

DISCUSSION DRAFT – NOT SOLGM POLICY

A Template for Reporting Local Government Funding Needs – An Exploratory Paper

1.0 What is this Paper?

This paper is an exposure draft of a standard template for reporting local government funding needs and whether such a template can be used to help the public better understand local government funding issues. This paper discusses:

- how and why this initiative has come about
- criteria for developing a useful, balanced template
- some initial thoughts on a set of indicators that make up the template.

The intent of the paper is to 'start the ball rolling' by seeking the sector's views as to whether an initiative is necessary and desirable, and if so, what measure or measures provide the fairest, most accurate indication of the funding needs of each council. For this reason, the paper is a thinkpiece rather than a statement of policy of the New Zealand Society of Local Government Managers.

Throughout the paper you will find a series of questions for discussion and debate – and these are listed in the one place on pages 12 and 13. We seek your views on these, as well as any other aspect of the paper (and, of course, any issues that you think the paper has missed).

Comments on this will be due with Raymond Horan by **midday on Tuesday 2 June, 2009**. Comments should either be emailed to rhoran@solgm.org.nz or faxed to 04-978-1285.

Remember that the overall purpose of the template is to improve public understanding of rates and local government finance to help the public find the 'right questions to ask'. It is intended to provide a fair, balanced and accurate picture of local authority funding requirements to the public. The template should not be viewed as a tool for allowing anyone to pillory individual councils (or similarly a tool for promoting others).

Important – the Financial Management Working Party ('FMWP') is taking a principled approach to the development of the template, it will not be seeing any data until the trial process described in section 5.0. FMWP asks that comments focus on whether the indicators meet the tests imposed in section 3.1, and any matters of practicality involved in the collection of the measure. If you consider a measure is invalid then please explain why with reference to section 3.1, and provide an alternative (with reasons why this is a better measure). The position of any individual council in respect of a particular measure is not likely to invalidate a measure in and of itself.

SOLGM wishes to thank the following people who participated in the initial discussions and development of this paper:

- Blair Bowcott, Hamilton City Council
- David Foster, Manukau City Council

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- Norman Jones, Taupo District Council
- John McLaren, North Shore City Council
- David Paris, Masterton District Council and
- Helen Sellwood, Environment Canterbury.

2.0 Why a Good Practice Template?

1. ***Most local authorities ‘benchmark’ financials in some form or another, but it tends to be flawed by methodological differences between authorities.***

While some in the sector oppose this kind of reporting ‘on principle’ the volume of traffic on the listserves suggests that many, if not most of the sector take at least some account of rates levels in local authorities nearest them, or of those of a similar size etc. Traffic on the listserves has also revealed that there is not much consistency in the measures being used from council to council¹ and therefore there is potential for genuine misunderstanding and misuse (whether intentionally or unintentionally).

2. ***A standard template is a tool for promoting better community understanding of rates.***

The Report of the Independent Inquiry into Rates (‘the Shand report’) found that public understanding of rates and the drivers of rates is generally poor. The Shand report concluded that some councils do not assist public understanding by ‘fudging the real level of rates and rates increases’² (sic). The Inquiry recommended that LGNZ and/or SOLGM

“in consultation with other stakeholders, produce a template as a good practice guide so that the amount of rates and annual increases can be better reported and compared between councils. This template would set out:

- *total rates and individual components (general rates, targeted rates, user charges and CCO charges)*
- *the real change in rates (that is, adjusted for inflation as measured by the Consumers Price Index)*
- *the adjustment for increases in the number of rateable properties*
- *the average total rate, its change over time, and rates broken down by ward*
- *the relative amounts and average rate borne by residential, business and rural ratepayers and how this has changed from the previous year.’³ (sic)*

Although FMWP does not necessarily agree that local authorities ‘fudge’ their reporting of rating needs (deliberately or otherwise), *Getting Real* (the joint SOLGM/LGNZ

¹ Examples of different measures used as an indicator of ‘the rates increase’ included the increase in the rate in the dollar, the increase in the total rate take (with or without inflation, with or without an adjustment for growth in the rating base), increase in the general rate, increase in rates on the median property in the district or parts thereof and so on.

² Independent Inquiry into Rates (2007), *Funding Local Government – Report of the Independent Inquiry into Rates*, pp 253-254.

³ Independent Inquiry into Rates, page 254.

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submission to the Inquiry) did comment that public understanding of rates could be improved. A plethora of different approaches to reporting what is (or should be) very basic information does little to help.

3. *Standard reporting of funding needs promotes the accountability of a local authority to its community.*

With comparable information between local authorities attention can be focussed on the reasons for differences between local authorities rather than on data where the prime cause of difference is a methodological one. For example, council A provides a wider range of services than council B, or council C is undertaking that major piece of capital expenditure thus its rates are higher than council X which is concentrating on maintaining present service levels. Such reporting promotes better accountability of local authorities to their communities and by allowing for a clearer linkage of funding needs and levels of service provides for a more informed debate about priorities.

There is a risk in this kind of reporting – that some local authorities manage to the reporting framework rather than to the needs of communities. The counter to this is that the degree of improvement in non-financial performance management that is likely in 2012-22 LTCCPs will make the consequences of what is effectively ‘governance by front page of the paper’ a lot more evident to the community.

4. *If the sector doesn’t take the lead itself, the information vacuum will be filled by others.*

The list of those monitoring local government funding goes much wider than 85 local authorities. Some sector groups (e.g. Federated Farmers), the media and the general public also readily undertake reporting and comparative exercises with varying degrees of rigour. Others, such as the Department of Internal Affairs, undertake occasional analyses for policy-making purposes⁴.

The approach much of the sector has taken in the past is to ignore these analyses or critique them as they are released. The ‘ignore’ approach leaves what is usually misleading and occasionally incorrect data and conclusions uncontested in the public arena. The ‘critique’ approach tends not to present the sector in its best light (on occasion responses can appear to be self-justifying or carping) and invites the inevitable questions about why the sector doesn’t maintain this type of information itself.

5. *So isn’t the decision a ‘no-brainer’?*

The decision for the sector then is to either:

⁴ For an example of the sorts of analysis DIA has prepared in the past, see Central/Local Government Funding Project 2005, *Report of the Central/Local Government Funding Project Team*. This is a good example of analysis that was designed with a policy-making objective in mind, rather than the development of comparators (although the information was subsequently released at the request of the sector).

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- prepare its own standard approach to reporting rates and make it as fair and rigorous as possible so that any analysis focuses on true differences in levels rather than differences in methodology, or
- continue to leave the door open for external comparisons or for an external agency to develop a template for us.

FMWP's view is that this is indeed a 'no-brainer' and that the sector should be leading the development of its own templates for reporting funding needs. A template developed by the sector with honesty of purpose, and of methodology is preferable to something done externally which may have neither.

Question for Discussion

1. **Should the sector develop its own template for reporting on its funding requirements ? Why or why not?**

3.0 A Possible Template

3.1 Characteristics of a Good Template

Given the above objective, FMWP considers that any template needs to be:

- *fair and unbiased* – there should be no systematic bias towards 'under' or 'overstating' the true picture of affairs.
- *as difficult to manipulate as possible* – the template should not provide incentives to make particular funding decisions or arrange and report financials in such a way as to present a 'better picture'
- *applicable to all local authorities* – measures should be equally valid for metropolitan, rural and regional authorities. This does not necessarily mean that the results from each group could or should be presented together
- *meaningful to the public at large* – in particular the measures selected should be readily understandable to the media – some of the more technical indicators that local authorities use to track their financials are unlikely to have much meaning to the general public, no matter how well they are explained
- *efficient* – in the sense that measures should not place undue cost on local authorities to collect and report. Detailed benchmarking of the type undertaken by the Audit Commission in the United Kingdom is time-consuming. Measures should be drawn as much as possible from readily available information.

Question for Discussion

2. **What characteristics do you think a template for reporting local government funding requirements should have? Why do you think these are important?**

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3.2 Scope of a Template

The template that the Shand report appears to have had in mind was a tool for reporting rates information, and rates information only. While that is an improvement over the information vacuum that exists at present, a template that focuses on rates only:

- does not provide a complete picture of local government's financial needs (i.e. debt, charges, development contributions are all excluded, also there is no linkage drawn between rates and expenditure)
- could be manipulated through deciding to move to fees, development contributions and the like
- is therefore open to misinterpretation by the public (e.g. is the reason council A's rates are highest because it has little revenue from other sources or is it because the cost of services is higher in council A, for whatever reason).

A template that includes a wider range of measures provides a more complete picture of local government finance, although a manageable template will require careful selection of the measures and other analysis therein. To get the concept of a template established, measures regarding rates should be included, but also included in these would be measures around:

- *local authority debt* – in part because the sector has recently been criticised for its reluctance to borrow⁵ and, paradoxically, because local government is regularly criticised for borrowing too much. Debt measures are an indicator of a local government's judgements about intergenerational equity (put crudely how much of the local authorities expenditure should be funded by current ratepayers vis-à-vis others)
- *expenditure* – some measure of total expenditure is required because it shows the total impost that a local authority has on its community. Expenditure information helps provide context for the other information e.g. a percentage of rates to total expenditure can be calculated to help interpret rating information and so on.

The intention of the template is to build public knowledge of local government finance and affairs generally. It is not designed as a formal benchmarking tool as such – therefore the financial information should be collected at 'global' level rather than activity by activity. Differences in the treatment of activities from local authority to local authority mean that an attempt to move below council level will invariably require a high level of disaggregation of data, and become unwieldy to administer and respond to⁶.

The information collected should be for the core council only – the activities of council-controlled organisations can potentially distort expenditure and debt data (though not rate data).

⁵ For example, see Local Government Rating Inquiry (2006), *Funding Local Government* and Joint Central/Local Government Funding Project Team (2005), *Report of the Central/Local Government Funding Project Team*

⁶ For example, the Local Government New Zealand/KPMG Database Survey of the 1990s disaggregated information to 45 distinct activities. It took 2-3 working days to complete and 2-3 months to administer, collate and write up.

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Questions for Discussion

3. **Should a template of the type envisaged here be limited to rates information or should it include a wider set of local authority financial data? Please give reasons for your answer.**
4. **Should the template report on information at an activity level or at council level? Please give reasons for your answer.**
5. **Should the template include or exclude the expenditure and debt information of council controlled organisations? Please give reasons for your answers?**

3.3 What Measures Should Be Included In The Template?

3.3.1 Rates

What should be included within the definition of rates? This may seem like a basic question, but different local authorities treat various rates quite differently. For example, many local authorities that meter water under section 19 of the Rating Act treat this as a user charge for reporting purposes.

For the purposes of this template we propose a very simple basic definition – a rate *is anything set using the authority of the Local Government Rating Act 2002 regardless of the basis of calculation*. This captures, and is intended to capture anything under sections 13-19 of the Rating Act⁷, and any powers added to the Rating Act in future.

The Rating Inquiry added a second layer of issue in that it considered that the charges levied by organisations delivering water and wastewater services on behalf of a local authority⁸ should fall within the scope of the template. The charges set by these agencies effectively act as the equivalent of a rate (using a mechanism that is identical to section 19 charging). To exclude these charges from the template, means that comparisons between local authorities are could mislead the user. However, there are other charges of a similar nature (for example, most Wellington ratepayers do not pay a refuse rate as such, but rather fund the refuse collection activity through the purchase of 'official' council rubbish bags, many rural properties supply their own water and wastewater) and the issue quickly becomes one of delineation. As a matter of principle, FMWP considers that items like this should either be 'all in' or 'all out' – and as it is not practicable to capture all, water and wastewater by CCO should be excluded.

⁷ Metered water charges set under the authority of section 12 of the Local Government Act should also be included for consistency.

⁸ At the time of writing we were aware of three such organisations – Manukau Water, Metrowater (both council controlled organisations) and United Water (a consortium delivering water to Papakura under a franchising arrangement).

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Measures that are currently being considered for inclusion in the template are:

- *the total rate take* – which should be separated into the general rate take, revenue received from targeted rates and a total of the two. A potential measure of the level of increase in rates could then be the increase in the total rate take (although some would argue that this needs adjustment for growth – otherwise the measure would automatically be biased in favour of low-growth councils⁹)
- *the average rate* – calculated as the total rate take divided by the number of rating units (less non-rateable properties). There could be some reservations about use of an average rate in local authorities with a significant number of targeted rates (the higher the number of targeted rates the more likely it is that the average rate becomes a statistical construct ‘that no-one actually pays’). The average rate can also be artificially distorted by a few very high or very low results. Notwithstanding this *movements in the average rate* may be a better indicator of movements in rates over time as it automatically adjusts for the growth factor. A median rate also achieves the same end result, and because it is derived by sorting the rates paid highest to lowest and taking the middle result, it is actually an amount that somebody in the district pays!
- *average or median residential rate* – this is a piece of information that the media often ask for, and other measures are often confused with the average residential rate¹⁰. The immediate response is that a significant number of local authorities do not have differentials based on property use – however the Rating Valuations Rules require that all valuation rolls contain information on property use¹¹. This is a core piece of information for any local authority that wants to make *evidence-based* judgements about the affordability of its rates. Overseas jurisdictions such as the United Kingdom, Canada, and some Australian states use this as their main indicator for tracking rates (in some cases their only indicator).

Questions for Discussion

6. **Do you agree that the definition of rates for the purposes of this template should include all rates set under the authority of the Local Government Rating Act? Why or why not?**
7. **Do you agree a measure of the total rate take and changes in the total take would be a useful addition to the template? Why or why not? Would you adjust changes in the rate take for growth, if so using what information as your growth factor?**

⁹ The working group discussed several alternative ‘growth factors’ before settling on growth in the *number of rating units* as the measure of growth.

¹⁰ Those with memories of the Local Government Funding Project may recall some of the ‘interesting’ reports in the media of a measure that had nothing to do with average residential rates, even when such a note was attached to the table.

¹¹ Rule 2.2(e) of the Rating Valuation Rules. Property use codes are described in Appendix C of the rules – for the purposes of this part of the template we would probably be looking at all property where the first field of the code is ‘9’.

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8. **Do you consider that a measure of average rates or median rates should be included in the template? If so, do you have a preference? How easy (or otherwise) would it be for your local authority to calculate median rates?**
9. **Do you consider a template should include a measure of movements in residential rates? What do you think the costs and benefits of collecting this information would be?**
10. **Should non-rateable rating units be included in the calculation of any averages? Why or why not?**

3.3.2 Debt

With debt there are two key issues – the amount of debt relative to the size of the local authority, and the ability to service the debt. With this in mind the template could include the following:

- *total net debt* – including both external and internal borrowing, including the current portion of any term debt, but excluding any other current liability and taxation liability (i.e. that which arises out of a conscious policy decision to borrow as opposed to the normal day to day operation of a business)
- *either net debt/total rates or net debt/total operating revenue* – a measure of the ability of a council to service its debt
- *either net debt/capita or net debt/rating unit* – a metric of debt relative to the size of the council. If the template includes a measure of average rates then it would be wise to use the net debt per rating unit measure¹²

At this point readers may be asking why the template does not include some measure of financial gearing (debt/assets or debt/equity). These ratios are very easily misunderstood by the general public as typically they indicate that local authorities level of gearing is generally well below a corporate body (or even that of central government). What is not often recognised as that the infrastructure held by local authorities is often not readily realisable (particularly network infrastructure).

Questions for Discussion

11. **Do you agree that the definition of debt for the template should exclude current liabilities (other than the current portion of term debt), taxation liability, employee entitlements and any other liability not arising from a conscious decision to borrow? If not, what is your alternative definition, and why do you prefer this?**

¹² And where the number of rating units is defined in the same way as with the average rate (i.e. non-rateable rating units are excluded).

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- 12. Should the template include a measure of financial gearing? Why or why not? Assuming you answered ‘yes’ would that measure be debt/equity or debt/assets?**

3.3.3 Expenditure

The proposal is that the template include four self-explanatory expenditure measures:

- *total operating expenditure*
- *total capital expenditure*
- *operating expenditure/rating unit*
- *capital expenditure/rating unit.*

3.3.4 Contextual Information

It has been suggested that gathering and publishing some contextual information might help the sector and other users better identify ‘like with like’. Although benchmarking is not an objective of the template, it is fair to say that some will attempt to use the data for this purpose.

The following could be useful in interpreting results:

- population – from the last Census
- number of rating units
- percentage of urban/rural rating units
- percentage serviced by local authority water and wastewater disposal schemes (regional councils might also include flood protection)
- percentage of the rates paid by the ten highest paying properties – if the template reports averages then this could be an indicator of the likely degree of distortion arising from having several very high paying ratepayers.

Questions for Discussion

- 13. Do you agree that the above measures of expenditure should be included in the template? Why or why not?**
- 14. What other information should be included in the template? Why do you consider this information to be important?**

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4.0 Reporting and Presentation

FMWP is open at this point as to how results should be presented, as long as it is in accordance with following general rules:

1. Benchmarking is not a purpose of the template. When multiple council data is presented it will be presented in alphabetical order, rather than in a 'league table' format. (For that reason all publication of data will be in PDF format to make manipulation of tables as difficult as possible). From time to time we may reverse the alphabetical order or randomise so Ashburton and Auckland Region are not always first!
2. Results will be presented with a short covering note explaining that good governance and local service delivery are the key factors in assessing the performance of any local authority. The purpose of the template is to provide ratepayers with information to help them determine what questions to ask – and to that end the contextual information will be reported alongside other information.
3. Results for regional councils and territorial authorities should be separated as functions and the expenditure required to fund them are quite different. Unitary authorities will be treated as a territorial for this purpose, but all reporting will contain an explanation of the difference in functions between the unitaries and the territorials. We are open on the question of whether the territorial authorities need to be separated (for example by sector groupings) and would welcome views on this.
4. Reporting of partial results (that is some indicators and not others) will be avoided where possible. The reason for developing a set of measures that goes wider than rates is to avoid the potential for misleading conclusions – partial reporting of results has the same risk. While we can't control how agencies within, and outside the sector choose to interpret the data, we can minimise the risks of accidental or deliberate misinterpretation.
5. Reports will be accompanied with an explanation of each of the measures and how to interpret them, as well as their strengths and weaknesses.

Questions for Discussion

15. **Do you think that the reporting of territorial authority data should separate this grouping further (for example, by sector)? Why or why not?**
16. **Do you agree with the five rules for presenting and reporting the information? If not, which ones and why?**
17. **Do you have any suggestions for reporting information from the template?**

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5.0 Next Steps

The SOLGM Financial Management Working Party has approved this paper for circulation as the basis for discussion and debate within the sector.

When feedback in this paper has been collated and considered by FMWP then:

- the SOLGM Executive will make a decision on whether to proceed with a template – that decision will be based not only on the level of support for a template within the sector, but other factors such as the ongoing resource needs for supporting production of the information
- assuming the Executive wishes to proceed with a template, then an interim template will be released within the sector for trialling based on the 2008/9 annual reports and projected financials for 2009/10 from the 2009/19 LTCCP. The intent of the trial process is to determine whether there are any unexpected 'quirks' in the methodology that become evident only when each local authority's data is put side by side with others.
- results from the trial will be assessed by FMWP and a final template issued in October/November 2009. The template will 'go public' for the first time with data based on 2009/10 *annual reports* (if the results of the trial are sufficiently robust this data may also be issued to give context to the 2009/10 numbers).

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DISCUSSION DRAFT – NOT SOLGM POLICY**List of Questions for Discussion**

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2. **What characteristics do you think a template for reporting local government funding requirements should have? Why do you think these are important?**
3. **Should a template of the type envisaged here be limited to rates information or should it include a wider set of local authority financial data? Please give reasons for your answer.**
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- 13. Do you agree that the above measures of expenditure should be included in the template? Why or why not?**
- 14. What other information should be included in the template? Why do you consider this information to be important?**
- 15. Do you think that the reporting of territorial authority data should separate this grouping further (for example, by sector)? Why or why not?**
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Sample Reporting Formats for Template Data

Territorial Authority	Population (2006 Census)	Number of Rating Units	% of Rural Rating Units	% of Rating Units Served by Council Water and Sewage Schemes	Total Rate Take (\$000s)	% Change over Previous Year (%)	Either Average or Median Rate (\$)	Either Average or Median Residential Rate (\$)	Total Net Debt (\$000s)	Either Net Debt / Total Rates or Net Debt / Op Revenue (%)	Either Debt Per Capita or Debt per Rating Unit (\$)	Opex (\$000s)	Capex (\$000s)	Opex Per Rating Unit	Capex Per Rating Unit
Ashburton															
Auckland															
Buller															
Central Hawkes Bay															
Central Otago															
Christchurch															
etc															

Each table would then be followed by the appropriate footnotes.

Regional Council	Population (2006 Census)	Number of Rating Units	% of Rural Rating Units	% of Rating Units Served by Council Flood Protection Schemes	Total Rate Take (\$000s)	% Change over Previous Year (%)	Either Average or Median Rate (\$)	Either Average or Median Residential Rate (\$)	Total Net Debt (\$000s)	Either Net Debt / Total Rates or Net Debt / Op Revenue (%)	Either Debt Per Capita or Debt per Rating Unit (\$)	Opex (\$000s)	Capex (\$000s)	Opex Per Rating Unit	Capex Per Rating Unit
Auckland Region															
Bay of Plenty Region															
Canterbury Region															
etc															

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