SmartGrowth

Alternative Approaches to Funding the Costs of Growth

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Updated May 2004

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1 Introduction

Funding the costs of growth is a fundamental tool for implementing the SmartGrowth strategy. The funding issues relate less to the exact quantum of costs that are difficult to identify with any certainty beyond 10 years, than to:

- an acceptance that there is a significant funding gap between existing approaches and the levels of expenditure necessary to support ongoing growth particularly in the areas of transportation, community facilities and stormwater.
- a reluctance by parts of the community to pay the true costs of growth
- the basis on which the costs of growth are allocated within the community –i.e. who pays?

This report outlines the work done for SmartGrowth in examining funding alternatives and how this issue can be incorporated into the SmartGrowth Strategy.

The report concentrates on a more applied use of current local government funding tools together with additional tools or refinements that need to be progressed.

It explores a range of new approaches, since some fresh thinking is required to ensure that there is the level of ongoing commitment since community facilities and infrastructure need to be funded in a timely manner.

It also accepts that Government has recently undertaken a review local government funding and that the provisions of the 2002 Rating Powers legislation are likely to remain for a time, although there is substantial pressure to look at funding methods other than the traditional property tax approach..

Also the Local Government Act 2002 provides new tools for Councils to recover growth related capital expenditure through development contributions.

Finally the report does not address the increasingly vexed issue of the ability of Government to provide its share of infrastructure in a timely manner. Government is aware of this issue and has appointed a Cabinet Committee headed by the Minister of Finance to generate solutions. The issue is of significance in the growth areas of New Zealand, which are predominantly the upper North Island.

It should be noted that a separate report will be produced which specifically identifies the growth related funding gaps in key areas of infrastructure;

- Transportation
- Community facilities and infrastructure
- Stormwater.

Inevitably some of the growth related gaps will overlap with

- Historical catch-up in lag infrastructure e.g. reducing the stormwater problems in an area of proposed development or need for open space areas where intensification is already occurring.
- Increased levels of service.

This report is an interim report, mad available to share current thinking on issues with the community. The Joint Committee received the report in September 2003. At that meeting a request was made for further investigation to take place into methods of regional funding including public partnerships that have a record of generating good support, and the use of Council superannuation schemes.

2 Background

The Inception Report for the SmartGrowth Project includes the development of a detailed implementation framework. One of the key tasks is to investigate funding tools, and more specifically to refine the financial contributions strategy that is consistent across Tauranga District Council and Western Bay of Plenty District Council.

In February 2003, the Joint Committee received a report "Funding Options" that outlined a range of issues and principles for taking this task forward. The scope of this discussion extended to consideration of a range of innovative methods to assist in closing any gap in funding into the future.

The Joint Committee adopted a series of principles for developing approaches to funding. These were as follows:

- The costs of growth must be the subject of ongoing refinement, but at this point it is accepted that the gap in funding growth costs with current methods is significant enough to warrant joint work continuing.
- The process for working on joint funding issues must include an understanding that progress will only be made in the context of positive working relationships.
- It is essential to understand the current situation of each participant in terms of funding and resourcing, and the implications of policy changes.
- The independent status of SmartGrowth should be used to promote community discussion on alternative funding approaches.
- There is no "silver bullet" (such as a "Regional Funding Bank") – any solution will be in the form of a comprehensive package.
- Form should follow function – it is important not to focus on the detail before the broad approach is generally agreed.
- Policy should recognise different methods will be required, depending on whether the nature of the service provided is:
    - Regional
    - Sub regional
    - District
    - Sub district
- Policy should consider benefits to citizens rather than just rate payers.

The Committee identified the following funding options and actions for further development within SmartGrowth.

Funding options	Status	Future action
1)Smart Growth member Councils (rating, user pays, development and financial contributions)	Current policies not commonly understood	Finance Project team to prepare a précis, for circulation. Presentation by each Council to SmartGrowth to follow
2) Existing sub-regional wealth	Predominantly held by, Environment BOP, BOP Community Trust and Tauranga ECT.	SmartGrowth to approach each organisation to develop a protocol which establishes the basis for supporting future

		growth related infrastructure
3) A regional funding bank	Seen as a good idea	Take the concept further using the Infrastructure Auckland and any other related NZ/international approaches as models
4) Tolling and PPP's for roading	New provisions outlined in the Land Transport Management Bill	Government policy position still evolving. Submissions closed end of February 2003. Following some delay the Bill is due to be reported back to Parliament for enactment later in 2003. The final form of the implementation measures will determine their effectiveness
5) Government investment through the superannuation fund	the idea has been mooted, given adverse offshore returns	Raise directly with the Minister of Finance
6) New taxes, eg poll tax, a growth related sub-regional tax, visitor tax etc	No current provision	Would need legislative amendment. Government unlikely to implement given its historical reluctance to undertake revenue sharing with local government
7) Any other approaches to be raised by Joint Committee Members		

Funding issues were raised in a general way as part of the Public Discussion phase during March-May 2003, highlighting the various tools available for funding growth related costs.

The SmartGrowth Finance Project Team developed a methodology for reviewing the funding options used in this report. The team also decided to include the following additional methods within the assessment framework:

Funding option	**Status**	**Future action**
Rates and Uniform Annual Charges	Major current funding source.	Consider possible changes to align with sub-regional growth management approach.
Financial and Development Contributions	Major current funding source	Government has accepted the limitations of the RMA financial contributions model. The LGA 2002 contains new development contribution powers which focus on the impacts of growth on asset and financial management

3 Current Funding Position

The Finance Project Team complied a detailed schedule of financial policies of each Council as part of the definition of the "current approach" with growth management. It is available as a separate document.

Appendix 1 includes presentations made by the Councils to the Joint Committee and provides an overview of the current situation of each Council as at March 2003.

Key issues are:

Environment Bay of Plenty

- Regional wealth has been significantly enhanced through prudent management of investment capital, and the excellent performance of the Port of Tauranga Ltd
- Investment income provides a substantial funding resource for offsetting regional rates. Any reallocation of this will increase rates throughout the region, with substantial impacts on larger land holdings.
- Income from investments has increased substantially, but growth is expected to plateau.
- Funding is managed having regard to needs assessed at a regional scale which extends from Opotiki, through the Western Bay of Plenty through to Rotorua.

Western Bay of Plenty District Council

- Limited wealth was provided in 1989 and the Council has struggled to fund deferred capital and growth costs since this time.
- Efforts to fund growth from financial contributions have reached a ceiling with respect to market acceptance.
- The Council is likely to reach the prudential limits for debt by 2005.
- Growth funding is managed having regard to the needs of geographic "areas of benefit" with varying financial impacts.

Tauranga District Council

- Wealth from investment has been prudently managed and is used to internally fund part of capital needs.
- The Council is likely to reach acceptable prudential limits for debt by 2013.
- Funding from developer contributions is considered to be too low.
- Growth funding is managed on both a district wide and local area basis with generally even impacts.

4 Current Work in Progress on Funding Policies

4.1 Environment BOP

Environment Bay of Plenty adopted its Revenue and Financing Policy on 3 July 2003 for the 2003/2004 financial year. It is, in essence, the Funding Policy adopted two years ago.

Council is presently embarking on a series of workshops to consider funding of infrastructure throughout the region related to sewage reticulation; stormwater disposal; land purchase on lake margins for soil conservation/land retirement/nutrient barriers; land purchase for regional parks etc. In the lead up time to the preparation of the 2004/2005 Long Term Council Community Plan (LTCCP), the Council will address the usage of UAC's and additional targeted rates and will discuss the ramifications of moving from land value based general rates to capital value based general rates.

These matters will be discussed at Council meetings and between senior staff of the Councils in the lead up time to the adoption of the LTCCP.

4.2 Tauranga District Council

As required by the LGA 2002 Council has developed, consulted and adopted a Revenue and Financing policy which became operative from the 1st July 2003. This policy is a translation of Council's former Funding Policy and makes no material change to funding sources and activity funding. This was done because Council has said it will fully consider and consult on how activities of Council should be funded (if at all) during the development of the LTCCP in the 2003/04-year.

In addition to this TDC will look at alternative funding sources and whether current funding burdens are appropriate.

TDC has initiated a Rating Review Project to ensure the most equitable methodology is used. This project will be completed in February 2004, to be followed by public consultation.

TDC has also initiated a Financial Contributions Review Project to ensure that appropriate levels are charges are being met by development. This project will be completed by November 2003.

4.3 Western Bay of Plenty District Council

Currently the Western Bay of Plenty District Council is working with the Department of Health to obtain subsidies for Omokoroa and Maketu / Pukehina /Little Waihi sewerage schemes. The outcome of this is unknown due to the complexity of the rules that Council is required by central government to comply with in terms of funding it's share of the subsidy. This is now a national issue. A meeting iwas held between the Minister of Health and 24 other local authorities on 11 August 2003.

If the rules as to the application criteria change this could have a positive impact on Western Bay of Plenty District Council's balance sheet as well as affordability for the two sewerage schemes.

Currently, Maketu / Pukehina / Little Waihi has been excluded from our projected balance sheets as Council has yet not to confirm it's preferred option and lodge resource consents.

4.4 Joint Work

4.4.1 Sub-regional financial contributions for community facilities

This is a joint project between Tauranga District and Western Bay of Plenty District. A project outline has been presented to the joint committee of both Councils. Currently staff are working through the programme. A number of significant issues will need to be dealt with before this initiative can either be notified under the Resource Management Act 1991 or included in both Councils Long Term Council Community Plan and Annual Plans.

5 Alternative Funding Approaches

The objective of this work is to identify the alternative approaches that provide the greatest potential gains in closing the identified funding gap.

The following analysis has been carried out for each identified alternative:

- Description – what is it?
- Statutory Framework – can it be done?
- Current Situation – what is being done now?
- Potential - how much money can it generate?
- Risks – how reliable will the cash flow be?
- Best practice – who is doing this well elsewhere?
- Conclusion – whether any principles and actions can be taken forward into the SmartGrowth Strategy

5.1 Regional Wealth

5.1.1 Description

Sub-regional wealth includes financial and investment assets maintained by the three Councils and could include assets excess to requirements, and indeed, the access to long term funding, secured over the rating base of the region. In addition, sub-regional wealth also includes those funds held in community trusts.

5.1.2 Statutory Framework

Sub-regional wealth is not defined in any Act but, as a consequence of the enactment of the Local Government Act 2002 and the resulting increase in the powers of general competence, there is provided a greater discretion for councils to contribute to a wider range of activities not provided for in the now defunct Local Government Act 1974.

5.1.3 Current Situation

Environment Bay of Plenty, through its 55% shareholding in Port of Tauranga Limited, subsidises its net funding requirement by up to 70% by way of dividend and investment income, in such a way that every rate payer in the region is advantaged to the same extent in proportion to the amount of general rates paid. Trust funds are distributed to successful applicants based generally on community benefit.

5.1.4 Potential

Environment Bay of Plenty, with considerable investments, principally through its majority ownership of Port of Tauranga Limited and to a lesser extent to other interest/dividend bearing equity investments, has potentially available, funds for investment in infrastructure or regional development. Equally trust funds in the Bay of Plenty are substantial and could be available for infrastructure creation and regional development, subject to the terms of reference for each of the trusts.

5.1.5 Risks

The principal risk to sub-regional wealth through converting assets from one type to another (cash/investments into physical assets) is a depletion of the original investment, and in the case of Environment Bay of Plenty the return on which is currently being utilised to offset rates to every ratepayer of the region. Depletion of the capital bases, results in less income resulting in turn in an overall potential rate increase of the same extent. Likewise depletion of trust funds reduces investment income in the available funding for distribution.

5.1.6 Best Practice Examples

Environment Bay of Plenty and the various trusts in the Bay of Plenty region currently fund, albeit to a very minor extent, by way of grant, subject to application and scrutiny, to infrastructure and development in the Bay of Plenty. Funding of the Environment Bay of Plenty Environmental Enhancement Fund is through rating and of the trusts presumably by way of investment earnings.

5.1.7 Conclusion

Distribution of sub-regional wealth, whether in the hands of Councils or community trusts would depend on strategic decisions made by those Councils, taking into account the potential depletion of that wealth and the consequential loss in distributable income. Alternate funding, by way of loan secured over the assets of the Councils needs to be considered. This matter requires further consideration as part of the SmartGrowth implementation plan .

5.1.8 Regional Funding Bank

5.1.9 Description

This concept would comprise the SmartGrowth partner Councils pooling funds in a formal manner to assist with sub-regional development.

5.1.10 Statutory Framework

Depending on the exact nature of “the bank” special legislation could be required

5.1.11 Current Situation

Some limited joint funding occurs between Council. For example for regional reserves.

5.1.12 Potential

On the surface, the concept seems to have appeal. However it would probably achieve little more than the partner Councils can do already through collaboration.

5.1.13 Risks

Compliance costs could outweigh any advantages

5.1.14 Best Practice Examples

None known of in New Zealand.

5.1.15 Conclusion

Initially an interesting idea based on the pooling of resources in order to achieve greater critical financial mass. Likely to be unable to achieve anything more than the individual SmartGrowth partners could achieve through voluntary co-operation at substantially lower compliance costs.

5.2 Tolling and Public-Private Partnerships

5.2.1 Description

A public private partnership (PPP) to build infrastructure is likely to occur where the public sector has a need and the private sector helps to meet that need by direct investment. It is a model that is used to a limited extent internationally. The "City Link" downtown Melbourne motorway system is an example.

The capital as well as an investment return is usually recovered through a user pays road toll.

Funding approaches of this nature fall outside the usual government and local government legislation.

5.2.2 Statutory Framework

Given the New Zealand Government's concern with the increasing gap between transport funding needs and the current petrol tax revenue base, Government is attempting to provide the nation with a wider funding base through the PPP mechanism. An investigation of the tools for the NZ context is evolving but their final form is dependant on Land Transport Bill enactment.

5.2.3 Current Situation

Toll funding has previously been used successfully by Tauranga District Council to fund the construction of the existing harbour bridge. It is currently in place through special legislation for Route K, New Zealand's only toll road.

For the Western Bay situation, the legislation will only be effective if Government enacts it with a special schedule which provides for the strategic roading network to be tolled as one interrelated piece of infrastructure.

5.2.4 Potential

Very high revenue potential with the capability to give the community the infrastructure it wants. The PPP component works best where there is a public sector capital shortage and a community is prepared to pay for the higher costs of private sector funding.

Tolls offer potential to obtain revenue directly from users of services from outside the region. There are few alternatives that have this characteristic.

5.2.5 Risks

Tolling: People refuse to / don’t use the tolled facility. Income for debt servicing is less than expected and has to be “topped up” from other sources.

PPP: may not be a cost effective solution for the community in the long term (eg. Private cost of borrowing higher, profit requirement by private sector).

Extensive reliance on toll income may affect a Councils credit rating and costs of borrowing.

5.2.6 Best Practice Examples

Tauranga Harbour Bridge, Takitimu, Route K, City Link Melbourne, Gateway Motorway Brisbane.

PPP: Nothing in New Zealand at present.

5.2.7 Conclusion

This is a feasible option but needs to be part of a co-ordinated approach to regional funding.

5.3 Government Investment of Superannuation Funds

5.3.1 Description

The investment of a portion of the Governments recently established dedicated superannuation fund in growth related infrastructure.

5.3.2 Statutory Framework

No known statutory impediments.

5.3.3 Current Situation

Government has recently established a Superannuation Fund with the aim that it will provide an alternative to direct taxpayer funded age benefits. These will be under increasing pressure as the population ages and the tax base of the country reduces.

Australian has a similar scheme, which invests heavily in onshore infrastructure..

5.3.4 Potential

There is potential for this fund to be used for infrastructure investments in a manner similar to the former National Provident Fund.

To make the proposition work money would have to be loaned at a rate lower than local government’s ability to borrow.

Currently the fund has an offshore investment emphasis in order to “grow the capital”.

5.3.5 Risks

Potential reliance on funding which may never happen.

5.3.6 Best Practice Examples

Australia

5.3.7 Conclusion

A potential funding source which has considerable potential. Would need a significant change in current Government thinking. SmartGrowth needs to lobby for a change in this thinking as part of its "approach to Ministers" once the SmartGrowth strategy has been adopted for public consultation.

Government could borrow from the fund itself to help fund a range of lead infrastructure such as transport, health and education facilities.

5.4 New Taxes

5.4.1 Description

This refers to the implementation of new taxes at a regional level (considered to be the minimum practical scope). Such taxes could take the form of a regional sales tax, a poll tax or a regional income tax.

5.4.2 Statutory Framework

As a tax these options would require legislative change by central government. There has been a historical reluctance by central government to engage in 'revenue sharing' with local government. As such, it is considered unlikely that the statutory framework will be amended to allow such taxes in the short- to medium-term.

5.4.3 Current Situation

None of the taxes mentioned above are currently applied or allowed for by existing legislation for the partner councils.

5.4.4 Potential

The potential for revenue generation is of course dependant on the type of tax levied and the rate of taxation. However, in general it is reasonable to suggest that there is the potential for significant revenue generation.

<u>Regional Sales Tax</u>

Given the geography of New Zealand, it is unlikely that differential tax rates would be practical i.e. each region or district setting their own sales tax. It would be very easy for consumers to drive to another region to take advantage of a lower sales tax on significant purchases if there were differences between the rates of tax applied in different parts of the country. As such, a uniform rate across the country would be more appropriate.

Using a variety of publicly-available information on GST revenue, regional retail sales, and average weekly household expenditure turnover and assuming regional sales tax would have no impact on current retail sales, a 1% regional sales tax would generate somewhere between $14.3m and $24.8m for the sub-region annually.

<u>Poll Tax</u>

A poll tax refers to a tax collected equally from all peoples. The potential for revenue generation will depend upon:

- the breadth of the charge (at what age it would be first levied),
- the extent of exemptions (for low income groups for instance), and
- the quantum of the charge.

At the 2001 census, there were approximately 130,000 people in the sub-region, of which approximately 30,000 were under the age of 15. If it is assumed that any poll tax would not be collected from, say, the least wealthy 20% of the population, then that leaves 80,000 people potentially subject to the new tax. At a rate of, say, $100 per person this would generate $8m per annum.

Regional Income Tax

As for the above examples, the potential revenue that could be generated from a regional income tax depends on the rate that tax is set at. Detailed figures for income tax broken down by region are difficult to obtain, and would be even more difficult to extrapolate due to the range of specific case and statute law that affects income tax.

5.4.5 Risks

Some taxes can be regressive (as income rises average tax falls) and therefore fall unevenly on different groups. . May take considerable time to get this through central government.

Regional Sales Tax

Depending on how it would be introduced, a regional sales tax may create a further administrative burden for business owners, particularly if the new regional sales tax was administered separately from GST. If the regional sales tax was administratively absorbed into GST, creating a GST rate 0f 13.5% say, with one per cent returned to the region, then the administrative burden would fall less on the business owner and more on the IRD.

Poll Tax

"The (poll) tax has long been attacked as an unfair burden upon those less able to pay."[1] The most recent attempt to introduce a poll tax in the industrialised world, by Margaret Thatcher in Britain in 1990, was massively unpopular, leading to wide-spread public revolts, riots, and the eventual political downfall of Thatcher herself.

Regional Income Tax

One of the key issues regarding a regional income tax is the complexity of the existing income tax system, and the further complexities that may occur if an additional tax was added to that system. There is a significant risk that the direct and indirect compliance costs for individuals, businesses, and the administering body (presumably the IRD) would outweigh the benefits of the addition revenue raised. A second significant risk related to regional income tax is avoidance by those able to structure their financial affairs tax-efficiently (i.e. family trusts, tax-efficient investments and so on). This could result in the incidence of taxation falling less equitably than intended.

5.4.6 Best Practice Examples

Within New Zealand, the recent decision by central government to apply an additional nationwide tax on petrol and diesel for application in the Auckland region offers a glimmer of hope that targeted solutions may become more appropriate in the future. However, the transparency of the application of that additional fuel tax is not clear – figures for amounts raised by the additional tax, and identification of

[1] www.infoplease.com/ce6/history/A0839551.html - an encyclopedia website

specific projects funded are not available. In addition, the additional revenue is not being returned to local government in Auckland to invest as they see appropriate but is instead being held by central government; an example of the reluctance to 'revenue share' as identified above.

Regional Sales Tax – overseas experience

Several overseas countries impose regional sales taxes, notably Canada and the U.S.A., while other countries impose only a nationwide tax, such as Australia, the U.K., and New Zealand. In the U.S.A. there are two levels of sales tax, a state tax and then a local city or county tax. Typically the state tax is significantly larger than the city or county tax. For example, in Texas state taxes are currently 6.25% while city, county and 'transport authority' sales taxes range from 0.0125% to 2% with all combined sales taxes on any single purchase limited to a total of 8.25%.

"Canada's system of indirect taxation is unique among industrialised countries in that there are two levels of government, federal and provincial, that impose a general sales tax on the same transactions."[2] It is this 'unique' system that New Zealand would have to emulate, with central government retaining GST and local government permitted to impose a separate and additional local or regional sales tax.

Note that in the U.S.A. combined sales taxes (state and local) are typically between 7% and 9% (only Alabama have sales taxes in double figures). In Canada combined federal and local taxes range from 7% to 17.7%, with most around 15%. Nationwide sales tax in the U.K. is 17.5% while in Australia it is 10%. New Zealand's current rate of GST is 12.5%.

Poll Tax – overseas experience

"Although no longer a significant source of revenue for any major country, the poll tax did provide large sums for many governments well into the 1800's. In the United States, the poll tax has been connected with voting rights. By the 1940's some of these taxes had been abolished, and in 1964 the 24th Amendment to the U.S. Constitution disallowed the poll tax as a prerequisite for voting in federal elections.

"In 1990, the British Prime Minister Margaret Thatcher introduced a poll tax with exemptions for people with low income or disabilities. The measure was extremely unpopular and played a role in her replacement as prime minister later that year. "[3]

Regional Income Tax – overseas experience

Regional income taxes occur in some states in the U.S.A.. For example, in Ohio 89 municipalities have banded together to create a Regional Income Tax Agency that administers local income taxes that typically benefit the particular town or municipality in which they are levied. Rates in Ohio are different for different locations but are typically between 0.5% and 2%. In Maryland, local income tax rates range from 1.25% to 3.15%, while in Pennsylvania, local income taxes are limited to 2%.

In other states, there is political resistance to a local (state) income tax, despite individual cities pushing for one: "Despite repeated statements by Gov. Frank Murkowski that he will not institute a state income tax, Alaska cities are planning to push for it as part of a long-range fiscal plan next year in the Legislature."[4]

5.4.7 Conclusion

Progression of new taxes as an option would depend on central government interest in using this tool and the administrative/ equity issues associated with a targeted tax. If central government interest was

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[2] www.benderoff.ca/comtaxes.htm - the website of Cliff Benderoff and Associates, a Canadian tax consultant and specialist in indirect taxation

[3] www.infoplease.com/ce6/history/A0839551.html - an encyclopedia website

[4] www.juneauempire.com/stories/072503/sta_citiespush.shtml - Alaskan newspaper

obtained, the potential revenue streams for sub-regional local authorities, and all local authorities around New Zealand, are significant. As part of the SmartGrowth implementation plan , discussions with government on this matter need to be pursued.

5.5 Rates and Charges

5.5.1 Description

Rates are set under the new Local Government (Rating) Act 2002 and can be levied by any local authority being a regional or territorial.

Charges are predominantly under the Local Government Act however they also given effect to under other legislation.

Rates and charges are the most reliable sources of income for Councils. Generally most Councils receive at least 50% of all income from rates.

5.5.2 Statutory Framework

The major requirement for income setting for Council is the Local Government Act 2002 with the through the Revenue and Financing Policy. In conjunction with that legislation rates are set under the Local Government (Rating) Act 2002 which enables Council to set rates using a variety of techniques..

Fees and charges for specific services can be charged under a variety of legislation but these generally cannot be for profit and only are for cost recovery purposes.

5.5.3 Current Situation

Currently, as outlined above there is the new Local Government(Rating) Act 2002 which gives Councils greater flexibility in terms of the ability to set targeted rates. Generally rating is understood by the public however there is still some views of the community that rates are for a specific service and not for the broarder community good.

5.5.4 Potential

The potential for increased rates is very much a political decision, in that any additional rate burden on the community could have an adverse fallout. There are also ability to poay issues especially for the lower income households in the community. A current example of fallout is the nationwide media focus on the Auckland Regional Council rate increases as well as their change to both the method of assessing and collecting rates.

The potential to increase rates therefore is limited to people's willingness to pay.

5.5.5 Risks

The significant risk is people's willingness to pay and the consequences of that. This is quite clearly a significant issue for the Auckland Regional Council. The lesson is that any changes to the basis on which rates are collected eg altering the basis from land to capital value as well as any significant increase in rates must be clearly managed.

The other risk with the rates is the inability to correctly target those who should be paying more and those who should be paying less.

5.5.6 Best Practice Examples

The KnowHow guides on rating published jointly by the Society of Local Government Managers and Department of Internal Affairs provides a best practise guide for rating.

The best practise guidelines recommend that Councils should ensure that when setting and collecting rates that the community or individuals being charged the rates should be receiving the broad benefit of those rates at the same time. This is known as intergenerational equity and because of the long life of Councils infrastructure, payment for the services received should extend over the life of the asset as well as provision being made for the asset to be replaced. Reaching agreement on concepts such as this is a challenge.

To do this adequately there must be use of debt where Councils have sufficient rate debt ratios.

This is considered best practise where 20% of debt servicing costs are funded from rates. Any increase on this has a negative effect on the margin that Council is required to pay lenders.

5.5.7 Conclusion

Rates and charges are the predominant income stream for Councils and therefore are the most likely source of additional income particularly where there are increases in ratepayers – those ratepayers should also be included in the additional rate requirement. However there needs to be continual action to achieve a fairer way of funding local government, so that rates becomes only part of a range of funding tools

5.6 Financial/Development Contributions

5.6.1 Description

Financial contributions are charges mandated by the Resource Management Act 1991 and imposed on new activities such as buildings, landuse, or subdivision. The charges are to meet the cost of providing new or additional services to those activities, as a means of mitigating the effects of growth on the environment.

Financial contributions can applied at a range of spatial scales.

At individual "site" level, development may take place that results in new public services being installed and vested in the ownership of a Council or other utility provider. At this level, there is a very strong and direct relationship between the service provided and the beneficiary. Works rather than cash is provided at this level.

At local or neighbourhood level, where a few or many sites require provision of new or upgraded services for shared use, a Council or utility provider often provides services. Costs are recovered via a financial contribution charged to the beneficiary typically on a standardised unit based formula. The relationship between the service provided and beneficiary is usually strong and direct.

At district level, where new activities lead to a need for additional services and costs are also charged on a standardised unit based formula. There is potential for sub-regional and regional level contributions.

The Local Government Act 2002 provides Councils with boarder development contribution powers based on the ability to recover contributions for a broad range of infrastructure and community facilities directly related to the capital expenditure a council expects to incur arising from growth.

5.6.2 Statutory Framework

Financial contributions are authorised under the Resource Management Act 1991. In the growth areas of New Zealand most local authorities have struggled to anchor through the planning process levels of financial contributions that reflect the costs of growth. Most are subsidising the costs by at least 50%. Also many financial contributions concentrate in local level mitigation, whereas the high costs of growth occur in the district wide infrastructure networks such as roading.

The Resource Management Act 1991 was the sole empowering statute until December 2002, when the LGA was enacted. Provisions for development contributions were included in the Local Government Act following pressure from the local government sector to address the limitations of the RMA. The procedural delays inherent in RMA plan making meant that financial contributions were an inflexible tool, and highly prone to lag as a result of litigation led by developers.

Financial contribution and development contribution policies are mandatory and are provided for under Sub-part 3 Financial Management: Section 106 of the LGA 2002. This section requires:

- An explanation of capital expenditure needed to meet growth demands for "community facilities"(a very broad term including .
- Source of funding
- Reasons for choosing certain funding sources
- Information on activities to be funded by contributions

A local authority can decide whether it wishes to use the RMA or LGA regime for contributions, however it cannot charge under both on a single development. The funding policy must spell this out.

If the Local Authority decides to use LGA development contributions, it must include detailed information in its policy explaining each contribution, how the contributions are calculated, and administrative information. A schedule is required setting out details of how individual contributions are calculated for reserves, network infrastructure and community infrastructure. Policies are made through a special consultative procedure as part of the adoption of a comprehensive funding and finance policy. There are no rights of appeal to the Environment Court, with the only review process being via the high Court on procedural review.

Maximum contribution levels are prescribed for reserves (7.5% of land value or 20m2 of land per unit), There is no upper level of contribution for and more either community or network infrastructure.

Development contributions can be charged on resource and building consents and service connections. Contributions can only be used for the purpose for which they were taken, and cannot be used for maintenance.

The procedural advantages of using the LGA process are offset in part by the inclusion of more prescriptive standards. However the LGA provisions are a far more flexible and workable regime than the RMA. It is likely that most Council's will move to this regime in due course, subject to any adverse Court rulings that place unforeseen burdens on implementation.

5.6.3 Current Situation

Both Tauranga and Western Bay District Councils have policies on financial contributions.

While the basic philosophy behind each policy is similar, there are several differences between the two District Council regimes.

The "areas of benefit" differ as a result of settlement patterns and scale, but these differences are not significant.

Tauranga collects a standardised contribution from residential development as a separate contribution at the time the new dwelling is built, whereas WBOP charges all contributions at the subdivision stage. This is in effect a timing difference.

WBOP has a district wide approach to reserves contribution, whereas Tauranga funds these at the Urban Growth area "local" level.

WBOP has provision for funding the costs of capital. This is calculated on a standard formula

The interest is based in Council's assumptions in the LTCCP and financial models.

Fee levels are relatively similar, and range between $5,000 and $10,000 per lot. Recent Tauranga District policy development will mean for example in Bethlehem a Subdivision Impact fee of $19,000 plus GST will be required.

The main difference in approach lies in how the contributions received are applied. WBOP fund services generally to the extent of the funds received in the previous financial year. Large stepped provision of infrastructure is funded by loan.

Tauranga funds services according to development forecasts and predictions of areas of likely development. The larger scale of the Tauranga operation means that a less conservative approach is taken. It assumes that any shortfall in one area can mitigated by additional revenue in another area. Services are funded to the extent of the predicted revenue for the coming year. Any spending beyond this level is loan funded.

A recent divergence in policy between the two Councils is the WBOP decision to take into account affordability in setting fee levels. This reflected a concern that fees may be set too high and discourage development in areas where an upfront investment had been made for infrastructure.

Tauranga District is currently undertaking a complete review of its financial contributions as part of a wider financial review. This is focussed on achieving a significant increase in funding from this source, as well as looking to migrate policies to the new LGA regime.

A joint project is underway between the two districts investigating potential for Subregional development contribution toward Subregional scale facilities.

5.6.4 Potential

The more flexible LGA regime puts Councils in a potentially stronger position to use development contributions. In theory, the level of possible funding from this source is the actual capital costs generated by growth. In practice, the level of funding will constrained by the availability of data that is rigorous enough to stand challenge, potentially in a court situation.

Obtaining sufficient information to justify specific contributions is a limiting factor for maximising the level of funding provided through contributions. Services that are already funded through contributions tend to be those that are relatively straightforward to plan for, cost and assign benefits. Services that are not funded are conversely likely to be more difficult, with higher costs of assessment, and higher margins of uncertainty that may open policies to challenge. This risk needs to be managed carefully.

The main areas of further opportunity for funding from this source are roading, reserves and community infrastructure.

A large component of long-term growth costs (30-40%) are in the provision of arterial and sub-arterial road network development. At present, virtually none of this cost is funded from development. In order to fund any of these costs from development contributions, analytical tools such as traffic models will need to be employed to determine the extent of benefit received by new development as opposed to general growth in traffic density, and through traffic. It will also be necessary to separate the effects of the various modes of transport, for example residential and commercial traffic.

A further determining factor will be the extent to which the development of arterial roads are funded from other user sources such as central government funds and tolls.

For reserves, Tauranga has identified a significant shortfall in its current funding to achieve desired service levels. This work is well advanced. As noted above, investigations are also underway to assess the potential to fund Subregional facilities by development and other contributions..

5.6.5 Risks

Both development and financial contributions are a long-term commitment. They tie the community into a partnership with the development community to fund growth related infrastructure in a prescribed manner. In this partnership, many of the risks are imposed on the public partner with little obvious dividend. The main return from the community's investment is a high degree of control over the timing and standard of infrastructure provision.

If development occurs at a slower rate that anticipated, the ratepayer community must bear the cost of finance. If standards change and contributions collected are insufficient, there is no way of recouping the shortfall from completed development. Withdrawing from the partnership midstream is virtually impossible. Poor planning and analysis can be heavily punished in an area of rapid growth. With this degree of risk, Councils must invest in sound analysis of costs, identify risks, and be fully satisfied with all matters before allowing development to proceed.

Court challenges to both development and financial contributions are a risk to implementation that requires careful management. Councils need to have a sound information to manage the risks of using these tools, regardless of this threat.

Development contributions are subject to Judicial Review in the High Court. The scope of the review is compliance with process, rather than outcome. Any review is likely to occur within months of the financial year in which the contributions have been implemented. It would be concluded within a few months.

Financial contributions are subject to references through the Environment Court as well as an extensive body of "effects based" case law.

Funding the costs of residential intensification presents new and different challenges: planning (upgrades/retrofitting and complex benefit assessment), development (disruptive, difficult to build incrementally), and funding (less predictable uptake, more variable circumstances) and is an untested area under existing legislation.

For developers, concern over development contributions increases as the quality of the land and sale price decreases. The lower end of the price range will always be relatively more affected by increases, and hence the effect of increases will always fall more heavily on lower income land/house package home -builders.

F3 This is an important consideration for any significant lifting of contribution levels. SmartGrowth has already identified growing problems with affordability of housing, and the effects of increased contributions will need to be taken into account. Market price settles around certain cost structures. If a component changes significantly, instability is caused particularly in more inelastic lower -price end of the market. Introducing change requires sensitivity to cost structure and possibly graduated increases to allow the market to adjust while maintaining stability.

As contributions increase, challenges are likely to become stronger. Moves to extend contributions to new areas need to be backed by a strong analytical base and a clear understanding of the uncertainties in the information so these can be factored into the setting of contributions.

Both development and financial contributions can potentially threaten the stability of overall revenue streams, as they are directly tied to activity levels and indirectly to the state of the economy. In times of low activity, the level of funding will decline. Cycles will also affect the level of capital expenditure, but there is likely to be a lag between the peaks, with high levels of spending catching up at the end of a cycle, corresponding with declining revenue. In the US, in the early 1990's, a recession saw many authorities facing severe short-term financial difficulties due to the very high level of dependence on sales tax and development levies.

Development and financial contributions have complex administrative systems. Systems must be capable of meeting the legal requirements for transparency and accountability. Small areas of benefit are desired by those paying as it is easy to see what is being spent and where. However, this can have an adverse cumulative effect, increasing administrative costs and tying the provision of services to needs defined rigidly by the system as opposed to the wider operating environment. The size of area of benefit should be kept at the minimum that allows reasonable accountability.

5.6.6 Best Practice Examples

After more than 10 years of operation under the Resource Management Act, several Councils have successful financial contributions policies in place. Both the Western Bay of Plenty and Tauranga District are recognised as sites where early innovation took place under the RMA, and are now in the position of having second and third generation provisions.

With the enactment of the LGA 2002, Local Government New Zealand and the Society of Local Government Managers have collaborated to produce a best practice guide for development contributions. This is to be published at the end of September, “if we are lucky”.

A number of Councils have moved to introduce new provisions under the LGA. However, it is too early to judge whether these represent good practice as they have barely begun to be implemented.

Affordability for families on low incomes is a factor being taken into account in the Far North. In this case, an abatement policy applies on land and buildings under $120,000.

In the US, financial contributions are used to fund a wide range of activities, including social housing. A relationship has been identified between achievement of specific economic development objectives and provision of affordable housing to attract workers.

5.6.7 Conclusion

Both development and financial contributions are likely to be a significant source of funding for growth related infrastructure into the future. There is a very clear legislative mandate for development contributions , enhanced by the recent enactment of the LGA 2002. There is also a strong community mandate to use this method, as it has the perception of targeting newcomers to the district, at least indirectly.

Strengths include the potential to develop into untapped areas such as roading and community facilities. However, these areas are considered to be more difficult to operate in than those already funded from contributions. These activities have greater complexity and uncertainty, and have a varied mix of beneficiaries, both growth related and otherwise. .

Experience has proven that a robust contributions regime is dependent on strong planning and analysis. This requires a substantial upfront public investment in work such as structure planning and costing. There are also costs in ongoing maintenance and updating, and the management of revenue and expenditure.

Significant increases in contributions may well require a graduated approach to avoid creation of market instability. Increasing reliance on financial contributions will also highlight affordability issues at the lower price end of the market and a policy response is likely to be required.

Best practice under the new legislation will emerge over the next 12 months and it will be important to maintain networks with other sites dealing with these same issues.

5.7 Collaborative “share club ” infrastructure funding

5.7.1 Description

This is a method of funding clearly identified future infrastructure, particularly land purchases for openspace, reserves and facilities which uses the funding strengths of individual Councils but in an arms length manner.

The three SmartGrowth partners would agree to contribute capital at a rate sufficient to either buy or fund the purchase of key community infrastructure within the policy contained in the SmartGrowth strategies. structure could be established either formally such as a LATE Committee to The aim is to make provision for purchasing independent of the Councils as well as avoiding some of the price hikes that public bodies have to endure and undertaking land purchase prior to any zoning or designation of the land which often results in significantly increased prices. It is about developing an entity that can work without some of the restrictions of local government and be responsive to opportunities prior to and when they arise.

One of the principles particularly in respect of open space it the land being purchased may not need to hbe available for public access and therefore rural activities such as farming and horticulture could continue and provide the basis for debt servicing and capital repayments.

It is considered this option is worthy of further investigation and development.

5.7.2 Statutory Framework

The technique is permitted within the existing law.

5.7.3 Current Situation

Not used currently although Tauranga District has purchased land for reserve purposes but is currently used for horticultural purposes. An adjacent Council has purchased land for industial purposes and this currently has a share milker on it until the outcome of the rezoning process is known.

5.7.4 Potential

Has significant future potential. Could be established as part of the SmartGrowth Memorandum of Agreement process in early 2004.

5.7.5 Risks

A change of priorities between the partners. Founding documentation would need to anticipate a process for dealing with this.

5.7.6 Best Practice Examples

Dunedin City Council in conjunction with other Councils.

5.7.7 Conclusion

This alternative has merit and requires further development. It would need a clearly defined establishment and operational policy structure together with establishment funding. However, methods such as this require consideration if progress is to be made on developing alternative funding and land acquisition approaches.

5.8 Community funding

5.8.1 Description

This is a method of funding major community projects by formally seeking targeted community sponsorship for a significant capital share, through public and private donors.

5.8.2 Statutory Framework

The technique is permitted within the existing law.

5.8.3 Current Situation

Tauranga District Council proposes to seek substantial sums of money (up to $120 million over the next 10 years to get projects currently planned, off the ground.

5.8.4 Potential

Has significant future potential.

5.8.5 Risks

Reliance on community funding which may not be forthcoming. For example a change in donor circumstances.

5.8.6 Best Practice Examples

Has been used by many communities to fund major facilities

5.9 Conclusion

This funding method will continue to be developed by Tauranga District.It needs to be taken into account when discussing any gap closing strategy.

6 Conclusion

Existing and potential funding tools have been reviewed to assist in identifying where the best opportunities lie for funding the costs of future growth.

The principal conclusion reached is that the conventional tools such as rates, charges and financial contributions are still likely to be a major source of funding.. Central government has recently reviewed local government funding legislation Whilst it seems unlikely to make major changes to the law in the foreseeable future., there is an opportunity to pursue discussions on such matters with senior government ministers as part of the SmartGrowth process. It has been clearly signalled that this approach should be pursued before decisions are made not to pursue significant funding alternatives.

However , resources still need to be focussed on enhancing current sources as a priority in the short term.

An important consideration is whether a funding alternative will increase the revenue stream, or simply reallocate the imposition of costs. Methods that may add revenue rather than redistribute impacts within the region include

Tolling is not seen as entirely straight forward . Also financial assessment agencies such as Standard and Poors downgrade the credit rating of a Council if there is too great a reliance on toll income. Rates provide the basic equity for borrowing.

Private/ public partnerships may be useful to move cost from balance sheet and focussing on innovative new methods such as a collaborative “share club” which sharpen up existing tools are worth taking to the next stage.

Finally the quantums of development cost is not usually the issue. Of prime importance is the cashflow and the equity of who pays.

7 Addendum – Project Managers Report –April 2004.

In April 2004 the Project Manager reported to the Joint Committee as a followup to the interim assessment of funding alternatives.

The purpose of this report was to close off issues and to focus on three funding approaches which the Project Manager felt should be implemented in the future. They are based on the observation that generally the sub-region is managing to fund growth impacts on water, wastewater and possibly stormwater infrastructure, but is seriously challenged in the areas of:

- Transportation and
- Community facilities including openspace sports, arts and leisure facilities.

These are the facilities which impact on the current and future economy and on the future quality of life.

In order to achieve more timely, funding the following actions are suggested,

Transportation.

A detailed analysis with the proposed Joint Officials Group for the western Bay of Plenty, using the SmartGrowth data to persuade Government to adopt a “catch-up” funding approach similar to that announced for Auckland in December 2003.

The scope of this needs to be worked through in detail alongside the SmartGrowth transportation strategies. In particular the Strategic Roading Network implementation challenges, once the projects are further refined from timing and cost perspective, as part of the work leading up to the Draft Regional Land Transport Strategy which is due for adoption in September 2004

Provisions would be incorporated in the Governments 2005-06 budget. Negotiations would need to be completed by December 2004.

The application of a sub-regional development contributions levy, under Schedule 13 of the Local Government Act 2003 (the Act)), to assist with funding the transportation network of the sub-region, should also be promoted.

This is a logical extension of the current policies and is being applied elsewhere in New Zealand.

It fits squarely within the provisions of the Act which enable recoveries for growth related capital expenditure. It needs to be approached on a cross boundary and sub regional basis between Tauranga City Council and the Western Bay City Council.

Community facilities including openspace sports, arts and leisure facilities.

Despite the very innovate approach of Tauranga City Council toward future facilities provision through its City Investment Strategy and well as the financial and development contributions policies of the Councils, it remains a significant future challenge to raise the levels of capital to necessary to implement the range of facilities contained in both the SmartGrowth and other strategies.

Timely provision of many of these facilities has a significant economic benefit for the community as well as making a very direct contribution to future sub-regional amenity.

It is this quality of life issue (along with transportation) that citizens of the future will judge the success of growth management strategies.

The Rating Act 2002 permits targeted rating. The application of the technique is one of the more significant successes in South East Queensland growth management, which the small study tour saw last year.

Sub-regional collaboration

There is also an ongoing need across the partner Councils to collaborate on the development of funding tools. This is a good area to combine skills and resources of the organisations.

That the Committee resolved, firstly, to refer the two approaches on future transportation funding and the targeted rating approach for community facilities/open space to the SmartGrowth Implementation Committee for analysis and implementation in the 2005-06 financial year and, secondly, to take a more collaborate approach to funding tools to the Chief Executives Advisory Group for a report back to the SGIC on how this might be achieved

8 Recommendations

The findings and direction agreed following on from this review be incorporated into the draft SmartGrowth Strategy.

It is noted that the draft Strategy already includes a Statement that incorporates the following "vision" with special relevance to funding:

"Provide an Efficient and Affordable Infrastructure";

and the following "outcome",

"Innovative funding methods bridge the gap between cost and affordability".

The Strategy also requires definition of "principles" that will guide the development of "actions" to achieve this outcome.

The following principles are suggested based on those established in current policies, during the initiation of this review, and from the findings of this review.

Principles

- The costs of growth are identified in a transparent manner.
- There will always be a funding gap between capital needs and the communities ability/willingness to pay.
- Acceptance that key infrastructure such as arterial roading underpins both the location and timing of growth. For example in respect of the Eastern Arterial or the Pyes Pa Bypass , funding of this infrastructure in a fair and timely manner is a key challenge. If it is not provided in a timely manner, levels of service and amenity values will decline sharply.
- An understanding that with the ongoing demands for services, that both Tauranga and Western Bay District Councils will reach their prudential financial limits within the next 5 years.
- There is maximum use of the development contribution tools provided by the Local Government Act 2002, in order to minimise the cross subsidisation of growth related costs by existing ratepayers
- Acceptance of the need to keep the growth related funding issues in front of Government, to ensure that there is timely budget funding for critical community infrastructure facilities such as health, education and transportation.
- An acknowledgement that the Government if left to due process, will only fund lag facilities, whereas lead facilities are essential for mitigating the effects of ongoing growth and providing a long term framework for growth to occur efficiently.
- That Councils partner with other organisations/seek sponsorship to provide future community facilities in a timely manner
- An understanding that as the western bay community continues to grow, the community will expect a more diverse range of well located facilities to meet community expectations
- The SmartGrowth strategy provides a framework for the future application of the regions public wealth throughout the region.
- The project partners support Government legislative and policy initiatives which result in wider funding opportunities especially for network infrastructure. For example, the current Land Transport Management Bill.
- The project partners will use innovative funding and administrative tools in order to provide key areas of open space and facilities

- Acceptance that the current reliance on rating and development/financial contribution tools is only one way of funding growth and that the pursuit of alternative funding methods needs to remain top of mind and continued actions taken to pursue such methods

The following Actions are proposed

1.	**Continue identifying the costs of growth in particular secondary network infrastructure costs arising from development intensification at neighbourhood level, until the strategy is agreed and published in April 2004. Identify and programme any remaining costing work still to be completed after that time.**				
Explanation					
Priority	Lead Agency	Support Agencies	Cost Estimate	Plan	Linked Actions

2.	**Acknowledgement that the directly non recoverable costs of growth will largely be for district wide infrastructure in the areas of:** • Transportation • Recreation and open space and • Future stormwater provisions				
Explanation					
Priority	Lead Agency	Support Agencies	Cost Estimate	Plan	Linked Actions

3.	**Complete the current review of approaches to infrastructure funding by both partner district councils in time for changes to be implemented in the 2004-05 financial year**				
Explanation					
Priority	Lead Agency	Support Agencies	Cost Estimate	Plan	Linked Actions

4.	**Environment Bay of Plenty to consider the use of development contribution tools for activities such as regional open space by December 2004**				
Explanation					
Priority	Lead Agency	Support Agencies	Cost Estimate	Plan	Linked Actions

5.	**Negotiation with key government ministers/departments in late 2003 and if necessary in early 2004 on the critical areas of Government services which have to be funded into the future**
Explanation	

Priority	Lead Agency	Support Agencies	Cost Estimate	Plan	Linked Actions

6.	For sub-regional facilities, reach agreement of a formal programme with clear timeframes, costs and potential areas of partnering, sponsorship by the end of 2004				
Explanation					
Priority	Lead Agency	Support Agencies	Cost Estimate	Plan	Linked Actions

7.	Formal negotiations during February to April 2004 to establish the likely quantum of assistance which can be expected from these sources				
Explanation					
Priority	Lead Agency	Support Agencies	Cost Estimate	Plan	Linked Actions

8.	Active advocacy of the Western bay of Plenty case before Government to ensure that national legislation is tailored to the local situation				
Explanation					
Priority	Lead Agency	Support Agencies	Cost Estimate	Plan	Linked Actions

9.	Formation of a joint-arms length "share club" in particular for land purchase which could either operate as a LATE or similar with the aim of buying in advance of need while continuing to use the asset to generate income to fund the cost of capital.				
Explanation					
Priority	Lead Agency	Support Agencies	Cost Estimate	Plan	Linked Actions

10.	Obtain a formal commitment from Government by April 2004 to widen the existing funding basis local government using the both the SmartGrowth Strategy and the accompanying SmartGrowth Alternative Funding Approaches paper September 2003 as key tools.				
Explanation					
Priority	Lead Agency	Support Agencies	Cost Estimate	Plan	Linked Actions