housing portfolio. Indeed, it has done so for many decades, owning more

than 2,200 social housing units with a book value of \$353 million in 2012.⁸¹ Wellington City Council could possibly take over the state’s social housing responsibilities in the district if the community sanctioned this action and the council showed it could produce better outcomes. However, expecting present day Porirua City Council, with its financial constraints, to do the same is unlikely to help its social housing tenants. This is not to suggest central government should hand over its Wellington social housing portfolio to the council, or to assess whether local authorities should provide social housing. It is rather to illustrate that some councils can perform some of the functions currently delivered centrally. Where there is a reasonable expectation of better outcomes, and councils are willing to accept this responsibility, they should be allowed to do so.

A flexible local government framework can allow capable and willing councils to assume more responsibility. Devolution is taking place on a case-by-case basis in the United Kingdom, subject to negotiations between the two parties. The *Local Government Act* should be amended so contractual devolution can take place in New Zealand too, provided local authorities can show they are likely to produce better outcomes. A legislative structure is needed to set up these deals expediently. Currently, devolutionary deals like the Tamaki project require discrete legislation to be enacted.⁸²

Such a structure would allow councils to experiment with different policies to improve service delivery at the local level, or trial ways of tackling long-standing problems in a way a national rollout never could. The New Zealand Initiative has proposed a similar framework for voluntary devolution, only using special economic zones instead of amendments to the *Local Government Act*.⁸³ It largely amounts to the same

⁷⁹ Education Counts, “Funding to Schools,” Website.

⁸⁰ Jason Krupp, “The Local Benchmark,” op. cit. 11.

⁸¹ Wellington City Council, “About the Council’s social housing,” Website.

⁸² *Local Government (Tamaki Makaurau Reorganisation) Act 2009*.

⁸³ Khyaati Acharya and Eric Crampton, “In the Zone: Creating a Toolbox for Regional Prosperity” (Wellington: The New Zealand Initiative, 2015), 1–2.

outcome. If the recommendations in this report are adopted, it would create a platform for good ideas to be shared with other jurisdictions, or used to shape national legislation, while bad policy ideas can be quickly isolated and abandoned. Furthermore, as in Greater Manchester, negotiations between central and local officials will allow performance benchmarks to be included in any devolutionary deal; performance will also be measured – a feature often underemphasised or missing entirely from centrally run programmes. That said, care needs to be taken in designing these performance measures to avoid gaming the system.

SAFETY VALVE

In both devolutionary mechanisms proposed above, there is a real possibility local communities will make decisions that suit them, but which have wider negative spill-over effects. The case of NIMBY-ism (Not In My Back Yard) in Auckland is a good example of local residents opposing moves to lift height restrictions on inner city suburbs to preserve suburban amenity value. These well-organised actions have for many years constrained the supply of housing in the city, materially contributing to rising housing costs. Many households have now taken on so much debt to buy a house in Auckland that should the market correct, it could pose a much wider financial risk to banks and the New Zealand economy. This risk is well known by now. However, attempts to address the NIMBY problem are often thwarted by the local democratic process, wherein lobby groups and local politicians use their influence to resist change regardless of the wider implications.

The Productivity Commission, in its draft review of the planning system, has proposed giving central government the power to override local preferences and plans where these clash with national goals or have wider negative spill-over effects. Specifically, where the difference between the price of developable and undevelopable land exceeds a certain threshold, the commission wants central government to force councils to release land and build infrastructure until the differential narrows.

Although the commission's recommendation is specific to the planning system, it underscores the need for checks and balances, particularly where powers are devolved to local communities. Similar checks and balances should be mandatory for any devolutionary process. They must include appropriate and tangible thresholds, such as the land price differential proposed by the Productivity Commission; detail the powers central government will have to remedy problems; list the terms for their expiry; and list the conditions attached to prevent moral hazards, where local councils may be lax in performing their duties under the belief that central government will fix the problem at a later date.

The Productivity Commission has proposed charging councils for the remedial costs as a means of avoiding moral hazards. This mechanism is suitable to other policy areas, and will incentivise local councils to avoid central government intervention by making sound decisions wherever possible.

SHOW ME THE MONEY

Funding is critical to the success of this kind of devolution. If local authorities have to fund these costly programmes from their own tax base, many potentially beneficial devolutions might never even get started, given existing concerns about the affordability of rates. For that reason, central government should fund these programmes, using the DHB or education funding models as a starting point. These are good illustrations of services being managed locally but funded centrally on a per capita weighted basis. This ensures the quality of schooling in a rural municipality does not suffer because it is less affluent or has a lower tax base than an urban counterpart. A similar approach should be considered in New Zealand. However, care must be taken not to tie down funding too tightly to a set model as this could hamper policy innovation. For example, central government has restored a very limited degree of bulk funding in education with partnership schools. Students in these schools receive the same funding as students

in public schools on a per head basis. However, principals of partnership schools have significantly more flexibility in allocating resources compared to their public school counterparts, particularly in salaries. If local authorities can take over delivery of a service provided by central government, Wellington could also choose to block grant funding equivalent to their spending in the region.

In other cases, some worthwhile projects may not fit a conventional funding model. For example, central government has transferred 2,800 state houses to the Tamaki Redevelopment Corporation. These old houses will be replaced with modern, medium-density equivalents that use less land. The surplus land will be used for housing, which will be sold to private buyers. Critically, the proceeds from these sales will fund the social housing rejuvenation.

WHAT IS IN IT FOR ME?

A key feature of the Dutch, Swiss and increasingly UK local government structures is the direct incentives for authorities. In Switzerland, a resident moving from one commune to another brings with her direct tax revenues. (In New Zealand, property taxes complicate this process since a property owner would have to sell up and buy another property in another district for the same result). In the Netherlands, a household that changes municipalities takes with it the capitation grants that central government uses to fund local government activities. In Greater Manchester, local government shares any tax uplift that comes from the city's investment in local infrastructure. These financial incentives are structured to align the interests of local authorities and the country. In Switzerland, many local authorities strive to open sufficient land for development so housing remains affordable and attracts more taxpayers to their jurisdiction. Successful communes receive more tax revenue, while homebuyers benefit from stable house prices.⁸⁴ The country as a whole

also benefits because it neatly sidesteps the problem gripping Auckland: the underprovision of public infrastructure and a housing shortage. In Manchester, local government is investing heavily in public transport across the city-region to grow the effective size of the labour pool for its most productive centres (central Manchester and the airport). The Key Government has a stated goal to increase the pace of economic growth and increase exports. A 'tried and tested' means of achieving this is to financially reward local government for encouraging economic growth.

The current rating system is generally considered to provide sufficiently strong financial incentives to councils to pursue growth enhancing activities such as investment in housing infrastructure. The first report in this series did indeed find a link between council revenue and population growth.⁸⁵ However, it also found a funding gap arising from the period between when councils spend public money on infrastructure for new housing development and when new residents start paying local taxes. Ratepayers are reluctant to allow debt to fund the gap. As a result, the incentive from ratings base growth is weaker than many people think, as councils are politically rewarded in the short term for limiting the scale of their infrastructure investments to keep their books in order. This has, however, constrained the supply of housing in Auckland and other fast growing regions in New Zealand. It also provides little incentive to existing residents to accept this development, since they tend to only see the costs of new residents (congestion, higher taxes in the short to medium term) and not the benefits (potentially lower local taxes in the long term). This may further encourage NIMBY attitudes to development. Direct financial incentives could help reverse this trend. It is beyond the scope of this report to develop a specific incentive model, a major task best undertaken by officials. Nevertheless, three incentive models could be a starting point for the discussion.

⁸⁴ OECD, "OECD Analytical House Price Database" (Paris: OECD Publishing, 2015).

⁸⁵ Jason Krupp and Bryce Wilkinson, "The Local Formula," *op. cit.* 29.

PERFORMANCE PAY

A simple and straightforward method would be to link the pay packages of councillors and mayors to a measure of their local growth rate. To do this, the Ministry of Finance might set aside a sum of money for a local government bonus pool. This is to recognise that central government is the main beneficiary of local economic activity, since it receives all the salary, sales and profit taxes generated from local economic activities.

At the beginning of an election cycle, the elected officials in conjunction with the chief executive could develop a three-year plan, laying out their objectives over the next three years. The Minister of Local Government can negotiate with local government on the specifics until they agree on the plan. For multi-year projects, the performance pay could be split between immediate financial rewards for meeting targets within their political tenure, as well as long-term rewards. This is to prevent local politicians from picking projects that will reward them in the short term but that could prove costly or problematic later. Six months before the next election, the Department of Internal Affairs, or an independent third party such as the Office of the Auditor-General, would assess performance against the plans and award financial bonuses accordingly.

There are several advantages to performance bonuses. Local authorities across the country are struggling to find high calibre individuals to stand for local public office. A performance bonus might make a councillor's job attractive enough to lure skilled people from the private sector who would not otherwise consider such a role (although the direction of causality could run the other way). It would also allow central government to ensure local objectives are broadly aligned with national policy. The fiscal costs of a local government performance package are likely to be trivial. The \$26 million spent on the flag referendum would give each council a bonus pool of \$334,000. That is a substantial sum for most councils, and could be apportioned across various portfolios. It is, however, trivial compared to the total economic activity possible if councils had a positive attitude to development.

Adding financial incentives into the mix may also increase the chances of local officials working towards a tangible set of goals. A cynic might say local officials only have one primary concern – to be re-elected. To this end, all they need to do is cater to the concerns of their constituency, even if these concerns run counter to the strategic objectives of a jurisdiction, such as investing in arterial roading to ease congestion. By introducing a second financial incentive, councillors would have to balance their interests more carefully (although free-riding will be a temptation for some). Lastly, the bonus structure would give the electorate a mechanism to assess council performance, and hold officials accountable to the performance contract.

TAXING MATTERS

There are two potential weaknesses of the performance pay scheme: the benefits may be seen to be concentrated too narrowly on elected officials, and the local community has little say in the targets. It also does little to incentivise residents of inner city neighbourhoods to accept greater levels of intensification when the benefits from doing so accrue to local politicians and the costs fall on them. Furthermore, some may see performance pay as incompatible with the ideals of public service.

One way to fix this is to let financial incentives, augment a council's budget. The Initiative recommends central government pay local councils for every new house completed within a specified period. The payments could be benchmarked on the goods and services tax (GST) charged on residential building (excluding land value), or be a fixed sum.⁸⁶ Under the GST model, if each of the 9,400 residential building consents issued

⁸⁶ Michael Bassett, Luke Malpass, and Jason Krupp, "Free to Build: Restoring Housing Affordability in New Zealand" (Wellington: The New Zealand Initiative, 2013), 17.

in Auckland in 2015 resulted in construction,⁸⁷ and each home had a build value of \$200,000, Auckland City Council would have netted \$282 million.

That is a substantial amount of money, but if it meaningfully results in a faster home construction such that the pace of house prices increases flattens or declines, central government could reasonably hope to be compensated by improved economic performance. Recent research in the United States has shown how high rates of house price inflation relative to wage growth due to land use regulations have driven lower income households away from productive areas.⁸⁸

Auckland's current housing crisis and the rise of homelessness suggest the same effect is dragging on the country's biggest regional economy. As it stands, Auckland housing ranks as one of the least affordable in the world, with a median house price equivalent to 9.7 times the median household income.⁸⁹ Our recommendations would also signal to existing residents that new arrivals to the city are unlikely to increase local taxes, since new infrastructure investments would be funded to some degree by the housing subsidy. Councils could also use the funds to improve neighbourhood amenities to compensate existing residents for the development happening in their area.

This kind of incentive package only targets districts struggling with housing affordability problems, which makes it too narrow an option for New Zealand's heterogeneous local government landscape. But there are options to put in more comprehensive incentive packages that apply to all councils, regardless of individual characteristics. The Initiative's tax sharing framework is an

option.⁹⁰ Under this model, councils would get a proportionate share of any increase in tax revenues that central government receives, relative to a baseline projection. So if Treasury projected Auckland's economy would grow at 5% over a 12-month period, and the actual growth rate was 6%, the council would get a share of the taxes collected by central government resulting from that additional one percentage point growth in regional GDP. Using 2014 figures, the framework estimates the council's share at \$108 million, equivalent to 3.1% of Auckland Council's total revenue for that year.

That is not insubstantial, but importantly it would provide a clear incentive to local government to implement pro-growth policies. Under the model, should Auckland's economy beat baseline projections by 5 percentage points, the council's share of local taxes would be \$542 million, or 15% of the city council's total revenue. Importantly, the region's performance is measured relative to expectations, which can be adjusted as necessary.

The advantage of such an arrangement is it could be applied to provincial and rural councils as well, where urbanisation and an ageing population are acting as a drag on the local economy. Under this scenario, if the local economy shrinks at a slower pace relative to official projections, councils would share in the tax revenue that central government would have otherwise forfeited.

Some critics may be sceptical about the capacity of small rural councils to curb the decline of their economy. However, towns like Kaitangata on the South Island have shown it is possible to attract people from other parts of the country by offering incentives.⁹¹ The main attraction was affordable housing, made possible by a private donation of land. If central government sweetened the deal with financial incentives, so to speak, more rural towns could be encouraged to experiment with different strategies to reverse their population

⁸⁷ Statistics New Zealand, "Building consents issued, August 2016," Website.

⁸⁸ Peter Ganong and Daniel Shoag, "Why Has Regional Income Convergence in the U.S. Declined," Manuscript (Harvard University), 26–28.

⁸⁹ Demographia, "12th Annual Demographia International Housing Affordability Survey: 2016," op. cit.

⁹⁰ Khyaati Acharya and Eric Crampton "In the Zone," op. cit. 1–2.

⁹¹ Newshub, "Jobs and land galore in Kaitangata," Website.

decline where Kaitangata-type altruism cannot be relied on. Central government is also a potential winner under these arrangements. It has to share tax revenue at the margin with local authorities that exceed benchmark performance, but it is tax revenue it would not have otherwise received.

POPULATION BONANZA

A possible weakness of this tax sharing approach is that the government statistician's systems are not sophisticated enough at present to calculate GDP at a territorial authority level. Nor can Inland Revenue calculate sales taxes at a territorial authority level. The department is undergoing a major systems upgrade, but it is uncertain whether the new infrastructure will be sufficient for the Initiative's proposed model to work. An alternative is to use other data as a proxy for GDP.

One such source is Statistics New Zealand's (SNZ) population projections, which are conducted at a local authority level. Local authorities use these projections for their 10-year and longer-term plans. The scheme would have each local authority negotiate with Wellington on 10-year population projections in that region, calibrated against recent local growth and SNZ's medium scenario projections. Local authorities would propose the growth rate, and central government would need to justify overturning the proposal. But central government would have the power to scale up or down all projections so the total sum for all New Zealand matched the growth in SNZ's medium scenario. A *force majeure* clause would reset the agreement if an unexpected development were to substantially affect either party, such as the Canterbury earthquakes. Local authorities that beat this projected population growth rate, as measured by SNZ, would receive incentive payments from central government. To ensure these incentives are effective, they should be made on a rolling annual basis. Councils that miss the negotiated target would incur a debt with central government equivalent to the incentive.

This arrangement has many of the same advantages as the tax sharing model, in that it applies to

communities experiencing population growth or decline. It would only represent a net cost to central government if overall population growth exceeded the benchmark. It also places a strong incentive on local authorities to experiment with different policy settings. The Initiative views the current arrangements, whereby a council's operating costs are simply apportioned across its population on a weighted basis, as a weak incentive to innovate. That is because whether councils perform well or poorly, their expenses are covered by the existing population.

Some may criticise the proposed incentive setup as a beggar-thy-neighbour framework, since local authorities would compete for local residents. However, their neighbours will have the same incentives structure, and the point is to improve community wellbeing (not to protect non-performing councils). Indeed, central government could choose to use the special economic zone framework to roll out the incentive scheme, and gain the ability to veto proposals it objects to. If this arrangement results in more competition between local authorities, then it is a positive outcome. As in Switzerland, policies that increase local revenues are likely to be quickly copied, and the costly ones corrected or isolated. Switzerland is ranked as the most competitive economy in the world by the World Economic Forum.⁹² Furthermore, in Switzerland a race-to-the-bottom scenario is prevented by equalisation payments, which ensure public services are equally funded on a per capita basis across the country. New Zealand could expect the same protections, since central government funds many state services (e.g. education, health). Again, much like the other incentive packages outlined in this chapter, payments tied to population growth would increase transparency and accountability, as local residents would want an explanation for why their council has not received a payment, or indeed why it has incurred a debt with central government.

⁹² Klaus Schwab, "The Global Competitiveness Report 2015–2016," op. cit. 7 and 23.

MINISTERIAL MUSCLE

Implementing the kind and scale of change recommended in this report will require a high level of political management. For this reason, the local government portfolio should be given much greater prominence in central government than is currently the case. For much of New Zealand's history, the portfolio has either been handled by a junior minister, or only briefly by a senior minister enacting major change. This is incongruous with the importance of local government, let alone the scale of reform needed to turn this sector around. A senior minister should handle the local government portfolio, possibly by assimilating the portfolio into the Department of the Prime Minister and Cabinet (DPMC). This would give it equal standing with the Greater Christchurch Regeneration and Civil Defence and Emergency Management portfolios, which are managed by the DPMC.

The final recommendations cannot be written into policy because they are attitudinal – but necessary. The first is for central government officials to accept that fundamental change is needed if local government is to become a driver of economic growth. More than 170 years of centralisation and

amalgamation have failed to create the right size of local authority to maximise efficiency (it is a pointless exercise because different tasks have different economies of scale). It would be unwise to say doubling down on this consolidationist strategy will pay dividends now, when they have not delivered an optimal size for local government to date.

Second, shifting to a localist form of government will present risks to central government. Indeed, it is foreseeable that in devolving powers to local government, situations will arise where central government will be tempted to step in and take over a struggling council. The Prime Minister or the Minister of Local Government need to restrain themselves in such cases. If local authorities and the communities they represent are not allowed to face the consequences of their decisions, how can they be expected to act wisely in the future? After all, the behaviour of local authorities is an outcome of the current incentive framework.

That said, there is every reason to expect failures will be marginal, and that local authorities are ready to play a more active role in promoting the pace of economic growth in New Zealand.

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LAKE TAUPO

CHAPTER SIX

BOTTOM-UP SIGNALS

This report has laid a significant challenge before central government. If the recommendations in Chapter 5 are adopted, local authorities will have more autonomy from central government in performing their current duties and tasks. They will also be able to take on functions that are now the exclusive domain of central government. Councils will share to a greater degree in the benefits of the economic growth they facilitate in their jurisdictions. It is a significant amount of power that central government is being asked to cede. Even with the promise of greater economic growth, lighter regulatory drag, and region specific policy setting, no responsible government would enact these reforms unless it was dealing with a capable and credible partner in local government.

Can local government be a capable and credible partner? The answer depends on who you ask. The view among central government officials, based purely on anecdotes, is probably a ‘no’. This is likely a reflection of the fractious relationship between central and local government, particularly under the Key Government.⁹³ But there does seem to some truth there. Dunedin City Council’s decision to proceed with a \$200 million sports stadium upgrade instead of fixing its crumbling sewer system is a popular example of local government profligacy.⁹⁴ (This example should be taken with a pinch of salt, as central government encouraged the stadium project ahead of the 2011 Rugby World Cup and provided \$50 million in funding).⁹⁵

Attitudes towards local government are not much better among the public, who rated the sector’s overall performance as 29 out of 100 in a 2015 poll.⁹⁶ To put this into perspective, in 2014 the UK public rated local government’s overall performance at 68 out of 100 – higher than that of central government.⁹⁷ And although the Initiative’s own research showed councils performed at a higher standard than many perceive, including central government, there is still room for councils to proactively lift their game, particularly if they want more powers devolved to them.

The theme of this report is that local communities are best placed to solve their own local problems, so this report eschews making individual recommendations for each authority. To do so would be to repeat the ‘one size fits all’ or ‘some analyst in Wellington’ mistake of the current highly centralised governance arrangements. Instead, this report focuses on two areas, with recommendations sufficiently broad that they can be adapted and amended to suit local characteristics. Councils that show notable improvement in these areas indicate a potential capacity for taking over more responsibility from central government.

SOBER VIEWING

One of the most common critiques of local authorities is a lack of spending discipline. Anecdotes about profligate use of ratepayer money by local officials abound. Indeed, central government continues to use the pace of rates increases, which have exceeded the pace of wage

⁹³ Michael Reid, “Managing Central-Local Government Relationships,” *op. cit.* 29.

⁹⁴ Dunedin City Council, “Forsyth Barr Stadium Review” (Dunedin: 2014).

⁹⁵ John Key, “Govt announces \$15m for AMI Stadium,” Media release (Wellington: New Zealand Government, 30 April 2009).

⁹⁶ Local Government New Zealand (LGNZ), “The New Zealand Local Government Survey,” *op. cit.*

⁹⁷ Local Government Association (UK), “Polling on Resident Satisfaction with Councils” (London: LGA, 2014).

increases and consumer price inflation over the medium term, as a rationale to further consolidate the sector.⁹⁸

Caution must however be taken not to judge the sector's performance on these metrics alone. The Initiative's research has found that while spending by local authorities has increased faster than consumer prices, consumer items make up only a tiny fraction of council spending.⁹⁹ Roading, transportation, water supply, and waste water and solid refuse removal accounted for 46% of the sector's total operating spending in 2015,¹⁰⁰ and cost inputs into these activities do not tend to match those that go into calculating consumer price inflation. Nevertheless, spending and rates increases in many councils have exceeded the annual increase of the Local Government Cost Index.¹⁰¹

Council expenditure has remained broadly flat as a share of GDP since 1940.¹⁰² In fact, it may be desirable for spending to exceed the prescribed level in the short term. In places like Auckland and Tauranga, commitments to keep rates flat resulted in underinvestment in infrastructure (now being rectified by opening land for housing development). All these measures and considerations create a muddled picture, and may explain why it is hard for the layperson to assess council spending.

A better means of assessing spending is the basis upon which spending decisions are made. As Derek Gill notes, "What matters is that councils are able to explain the reasons why they may

have exceeded a benchmark".¹⁰³ Under s 32(2) of the *Resource Management Act*, local authorities are required to assess the costs and benefits of any major spending item proposed in the district plan.¹⁰⁴ This analysis must include environmental, economic, social and cultural effects, but special consideration must also be given to the anticipated effect on economic growth and employment. The legislation also requires that where practical, councils should quantify these costs and benefits.

A random examination of s 32 analyses from various district councils shows that in many cases they fall short of the standard implied by the legislation, or what an economist might recognise as a robust cost-benefit analysis. For example, in the Kapiti Coast District Council's 10-year plan, the cost-benefit analysis that accompanies the infrastructure, services and associated resource use section amounts to little more than a list of what might or might not be costs and benefits, with the decision tipped to whichever list is longer.¹⁰⁵ This bears no resemblance to what an economist would recognise as a cost-benefit analysis, which seeks to systematically measure the expected net benefits of a proposal for affected members of a community. Kapiti District Coast Council is not the only local authority to take such a cavalier approach to its s 32 obligations (this is not to argue central government is much better).

If local authorities want to demonstrate they can be trusted with additional responsibilities and financial incentives, they need to prove they are wise spenders of ratepayer money, or at the very least better than central government. On significant matters, councils should produce robust cost-benefit analyses as part of the 10-year

⁹⁸ Cabinet Economic Growth and Infrastructure Committee, "Local Government – Better Local Services Reforms," op. cit. 4.

⁹⁹ Jason Krupp and Bryce Wilkinson, "The Local Formula," op. cit. 18.

¹⁰⁰ Statistics New Zealand, "Local Authority Financial Statistics Income and Expenditure by Activity (Annual-Jun), 2014," Infoshare.

¹⁰¹ BERL, "Forecasts of Price Level Change Adjustors – 2015 Update" (Wellington: Society of Local Government Managers (SOLGM), 2015), 16.

¹⁰² Jason Krupp and Bryce Wilkinson, "The Local Formula," op. cit. 17.

¹⁰³ Derek Gill, "Fiscal Measures, Parameters and Benchmarks" (Wellington: New Zealand Institute of Economic Research (NZIER), 2012), 26.

¹⁰⁴ *Resource Management Act 1991*, s 32(2).

¹⁰⁵ Kāpiti Coast District Council, "Kāpiti Coast District Plan Review Section 32 Analysis – Summary Report Infrastructure, Services and Associated Resource Use (Part 1: Infrastructure & Network Utilities)" (2012).

planning process mandated under the *Resource Management Act*. Councils need to have the expertise to distinguish between competent and incompetent assessments, but they can contract out the actual assessment to an independent economic consultancy. Auckland Council, for example, hired the New Zealand Institute of Economic Research to assess the benefits and costs of the Proposed Auckland Unitary Plan.¹⁰⁶

This process will incur an additional expense but it will also reduce wasteful spending. Councils that undertake it would allow interested parties such as central government and the business community to assess the quality of their decisions. The greater transparency should improve confidence that ratepayer money is being well spent.

Improved economic analysis is essential for local authorities to improve their standing in the eyes of communities and central government. However, as Greater Manchester shows, it is probably not sufficient in itself to convince central government to devolve power. A track record of sound governance and management is also necessary. Local Government New Zealand recently launched its Excellence Programme, an independent performance rating benchmark of local authorities. Participating councils will be assessed on four categories: governance, leadership and strategy; transparency in financial decision-making; standards of service delivery and asset management; and stronger engagement with the public and businesses.¹⁰⁷ The first set of ratings has yet to be completed, but 21 out of New Zealand's 78 local authorities have signed up to the programme. Councils should be encouraged to persevere with the performance management scheme.

TALK WITH ME

Under the devolved model of government recommended in this report, local authorities are agents of community as distinct from central government in performing their duties. A primary duty of local government is to consult with its community, and then to use this information to develop a 10-year plan. This mandated planning process is overly complex and makes many people feel disenfranchised, as was recently noted by the Auditor-General's office.¹⁰⁸ Central government sought to correct this in 2012 by requiring local authorities to produce consultation documents instead of the draft Long Term Plan (LTP). The purpose was to start a discussion between local authorities and communities over the proposed long-term objectives in a transparent fashion.

This is a welcome development, but one that has not met its intended purpose. The Auditor-General's review of the consultation documents found that many local authorities failed to meet the new standard for consultation. Many of the documents were poorly written and failed to explain the significant issues facing a community. Even where the issues were explained, many documents did not spell out different options, the implications and consequences.¹⁰⁹ In one case, an authority was found to have excluded the most important issue facing it from the draft consultation document.¹¹⁰

Such shortcomings need to be rectified if residents are to have greater confidence in their local representatives. If the level of local government accountability is to be meaningfully improved, communities need to know what options are available to them, the trade-offs associated with each, and the consequences of their choices. The need for community buy-in is doubly important if local authorities are to convince central

¹⁰⁶ Auckland City Council, "Section 32 RMA report of the Auckland Unitary Plan" (Wellington: New Zealand Institute of Economic Research, 2013).

¹⁰⁷ Local Government New Zealand (LGNZ), "Local Government Excellence Programme," Website.

¹⁰⁸ Office of the Auditor General, "Consulting the Community About Local Authorities' 10-year Plans" (Wellington: New Zealand Government, 2015), 3.

¹⁰⁹ Ibid. 9.

¹¹⁰ Ibid. 13.

government to give them more autonomy and independence.

Clearly councils must establish a means of establishing dialogue. Given the plethora of digital communication platforms available today, there are many ways to achieve this. However, councils would be well-served to stick to clear, simple strategies. An excellent example is Wanganui's annual referendum conducted between 2005 and 2010.¹¹¹ Under this scheme, residents of the district were asked to weigh in on the council's proposed spending objectives, and in one case residents were asked to say which level of rates they preferred with the respective spending priorities attached to each (high, medium and low).¹¹² Although the referendum was not binding, Wanganui District Council used the information to steer its LTP. A review of the referendum by the Department of Internal Affairs found strong community support for the annual referendum as a means of engaging the community. In the five years reviewed, voter participation varied between 46% and 61%, only slightly lower than the turnout for local government elections (67% in 2004, 63% in 2007, and 60% in 2010¹¹³). Interestingly, one of the profiled stakeholders said that as a result of the referendum, they did not feel the need to participate in further consultation processes associated with major council-led developments, in this case the Splash Centre expansion.¹¹⁴

Putting tax measures to a referendum risks citizens favouring present consumption over future consumption. That is to say, they may favour lower taxes now by deferring investments that would benefit them in the long-term. Some jurisdictions have gotten around this problem

by forming citizen juries. These are panels made up of randomly selected residents and business asked to assess local plans, and given access to the supporting documentation used to develop these plans. The jury then reaches a verdict on the plan, which is used to steer amendments to it. The city of Melbourne used a citizen jury to get community buy-in on a AU\$5 billion financial plan. Under the original proposal, local taxes would have increased by 2.5% a year above the rate of inflation. But under guidance from the citizen jury, this was brought down by lifting developer contributions and selling non-core assets. The jury also accepted an increase in borrowing to fund infrastructure spending, a long-standing roadblock holding up the city's investment programme.

The bottom-up recommendations in this chapter should not be viewed as an exhaustive list of to-dos local authorities need to cross off to trigger the devolutionary discussion. Rather, they are proposed as signals to show local government can be credible on democratic economic growth matters. These signals should not be used passively. As in Manchester, local authorities seeking greater autonomy need to demonstrate a track record of sound decision-making, backed by clear community support for their strategic direction. They have to make the case in Wellington that devolution will make New Zealand better off. Hiding their light under a bushel and hoping central government notices them is pointless. This report has illustrated the capacity of local government to innovate. This advantage should be used to show how local authorities can meaningfully help speed that pace of economic growth and tackle long-standing social and economic problems.

¹¹¹ Local Government Information Series, "Case Study: Wanganui District Council" (Wellington: New Zealand Government, 2008).

¹¹² Referendum questions were not always limited to three options, and varied between one yes/no option, and 14 topics in one case.

¹¹³ Department of Internal Affairs, "Local authority election statistics 2004–2013," Website.

¹¹⁴ Local Government Information Series, "Case Study: Wanganui District Council," op. cit. 21.

CONCLUSION

In wrapping up the final report of the Initiative's three-part series on local government in New Zealand, it is worth restating the problem we sought to address: the poor relationship between central government and local authorities. It is a problem regularly encountered in all areas of our lives, be it housing affordability, resource use, or speeding up economic growth in New Zealand.

It is a fractious relationship resulting from the way New Zealand has chosen to structure its governance affairs. Poor lines of accountability and double regulatory responsibility have made it difficult for the public to tell which tier of government is ultimately responsible for the various public services. The same muddled arrangements mean central government gives too little consideration to the costs its policies impose on local communities and, in turn, allow councils to blame their poor performance on central government. Meanwhile many of the day-to-day issues that affect ordinary people's lives, or the issues they care deeply about, remain unresolved.

In this environment, it is hardly surprising that communities are becoming increasingly intractable to local investment even if they can benefit from these activities in the long term. This political constraint identified in the first report is clearly evident in New Zealand's fastest growing regions, where the slow pace of infrastructure provision has fed directly into high house prices. It also explains the tense relationship between central and local government to some degree, particularly where local government is seen as frustrating central government's plans to 'grow the economy'.

The policy recommendations in this report provide a practical means of addressing this problem, and further the common aim of both tiers of government to improve the wellbeing of New Zealanders.

This report advocates a progressive shift towards greater accountability by making local government directly accountable to communities over the local activities they perform. Amending the *Local Government Act* is the most effective and

efficient means to achieve this as it sidesteps the needs to pass legislation for each devolutionary arrangement, as in the Tamaki project.

However, local authorities must meet central government half way by demonstrating through local referenda and citizen juries that they are acting according to the wishes of their community. Furthermore, local authorities need to demonstrate they are wise spenders of ratepayer money. Councils could substantially improve any devolution pitch they make to central government by dramatically improving the quality of the cost-benefit analyses on their proposed long-term plans.

Local government's ties to place and proximity to their community mean they are often best placed to see links between social problems not obvious to central government. The Matamata-Piako partnership with Kawerau to tackle youth unemployment and skills shortage are excellent examples. Councils also have a track record of policy innovation, as the Southland roading project shows. This needs to be embraced. Local authorities should be allowed to take on additional responsibilities from central government if they can demonstrate improved outcomes. This will allow the country to experiment with different policy solutions in a way central government cannot.

Lastly, if central government seeks to address the political constraint among local communities, it needs to create clear financial incentives that encourage communities to welcome development in their area. Communities need to share in the benefits of economic growth, not just the costs, to change NIMBY attitudes. Incentives can range from performance pay for local officials to tax sharing.

It is worth restating that central and local authorities are working towards the same aim. They ultimately serve citizens, who entrust these agencies with a range of powers to make their lives better. The localist framework put forward in this report will allow these two important tiers of government to work in partnership towards this goal.



AUCKLAND

KEY POLICY RECOMMENDATIONS

TOP-DOWN REFORMS

- Amend the *Local Government Act* (LGA) to make district, regional and territorial authorities 100% responsible for the services they already deliver. Except where there are large negative spill-over effects, central government should refrain from interfering in local matters.
- Where there are spill-overs or benefits from central government putting nationally consistent regulatory frameworks in place, these should be clearly set out in the LGA, including mechanisms to introduce new matters as they arise.
- To restrain central government from unduly expanding its mandate, councils should be allowed to opt out of central policy that affects their jurisdiction, provided the opt-out is approved by a local referendum.
- Where communities choose to opt out of a specific policy, they should be liable for any costs opting out imposes costs on central government to avoid a moral hazard.
- Some local authorities may be better placed to take on tasks currently managed by central government in their jurisdiction. A good example is the Tamaki regeneration project. Where councils are likely to achieve better outcomes, councils should be allowed to negotiate with central government to have these functions, including funding, handed over to them.
- Financial incentives should be introduced to encourage councils to ensure local government

aligns its activities with central government's economic strategy. Possible options include:

- Central government pays bonuses to local politicians that meet agreed-upon performance targets
- Pay housing encouragement grants to fast-growing local councils for every new house built in the jurisdiction within a minimum time frame, and
- Allow councils to share in the economic growth that occurs in their region via a tax-sharing arrangement should growth exceed central government projections. Population growth projections might be used as an alternative to territorial GDP.

BOTTOM-UP REFORMS

- Local authorities need to show they are prudent spenders of public money. To do this, councils need to improve the quality of cost-benefit analyses of long-term plans. Current assessments fall far short of what an economist would recognise as a cost-benefit analysis.
- The purpose of local government is to “enable democratic decision making and action by, and on behalf of, communities”. Current consultation processes are overly technocratic and complex – and disenfranchise many communities. If councils are to be allowed more autonomy, they need to show their actions are steered by local democratic preferences. Two excellent mechanisms worth considering are local referendums and citizen juries.

APPENDIX 1

LOCAL AUTHORITY MANDATE FOR INVOLVEMENT IN REGIONAL ECONOMIC DEVELOPMENT

The Department of Internal Affairs
Te Tari Taiwhenua

Memo

To	Chief Executive Environment and Economy Forum
From	Helen Wyn, Deputy Chief Executive, Department of Internal Affairs
Date	17 August 2016
Subject	Local authority mandate for involvement in regional economic development

Purpose

This memo provides comment on The Department of Internal Affairs' position in relation to a concern expressed that regional councils (and local authorities more generally) may have no legal mandate to be involved in economic development activities. As expressed at the meeting in May, this concern relates to amendments to the statement of the purpose of local government in the Local Government Act 2002 (LGA02).

Background

As statutory bodies, local authorities can only act in ways that have been authorised by Parliament. The LGA02 marked a move from the previous detailed and prescriptive approach to local authority powers, to giving each local authority the power "to carry on or undertake any activity or business, do any act, or enter into any transaction [for] the purpose of undertaking its role." This empowerment was subject to other provisions in the LGA02, all other Acts and the general law.

Importantly, the LGA02 also includes a hierarchy of purpose statements and principles to guide local authority discretion, and a framework of process requirements designed to ensure transparency and community accountability. This reinforces the fundamental purpose of local government, which is to "enable democratic local decision-making and action by, and on behalf of communities".

The 2012 amendment to the LGA02's original statement of the purpose of local government replaced reference to promoting "the social, economic, environmental, and cultural well-being of communities" with meeting "the current and future needs of communities for good-quality local infrastructure, local public services, and performance of regulatory functions in a way that is most cost-effective for households and businesses".

The policy rationale for the change was to "assist local government [to] maintain focus on doing those things that only it can do".

Comment

The purpose statement should not be considered in isolation as the yardstick for legitimate council activities. The LGA02 prescribes a range of other principles and processes to guide local authority discretion. With the support of their communities, and subject to appropriate engagement and decision-making processes, Councils may be considered to have the necessary authority and legal mandate to be involved in the promotion of economic development.

DIA's position on the mandate for economic development activity by local government is that the 2012 restatement of the purpose of local government does not materially detract from the legal authority for local authorities to be involved in economic development activity.

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Local government for most of us is the sharp end of government. It's local government that decides where and when we can do our business and what we can and can't do in our homes. We are also more acutely aware of what local government costs us in rates compared to central government where the much greater cost is hidden in PAYE and GST.

It's little wonder that it's local government that bears the brunt of our criticism of government. The response has been a continual attempt to reform and improve local government.

Jason Krupp challenges us in his report that the solution to the problem of local government is not the present trend of fewer councils but more, not a local government that does less but one that does more. It's both a challenging and enticing report, especially to those of us who favour diversity, choice and competition over the rhetoric of uniformity and consistency.

Foreword, Rodney Hide

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