

# **Governance Options for the Wellington and Wairarapa Regions: An Economic and Financial Assessment**



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## 1. Executive summary

This report provides a high-level economic and financial assessment of governance options for the Wellington and Wairarapa regions<sup>1</sup>. The report involves a programme of investigations and analysis intending to deliver an independent, evidence-based assessment of the available options for restructuring governance arrangements in the Wellington and Wairarapa regions.

The three governance options considered are:

- i. the enhanced status quo: amalgamation of the three Wairarapa councils and the formation of a Wairarapa unitary authority with no other amalgamations of the local or regional councils supplemented by the establishment of single network-wide entities for land transport and water services;
- ii. four unitary authorities, with unitary authorities covering each of the Hutt, Kapiti, Wairarapa and Wellington; and
- iii. a single unitary authority covering the entire Wellington and Wairarapa regions.

The options are assessed in terms of the statutory purpose of local government. Under the Local Government Act 2002 (s10 (1)) as amended in 2012, the purpose of local government is twofold:

- “(a) to enable democratic local decision-making and action by, and on behalf of, communities; and  
(b) to meet the current and future needs of communities for good-quality local infrastructure, local public services, and performance of regulatory functions in a way that is most cost-effective for households and businesses.”*

Our report focuses primarily on cost-effectiveness. We review the international literature on the relationship between size and cost-effectiveness of local government. We also examine the expenditure data from the approximately 70 territorial authorities in New Zealand over the last five years to assess the relationship between size and cost-effectiveness across the different functions of local governments in New Zealand and for the councils’ operations as a whole.

Our review of the extensive international studies<sup>2</sup> on the topic reveals no consensus on the optimal size of local government. Some studies find that smaller councils are more efficient, some find that larger councils are more efficient and some find a U-shaped cost curve (where per capita costs first decline then level off and then start rising as population increases). In

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<sup>1</sup> In this report we refer to the area comprising the Wellington City Council, Porirua City Council, Kapiti Coast District Council, Hutt City Council (HCC) and Upper Hutt City Council (UHCC) as the “Wellington region”; the area comprising the South Wairarapa District Council, Carterton District Council and Masterton District Council as the “Wairarapa region”; and the area comprising the Wellington and Wairarapa regions as the “greater Wellington region”.

<sup>2</sup> See section 4.

their literature review on the existence of economies of scale in local government, Byrnes and Dollery make a similar observation:

*“Overall, 29% of the research papers find evidence of U-shaped cost curves, 39% find no statistical relationship between per capita expenditure and size, 8% find evidence of economies of scale, and 24% find diseconomies of scale. From this evidence alone we can conclude that there is a great deal of uncertainty about whether economies of scale exist in local government service provision.”<sup>3</sup>*

Our assessment<sup>4</sup> of the New Zealand data finds a similar lack of a simple unequivocal relationship between size and efficiency in local government. The New Zealand data indicates that there are likely to be efficiency gains from combining councils of up to around 50,000 people but beyond that there is no evidence that further efficiency gains are available from amalgamation in respect of the majority of local public services provided by councils.

Most importantly, the evidence suggests that, when considering the optimal structure of local government, it is necessary to differentiate between the different functions of local government: i.e., to follow the principle that “form should follow function”. Our and the NZIER’s analyses of expenditure data from the approximately 70 territorial authorities in New Zealand over the last five years indicates:

- for the capital and expertise-intensive network operations like land transport and the three waters (potable water, storm water and waste water), there are economies of scale that merit a region-wide perspective regardless of the structure of other local government functions. In the case of water, for example, PricewaterhouseCoopers (PwC) found benefits of up to around \$5m annually could be expected if the three waters were managed by a single organisation (e.g., Capacity Infrastructure Services (Capacity)) across the Wellington region<sup>5</sup>. These capital-intensive functions, where our analysis suggests there is also a good case for network-wide amalgamation, account for around 34% of local government expenditure in the Wellington and Wairarapa regions; and
- in regard to the other, more labour-intensive, activities of local councils – like environmental protection, recreation and sport, noise and dog control – the case for amalgamation is weak. The evidence suggests that councils are likely to gain more from moving to best practice management and operational techniques than from increasing their scale through amalgamation with other councils. The Productivity Commission in its recent review of local government regulation reached a similar conclusion. The Commission found that the size of the local authority did not seem to be a factor in the extent councils followed adequate regulatory decision-making

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<sup>3</sup> Byrnes, J. and Dollery, B. (2002).

<sup>4</sup> See section 6.

<sup>5</sup> PricewaterhouseCoopers (2012).

processes. Rather, leadership, culture and organisational management are the key driving factors<sup>6</sup>.

For many of these more labour-intensive functions of local council, and those capital-intensive functions that do not exhibit signs of economies of scale (which together account, on average, for around 66% of council expenditure in the Wellington and Wairarapa regions), there may be disbenefits from amalgamations. Potential disbenefits include increased bureaucracy and expenditure, and service level creep from amalgamation<sup>7</sup> as councils with different cost structures, service levels and revenue models merge. Experience in Auckland and elsewhere suggests there will be pressures with amalgamation for practices and policies in the territory with the highest costs, highest service level or lowest user-charge to apply across the region as a whole.

At the aggregate council level, our analysis suggests therefore that there would be likely to be cost-efficiencies gained from amalgamating the three small Wairarapa councils (with a combined population of around 40,000) but beyond that the benefits from amalgamating councils in the Wellington and Wairarapa regions are less clear.

Even if there were expected to be ongoing net benefits from amalgamations, the costs of change also need to be taken into account. Evidence from New Zealand and offshore (e.g., Toronto where the costs of amalgamation totalled C\$400m) indicate that these adjustment costs can be major. Further, where after-the-event studies of council amalgamations have attempted to reconcile actual with expected transition costs, the general conclusion is that the estimates were too optimistic.

Turning to the second statutory purpose of local government, that of enabling local decision-making, the risk that local interests get overlooked increases the larger and more remote the local authority becomes. New Zealand already has relatively large local councils, on average, compared with most countries to which we typically compare ourselves. With an average population per council of 67,000 if the Auckland Council is included or 47,000 if it is excluded, New Zealand's average council population base already exceeds that of most European countries (which range from 1,300 in France to around 123,000 in England and Wales) and is well above that in Australia (with an average of around 37,000 people) and the United States (with an average size of less than 9,000 people).

For people wishing to engage with the council and, in particular, to have ready access to elected members, it is not just the population of the council area that matters, but also the ratio of residents to elected members. On this basis, New Zealand compares even less well with especially both the UK and European councils. In the UK on average one councillor represents 2,605 citizens. In France the average is one councillor for every 116 citizens; Germany 250 citizens; Italy 397 citizens; Spain 597 citizens; Sweden 667 citizens and

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<sup>6</sup> New Zealand Productivity Commission (2013).

<sup>7</sup> See section 6.5.



Denmark 1,084 citizens. In the Wellington region currently there is one elected member per 7,065 citizens while in the Wairarapa region there is one elected member per 1,345 citizens.

It is argued by some that local boards will preserve local democracy under a single unitary authority. A contrary argument is that the local boards will derive their functions and funding from the unitary council that they are a part of and this will limit their scope to represent the interests of residents and ratepayers. Further, even if the local boards were independent, they are likely to have only a relatively minor role in resource allocation, with current indications in the greater Wellington region being they are likely to be responsible for only around 5% or less of total council expenditure<sup>8</sup>.

Our financial analysis shows there are likely to be significant re-distributional impacts from amalgamation(s) within Wellington and Wairarapa. Assuming, as is likely, that any new council sets its rates uniformly across its region (albeit after some transition), territories like Porirua that currently have relatively high rates per dollar of capital value are likely to see their average rates reduce in relative terms, while territories like Upper Hutt with relatively low rates per dollar of capital value are likely to see their average rates increase in relative terms<sup>9</sup>. For no territory to be worse off on average in financial terms under a single unitary authority, the efficiency gains from the amalgamation of the eight councils would need to be close to 20%. However, most projections assume that any efficiency gains are likely to be of the order of around 3%.

There will also be re-distributional impacts on the average level of council debt per household across the Wellington and Wairarapa regions from the amalgamations<sup>10</sup>. The councils' current debt-servicing costs are typically only around 3% to 7% of their operating expenditure, but for Kapiti District Council debt-servicing costs are around 13.5% of operating expenditure. Our analysis indicates that establishing a single unitary authority could result in debt-servicing charges (as a per cent of operating expenditure) for the Kapiti area reducing from 13.5% to around 9% while debt-servicing charges for low debt areas would rise (e.g., Hutt City from 3% to 5.5% of operating expenditure).

Finally, we note that there are other claimed benefits from amalgamation of councils in the greater Wellington area: most notably, the perceived benefits of having a “single voice” for the Wellington and Wairarapa regions at a national government level. However, there may be other ways of achieving a “single voice” where it matters – such as through the mayoral forum or through a legislatively established regional committee – without incurring the potential losses in cost-effectiveness and losses in local democracy, and without incurring the disruption and transition costs of council amalgamations.

Overall, our analysis supports the establishment of single specialised network-wide organisations for land transport and the “three waters”. There is a good case for such

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<sup>8</sup>Wellington City Council (2013).

<sup>9</sup> See section 7.3.

<sup>10</sup> See section 7.4.

infrastructure networks being managed in an integrated way and not separated by local political boundaries. Our analysis also supports amalgamation of the three small councils in the Wairarapa region from an economic efficiency perspective but the financial impacts will depend on the level of efficiency gains achieved and whether the current cross-subsidy from the Wellington central business district (CBD) to the Wairarapa continues. Beyond that, there is little evidence that there are likely to be gains from further amalgamations in the Wellington region, especially once the losses of local democracy and the costs of change are taken into account.

Our analysis therefore concludes in favour of the enhanced status quo option, supplemented by the establishment of single network-wide entities for land transport and water services. We note that the enhanced status quo is favoured by the surveys conducted by six of the eight councils. If there is to be further amalgamation, our analysis favours having four unitary authorities rather than a single unitary authority for the Wellington and Wairarapa regions. Having multiple unitary authorities has less risk of creating a large bureaucracy, smaller adjustment costs and less risk of a loss in local democracy compared to having a single unitary authority (regardless of whether the single unitary authority has local boards or not). In addition, the multiple unitary authority leaves open the option of progressing to a single unitary authority at some stage in the future if there is convincing evidence to justify such a change.

## 2. Introduction

### 2.1 Purpose of the report

Hutt City Council has engaged TDB Advisory Ltd (TDB) to evaluate governance options for the Wellington and Wairarapa regions. This report involves a programme of investigations and analysis aimed at providing an independent, rigorous and evidence-based assessment of three commonly cited options for local government reorganisation.

There may be a case for change to governance in the Wellington and Wairarapa regions – but there is not (as yet) a universally agreed destination for the change. Change should:

- make strategic sense;
- align communities of common interest;
- provide solutions to local issues as well as network-wide service delivery;
- allow for “local voices” to be heard (and local democracy to continue); and
- make economic sense:
  - improve efficiency and effectiveness; and
  - allow for differing financial strategies (in terms of inter-generational equity, debt, investments, accountability and growth).

There is a variety of work under way and a range of opinions on schemes for reorganisation within the Wellington and Wairarapa regions. What seems to be broadly accepted is that the original rationale for having regional authorities separate from city and district councils is not necessary for the cost-effective delivery of infrastructure and local public services, and therefore a tier of government could be removed. Further, the amended or enhanced use of council-controlled organisation (CCO) structures is a possibility for delivering regional services across a wider area without necessarily having a regional council organisation in place<sup>11</sup>.

This report has a focus across the Wellington and Wairarapa regions – it is not centred on Hutt City’s needs only. The report considers the local and international evidence available on council amalgamation and builds financial models for the scenarios under which the area has a single unitary authority and multiple unitary groups.

### 2.2 Information sources

In preparing this report we reviewed a wide range of international and New Zealand literature and met with or worked with a number of key people, including in local and central government.

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<sup>11</sup> Annex 3 provides further details on the current CCOs.

The literature we reviewed is provided in the bibliography. The people we met with in the course of this review are listed in Annex 1.

## 2.3 Peer reviews

A draft version of this report was peer reviewed by two independent experts: Greg Dwyer of Dwyer G Ltd and Peter McKinlay of McKinlay Douglas Ltd.

Their respective peer review reports are available on request and are attached to the Hutt City's alternative reorganisation application to the Local Government Commission (to be publicly available by August 16<sup>th</sup> 2013).

## 3. Context

### 3.1 Background

The Better Local Government Reforms initiated by central government in its 2012 amendment of the Local Government Act 2002 has a twofold purpose:

*“(a) to enable democratic local decision-making and action by, and on behalf of, communities”;* and

*“(b) to meet the current and future needs of communities for good-quality local infrastructure, local public services and performance of regulatory functions in a way that is most cost-effective for households and businesses.”<sup>12</sup>*

This has prompted many to consider reorganising the councils in the Wellington and Wairarapa regions as people ask: how are these two purposes of local government best achieved? A number of interest groups in the two regions are in the process of trying to answer that question as it relates to the current local councils and the Greater Wellington Regional Council (GWRC).

In broad terms this questioning has thrown up three high-level approaches to the governance of the Wellington and Wairarapa regions:

- a) retain the status quo of two tiers of governance with increased use of shared services<sup>13</sup>;
- b) abolish the regional council and amalgamate the local councils into four unitary authorities; or
- c) amalgamate all nine existing councils into a single unitary authority.

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<sup>12</sup> Local Government Act 2002, Section 10.

<sup>13</sup> The experience in New Zealand with shared services has been relatively mixed, with many councils reluctant to commit to sharing significant services. This is beginning to change with the emergence of a number of regionally based shared-services companies that are demonstrating a superior ability to engage councils and implement substantial shared-services initiatives.

Subsidiary options consider whether, and to what extent, services such as water services and land transport might be organised under jointly owned CCOs.

It is a widely held belief that larger councils will govern better and more cost-effectively, and it is this belief that has prompted proposals to amalgamate all nine local and regional councils in the Wellington region. This push for region-wide local government amalgamation in New Zealand is demonstrated by the formation of Auckland Council. The Wairarapa also has considerable local support for the area to become an independent unitary authority but has little appetite for joining the Wellington region as part of a single combined unitary authority.

The Hutt City Council wants the area to have governance structures that best provide for the needs and preferences of its constituents. Hutt City and its residents and businesses have articulated preferences for spending, investment, service provision and debt financing that differ materially from those in other parts of the Wellington and Wairarapa regions. There is some support for a Hutt Valley unitary authority incorporating Hutt City Council and Upper Hutt City Council. The proposed Hutt Valley unitary authority would be one of four unitary authorities in the Wellington and Wairarapa regions.

The multiple unitary authority option needs to be considered in comparison with the proposed single authority option and a credible “status quo” option. To inform this comparison and assessment of the options, there is a need for greater clarity around the unitary authority options in terms of:

- strategic implications;
- the implications for service provision levels and quality; and
- financial implications.

The assessments need to be like-for-like, in the sense that they relate to comparable service levels and quality. Further, the “status quo” option needs to take account of the likely evolutionary path if current structures are maintained, and is not simply a “do nothing”. The assessments also need to be clear about the transitional implications while business as usual is maintained, the time frames and the potential for redundancy in people, systems and resources.

### **3.2 The Wellington and Wairarapa regions**

Wellington is the capital city of New Zealand and the urban area is the third-most populous urban area in the country behind Auckland and Canterbury. According to the councils’ long-term plans, the 2013 population for the entire Wellington and Wairarapa regions is around 492,526.

The two regions are home to eight territorial authorities and a regional council. The Wellington region accounts for the majority of the population base and five of the territorial authorities:

- Kapiti Coast District Council (serving 51,160 people);
- Porirua City Council (serving 52,940 people);
- Wellington City Council (serving 202,760 people);
- Hutt City Council (serving 103,740 people); and
- Upper Hutt City Council (serving 41,580 people).

The remaining 40,000 people reside in the Wairarapa, which is comprised of:

- Masterton District Council (serving 23,400 people);
- Carterton District Council (serving 7,560 people); and
- South Wairarapa District Council (serving 9,386 people).

The GWRC provides regionally focused council services to the entire Wellington and Wairarapa regions. As seen in Figure 1 below, although Wellington contains the majority of the population, the Wairarapa covers the larger geographic area: approximately 74% of the land area seen below.

Figure 1: Map of Wellington and Wairarapa regions



The differences in population concentration are indicative of key differences between the two regions. Wellington is a well-populated urban region while the Wairarapa is a relatively rural community. As the capital city of New Zealand, public administration and health and safety are the biggest industries in Wellington in terms of the number of people employed. On the other hand, the largest industries in the Wairarapa are agriculture, forestry and fishing.

However, within the Wellington region there are also key differences. Kapiti has a district council like the three Wairarapa councils, indicating it is less urban than the four city councils in the region. Porirua, Lower Hutt and Upper Hutt are, in some ways, dormitory suburbs to the central commercial hub that is the Wellington City CBD.

Council policies across the greater Wellington region differ significantly in terms of investment, borrowing, rates, service quality and quantity, and community support. These policy differences are indicative of the underlying differences in the preferences and demographics of the communities the councils represent.

### **3.3 What is the problem?**

The government has identified potential areas for improvement in local councils in New Zealand. The recent Better Local Government Reforms are aimed at improving local government around the country by:

- improving local government internal efficiency; and
- improving local government external efficiency (regional productivity); while
- improving, or at least retaining, local democracy.

In considering the options, detailed below, for the Wellington and Wairarapa regions we must take into account:

- the effects on local democracy;
- the transition costs: time, disruption and expense as new structures are formed; and
- the potential effects on cost-effectiveness and efficiency.

There are many difficult questions and trade-offs that must be considered in assessing the optimal size of local government. What is the appropriate level of decision-making for local government? How closely should the council deal with the community? How large is the community affected by any given issue? Does this differ for different services? What is the relationship between local government size and the wider economy's efficiency? How much will it cost to transition to a new structure?

Many functions of local government are inherently suited to coordination and/or engagement on a particular level. For example, some functions are inherently “regional” such as water, land-transport planning, and aspects of land use, and therefore should be managed at this level. Some functions – such as local library services, noise control or the location of brothels – directly affect a small community group (perhaps an area of 1,000 people or 5,000 or 10,000). Therefore, ideally these issues would involve close engagement with the community affected.

This suggests that local government is not necessarily about being the provider of a service. It is about managing the provision of services at the right level and engaging with the community at the right level. This requires a local government that is flexible, has good avenues of communication with its constituents, and is structured in such a way as to allow



the provision of services to be managed at the level any given service is inherently suited to. Further, any future structure of local government should be sufficiently flexible to allow for the changing demands of citizens in the future. The question underlying this report is: what governance arrangements will best meet the needs of the Wellington and Wairarapa regions now and into the future?

### 3.4 The options

We consider three governance options for the Wellington and Wairarapa regions as detailed below: a status quo option, a multiple unitary authorities option and a single unitary authority option.

#### Option 1: “Enhanced” status quo

The key points for Option 1 are:

- Masterton District Council, Carterton District Council and South Wairarapa District Council would be amalgamated. Preferably, local government in the Wairarapa would be structured as a unitary authority in line with community support in the region;
- Kapiti Coast District Council, Porirua City Council, Wellington City Council, Hutt City Council and Upper Hutt City Council would remain as distinct local authorities. Greater Wellington Regional Council would continue to function in its current capacity for these areas;
- the establishment of single network-wide entities for land transport and water services; and
- there would be greater emphasis on shared services including potentially establishing regional committees with the power to make legally binding decisions.

The long-term plan population forecasts for 2013 for each of the eight current territorial authorities are detailed in Table 1 below.

**Table 1: Long-term population forecasts – territorial authorities**

LTP forecast 2013	Kapiti	Porirua	Wellington	Hutt City	Upper Hutt	Wairarapa
Population	51,160	52,940	202,760	103,740	41,580	40,346

#### Option 2: Multiple unitary authorities

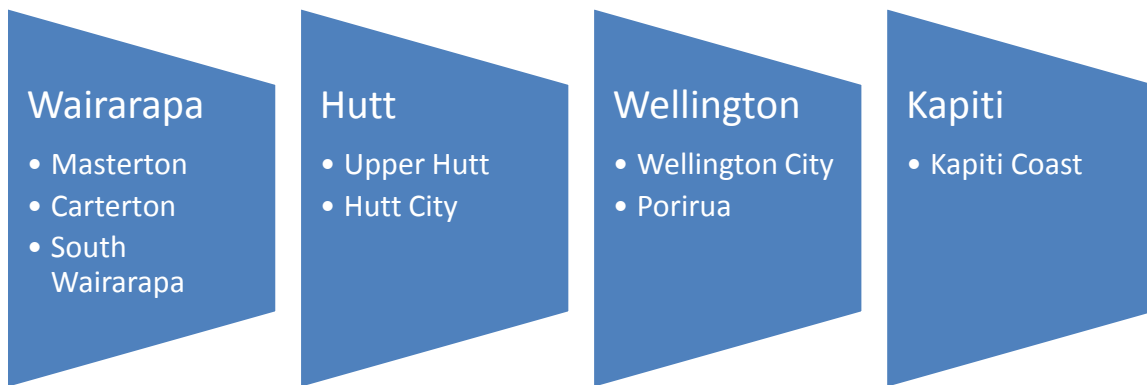
The key points for Option 2 are:

- the eight current territorial authorities and the greater regional council in the Wellington and Wairarapa regions would become four unitary authorities as follows:



- Wairarapa Unitary Authority from the amalgamation of Carterton District Council, Masterton District Council and South Wairarapa District Council and relevant functions currently undertaken by GWRC;
  - Hutt Valley Unitary Authority from the amalgamation of Hutt City Council and Upper Hutt City Council and relevant GWRC functions;
  - Wellington Unitary Authority from the amalgamation of Porirua City Council and Wellington City Council along with relevant GWRC functions; and
  - Kapiti Unitary Authority from the amalgamation of Kapiti Coast District Council along with the relevant GWRC functions;
- the Greater Wellington Regional Council would cease to exist. Its functions would be allocated as follows:
    - land-transport planning and delivery, together with the land-transport responsibilities of the antecedent councils would be transferred to a greater Wellington regional transport authority. This entity would be a jointly owned CCO and could be a joint venture with central government as is the case for Auckland Transport;
    - the Wellington region’s “three waters” services would be managed and operated by a CCO that would be jointly owned by the unitary authorities and operated by Capacity under a concession contract arrangement (as proposed by PwC 2012);
    - harbour and water navigation under the Maritime Transport Act 1994 would be carried out by the Wellington Unitary Authority; and
    - the relevant unitary authorities would each take over from the regional council responsibility for resource management functions (spatial and natural resource planning, soil conservation, water quality and ecosystems, natural hazards, hazardous substances, coastal marine environment), and other functions (flood and river control, reserves, civil defence, pest management and hazardous waste). Some of these functions could be undertaken on a shared-service basis;
  - under this option the governance of the Wellington and Wairarapa regions would move from two tiers of elected representatives to a single tier at the local council level. Currently there are similar unitary authorities in Gisborne, Nelson, Marlborough and Tasman, and since 2010 in Auckland.

**Figure 2: Potential unitary authorities**



The populations for each of the proposed unitary authorities based on the long-term plan population forecasts for 2013 are detailed below.

**Table 2: Long-term population forecasts – multiple unitary authorities**

Wairarapa	Hutt Valley	Wellington	Kapiti
40,346	145,320	255,700	51,160

### **Option 3: A single unitary authority**

The key points for Option 3 are:

- all eight current territorial authorities and the greater regional council would amalgamate to form a single, greater region-wide administration;
- land-transport planning and delivery could be undertaken in-house by the single unitary authority or under a greater regional transport authority. Similar considerations apply for ownership, management and operation of water services, which could either be provided in-house or via a concession arrangement with Capacity; and
- a single unitary authority could come in the form of a two-tier or a single-tier authority. Under the two-tier model local boards would be established based largely on the current territorial authority boundaries. A single-tier model could have community boards as considered appropriate.

The population of the proposed single authority based on the long-term plan population forecasts for 2013 is detailed below.

**Table 3: Long-term population forecast – single unitary authority**

Single authority
492,526

### **3.5 Local government statutory objectives**

As noted in section 3.1 above, the purpose of local government as defined under the Better Local Government Reforms (and specified in the Local Government Act 2002, Section 10) is twofold:

*“(a) to enable democratic local decision-making and action by, and on behalf of, communities”*; and

*“(b) to meet the current and future needs of communities for good-quality local infrastructure, local public services and performance of regulatory functions in a way that is most cost-effective for households and businesses.”*

Further details on the statutory objectives for local governance are provided in Annex 2.

#### **3.5.1 Local democracy**

In general, smaller councils are likely to be more responsive to local needs and preferences. A smaller council will tend to be better able to tailor the range and quality of services it provides to the wishes of its local community. In contrast, it is more difficult for a large council to tailor services, service levels and appropriate rates to small subsections of its jurisdiction.

Further, as a council increases in size, either in population or area, it naturally becomes more distanced from the individuals it represents. It is more difficult for decision-makers to make time for individuals and groups of individuals within the wider community. Therefore, the greater the distance between councillors and constituents the less approachable a council tends to become. This distance can lead to further issues such as a lack of transparency and reduced accountability. It may be more difficult to hold elected representatives to account as the distance from their ratepayers and citizens increases.

“Communities of interest” within a region can be diverse and overlapping. Some communities of interest are defined by the area in which citizens live, such as a neighbourhood or suburb, while others span a wide region linked by a common interest (e.g., cyclists). There are a few instances where region-wide jurisdiction may give a council the appropriate authority to meet the needs of a dispersed community of interest. However, mostly communities of interest are grouped geographically. This geographical concentration makes it easier for a council to tailor council services and functions to a specific area. As mentioned above, smaller councils are likely to be better at targeting the preferences of communities of interest.

If a resident, ratepayer or business becomes unhappy with a council’s policies or decisions, then citizens may be able to relocate to another district. However, larger councils provide less choice for citizens and make relocation more costly. Smaller councils may also be able to better meet the needs of residents, as preferences are likely to be less diverse within a smaller

group, particularly when residents can relatively easily self-select into or out of local council jurisdictions.

Under a larger organisation, such as a single greater Wellington unitary authority, local boards can be set up to address the perceived loss of democracy at a community level. These boards will have varying degrees of success depending on the extent to which they have a budget and autonomous decision-making power to direct resources. In practice, local boards are likely to derive their role and funding from the overarching unitary authority: this relationship reduces the extent to which local boards can influence decisions for the communities that they represent. Even if granted independence, local boards typically have a relatively minor role with discretion over budgets significantly less than the budget that would be under the control of a city or district council governing a similar-sized area.

Schedule 6 of the Local Government Act sets out provisions for the establishment of community boards which can apply either in the course of a reorganisation or they can be triggered at any time by a community that wishes to achieve community board status.

Hutt City Council currently has three community boards<sup>14</sup>, each reflecting a distinctive community character, and each likely to attach high value to the ability to continue under any new arrangements. Any proposal that fails to recognise this would, we expect, lead to significant and unnecessary resistance.

Unless there are good arguments to the contrary, and those enjoy public support, it would be logical to provide for existing community boards to continue in existence as community boards of any new council structure. It would be sensible, in addition, for any reorganisation proposal to acknowledge the potential interest in community boards and incorporate a policy on the establishment of new community boards, and the matters that could reasonably be delegated to them.

A final point to consider is the impact council size has on mayoral candidates. Very large councils may limit the choice of candidates for mayor, as running for mayor in a large region can be very costly to the candidates. An informed political adviser has observed, for instance, that at least \$0.5m is required to run a credible mayoral campaign in Auckland and some candidates are understood to have spent much larger sums in the 2010 election.

### **3.5.2 Efficiency**

Economics distinguishes between three types of efficiency: productive efficiency, allocative efficiency and dynamic efficiency. In the context of this report, productive efficiency can be thought of as a council's ability to convert its inputs into outputs at least cost, while allocative and dynamic efficiency can be thought of as the council's contribution to the efficiency of the wider economy.

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<sup>14</sup> Eastbourne Community Board, Petone Community Board and Wainuiomata Community Board.

## **Productive efficiency**

Productive efficiency is a measure of the extent to which an activity has achieved the maximum possible outputs for a given quantity of inputs. Also related, but subtly different, is “cost-effectiveness”. The concept of cost-effectiveness is applied to the management of many types of organised activity. Cost-effectiveness compares the relative costs and effects of different organisation or approaches to delivering services. An assessment of cost-effectiveness takes the benefits arising from the activities of the programme as a given and asks whether these could have been produced at a lower cost compared with other options.

Throughout this report our focus is on cost-effectiveness.

## **Allocative and dynamic efficiency**

A society that is allocatively and dynamically efficient is one that effectively produces the goods and services people desire most, with proper consideration of the trade-offs between consumption and investment over time. We can think of these efficiencies as relating to the performance of the wider economy.

While there has been some debate about Wellington’s economic performance in recent years<sup>15</sup>, we are not aware of any evidence to suggest that the structure of local councils and the general economic performance of a region are linked<sup>16</sup>. Local councils may be able to facilitate or inhibit regional economic development through their regulatory, rating and expenditure policies, but we do not expect the number of councils in a region to be a critical factor in this respect. The quality of local infrastructure also can play an important role in the growth and growth potential of a region. Our report identifies reforms to the governance of land transport and water services, which have significant potential to enhance local productivity over time.

## **4. International literature on size and cost-effectiveness**

This section explores the international evidence on the relationship between the size and cost-effectiveness of local government. In their literature review on the existence of economies of scale in local government, Byrnes and Dollery make the following observation on the evidence:

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<sup>15</sup> Wellington has been charged by some recently with being a low growth and underperforming region. Despite these claims, it is not clear that Wellington is performing all that poorly. It is true that some indicators suggest poor performance in recent years but in terms of unemployment, productivity and income levels the region outperforms the national average.

<sup>16</sup> In a recent visit to New Zealand one of the world’s top urban economists, Edward Glaeser, gave a presentation on what makes a city successful. For Wellington he suggested the ability to transfer information is key: this is achieved through small firms, smart people and connections to the outside world.

*“Overall, 29% of the research papers find evidence of U-shaped cost curves<sup>17</sup>, 39% find no statistical relationship between per capita expenditure and size, 8% find evidence of economies of scale, and 24% find diseconomies of scale. From this evidence alone we can conclude that there is a great deal of uncertainty about whether economies of scale exist in local government service provision.”<sup>18</sup>*

Byrnes and Dollery’s findings highlight the uncertainty and conflicting conclusions that have arisen within the field of local government size and efficiency. The assumption underlying almost all more centralised models of local government is that “bigger is better”.

As far as the ratepayer is concerned, “efficiency gains” may come in the form of reduced rates or improved service delivery for the same price.

It is presumed that cost savings can be achieved through:

- *economies of scale*

Economies of scale are factors that cause the average cost of producing something to fall as the volume of its output increases.

- *economies of scope*

Economies of scope are factors that make it cheaper to produce a range of products or services together than to produce each one of them on its own.

- *managerial economies*

Managerial economies are a special case of economies of scale and scope that arise from specialisation of internal managers. Larger organisations are able to employ more skilled and experienced managers and thus obtain the benefits of managerial skill in delivering services to constituents at lower costs.

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<sup>17</sup> A U-shaped cost curve is one in which per capita costs first decline then level off and then start rising as population increases.

<sup>18</sup> Byrnes, J. and Dollery, B. (2002).

However, it is important to remember that increased size is attended by the risk of increasing costs through:

- *diseconomies of scale*

Diseconomies of scale are factors that cause the average cost of producing something to rise as the volume of output increases. In the case of local government, scale diseconomies could arise because of increased bureaucracy, “silo behaviour”, or other dysfunctional behaviours that are seen as organisations get larger.

Finally, we note an increasing emphasis internationally on strategic capacity as a key issue in determining local government structure. This is a focus on ensuring that local government entities have the depth and resilience of capacity and capability to deal with the complex challenges that they face.

#### **4.1 The U-shaped curve**

A key finding that stands out from the international literature is that there is often an observable U-shaped relationship between council size and observable cost-effectiveness. It is often observed that per capita costs initially decrease with population size for small councils before a period of stability, and then costs increase with population for very large councils: this relationship resembles a U-shape. In essence, the smallest and largest councils are predicted to be least cost-effective.

The extensive international literature provides little support for a size and cost-effectiveness relationship for larger councils. It can be noted that:

- smaller councils with a population somewhere between 20,000 to 80,000 are apparently not least-cost, but much of the literature argues that this is the effect of specialised services and the local service environment rather than low cost-effectiveness *per se*;
- there is little correlation between size and cost-effectiveness for populations above 20,000 to 80,000. The relationship tends to remain stable up to about 200,000 to 250,000;
- larger councils with populations approximately 250,000 or above tend to have higher costs per capita. As for very small councils, this seems to be an effect of the costs of operating in metropolitan environments rather than cost-effectiveness *per se*.

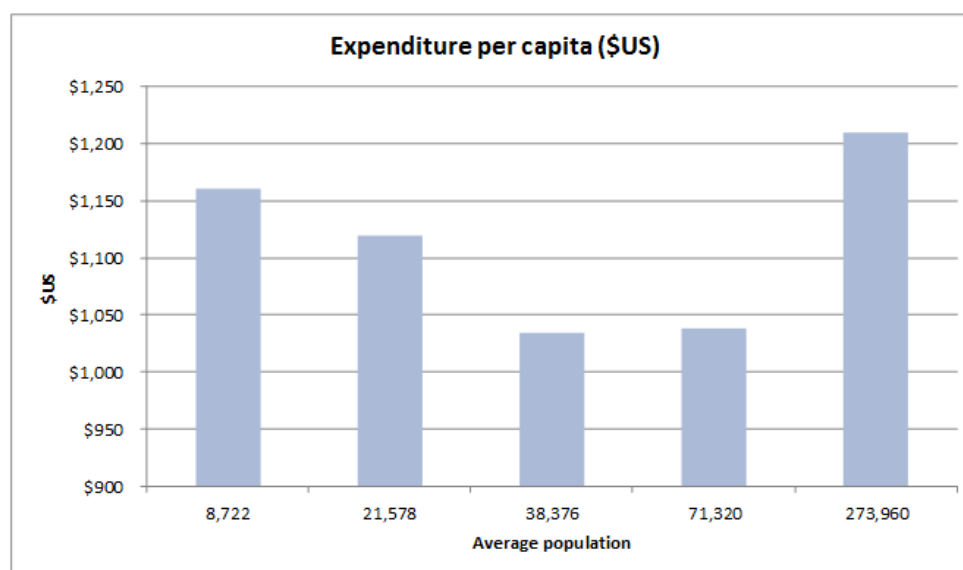
This U-shape phenomenon is evident in the 2003 Frontier research on local government amalgamation<sup>19</sup>. The study groups councils in the United States by population size and compares total council spending per person across groupings. We see that the smallest and the largest councils on average spend more per person.

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<sup>19</sup> Frontier Centre for Public Policy (2003).

Figure 3 below is an indicative example of the U-shaped cost curve.

**Figure 3: Expenditure per capita for US local governments**



Source: Reassessing Local Government Amalgamation, Frontier 2003

It is important to note that on a service-by-service basis local council functions tend to exhibit different relationships between size and per capita cost. The operational aspects of specific local public service delivery do not always obey the U-shaped relationship. The implication that is taken is that the diseconomies of size relate to swelling administrative layers as council organisations serve bigger populations rather than the operational conditions under which services are delivered. The particularly large councils have many “communities of interest” with a wider variety of needs and desires; these large councils can often end up delivering more services and services of a higher quality as result, therefore incurring greater cost.

## 4.2 Cost-effectiveness and population size

As we consider the evidence with the Wellington and Wairarapa regions in mind, there are two important questions to consider: do the “efficiency gains” from increased scale actually exist? And to the extent that they do, can they be achieved in other ways without incurring the transaction costs of council amalgamations?

Katsuyama (2003) states, “The consensus among researchers who have studied consolidation efforts is that nearly 80 percent of municipal services and activities do not possess economies of scale beyond a population of approximately 20,000 residents.” Gabler (1971) offered the opinion that “large cities tend to employ and spend more per capita than the smaller jurisdictions and this tendency is attributable – in part – to the effects of city size”.

The widespread acceptance among policy makers in Australia that larger municipalities would exhibit greater economic efficiencies lay behind amalgamations in that country.



Byrnes and Dollery (2002) however concluded, “The lack of rigorous evidence of significant economies of scale in municipal service provision casts considerable doubt on using this as the basis for amalgamations.”

The apparent inconsistency in the international research findings about the relationship between local government size and efficiency could be attributed to differences in the way some local public services are delivered. Thus the literature suggests that differences in per capita spending are a result of differences in the type and level of service functions, as well as the specific details of tasks within a service function. Additionally, the context in which local public services are delivered may be a more important influence on costs per capita than the size of the population served.

In his paper, Swianiewicz (2002) points out that the optimal size of local government may vary for different services. If this is the case, it is hard to weigh up the efficiency gains and losses that may result from any change in overall size of local government in a region.

However, one general distinction in the relationship between size and cost in local government services stands out: capital-intensive versus labour-intensive services. Generally, capital-intensive services – such as roading, water supply and solid waste management – become less costly with increasing size. Over five decades ago this was recognised by Hirsch (1959) who wrote,

*“... water and sewage services, which often account for about 8–10 per cent of total expenditures, tend to be rendered in a vertically integrated plant. Growth and consolidation will lead to a decline in per capita expenditures until a very large scale is reached, so large that few city and metropolitan areas have achieved it.”*

On the other hand,

*“... refuse collection, etc., accounting for around 80–85 per cent of all expenditures, will be furnished in horizontally integrated service plants. Growth and consolidation appear to have little, if any, significant effect on per capita expenditures for these services.”*

Thus for the more labour-intensive council services there seems little reason to assume that cost-effectiveness will improve with scale. This leaves us with a potential trade-off between cost-effectiveness in the provision of labour-intensive and capital-intensive services.

Caution needs to be taken when applying this conclusion to the New Zealand context since much of the international work in relation to labour-intensive services has been on police services, which are not a local government function in this country. Councils in countries in which studies took place may also provide primary and secondary education, which is labour-intensive as well, but again education is not a local government function in New Zealand.

Turning to the practice (or revealed preference) in other countries, European practice does not appear to support the belief that bigger is necessarily better. If anything, it suggests there is nothing even resembling a consensus about how big or small local councils should be. Swianiewicz (2002) presents evidence (refer to Table 4 below) on the average size of the population per municipality in Europe. The table indicates the average population size per municipality in Europe ranges from 1,300 in France to 123,000 in England and Wales, with the great majority of countries having less than 50,000 people per municipality.

Considering the greater Wellington region currently has eight councils at present and a population close to half a million, this would place the greater region (with an average of over 50,000 per council) near the top of the European list, at present.

A single authority in Wellington could potentially have as many as half a million people under a single governing authority, which would place it as an outlier in the European context.

Looking at New Zealand as a whole, with 67 territorial authorities<sup>20</sup> and around 4.4 million people, this equates to an average of over 67,000 residents per territorial authority. If Auckland Council is excluded, New Zealand's average council population base is still around 47,000. Regardless of the treatment of Auckland Council, New Zealand already has a relatively high number of people per council compared to Europe.

The population-to-local-council ratio in New Zealand is also significantly higher than in either Australia or the United States. The most recent local government national report in Australia stated that Australia had approximately 37,000 people per local council. The United States has an even lower ratio with fewer than 9,000 people per local government entity<sup>21</sup>.

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<sup>20</sup> A further 11 regional councils provide particular services at a regional level across multiple territorial authorities.

<sup>21</sup> This is calculated by dividing the United States' population by the number of municipal and town or township governments in the United States. It does not include state governments, county governments or special purpose local governments.

**Table 4: Average size of local governments in selected European countries**

Country	% of Municipalities Below 1,000 Citizens	Average Population	Average Area [sq. Km]
England and Wales	0	123,000	533
<i>Lithuania</i>	0	66,000	1,166
<i>Yugoslavia</i>	0	49,500	487
<b>Bulgaria</b>	<b>0</b>	<b>35,000</b>	<b>432</b>
Sweden	0	29,500	1,595
Holland	0.2	20,500	60
Denmark	0	18,000	150
<b>Poland</b>	<b>0</b>	<b>16,000</b>	<b>130</b>
<i>Macedonia</i>	3	15,800	209
<i>Slovenia</i>	3	10,300	106
<i>Albania</i>	0	10,000	77
Finland	5	10,500	730
Norway	4	9,000	710
<i>Croatia</i>	3	8,800	104
<i>Romania</i>	2	7,600	81
Italy	24	6,500	38
<i>Estonia</i>	9	5,700	178
Spain	61	5,000	60
<i>Ukraine</i>	NA	4,600	56
<i>Latvia</i>	32	4,300	115
<b>Hungary</b>	<b>54</b>	<b>3,300</b>	<b>32</b>
<b>Slovakia</b>	<b>68</b>	<b>1,900</b>	<b>17</b>
<b>Czech Republic</b>	<b>80</b>	<b>1,700</b>	<b>13</b>
France	77	1,300	15

Source: Size of local government, local democracy and efficiency in delivery of local services, P. Swianiewicz (2002).

Even on the lower average of 47,000, the population of a typical New Zealand local authority is significantly higher than its counterparts in other jurisdictions. Of perhaps more importance, however, is what is known as the representation ratio: the ratio of residents to elected members. It is this ratio that helps influence how easy it is for someone to make contact with an elected representative. In this respect, New Zealand performs even less well than might appear from the population figures by themselves.

For people wishing to engage with the council and, in particular, to have ready access to elected members, it is not just the population of the council area that matters, but the ratio of residents to elected members. On this basis, New Zealand compares even less well with especially both UK and European councils. In the UK on average one councillor represents 2,605 citizens. In France the average is one councillor for every 116 citizens; Germany 250 citizens; Italy 397 citizens; Spain 597 citizens; Sweden 667 citizens and Denmark 1,084 citizens.

For councils within the Wellington and Wairarapa regions, present representation ratios are shown in the table below (calculated as the population divided by the number of councillors, plus the mayor).

**Table 5: Representation ratios for the Wellington and Wairarapa regions**

<b>Wellington region representation ratios</b>		
Council	Population	Residents per elected member
Hutt	103,740	7,980
Kapiti	51,160	4,651
Porirua	52,940	3,781
Upper Hutt	41,580	3,780
Wellington City	202,760	13,517
<b>Total</b>	<b>452,180</b>	<b>7,065</b>
<b>Wairarapa region representation ratios</b>		
Carterton	7,560	840
Masterton	23,400	2,127
South Wairarapa	9,386	939
<b>Total</b>	<b>40,346</b>	<b>1,345</b>

One matter that will need to be considered, under each of the three options reviewed in this report, is the representation ratios that will result, and whether there is any need to make provision for what is known as sub-council governance to minimise the risk of residents feeling that they have lost representation.

Unfortunately, current international practice provides no clear path for New Zealand to follow. Theoretically, we might expect some combination of amalgamated councils to be able to generate some cost savings, if not through economies of scale, then potentially through economies of scope.

### **4.3 Are the potential benefits worth the cost of transition?**

The literature suggests that the evidence for cost savings arising out of amalgamations is limited. There is some evidence for potential efficiency gains or U-shaped cost curves for different services but the optimal size of local government differs across council functions. There is some indication that efficiency gains are possible for amalgamations of very small councils. However, the evidence is inconclusive at best that “bigger is better” when it comes to medium to large local councils. In practice:

- cost savings are often over-estimated;
- transition costs in terms of both time and expense are often under-estimated; and
- even when cost savings are achieved in one area, the funds are typically put to use elsewhere and rates reductions are rarely seen.

It is important to remember that the net present value (NPV) of future cost savings of any change in governance structure must be enough to outweigh the transition costs associated with the change. Further, in estimating these “efficiency gains” we should consider how the

councils will look in the future under the status quo to ensure we are making a fair comparison. Cost savings, new technology and changes in the quality or quantity of service provision will all affect a newly formed council into the future. However, many of these factors would still have influenced local council performance had the structure remained unchanged and these effects should be taken into account when assessing the net benefits of structural changes.

Efficiency gains are a good motivation for change, but if the potential cost savings are not supported by empirical evidence we need to think carefully about the best decision going forward. When we consider that there may be a trade-off between cost-effectiveness and local democracy and only questionable cost savings, and given the time and expense associated with structural transitions, then deciphering the appropriate solution is a complex task.

## **5. The New Zealand evidence: previous reports**

### **5.1 Introduction**

The Wellington and Wairarapa regions currently have two tiers of governance with the regions' local council services split between the Greater Wellington Regional Council and the eight local councils: Wellington City, Porirua, Kapiti Coast, Hutt City, Upper Hutt, South Wairarapa, Carterton and Masterton. Although theoretically we might expect some combination of amalgamated councils to be able to generate some cost savings, the international evidence indicates that this is by no means guaranteed. We must consider whether the benefits are worth the cost of transition, and to what extent and in what ways any new structure will outperform the status quo.

The Martin Jenkins/TDB<sup>22</sup> Wairarapa Council report assumed an overall level of savings of 3% from amalgamation. This assumption was supported by advice presented to the Royal Commission on Auckland Governance<sup>23</sup> that projected the savings on total expenditure to be achieved from the formation of the Auckland Council to be in the range of 2.5% – 3.5%; operating expenditure savings of 3% – 4%; and capital expenditure savings of 2% – 3%. However, what kind of cost saving assumption should be made regarding a single Wellington unitary authority? How do our expectations differ when we consider four unitary authorities in the greater region?

The literature review in section 4 above highlights the difficulties in answering these questions. Despite the underlying assumption behind many local council amalgamations that economies of scale exist in the provision of council services, the empirical evidence to suggest these cost savings are realised is limited.

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<sup>22</sup> Martin Jenkins and Taylor Duignan Barry Ltd (2013).

<sup>23</sup> Taylor Duignan Barry Ltd (2009).

Cost savings of between 2.5% and 3.5% due to “efficiency gains” from local council reform in Wellington were expected by the Wellington Region Local Government Review Panel<sup>24</sup>. The Panel cited that Auckland Council is expecting to meet the level of savings that were forecast prior to its creation. Separately, the Joint Working Party on Local Government Reform (“the Working Party”) assumed 3% to 4% can be shaved off operating expenditure through local government reform in the greater Wellington region<sup>25</sup>.

## 5.2 NZIER report

NZIER, in its 2012 report to Hutt City, analysed local government spending per capita compared to the population in each council area in New Zealand for the years 2006 to 2011<sup>26</sup>. NZIER’s conclusions were broadly consistent with the international literature. NZIER found different thresholds for points at which the per capita spending relationship with population changed but overall confirmed a “U” shape in the function. The report stated:

*“For councils with populations:*

- of 20,000 to 40,000 average per capita spending tends to be about 20 percent higher than average per capita spending for councils with a population of about 80,000;*
- 100,000 to 200,000 per capita spending tends to increase gradually with average per capita spending about 15 percent above average per capita spending for councils with populations around 80,000;*
- of 350,000 to 450,000 the evidence for correlation between per capita spending and population is weak.”*

However the variability of per capita spending by councils serving similar-size populations was such that NZIER also pointed to a range of other influences on spending choices by councils including:

- community incomes and preferences;
- population ages and demographic structure;
- the economic structure such as between councils service areas that had predominantly primary sector, manufacturing and services economic bases;
- geography and proximity to other large populations; and
- past spending, investment and financing decisions.

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<sup>24</sup> Wellington Region Local Government Review Panel (2012).

<sup>25</sup> Working Party on Local Government Reform (2013).

<sup>26</sup> NZIER (2012).

The report acknowledges that evidence of economies of scale in local government amalgamations is mixed and that two conclusions are typically drawn on council amalgamations and shared service delivery:

- amalgamations of councils do not automatically deliver savings; and
- shared service initiatives generally do not meet savings expectations.

NZIER further examined the pattern of per capita spending over 16 different spending type categories. This analysis revealed important information on the behaviour of per capita spending and population according to specific service type:

- thirty-two per cent of per capita spending increases with population size (transport, solid waste, recreation and sport);
- thirty-one per cent shows little or no relationship with population size (property, community development, economic development, governance, council services, other activities); and
- thirty-seven per cent declines with population size (roading, water supply, environmental protection, emergency management, planning and regulation).

On a total spending per capita basis, NZIER's results are similar to the international evidence. Table 6 below indicates a clear difference in average per capita spending between the smallest councils (less than 20,000 people) and the larger councils. NZIER's findings are in line with the international evidence that the very small councils are the most likely to experience efficiency gains through amalgamation. It is difficult to draw conclusions about the largest councils as there are so few examples in New Zealand.

**Table 6: Council population and per capita spending 2010**

Population	Number of councils	Average per capita spend (\$)	Range of per capita spend (\$)
Below 20,000	25	2,001	1,292 to 2,678
20,000 to 49,900	27	1,669	1,199 to 2,852
50,000 to 100,000	11	1,566	1,353 to 1,861
101,000 to 199,900	5	1,677	1,438 to 2,164
205,000 to 230,000	2	1,610	1,353 to 1,707
376,000 <sup>1</sup>	1	1,356	
377,000	1	1,390	
450,000 <sup>1</sup>	1	1,970	

(1) Water supply, and waste/storm water services were provided by council controlled organisations for Manakau City and Auckland City. The cost of these services was charged directly to ratepayers and not fully included in the operating expenditure data provided by Statistics New Zealand. To adjust for this, the cost of these services stated in the annual reports for Metrowater (supplier of water services to Auckland in 2010) and Manakau Water Limited 2009/10 have been added to the operating expenditure data provided by Statistics New Zealand

Source: NZIER report 'Merger Options for Wellington Councils 2012'.



### 5.3 The Auckland experience

As from 1 November 2010, a unitary authority, the Auckland Council, has performed the functions previously undertaken by the seven territorial authorities and the Auckland Regional Council.

In some ways Auckland Council provides us with a useful case study in considering reorganisation options for the Wellington and Wairarapa regions. However, given that the Auckland Council is still in its early days, it is very difficult to judge the impacts of the reorganisation.

There is some anecdotal evidence of benefits from the amalgamation. Auckland Council has reported \$81 million of efficiencies in the first year and is forecasting \$1.7 billion of efficiency savings (in most instances, maintaining or improving service levels) during the next 10 years<sup>27</sup>. Some also note the new central government spending on light rail in Auckland and attribute that commitment to the existence of a single authority. As is discussed in section 8.1 below, we consider Wellington could also benefit from a coordinated approach to land transport.

On the other hand, others have noted the costs of transition<sup>28</sup>, increased wages bills in the new council, rising debt levels and the increased complexity from the sheer size of Auckland City and the expanded consultation process requirements. The draft Auckland Unitary Plan (including the appendices), for example, totals some 7,000 pages<sup>29</sup>.

Although we do not yet know whether the benefits of the reorganisation of the Auckland councils will outweigh the costs in Auckland, we are confident there are some positive aspects of the amalgamation. In particular, we expect certain complex, capital-intensive functions to be best suited to regional provision and we believe Wellington can follow in Auckland's footsteps on these issues.

In addition, it must be noted that Auckland is different to the Wellington and Wairarapa regions in many ways and the success or failure of a decision in Auckland should not lead us to assume the same success or failure is inevitable in Wellington and the Wairarapa.

Overall, regarding the lessons to be drawn for the greater Wellington region from Auckland Council, we reach a similar conclusion to that expressed by the Wellington Region Local Government Review Panel in their report:

*“Our conclusion is that the Auckland model cannot be imported into the Wellington region. What we have fashioned is a model for Wellington, based on Wellington geography and conditions designed to address the deficiencies that*

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<sup>27</sup> Controller and Auditor General (2012).

<sup>28</sup> A cost of \$500 million has been cited by some in connection with combining the IT platforms of the eight councils that were the antecedents for Auckland Council. However note the important qualifications to this estimate in section 6.5 below.

<sup>29</sup> Auckland City (2013).



*currently exist here. They are different from the problems that afflicted Auckland. That said, some of the developments in Auckland should be taken up in Wellington as a matter of urgency. Our twin aims for the Wellington region have been to provide strong regional leadership and enhanced local democracy.”<sup>30</sup>*

Our analysis below explores further where the benefits of amalgamation are most likely to be found.

## 6. TDB analysis

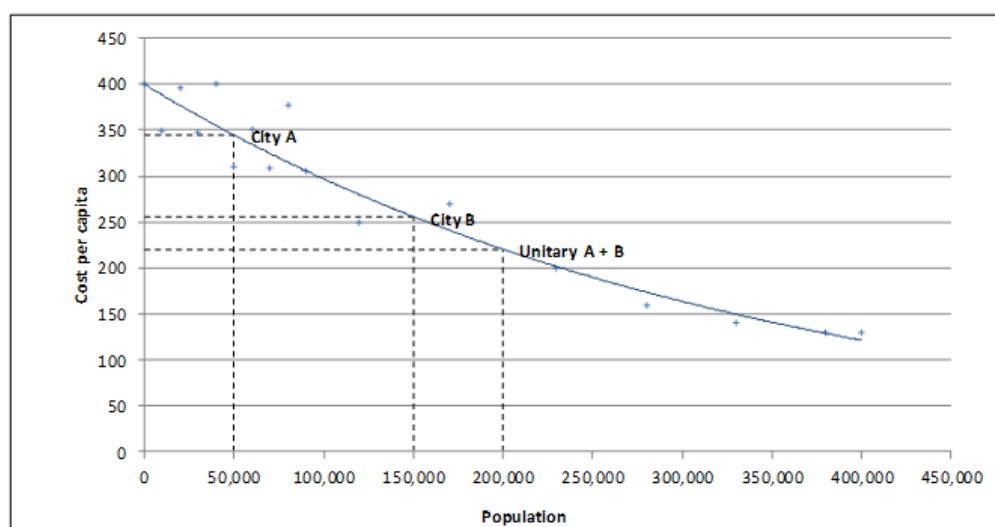
In this section we report our analysis of the relationship between size and cost-effectiveness in local councils in New Zealand.

### 6.1 Our approach

Based on historical spending by local councils in New Zealand, we estimate cost curves for individual local government functions. We use NZIER’s data on annual per capita spending separated by council and by function for the period 2006–2010. In modelling the relationship between spending per capita and population, we seek to estimate the savings that may result from council amalgamations. The conceptual approach we adopt is outlined in Annex 4.

Figure 4 below is an indication of how we arrive at our results. In the example below, the blue line can be considered the estimated cost curve for a particular local government function. We can compare the combined total spending of local authority A and local authority B with the total spending of unitary A+B to estimate the savings we might expect from an amalgamation of local authorities A and B. The blue line can be considered an estimate of the per capita spend by an average-performing local authority in terms of cost-effectiveness for a given population.

**Figure 4: Where size and efficiency merger gains come from**



<sup>30</sup> Wellington Region Local Government Review Panel, op cit.

Figure 4 above demonstrates that:

- an average local authority the size of A delivers the example service to a population of 50,000 people at a cost of approximately \$350 per capita;
- an average local authority the size of B delivers the example service to a population of 150,000 people at a cost of approximately \$250 per capita;
- an average local authority the size of Unitary A+B delivers the example service to a population of 200,000 people at a cost of approximately \$220 per capita; and
- when we compare the spending of Unitary A+B with the combined spending of A and B we estimate the measurable efficiency gains we might expect from council amalgamations.

## 6.2 Estimates of the size of the prize

We have extended the analysis undertaken by NZIER by fitting “cost function” curves to the available data on per capita service delivery spending. The purpose is to provide a basis for making estimates of the potential synergy gains from amalgamating service functions or councils in the Wellington and Wairarapa regions.

We estimate cost curves for sixteen separate functions and overall spending by local councils.

The figures below (Figures 5 to 10) show the functions and overall spending where the relationship between spending and population suggests that “efficiency gains” may be achievable through amalgamation. When interpreting the figures:

- the blue and orange points represent actual spending by local councils in New Zealand over the period 2006 to 2010;
- the red line is the estimated cost curve and indicates the relationship between spending per capita and population for an average performing council of a given size; and
- the twenty-five per cent top-performing councils are coloured orange. Our proxy measure of “top-performing” is the lowest per capita spend.

We find water supply, solid waste, roading, governance and emergency management are the council functions where improved cost-effectiveness may be achievable through amalgamation.

The steeper the downward sloping portion of the red curve, the greater the expected efficiency gain for councils over that population. In all cases the great bulk of the efficiency gains from amalgamation are only evident for relatively small local authorities. Observation of the figures below suggests:

- amalgamations up to around 50,000 people will likely lead to reasonable cost savings; and

- even for those six functions illustrated below where there are economies of scale initially, the per capita spend is unlikely to change materially after an amalgamation for a council serving a population of 50,000 or more, although with water and roading supply there is sign of some efficiency gains from larger-scale amalgamations.

Figure 5: Water supply

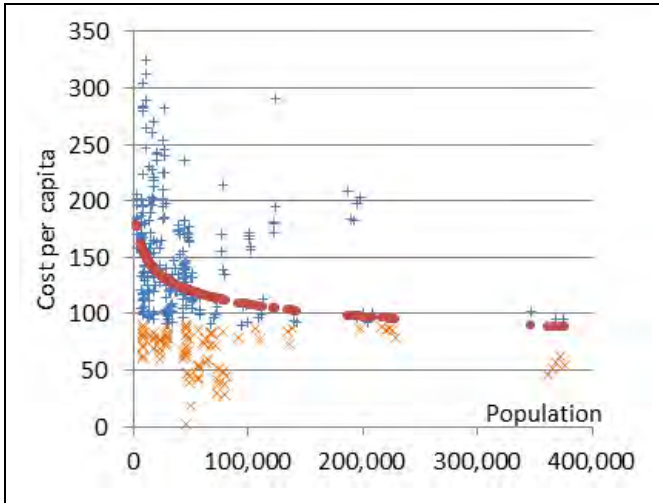


Figure 6: Solid waste

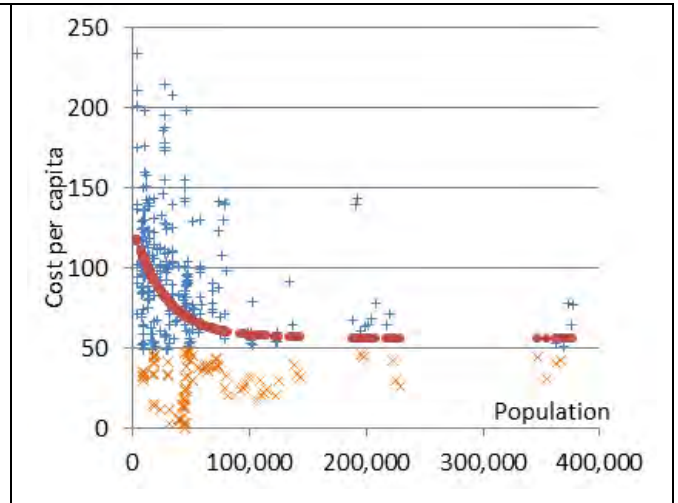


Figure 7: Roading

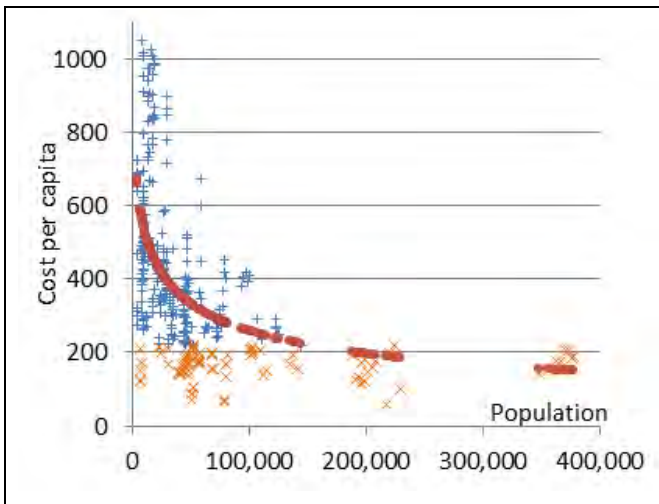
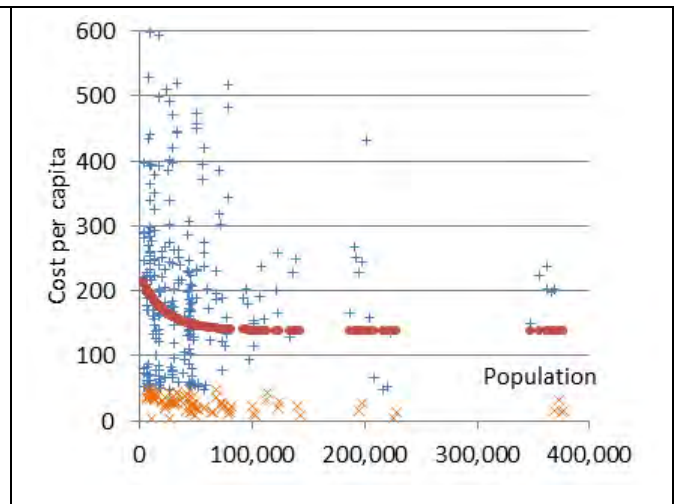
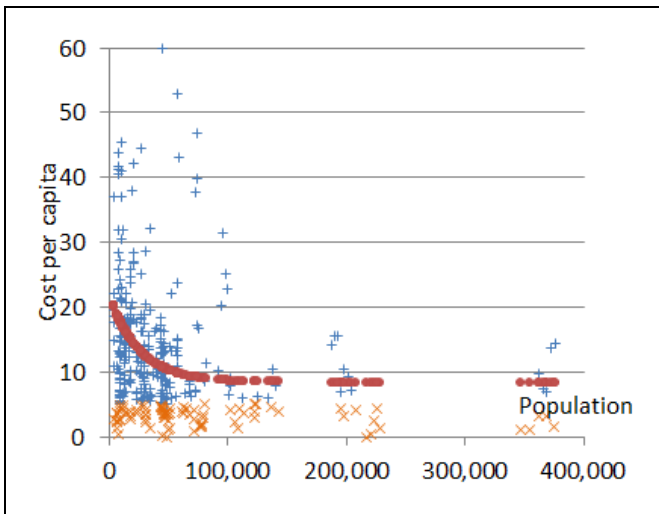


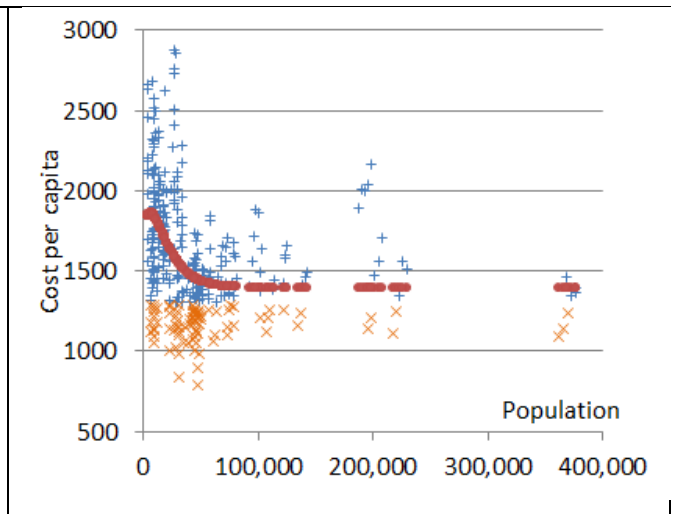
Figure 8: Governance



**Figure 9: Emergency management**



**Figure 10: Total spending**



Using our modelled cost-curves we estimate the expected savings we might expect from different possible amalgamations in the Wellington and Wairarapa regions. Two scenarios are examined:

- Option 2: four unitary authorities<sup>31</sup>. Under this option the following councils are combined:
  - Wellington City Council and Porirua City Council;
  - Hutt City Council and Upper Hutt City Council; and
  - Carterton District Council, Masterton District Council and South Wairarapa District Council;
- Option 3: single unitary authority. Under this option the eight local councils within the greater Wellington region are combined.

Based on the populations served by the current territorial authorities in the Wellington and Wairarapa regions we estimate how the combined spending of average performing councils of the same size compare with the total spending of an amalgamated equivalent. Our estimates are as follows.

**Table 7: Potential synergy benefits from council amalgamations**

	Whole Region	Wellington City and Porirua	Upper Hutt and Hutt City	Carterton, Masterton and South Wairarapa
Population	492,526	255,700	145,320	40,346
Overall 'savings'	3%	0%	4%	14%

<sup>31</sup> Kapiti is assumed to remain stand-alone for the purpose of this analysis.

The estimates presented in Table 7 above represent the possible cost savings that could result from amalgamations of average-performing councils of the same size as those in the Wellington and Wairarapa regions. Our analysis suggests:

- a single authority could result in an overall cost saving of around 3%;
- a Wellington City and Porirua amalgamation could result in no overall cost savings;
- a Hutt City and Upper Hutt City amalgamation could result in a cost saving of around 4%; and
- a Wairarapa unitary authority could result in a cost saving of around 14%.

These estimates are subject to some important qualifications. Most importantly, the estimates are based on data from all territorial authorities across New Zealand and thus reflect the results of “representative” New Zealand councils of the size of the various greater Wellington councils before and after amalgamation and not the cost structures of the actual greater Wellington councils (the latter is discussed in section 7 and Annex 7). Further, the cost saving estimates above could change if a richer analysis was undertaken. However, such a task would be extremely difficult as many of the influences cannot be measured or quantified. Finally, the above estimates do not account for the time delays and transition costs associated with council amalgamations and thus overstate the likely benefits to this extent.

At the individual council function level, the analysis suggests that reasonable cost savings for each of the functions pictured above – water supply, solid waste, roading, governance and emergency management – can be expected. These functions are most-suited to larger-scale provision. Large savings can be expected by amalgamating councils serving very small populations such as in the Wairarapa. However, many of the other functions not pictured above do not have similar cost curves and therefore efficiency gains do not materialise as a result of amalgamation or otherwise increasing scale.

Overall, our analysis of the New Zealand data suggests that population is not a major driver of council per capita costs. Although we have estimated some possible cost savings above, a variety of other factors will impact per capita costs to a greater extent than population (as described in section 6.4 below).

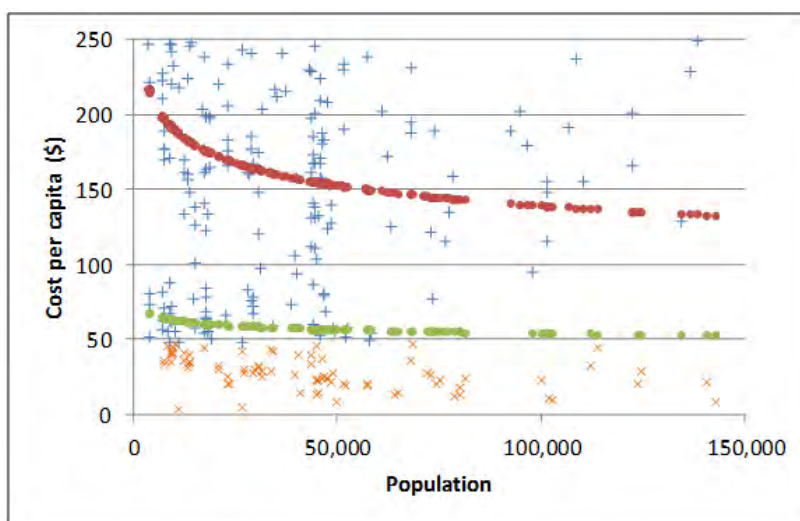
### **6.3 Best practice**

We also estimate a best practice cost-curve for each local council function: this line indicates the point below that 25% of territorial authorities have a lower cost per capita for the given function. It is important to note that cost per capita is an imperfect proxy for cost-effectiveness. Not all councils that fall within the lowest 25% in cost per capita for a given function will necessarily be cost-effective providers of that function. A low per capita expenditure may be driven by a variety of factors other than population size (further discussion of this issue can be found in section 6.4 below).

Best practice can be sought by councils of all sizes through efficiency gains, changes in management, new technology, or other means. The green cost curve in Figure 11 below is the

best practice estimate. The governance example provided in Figure 11 below is indicative of the shape of most other best practice cost curves for other functions. Surprisingly, almost all the best practice curves are flat or very close to flat. This suggests that councils of any size that have managed to achieve best practice have very little to gain from amalgamation. The significant gap between the average governance cost curve and the best practice cost curve is also telling: the graph suggests the average local authority could gain significant cost savings by moving towards best practice.

Figure 11: Best practice estimation: governance



A few local authority functions (as pictured above) exhibit an inverse relationship between per capita cost and population size for average performing councils. However, for almost every local government function it appears at the best practice level that there is little to no correlation between per capita spending and size. The implication of this lack of correlation is that if a council can achieve best practice, there is little or nothing more to gain from increasing the scale of operations. Good internal practices are the key to cost savings, not the scale of operations. The New Zealand Productivity Commission echoed this sentiment in its recent report on regulatory decision-making in local authorities. The Productivity Commission noted:

*“Local authorities generally follow adequate regulatory decision-making processes. This finding is not dependent on the size of the local authority. The review specifically tested the hypothesis that larger local authorities are able to follow better regulatory processes because of their greater financial resources and internal capability. The analysis revealed that while larger local authorities are able to draw upon a larger body of technical information when making regulatory decisions, smaller local authorities appear better able to incorporate specific community concerns, due to their closer relationship with the community. To some extent this reflects a trade-off between the resources available to a local*

*authority and the level of community responsiveness that can realistically be achieved.”<sup>32</sup>*

## **6.4 Per capita cost and population**

This section explains how much of the variation in per capita costs is able to be explained by the numbers of constituents served. As noted above, our analysis indicates there is only a very weak relationship between per capita spending and council size<sup>33</sup>. The fact that population is not a good explanatory variable suggests that potential benefits associated with amalgamation are likely to be limited if the only change that takes place is the size of the constituent base for each council.

There are specific instances or particular local council functions (pictured in section 6.2 above) where a correlation between population size and per capita council spending is observed. However, like Byrnes and Dollery (referenced in section 4.1 above), we cannot reasonably suggest, based on the evidence, that large economies of scale or large efficiency gains should be expected in the greater Wellington region. There is too much uncertainty surrounding the issue, and population size is but one of many factors influencing the differences in cost-effectiveness between councils of different sizes.

Cost per capita of the population served is the usual proxy measure for cost-effectiveness adopted in local government service delivery. However, there are many influences on cost per capita as a proxy measure of cost-effectiveness, leading to a lack of comparability between councils serving equal-sized populations, let alone populations of vastly differing sizes. A range of factors other than cost-effectiveness may practically influence variation in the cost of providing local public services in a region. Such influences include:

- the effect of the age of the community’s infrastructure relative to the requirement to replace or upgrade facilities and services;
- the effect on the demand for local public services of peaks and troughs whether seasonal or through the work day/weekends, such as affect dormitory communities and employment hubs;
- practical limitations on the rateable property base such as a predominance of residential properties or rural areas, numbers of retired or low-income residents, or a high proportion of non-rateable property, and the wealth and willingness to pay of residents;
- what local public services are chosen to be provided; and
- the level (i.e., the quantity and quality) of the public service provided in the region.

None of these factors is captured in the spending per capita figure but it is nevertheless the best proxy measure of cost-effectiveness available. The specific details of the local public

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<sup>32</sup> New Zealand Productivity Commission (2013).

<sup>33</sup> The R<sup>2</sup> estimates are mostly below 0.1.



services and the environment in which they are provided are very important in determining a council's spending on any given service. Population is a small driver of per capita spending and in a number of cases (culture, recreation and sport, property, etc.) population size and per capita spend do not seem to be inversely correlated at all.

It is therefore very difficult to predict the change in council spending as a result of amalgamation. Although cost savings may be available for certain services under certain conditions, the effect on overall council spending is unknown. The impact of transition costs will only make large-scale amalgamation a less attractive option. McKinlay Douglas Ltd in its report "Local Government Structure and Efficiency" provides a similar insight:

*"The literature on the evidence on economies of scale in local government services reveals a general acceptance that there may be economies of scale within individual services, but that, service by service, these will arise at quite different scales of operation. Rather than economies of scale providing a rationale for amalgamation, the weight of evidence suggests both that larger authorities may be less efficient, and that the better means of seeking economies of scale is to do so on a service by service basis – whether through collaboration, joint ventures, outsourcing or other means."*<sup>34</sup>

## **6.5 Amalgamation costs**

Council amalgamations produce costs as well as savings. Analysing the costs of amalgamation is difficult since it is not always clear what costs are truly additional and caused directly by the amalgamation, and what costs would have been largely incurred anyway.

Amalgamation costs may include the following:

- one-off costs caused by amalgamation that would not otherwise have been incurred. There is a broad range of such costs including legal, consultancy, staff redundancy and staff recruitment, through to advertising, marketing and signage;
- IT systems integration. Much has been made of the \$500 million figure mentioned in section 5.3 above in connection with combining the IT platforms of the eight councils that were the antecedents for Auckland Council. However such figures need to be regarded with caution as they need to be judged in relation to the previous levels of spending and possible under spending by the previous councils;
- employment conditions harmonisation or "wage creep". Smaller councils tend to have lower wage cost structures. Upon amalgamation, employment terms and conditions are likely to become uniform, generally increasing to the highest level prior to the amalgamation, leading to an increase in overall costs. In the surveys of overseas

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<sup>34</sup> McKinlay Douglas Ltd (2006).



council amalgamations the effect of wages harmonisation is the influence most often cited, along with IT, as the excess cost of amalgamation;

- fees and services harmonisation or “service creep”. Similar to the above point, services provided across the region generally become uniform and those areas where service levels were lower prior to amalgamation are improved and higher fees may be reduced to standardise the region, leading to an increase in overall costs;
- recalculation of rates (there is a balance between commercial versus residential, capital versus land value, and general versus targeted); and
- there is also upheaval in any amalgamation to council employees and users of council services and this should not necessarily be disregarded as immaterial.

What becomes clear is that amalgamation costs are generally significant enough to absorb the short-term benefits from amalgamations meaning that the benefits of costs savings are postponed. The further into the future a newly formed council will take to begin realising the possible net benefits of amalgamation, the less likely it is to be a positive net present value decision today.

## 6.6 Overall assessment

Although the literature and available New Zealand evidence do not reveal strong and consistent relationships between size and cost-effectiveness in the delivery of local government services, some relationships are evident:

- the first relationship describes the overall effect of size on cost-effectiveness. What appears to hold is that for medium-sized councils<sup>35</sup> per capita expenditure is largely independent of the size of the population served; and
- the general relationship, however, does not hold when specific services are considered:
  - services that require large-scale capital investments possess economies of scale in relation to the population served and are likely to be produced more efficiently when serving larger populations. Services where economies of scale are likely to be present account for around 34%<sup>36</sup> of spending by Wellington and Wairarapa local councils and include roading, water supply, solid waste, emergency management, and governance; and
  - services that are more labour-intensive and are performed relatively frequently and regularly are likely to possess diseconomies of scale. Such services that are unlikely to benefit from cost savings as a result of amalgamation, account for nearly two-thirds of spending by the Wellington and Wairarapa local councils. For these services (e.g., planning, regulation and environmental

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<sup>35</sup> Councils that broadly fall into this category serve populations around 80,000 or below up to around 250,000.

<sup>36</sup> Sourced from NZIER data detailed in Table 8 below.

protection), there is a generally weak relationship to size or no relationship to size at all.

Table 8 below provides a summary of the percentage of spend by function in the Wellington and Wairarapa regions for the year ending June 2010 and the observed relationship between cost per capita and population for each function across the New Zealand data.

**Table 8: Proportion of spend by service area**

Service	Proportion of spend in Wellington*	Change in cost per capita as population increases
Roading	16%	Rapid decline for populations below 100,000 then almost flat
Transport	11%	Rapid increase with population
Water supply	11%	Gradual decline as population increases
Waste and storm water	10%	Initial increase with population peaking for populations of 150,000 to 200,000 and 450,000
Solid waste	4%	Rapid decline for populations below 150,000 then almost flat
Environmental protection	3%	Gradual decline as population increases
Culture	5%	Increases as population rises, peaks for populations of about 150,000 to 200,000 but varies widely for higher populations
Recreation and sport	7%	Increases as population rises, peaks for populations of about 150,000 to 200,000 and then declines
Property	4%	Increases as population rises, peaks for populations of about 200,000 to 250,000 and then declines
Emergency management	1%	Initial decline as population increases, but rate of decline slows
Planning and regulation	7%	Decline for populations below 100,000 then almost flat
Community development	1%	Initial decline as population increases then gradual increase
Economic development	1%	Varies in a narrow band for populations up to 300,000 and then increases
Governance	2%	Initial decline as population increases, then flat
Council services	16%	Fluctuates in a narrow band
Other activities	1%	Fluctuates in a narrow band

Source: NZIER analysis of “Local authority financial statistics – Total operating income and expenditure by activity by local authority – Year ended June, 2010” and “Estimated Subnational Population (TA,AU) by Age and Sex at 30 June 2006–11 (2006 Boundaries)” from Statistics New Zealand.

\* TDB calculation for year ended June 2010 (includes Wellington and Wairarapa regions).

## 7. Financial analysis

### 7.1 Introduction

This section of the report considers the possible financial implications of reorganisation of governance in the Wellington and Wairarapa regions. This section focuses on the possible impacts on average rates and debt levels across the current territorial authority areas in the Wellington and Wairarapa regions from moving to a single unitary authority or to four unitary authorities.

## 7.2 Context

Local government in the Wellington and Wairarapa regions is a billion-dollar business. Revenue for the nine councils totalled around \$1 billion in 2012/13. This is comparable to the total funding to the district health boards that serve the regions received from the Ministry of Health for the 2012/13 year.

The financial performance of the nine councils in the greater Wellington area is summarised in Table 9 below.

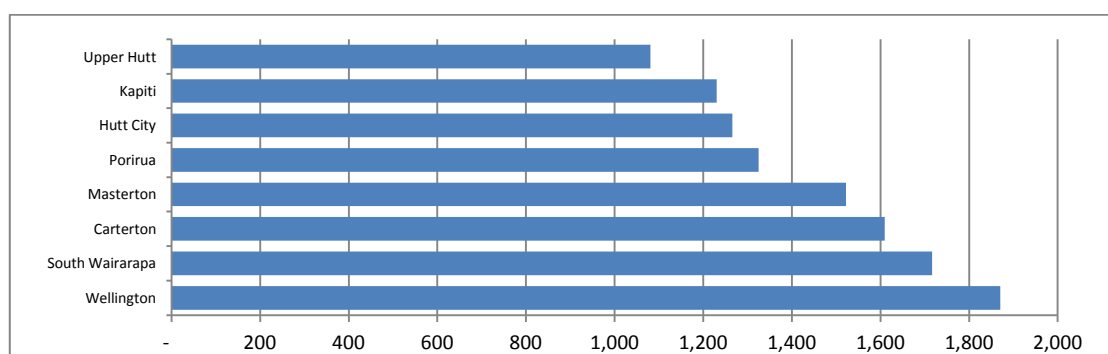
**Table 9: Summary of financial performance by council**

2012–13 (budget) \$'m	Total	GWRC	KCDC	PCC	WCC	HCC	UHCC	Wairarapa
Total income	1,006.7	220.7	63.2	66.7	416.6	132.7	42.4	64.5
Total expenditure	988.5	236.1	62.9	70.1	379.2	131.3	44.9	63.9
surplus/(deficit)	18.2	(15.4)	0.3	(3.4)	37.4	1.4	(2.5)	0.6

Source: Council long-term plans (LTPs), 2012–22<sup>37</sup>

Expenditure by councils in the Wellington and Wairarapa regions (excluding Greater Wellington) ranges from \$1,080 per person in Upper Hutt, to \$1,870 per person in Wellington. This is demonstrated in Figure 12 below.

**Figure 12: Spend per person**



Council balance sheets have significant infrastructure investments and generally low debt levels. However there are marked differences between the councils in terms of the levels of debt and investments that they hold. Table 10 below summarises the financial positions of the nine councils.

**Table 10: Summary of financial position by council**

2012–13 (budget) \$'m	Total	GWRC	KCDC	PCC	WCC	HCC	UHCC	Wairarapa
Total assets	13,159	914	902	1,211	6,842	1,352	637	1,302

<sup>37</sup> Although more recent figures are now available through adopted annual plans for 2013–14, data from the long-term plans have been used for consistency with other analysis that has been previously undertaken, including by PwC, Morrison Low and Martin Jenkins.

Total liabilities	<b>1,198</b>	232	161	75	512	102	32	83
Total equity	<b>11,961</b>	681	742	1,136	6,329	1,249	605	1,219

Source: Council LTPs, 2012–22

Further information on the current state of local government finances in the Wellington and Wairarapa regions is provided in Annex 7.

### 7.3 Rates implications of the reorganisations

This section assesses the possible impacts on average rates in the current territorial authority areas of the single and multiple unitary authority options being considered for the greater Wellington region. It must be noted that there is “devil in the detail” when it comes to evaluating the rates impacts of possible governance restructuring. The differing applications of targeted rates, differentials, annual charges, etc. across the greater region mean that any analysis is going to be at risk of becoming submerged in detail. However analysis at a high level is sufficient for understanding the broad impacts of the reorganisation options.

It is recommended that modelling at a more granular level is undertaken and assessed as part of any next step. It would be appropriate that this work is undertaken once a preferred option is chosen by the Local Government Commission.

We analyse the rates impacts in three steps:

1. merging two or more territorial authorities;
2. going unitary – adding in the relevant regional council costs and revenues;
3. identifying savings that can reasonably be expected from the resulting organisation(s).

#### 7.3.1 Impacts of amalgamation – merging territorial authorities

The first stage is meshing together the costs and income from the merging of two or more territorial authorities.

Table 11 below presents average rates per property for each territorial authority, as derived from the 2012/13 numbers in the long-term plans. It excludes regional council rates.

**Table 11: Effective average rates per property – current position**

Average rates	Total	KCDC	PCC	WCC	HCC	UHCC	Masterton	Carterton	South Wairarapa
Total rates (\$m)	<b>494.4</b>	47.2	46.5	239.4	87.6	30.2	23.6	8.5	11.3
Capital value (\$m)	<b>97,191</b>	10,171	7,755	46,375	16,902	6,450	4,449	1,897	3,192
Rates/\$1,000 CV	<b>\$5.09</b>	\$4.64	\$5.99	\$5.16	\$5.18	\$4.69	\$5.31	\$4.49	\$3.55
<b>Rateable properties</b>	<b>194,068</b>	24,327	17,811	74,526	38,404	16,115	12,200	4,686	5,999
Average property value	<b>\$500,809</b>	\$418,095	\$435,405	\$622,266	\$440,110	\$400,248	\$364,672	\$404,823	\$532,089
<b>Effective average rates</b>	<b>\$2,548</b>	<b>\$1,939</b>	<b>\$2,610</b>	<b>\$3,213</b>	<b>\$2,281</b>	<b>\$1,876</b>	<b>\$1,938</b>	<b>\$1,817</b>	<b>\$1,890</b>

Each council currently has differing revenue and cost structures. In addition, the rating base differs, and the capital values differ quite noticeably across the greater region. This is

particularly evident in Wellington City, which includes a significant commercial component, primarily in the CBD, and which therefore skews the average property value upwards.

It can be anticipated – and this point has been made by the Working Party – that following any reorganisation, the new council(s) will adopt a standardised rating methodology. In simple terms, it can be expected that capital value will be adopted as the rating base, and rates will be reset across the new organisation accordingly. As a result there will be “winners and losers” from any merger. Those councils with lower rates per dollar of capital value (“per \$CV”) at present will tend to see increases, while those councils with higher rates will tend to see decreases.

For the purposes of our analysis we assume, as was the case in Auckland, that rates are standardised across the region following amalgamation and that capital value is the rating base. The Commission or new councils could take a different approach. For this analysis we do not make any assumption about the pace of transition to the new rates levels: as has been the experience with Auckland, there will be ways to spread the immediate impact, for example by smoothing any transition over a number of years.

The following table shows the current average rates and (using the average property value) the new average rates should all councils be merged into a single authority (before allowing for any savings from the merger and excluding GWRC – these effects are considered in the next section).

These tables are also only based on a single point in time, and as such have not taken account of changes over the course of the long-term plans – such as population growth and planned increases in expenditure.

**Table 12: Effective average rates per property – single authority**

Average rates per household	Total	KCDC	PCC	WCC	HCC	UHCC	Masterton	Carterton	South Wairarapa
<b>Current</b>									
Average property value \$000	501	418	435	622	440	400	364	405	532
Rates/\$1,000 CV	\$5.09	\$4.64	\$5.99	\$5.16	\$5.18	\$4.69	\$5.31	\$4.49	\$3.55
<b>Effective average rates</b>	<b>\$2,548</b>	<b>\$1,939</b>	<b>\$2,610</b>	<b>\$3,213</b>	<b>\$2,281</b>	<b>\$1,876</b>	<b>\$1,938</b>	<b>\$1,817</b>	<b>\$1,890</b>
<b>Single authority</b>									
Rates/\$1,000 CV	\$5.09	\$5.09	\$5.09	\$5.09	\$5.09	\$5.09	\$5.09	\$5.09	\$5.09
<b>New effective average rates</b>	<b>\$2,548</b>	<b>\$2,127</b>	<b>\$2,215</b>	<b>\$3,166</b>	<b>\$2,239</b>	<b>\$2,036</b>	<b>\$1,855</b>	<b>\$2,059</b>	<b>\$2,707</b>
Change		10%	-15%	-1%	-2%	9%	-4%	13%	43%

The quantum that is transferred between council areas as a result of this first step in analysing the impacts of forming a single authority can be summarised as follows.

**Table 13: Quantum of rates change**

Total	KCDC	PCC	WCC	HCC	UHCC	Masterton	Carterton	South Wairarapa
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<b>Quantum of rates change</b>	<b>\$0</b>	\$4.6m	(\$7.0m)	(\$3.5m)	(\$1.6m)	\$2.6m	(\$1.0m)	\$1.1m	\$4.9m
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Amounts in brackets denote a decrease in average rates for that council area.

The above first step in the analysis indicates that merging the territorial authorities into a single authority without any other changes would be likely to result in:

- a net transfer of around \$5m out of the Wairarapa;
- South Wairarapa having the most adverse change, because property values there are relatively high and rates per \$CV are accordingly low;
- a reduction in average rates for Porirua; and
- a significant increase in average rates for Kapiti.

It is also important to consider how the potential options for reorganisation will affect each council in the future. In Table 14 below we estimate and compare the rates per property for the status quo and a single unitary authority in 2021/22 (considering the effects of merging the territorial authorities only: i.e., only step 1 above). We assume:

- the projected growth rates of households in the Wellington and Wairarapa regions are as estimated by Statistics New Zealand;
- total rates in the Wellington and Wairarapa regions are the same in 2021/22 under both options;
- under the status quo, rates increase as described in the councils' long-term plans;
- under a single authority, rates increase in each area by the regional average according to the long-term plans.

In Table 12 above, we see initially that Porirua, Wellington City, Hutt City and Masterton are all expected to be beneficiaries of a single authority. However, as seen in Table 14 below, after ten years Kapiti and Porirua are estimated to be the only beneficiaries of a single authority. A significant net transfer of \$9.4m is projected to come out of the Wairarapa in addition to a combined \$11.4m from Wellington City, Hutt City and Upper Hutt.

**Table 14: Estimated effective rates per property – single authority 2021/22**

2021/22	KCDC	WCC	PCC	HCC	UHCC	MDC	CDC	SWDC
Status quo	\$3,010	\$3,868	\$3,440	\$2,895	\$2,624	\$2,485	\$2,356	\$2,448
Single authority	\$2,648	\$3,956	\$2,870	\$2,967	\$2,695	\$2,497	\$2,726	\$3,643
<b>Percentage difference</b>	<b>-12%</b>	<b>2%</b>	<b>-17%</b>	<b>2%</b>	<b>3%</b>	<b>0%</b>	<b>16%</b>	<b>49%</b>
<b>Total difference (\$m)</b>	<b>(\$9.9m)</b>	<b>\$7.3m</b>	<b>(\$11.0m)</b>	<b>\$2.9m</b>	<b>\$1.2m</b>	<b>\$0.1m</b>	<b>\$1.8m</b>	<b>\$7.5m</b>

Table 15 below presents the estimated impact of establishing four merged councils (again prior to any regional council allocations). Kapiti remains as a stand-alone council, and thus there is no change there.

**Table 15: Effective average rates per property – multiple authorities**

Average rates per household	Total	KCDC	PCC	WCC	HCC	UHCC	Masterton	Carterton	South Wairarapa
Current									

Average property value	<b>500,809</b>	418,095	435,405	622,266	440,110	400,248	364,672	404,823	532,089
Rates/\$1,000 CV	<b>\$5.09</b>	\$4.64	\$5.99	\$5.16	\$5.18	\$4.69	\$5.31	\$4.49	\$3.55
<b>Effective average rates</b>	<b>\$2,548</b>	<b>\$1,939</b>	<b>\$2,610</b>	<b>\$3,213</b>	<b>\$2,281</b>	<b>\$1,876</b>	<b>\$1,938</b>	<b>\$1,817</b>	<b>\$1,890</b>
Multiple authorities		Kapiti	South-West		Hutt Valley		Wairarapa		
Rates/\$1,000 CV	<b>\$5.09</b>	\$4.64	\$5.28	\$5.28	\$5.05	\$5.05	\$4.56	\$4.56	\$4.56
<b>New effective average rates</b>	<b>\$2,548</b>	<b>\$1,939</b>	<b>\$2,300</b>	<b>\$3,287</b>	<b>\$2,221</b>	<b>\$2,019</b>	<b>\$1,663</b>	<b>\$1,846</b>	<b>\$2,427</b>
Change		0%	-12%	2%	-3%	8%	-14%	2%	28%

The transfers between each council area under this scenario are summarised in the table below.

**Table 16: Quantum of rates change**

	Total	KCDC	PCC	WCC	HCC	UHCC	Masterton	Carterton	South Wairarapa
<b>Quantum of rates change</b>	<b>\$0</b>	<b>\$0</b>	(\$5.5m)	\$5.5m	(\$2.3m)	\$2.3m	(\$3.3m)	\$0.1m	\$3.2m

Amounts in brackets denote a decrease in average rates for that council area.

The above analysis indicates that merging the territorial authorities into multiple unitary authorities (without any other changes) would be likely to result in:

- a higher average rate for the WCC/PCC group than under a single authority;
- a lower average rate for the Hutt group than under a single authority (but still a large increase for Upper Hutt and a corresponding decline for Hutt City); and
- a higher average rate for the Wairarapa than under a single authority, but still an increase for South Wairarapa.

As we did for the single authority, we estimate and compare the rates per property for the status quo and multiple unitary authorities in 2021/22. We assume under multiple authorities that the rates increase each area by the average across the unitary authority according to the long-term plans.

In Table 15 above, we see initially that Porirua, Hutt City and Masterton are all expected to be beneficiaries of the multiple authorities option. Table 17 below indicates that after ten years, Porirua and Masterton will remain the only beneficiaries. Kapiti is unaffected as it remains a stand-alone council and the transfers within the Hutt Valley authority are expected to have equalised after ten years. However, by 2021/22 the size of the transfer between Wellington City and Porirua is estimated to have increased to \$10.4m.

**Table 17: Estimated effective rates per property – multiple authorities 2021/22**

2021/22	KCDC	WCC	PCC	HCC	UHCC	MDC	CDC	SWDC
Status quo	\$3,010	\$3,868	\$3,440	\$2,895	\$2,624	\$2,485	\$2,356	\$2,448
Multiple authorities	\$3,010	\$3,993	\$2,897	\$2,893	\$2,627	\$2,150	\$2,348	\$3,137
<b>Percentage difference</b>	<b>0%</b>	<b>3%</b>	<b>-16%</b>	<b>0%</b>	<b>0%</b>	<b>-14%</b>	<b>0%</b>	<b>28%</b>
<b>Total difference (\$m)</b>	<b>\$0.0m</b>	<b>\$10.4m</b>	<b>(\$10.4m)</b>	<b>(\$0.1m)</b>	<b>\$0.1m</b>	<b>(\$4.3m)</b>	<b>\$0.0m</b>	<b>\$4.3m</b>



Amounts in brackets denote a decrease in average rates for that council area.

### 7.3.2 Impacts of amalgamation – moving to unitary status

The second key step in the analysis is to consider the effects of disestablishing the regional council and allocating the regional council’s revenue and expenditure to the new organisation(s).

While GWRC reports on rates revenue by territorial authority, there is not, and has not been in recent times, any robust cost allocation across the greater Wellington region’s territorial authorities. We therefore base our analysis on the recent work of PwC for GWRC<sup>38</sup>.

The modelling by PwC of the revenues and expenditures of GWRC by territorial authority was based on GWRC’s 2011/12 annual report. The results can be summarised as follows.

**Table 18: Allocation of GWRC revenue and expenditure by territorial authority area**

Summary income statement	Total	KCDC	PCC	WCC	HCC	UHCC	Wairarapa
Rates	63,416	4,235	5,307	29,451	14,081	4,860	5,482
Other	24,328	1,348	1,765	7,890	3,477	2,216	7,542
<b>Total revenue</b>	<b>87,654</b>	<b>5,583</b>	<b>7,072</b>	<b>37,341</b>	<b>17,558</b>	<b>7,076</b>	<b>13,024</b>
Operating expenditure	70,193	4,950	6,702	19,913	12,611	7,521	18,496
Financing costs	5,675	153	350	1,756	1,169	381	1,866
Depreciation	11,546	337	1,209	5,044	2,728	1,276	952
<b>Total expenditure</b>	<b>87,414</b>	<b>5,440</b>	<b>8,261</b>	<b>26,713</b>	<b>16,508</b>	<b>9,178</b>	<b>21,314</b>
<b>Operating surplus/(deficit)</b>	<b>240</b>	143	(1,189)	10,628	1,050	(2,102)	(8,290)

Amounts in brackets denote a decrease in average rates for that council area.

There has been some discussion about the observed surplus/deficit findings, in particular as a result of the Wairarapa proposal to establish a unitary authority. There has been some suggestion that, under a single unitary authority model, the current apportionment of rates could continue, and therefore rates adjustments would not be required.

While this would be a decision for the new organisation to make, it is likely to be a topic that provokes much debate. Now that the cross-subsidy between council areas has been highlighted, there is likely to be a requirement to review the basis for cost allocation and rates, regardless of the results of any reorganisation proposal. Much would depend on the view of the residents of Wellington City, given that they generate the largest surplus under the current funding model.

Our base working assumption is that the net operating surplus or deficit for each territorial authority area would need to be addressed through an adjustment to rates under either single or multiple unitary authorities but we also present the results of assuming no adjustment to the cross-subsidy occurs as a result of any reorganisations.

<sup>38</sup> PricewaterhouseCoopers (2013).

## ***Public transport***

Consistent with other analyses (e.g., by PwC and Martin Jenkins), public transport has been excluded from our analysis on the basis that it is difficult to identify an appropriate allocation methodology. For rail in particular, there is a high degree of fixed costs, and a greater region-wide network. It would be difficult to derive any cost allocation formula that is practical for the purposes of this analysis. Bus services are more specific to an area, but the costs have not been provided. PwC notes that a short cut approach could be to use the rates collected by territorial authority as a proxy, but do not recommend this. Having said that a cost allocation is not possible, PwC has noted an estimated cost for the Wairarapa, previously calculated by GWRC.

It is generally accepted that public transport would best be delivered by a single organisation, which would contain all costs, and would be tasked with determining whether any change is required to the current funding methodology. On that basis, it is pragmatic to assume no change at this time to the allocation of rates across the territorial authorities.

### ***7.3.3 Impacts of amalgamation – cost-effectiveness***

The third and final step in our financial analysis is to incorporate the impacts of the possible gains in cost-effectiveness from the amalgamations.

As noted in section 5.1 above, the Working Party identified potential cost savings in the range of 3% to 4% of operating expenditure annually. The extent to which these savings would be realised was considered to be dependent on the final structure – a single tier, single unitary authority being seen as having the greatest savings potential. The 2009 report of the Royal Commission on Auckland Governance assumed 2.5% to 3.5% cost savings from amalgamation of the eight councils in the Auckland region.

The savings estimated by the Working Party can be summarised as in the table below.

**Table 19: Savings estimated by the Working Party**

<b>Per annum savings</b>	<b>Low</b>	<b>High</b>
Single tier unitary	\$22m	\$29m
Two tier unitary	\$16m	\$22m
Multi-unitary	\$8m	\$10m

Source: derived from Working Party on Local Government Reform (2013).

It is reasonable to exclude depreciation and finance costs when estimating where the savings might be achieved. Based on 2012/13 long-term plan data, this leaves operating expenditure of between \$700m and \$740m, depending on whether the one-off transport grants to Greater Wellington Regional Council are included. It would be appropriate to exclude the one-off grants, and thus focus on operating expenditure of approximately \$700m. Applying the 3% to 4% cost savings estimated by the Working Party results in between \$21m and \$28m per annum in cost savings. We adopt their estimate as our high-level range.

The multi-unitary model – with four unitary councils – has been estimated by Wellington City to generate around 35% of the potential savings from a single unitary model, or between \$8m and \$10m<sup>39</sup>. This is around 1% of expenditure, and seems conservative, but much depends on the underlying assumptions. If Kapiti is to remain stand-alone, no savings will accrue there.

In their report to the Wairarapa councils, Martin Jenkins and TDB assumed that a Wairarapa unitary council could achieve 3% cost savings on local expenditure. They have conservatively assumed that there will be no savings on the regional functions. This accepts that there may be areas of diseconomy in some areas, and in other areas there may be savings.

As a high-level starting point, this seems the most appropriate approach. As above, excluding depreciation and finance costs, the operating expenditure for the greater region (excluding all GWRC and Kapiti expenditure) is approximately \$483m. Applying 3% cost savings will result in savings of around \$14.5m per annum.

For the purpose of evaluating the impact by territorial authority area, the potential savings have been pro-rated based on capital value. This is based on the principle that any savings would ultimately reduce the general rate (in the absence of specific areas of saving).

Tables 20 and 21 below provide the resulting estimates of the savings by territorial authority area under a single unitary authority and under multiple unitary authorities.

**Table 20: Single-unitary savings**

Single unitary	Total	KCDC	PCC	WCC	HCC	UHCC	Masterton	Carterton	South Wairarapa
Capital value (\$m)	<b>97,191</b>	10,171	7,755	46,375	16,902	6,450	4,449	1,897	3,192
Saving (p.a.)	<b>\$21.0m</b>	\$2.2m	\$1.7m	\$10.0m	\$3.6m	\$1.4m	\$1.0m	\$0.4m	\$0.7m

**Table 21: Multi-unitary savings**

Multi-unitary	Total	KCDC	PCC	WCC	HCC	UHCC	Masterton	Carterton	South Wairarapa
Capital value (\$m)	<b>97,191</b>	10,171	7,755	46,375	16,902	6,450	4,449	1,897	3,192
Saving (p.a.)	<b>\$14.5m</b>	\$0m	\$1.3m	\$7.7m	\$2.8m	\$1.1m	\$0.7m	\$0.3m	\$0.5m

### 7.3.4 The overall rating impacts

This section brings together the three steps in the sections above to present the overall estimated impacts on average rates levels. Tables 22 to 24 below summarise the overall estimated indicative changes in average rates by territorial authority area, when compared to the status quo, arising from the two options – a single unitary authority and a multi-authority structure.

<sup>39</sup> Working Party on Local Government Reform (2013).

While our analysis is high level and broadly applied, it provides an indication of the type and scale of these impacts.

### 7.3.4.1 Single authority

Table 22 below presents the estimated overall impact on average ratepayers by territorial authority of moving to a single authority.

On average the Wellington, Hutt City and Porirua areas would be likely to benefit financially from a single unitary authority model while the Wairarapa would have the most significant adverse impact (assuming the current GWRC cross-subsidy is withdrawn). Upper Hutt and Kapiti would also be likely to see adverse financial consequences overall.

**Table 22: Summary of rate impacts – single unitary authority**

Summary of impacts	Total	KCDC	PCC	WCC	HCC	UHCC	Wairarapa
TA mergers	\$0.0m	\$4.6m	(\$7.0m)	(\$3.5m)	(\$1.6m)	\$2.6m	\$5.0m
Absorbing GWRC	\$0.0m	(\$0.1m)	\$1.2m	(\$10.6m)	(\$1.1m)	\$2.1m	\$8.3m
Savings anticipated	(\$21.0m)	(\$2.2m)	(\$1.7m)	(\$10.0m)	(\$3.6m)	(\$1.4m)	(\$2.1m)
<b>Net change</b>	<b>(\$21.0m)</b>	<b>\$2.3m</b>	<b>(\$7.5m)</b>	<b>(\$24.1m)</b>	<b>(\$6.3m)</b>	<b>\$3.3m</b>	<b>\$11.2m</b>

*Amounts in brackets denote a decrease in average rates for that council area.*

We also consider what level of savings or efficiency gains would be required as a result of the amalgamations for the different council areas that are adversely affected to be no worse off. The approximate levels of savings required under the amalgamation for all council areas to be no worse off are:

- Kapiti 6%
- Upper Hutt 10%
- Wairarapa 19%

In Table 22 we assume that the creation of a single authority will result in the alignment of spending on current GWRC functions with rates payments for different areas. This alignment may also occur even if there are no council amalgamations. Alternatively, a single authority may choose to continue the current cross-subsidies. In order to fairly consider the potential impacts on the current council areas, we must consider the possibility that in practice a single authority is not the trigger for removing the current GWRC cross-subsidies. Table 23 below presents the resulting estimates of the rate changes.

**Table 23: Summary of rate impacts – single authority without GWRC adjustments**

Summary of impacts	Total	KCDC	PCC	WCC	HCC	UHCC	Wairarapa
TA mergers	\$0.0m	\$4.6m	(\$7.0m)	(\$3.5m)	(\$1.6m)	\$2.6m	\$5.0m
Savings anticipated	(\$21.0m)	(\$2.2m)	(\$1.7m)	(\$10.0m)	(\$3.6m)	(\$1.4m)	(\$2.1m)
<b>Net change</b>	<b>(\$21.0m)</b>	<b>\$2.4m</b>	<b>(\$8.7 m)</b>	<b>(\$13.5m)</b>	<b>(\$5.2m)</b>	<b>\$1.2m</b>	<b>\$2.9m</b>

*Amounts in brackets denote a decrease in average rates for that council area.*

In comparing the net change in Tables 22 and 23 we see the direction of the impact remains unchanged for each council area. The most noticeable differences are for ratepayers in Wellington City and Wairarapa. Wellington City ratepayers save on average \$10.6m less if the cross-subsidies are not removed, while ratepayers in the Wairarapa are expected to lose \$8.3m less overall. The magnitude of the impact on the four other council areas is no greater than \$2.1m and the direction of the overall impact on each remains the same.

### 7.3.4.2 Multiple authorities

Table 24 below presents the estimated overall impact on average ratepayers by territorial authority of moving to four unitary authorities.

On average the Wellington, Hutt City and Porirua areas would be likely to benefit financially from four unitary authorities. The benefits would be materially less for Wellington, and quite noticeably less for Porirua, than under the single unitary authority. The impact of having its own unitary authority for the Wairarapa would be significant, but 40% lower than under the single unitary model.

**Table 24: Summary of rate impacts – multiple unitary authorities**

Summary of impacts	Total	KCDC	PCC	WCC	HCC	UHCC	Wairarapa
TA mergers	\$0.0m	\$0.0m	(\$5.5m)	\$5.5m	(\$2.3m)	\$2.3m	\$0.0m
Absorbing GWRC	\$0.0m	(\$0.1m)	\$1.2m	(\$10.6m)	(\$1.1m)	\$2.1m	\$8.3m
Savings anticipated	(\$14.5m)	\$0.0m	(\$1.3m)	(\$7.7m)	(\$2.8m)	(\$1.1m)	(\$1.5m)
<b>Net change by current TA</b>	<b>(\$14.5m)</b>	<b>(\$0.1m)</b>	<b>(\$5.6m)</b>	<b>(\$12.8m)</b>	<b>(\$6.2m)</b>	<b>\$3.3m</b>	<b>\$6.8m</b>
<b>By new unitary authority</b>		\$0.0m	(\$18.4m)		(\$2.9m)		\$6.8m

Amounts in brackets denote a decrease in average rates for that council area.

The approximate level of savings (efficiency gains) required under the amalgamation for all council areas to be no worse off are:

- Upper Hutt 11%
- Wairarapa 14%

Table 24 above assumes that the creation of the four unitary authorities results in the alignment of spending on current GWRC functions with rates payments for the different areas. Again, we must consider the possibility that the multiple unitary authorities option is not in itself the trigger for the removal of the current GWRC cross-subsidies. We can compare Table 25 below to Table 24 to assess the importance of this assumption.

**Table 25: Summary of rate impacts – multiple authorities without GWRC adjustments**

Summary of impacts	Total	KCDC	PCC	WCC	HCC	UHCC	Wairarapa
TA mergers	\$0.0m	\$0.0m	(\$5.5m)	\$5.5m	(\$2.3m)	\$2.3m	\$0.0m
Savings anticipated	(\$14.5m)	\$0.0m	(\$1.3m)	(\$7.7m)	(\$2.8m)	(\$1.1m)	(\$1.5m)
<b>Net change by current TA</b>	<b>(\$14.5m)</b>	<b>\$0.0m</b>	<b>(\$6.8m)</b>	<b>(\$2.2m)</b>	<b>(\$5.1m)</b>	<b>\$1.2m</b>	<b>(\$1.5m)</b>
<b>By new unitary authority</b>		\$0.0m	(\$9.0m)		(\$3.9m)		(\$1.5m)

Amounts in brackets denote a decrease in average rates for that council area.

The two significant differences we notice moving from Table 24 to Table 25 is the negative impact on Wellington City and the positive impact on the Wairarapa. Wellington City’s savings become immaterial after the loss of the \$10.6m savings resulting from the unitary authorities absorbing the GWRC functions. On the other hand, a Wairarapa unitary authority moves from an estimated \$6.8m increase in average rates to a small saving of \$1.5m.

In Table 24, one of the three proposed amalgamations is predicted to suffer an adverse impact under the multiple unitary authorities option: the Wairarapa. Upper Hutt City Council and a Wairarapa authority are both adversely impacted by \$3.3m and \$6.8m dollars respectively. In Table 25, although Wellington City and the Wellington unitary authority save significantly less, the adverse impact on Upper Hutt reduces to only \$1.2m and all three unitary authorities are positively impacted.

If the outcomes of a multiple authorities option were to resemble those estimated in Table 25 it may garner support from many ratepayers.

## 7.4 Debt impacts of the reorganisations

This section examines at a high level the indicative impact of the different governance options on council debt. Our analysis focuses on gross debt as this section is mostly about the cost of debt servicing. We assume that the debt of the antecedent councils is consolidated into the new organisations. The Commission could take a different approach: with debt in particular it could choose to “ring-fence” the debt burdens to the current territorial authorities. The analysis below should be viewed as a possible scenario if debt burdens are allocated as assumed.

### 7.4.1 Debt per ratepayer as at 2012/13

Total budgeted debt for all councils for the 2012/13 year, per the long-term plans, is \$884m. Table 26 details the debt attributable to an individual ratepayer, broken down by council area.

**Table 26: Gross debt per ratepayer**

2012–13 (LTP)	Total	GWRC	KCDC	PCC	WCC	HCC	UHCC	Wairarapa
Total debt (\$m)	<b>884.1</b>	182.2	135.2	53.1	373.7	43.4	25.0	71.5
Number of residents	<b>492,526</b>	492,526	51,160	52,940	202,760	103,740	41,580	40,346
Gross debt per resident	<b>\$1,795</b>	\$370	\$2,642	\$1,002	\$1,843	\$418	\$601	\$1,773
<b>Number of ratepayers</b>	<b>194,068</b>	194,068	24,327	17,811	74,526	38,404	16,115	22,885
<b>Gross debt per ratepayer</b>	<b>\$4,555</b>	<b>\$939</b>	<b>\$5,557</b>	<b>\$2,979</b>	<b>\$5,014</b>	<b>\$1,130</b>	<b>\$1,550</b>	<b>\$3,126</b>

Table 26 shows that Kapiti and Wellington have the highest gross debt levels, measured by resident or by ratepayer<sup>40</sup>. The two Hutt councils have markedly lower gross debt levels. For some years now the Hutt councils have focused on keeping expenditure and debt levels down. Amalgamations in the Wellington and Wairarapa regions therefore have the potential

<sup>40</sup> Measured on a net debt basis (i.e., after deducting financial assets), Wellington’s level is considerably lower.

to cause fairly large redistributions in debt and debt servicing fees depending on how the new entities would manage the resulting debt burdens.

### ***Debt servicing***

Debt servicing as a percentage of total expenditure is a key measure of financial sustainability. If debt-servicing costs become too high this can generate a public reaction and force a change in financial strategy. Often debt-servicing costs increase beyond tolerable levels because the population growth that was expected has not materialised, and as a result current ratepayers are required to assume the financing and repayment burden. This has been seen recently in Tauranga, Hamilton and Taupo, for example.

In the Wellington and Wairarapa regions, the ratio of debt servicing to operating expenditure varies considerably. Table 27 shows the current finance costs for the 2012/13 financial year according to the various councils' long-term plans.

**Table 27: Debt servicing as % of operating expenditure, 2012/13**

<b>2012–13 (LTP) \$m</b>	<b>Total</b>	<b>GWRC</b>	<b>KCDC</b>	<b>PCC</b>	<b>WCC</b>	<b>HCC</b>	<b>UHCC</b>	<b>Wairarapa</b>
Finance cost	<b>52.2</b>	8.2	8.5	3.3	22.6	4.0	1.5	4.2
Total operating expenditure	<b>945.3</b>	192.9	62.9	70.1	379.2	131.3	44.9	63.9
Finance costs as % of total expenditure	<b>5.5%</b>	4.2%	13.5%	5.1%	6.0%	3.0%	3.2%	6.5%

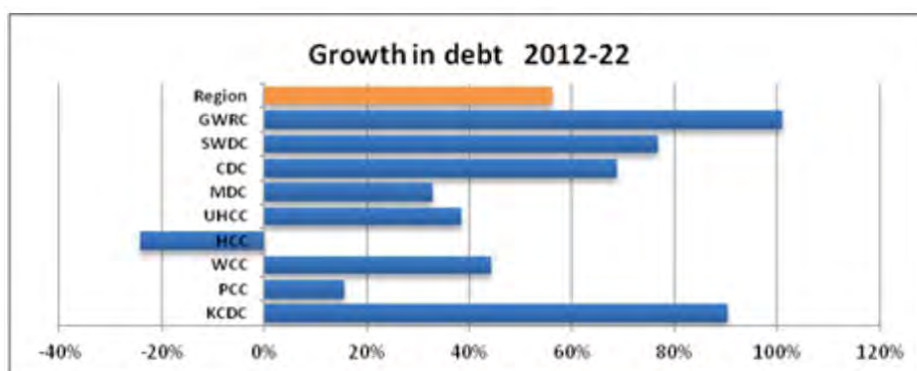
Within the greater region, only Kapiti stands out as having a high level of debt-servicing costs. The remaining councils have manageable debt-servicing costs. However, in the case of amalgamation, there will still be clear winners and losers in the greater region if total debt were to be apportioned across the Wellington and Wairarapa regions. Hutt City and Upper Hutt with noticeably lower debt servicing costs of 3% and 3.2% are likely to be the biggest losers under a single authority in terms of gross debt and debt servicing.

### ***Growth in debt***

Over the course of the long-term plans, most councils are forecasting significant increases in debt compared with their current debt levels. Hutt City stands out as the one council with plans to reduce its debt. Wellington City has a forecast increase that is lower than the average for the greater region.



Figure 13: Growth in debt from 2012 to 2022



Forecast 2021/22 debt-servicing costs as a percentage of total expenditure are generally not markedly different from current levels, with the exception of GWRC, which is projecting a significant increase largely as a result of the investment in rail. Wellington City and Kapiti, the two councils with the highest debt per ratepayer, are planning to take on more debt, although their debt servicing to expenditure rates do not increase dramatically.

Table 28: Debt servicing as % of operating expenditure, 2021/22

2021-22 (LTP) \$m	Total	GWRC	KCDC	PCC	WCC	HCC	UHCC	Wairarapa
Finance cost	88.5	23.9	13.5	4.5	34.7	3.8	3.0	5.0
Total operating expenditure	1,288.1	296.1	93.5	95.1	496.1	163.9	61.8	81.7
Finance costs as % of total expenditure	6.9%	8.1%	14.4%	4.7%	7.0%	2.3%	4.8%	6.2%

### *The debt impacts of restructuring*

Concern about taking on Wellington City and Kapiti councils' debt has been expressed by many other councils in the greater region. As Table 29 below shows, Wellington and Kapiti's debt impacts on most other councils under a single unitary authority model. A multi-authority model would result in a better debt-sharing outcome for the Hutt Valley and Wairarapa councils (compared to the single unitary authority).

Table 29: Debt servicing changes under the two options

Debt servicing per ratepayer 2012/13	KCDC	PCC	WCC	HCC	UHCC	MDC	CDC	SWDC
Current average	\$390	\$241	\$346	\$146	\$133	\$291	\$153	\$143
Single unitary authority	<b>\$270</b>							
Change per ratepayer	(\$120)	\$29	(\$76)	\$124	\$138	(\$20)	\$117	\$127
Quantum of debt-servicing change	(\$2.9m)	\$0.5m	(\$5.6m)	\$4.8m	\$2.2m	(\$0.2m)	\$0.5m	\$0.8m
	<b>Kapiti</b>	<b>South-West</b>		<b>Hutt Valley</b>		<b>Wairarapa</b>		
Multiple authorities	<b>\$390</b>	<b>\$326</b>		<b>\$142</b>		<b>\$224</b>		
Change per ratepayer	\$0	\$84	(\$20)	(\$4)	\$10	(\$67)	\$71	\$80
Quantum of debt-servicing change	\$0.0m	\$1.5m	(\$1.5m)	(\$0.2m)	\$0.2m	(\$0.8m)	\$0.3m	\$0.5m

Amounts in brackets denote a decrease for that council area.

*Note that the debt servicing figures include GWRC costs, which have been allocated across the other councils on a simple per ratepayer basis.*

Under a single authority the Kapiti, Wellington City and Masterton areas are the beneficiaries of reduced debt-servicing costs. On the other hand, the average debt levels would increase for Porirua, Hutt City, Upper Hutt, Carterton and South Wairarapa. Once again it is important to stress that these are simple averages, and do not attempt to provide definitive numbers. Their purpose is to demonstrate the broad effects from reorganisation. However, these indicative numbers suggest the changes could be material, with Hutt City, Upper Hutt, Carterton and South Wairarapa all seeing debt-servicing costs increase by at least 75%.

Under the multiple authorities option, the redistribution effects are far less pronounced as Kapiti is modelled as an isolated entity and only Porirua takes on Wellington City's debt. Porirua therefore faces a greater increase in debt under this option than a single authority, whereas the impact on Hutt City, Upper Hutt, Carterton and South Wairarapa is significantly reduced. In fact, Hutt City experiences a marginal reduction in its debt-servicing costs, along with Wellington City and Masterton.

As with all of this analysis, it is indicative. There are many possible ways that debt could be managed – for example, it could be ring-fenced against specific investments or locations. These would be decisions for the new organisation(s) to make.

#### **7.4.2 The overall debt impacts**

From the evidence presented above, debt levels and debt servicing costs are not at a level that is currently threatening the long-term viability of any council. However, the potential redistribution impacts may be significant enough to induce considerable opposition from adversely affected councils.

Kapiti is the only council with debt levels that could currently be considered high for the sector and, with a cumulative 90% increase over the next ten years, Kapiti is projecting significant growth in debt. Kapiti therefore stands to benefit most from a debt reallocation perspective from reorganisation into a single authority, along with Wellington City.

There are quite marked differences across the Wellington and Wairarapa regions in the approach to expenditure and debt. Some councils are investing quite significantly, while others are consciously holding down debt levels. Hutt City is the only council planning to reduce debt over the next ten years, and it is understandable that it may not wish to take on responsibility for the debt of other councils through any reorganisation.

There are significant impacts from the spreading of the debt-servicing burden, and these impacts are likely to make debt a point of contention. One of the key considerations is the “what’s in it for me” question, whereby each council considers the impact on themselves, and thus on the ratepayers of that area, as being more important than the overall impact. From a debt servicing perspective, a single unitary authority would be less attractive than the multi-

authority model for the Hutt Valley and Wairarapa councils, but more attractive for Kapiti, Porirua and Wellington.

## **8. Overall assessment of the options**

This report involves a programme of investigations and analysis intending to deliver an independent, rigorous and evidence-based assessment of the available options for restructuring governance arrangements in the Wellington and Wairarapa regions.

The economic analysis of the New Zealand evidence provided in section 6 of this report indicates there are no strong cost-effectiveness reasons for amalgamating council functions once a population-served threshold of around 50,000 is reached. Over half of councils' expenditure is on services that are predominantly labour-intensive and not amenable to obtaining efficiencies simply by getting bigger. However, for the rest of council expenditure, which is on services that either are capital-intensive or require specialist technical skills in their delivery, there is a strong case for region-wide amalgamation on a functional basis. We therefore suggest amalgamating key functions across the Wellington and/or Wairarapa regions rather than the councils themselves.

We discuss below firstly the two key capital-intensive functions of land-transport and regional water services before turning to our overall assessment of the three options for governing the other functions of local government in the Wellington and Wairarapa regions.

### **8.1 Regional Land Transport Authority**

Land transport is the single biggest local government activity requiring network-wide coordination for efficient delivery. Land transport is especially complex because of its linkages, the differing modes of transport (with varying mixes of public and private (self) provision), the impact on other spatial planning, long time frames, and the frameworks in which it is planned and funded. It is also the function of local and regional government that is most capital-intensive and technically complex. Moreover, responsibility for the delivery, funding and regulation of the region-wide transport network is shared between local, regional and national government. Special attention is therefore warranted to the organisation of land-transport planning and delivery, with land-transport planning a critical element of the overall spatial-planning process.

Our view is supported by the report of the Local Government Infrastructure Efficiency Expert Advisory Group, which noted the importance of a coordinated regional approach to infrastructure delivery:

*“Greater use of infrastructure delivery at a regional scale will facilitate substantial benefits where the assets being managed are also at that scale. For*

*significant expenditure, scale can provide the specialist skills needed to manage scope, procurement, timing, financing and operational issues.”<sup>41</sup>*

Currently, aspects of land-transport planning and delivery within the Wellington and Wairarapa regions are split across the nine councils. In the Auckland context, a solution to the planning and delivery of transport services that has been in effect since 1 November 2010 has been a regional transport authority (RTA) called Auckland Transport. Auckland Transport is a CCO of Auckland Council that combines the transport functions of the former local and regional councils and the Auckland Regional Transport Authority. It carries out all transport functions and operations for Auckland and is responsible for planning, maintaining and delivering all of the region’s transport services (excluding state highways and rail track) from roads and footpaths, to cycling, parking and public transport (train, bus and ferry services).

A RTA for Wellington could:

- combine the transport and public transport functions currently performed across the five territorial authorities and the regional council under a single CCO;
- undertake the statutory roles relating to the planning and delivery of land-transport services;
- be consistent with the Government Policy Statement on Land Transport Funding and the Public Transport Operating Model; and
- provide a focused channel for direct communications between the Wellington and Wairarapa regions and the national government on the single area in which central government’s funding and regulatory policies most directly affect the delivery of local public services and infrastructure.

The RTA would be responsible for planning and delivering local roading and public transport, including preparation of the Wellington Regional Land Transport Programme. Importantly it would provide a “one-stop-shop” for coordination with the NZTA and Police. The greater region’s councils would continue to have influence over the RTA’s planning and decision-making through appointments to the board and the formal consultation on the Regional Land Transport Programme. It is envisioned that the existing committee of mayors, NZTA, Police and relevant national government agencies would continue with the RTA also represented. The local councils would retain the ability to make decisions about local “place-shaping” transport improvements such as footpaths, cycle-ways, traffic calming, lighting, etc.

Forming a RTA from the relevant divisions of the regional and local councils would involve some transition costs but the costs would be less than combining all nine councils across all functions. NZTA supports a coordinated, regional approach to land transport planning as detailed in a letter from NZTA included in Annex 5 of this report.

We suggest that the land transport concerns of the entire Wellington and Wairarapa regions should fall under the jurisdiction of a single land transport CCO. With a regional transport

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<sup>41</sup> Local Government Infrastructure Efficiency Expert Advisory Group (2013).

authority as a key part of the greater Wellington regional governance arrangements, the coordination, expertise concentration and “voice” benefits envisioned by region-wide amalgamation proponents would seem to be mostly realised but without detracting from local-level democratic decision-making. Thus a RTA would largely obviate the need for further amalgamation in the Wellington region.

## 8.2 Regional water services

Changes could also be usefully made to the way the governance arrangements for the delivery of water services (potable supplies, waste and storm water removal and treatment). Hutt City, Upper Hutt City and Wellington City have combined elements of the delivery of water services by contracting Capacity to manage and operate the water networks that the respective councils own. Capacity is a joint venture between its three customers established in 2004. Upper Hutt is not currently a shareholder in Capacity and it pays a fee for service as a customer. GWRC and Porirua City both manage their water networks in-house and independently of the Capacity joint venture.

In its recent Application for Local Government Reorganisation, GWRC noted the importance of regional provision for large, capital-intensive infrastructure:

*“Size and scale are critical, particularly for the planning and delivery of capital intensive infrastructure.”<sup>42</sup>*

The GWRC’s application goes on to quote the findings from a recent PwC and GHD report – Implementing the National Infrastructure Plan in the Water Industry:

*“The study found a clear correlation between an operator’s scale and its results. Larger operators scored better than smaller operators. Increased size enabled improved strategic focus, specialisation of technical staff, purchasing power and economies of scale.”<sup>43</sup>*

PwC in February 2012 proposed a model for Wellington region-wide integration of water services under which GWRC and Porirua City would join the Capacity joint venture to complete regional water services delivery<sup>44</sup>. The report noted that since Capacity’s formation there had been financial and non-financial benefits to the participating councils, with network operating cost savings between \$1m and \$2m annually. In addition, PwC considered that capital expenditure had been deferred as a result of the joint venture being put in place by the three councils.

PwC in its report proposed a model for Wellington region-wide water services delivery. The model was a “concession” arrangement whereby the councils would each own their elements of the water services network assets and contract with Capacity as an integrated service

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<sup>42</sup> Greater Wellington Regional Council (2013).

<sup>43</sup> PricewaterhouseCoopers and GHD (2012).

<sup>44</sup> PricewaterhouseCoopers (2012).

provider. The contracting could be performance based for “outcomes” (or on a fee-for-service or cost recovery as at present). The annual financial benefits from regional integration of water services were estimated by PwC to be \$1.3m within the water business and \$3.8m within the councils.

We consider that a Wairarapa unitary authority under an enhanced status quo option would be best served by establishing a separate Wairarapa water services CCO. However, under a multiple unitary authorities option Wairarapa water services could be amalgamated with the Wellington region under a single water services CCO. However, as neither the Wairarapa nor Kapiti water systems are physically connected to the Wellington/Hutt water system, the benefits of a greater Wellington-wide amalgamation of water services are likely to be limited.

The PwC concession proposal provides a workable model for delivery of water services across the Wellington region (excluding Kapiti) under all of the options considered for the future governance of the Wellington region. However, under the option for four unitary authorities, consideration would need to be given to the ownership of the bulk water supply assets currently owned by GWRC. Various mechanisms are either to deal with the bulk water assets alone or to amalgamate all of the region’s water services assets into a single jointly owned council-controlled entity.

### **8.3 Overall assessment of the three governance options**

Our overall assessment of the three local governance options considered in this report – the enhanced status quo, multiple unitary authorities and a single unitary authority – for the Wellington and Wairarapa regions is based on the following criteria:

- democratic local decision-making;
- effective public representation;
- cost-effectiveness (i.e., delivering a better service or getting a better result for the same amount of expense);
- efficiency and productivity for households and businesses that use local public services; and
- the transition costs and complexity surrounding any restructuring.

The following table summarises our overall assessment of the three options in terms of the above criteria.

**Table 30: Criteria used to assess the options**

	Criteria used to assess the options					
	Democratic local decision making		Cost effective	Efficiency & productivity	Transition	
	Democratic process	Effective public representation	Services at least cost, or more services for the same cost	For households & businesses using council services	Cost	Complexity
<b>Option 1: An enhanced status quo</b>	No material change except in Wairarapa	Slight improvement for Wairarapa	Improvement for Wairarapa	Improvement for Wairarapa	Slight	Small
<b>Option 2: Three or four unitary authorities</b>	Some weakening. Broad communities of interest preserved. Decision-making by directly elected councils		Overheads associated with one tier of local government removed	Some improvement	Medium	Medium (mostly from re-organising regional council functions, transport and water services)
	Unitary authorities' elected councillors are directly accountable for all services		Some predicted economies of scale/scope from combining UH and Hutt			
<b>Option 3: Single unitary authority</b>	Weakened	Difficult for non-executive board to effectively influence decision-making process	Little evidence for significant broad-based efficiencies available that can not be otherwise obtained	Possible eventually but questions remain over how long before they will be achieved	Large	Large

Democratic local decision-making is not changed materially for the greater Wellington region by Option 1. Arguably Option 3 detracts materially from the exercise of local democracy in making choices about the level and quality of local public services. Community boards without independent funding and decision-making powers are not a substitute for locally elected councils with powers to raise rates and make decisions across a wide-range of functions in the local area. Option 2 is a middle ground between the other two options in terms of democratic local decision-making. Option 1 is the preferred option on this criterion.

Cost-effectiveness, as is analysed in sections 4 to 6 of this report, is unlikely to improve significantly as a result of combining the current nine entities into a single unitary authority. Even though Option 3 would remove a current layer of overhead relating to one tier of local/regional government, the balance of evidence does not support an authority of the resulting size being any more or less cost-effective than the alternative of four unitary authorities. Any benefits of greater size are likely to be absorbed in the greater complexity and diseconomies that would attract to such an entity. On this criterion, Option 3 ranks last while Options 2 and 1 are preferred.

Whether or not efficiency and productivity for households and businesses that use local public services would improve with fewer councils involved in the spatial planning and regulatory process is open for debate. Arguably it would take several evolutions of the planning process to achieve simplification of amalgamated plans. With regard to local authorities' regulatory services, the Productivity Commission concluded that best practice is a function of leadership and management practices in the local authority, not of the size of the authority. Overall, therefore, in our view none of the options is clearly superior on this criterion.



All the options incur some transition costs and complexity. These rise with the number of merging entities and the amount of post-merger rationalisation required. Transition costs and complexity are highest for Option 3 and lowest for Option 1.

Regardless of which option is adopted, we favour the network-wide integration of land transport and water services for the reasons discussed in section 8.1 and 8.2 above. These capital-intensive networks are the areas where most gains can be achieved from integration. If these two services are integrated, there is no need to risk undermining local democracy by integrating the other inherently local functions of the territorial authorities, especially given there is no compelling evidence that cost-efficiencies would be achieved.

Other than the network-based integration of land transport and water services, our analysis favours Option 1, the enhanced status quo. The reasons are that Option 1:

- captures the low-hanging fruit by merging the three small Wairarapa councils;
- best preserves local democracy across the rest of the greater region and the rest of the functions by retaining decisions on funding and control of local services at the local level;
- allows for different preferences for rates, borrowing, investment and service levels across the Wellington and Wairarapa regions to be maintained and adjusted across time by each local council;
- contracts, shared services and CCOs still provide the current smaller councils with the option of enjoying cost-effectiveness gains for functions best suited to large scale provision;
- multiple local councils will encourage competition and innovation as councils can learn from neighbouring authorities and experiment with a variety of different policies across the Wellington and Wairarapa regions;
- avoids the bureaucracy that is likely to arise with large council structures;
- avoids the redistribution of debt and changes in rates that would result from amalgamations; and
- avoids the costs and complexity of change that would be incurred with Options 2 and 3.

We note that Option 1 is the preferred option of the local communities according to six of the eight councils' surveys of public opinion undertaken in the Wellington and Wairarapa regions (refer to Annex 6). We suggest that the amalgamation of key services is of greater benefit than amalgamating the councils themselves.

If, however, further amalgamations are required, we prefer Option 2, the four unitary authorities, over a single unitary authority. The reasons are Option 2:

- allows amalgamation to occur between the most similar communities and the resulting councils would still be relatively close to the affected stakeholders;
- is likely to result in less extra bureaucracy than Option 3;
- involves less redistribution of debt and is likely to lead to smaller changes in average rates than a single unitary authority;
- is likely to have lower adjustment costs than Option 3; and
- it leaves open the option of moving to Option 3 at a later date should there be sufficient evidence to warrant such a move.

Option 2 would, however, require coordination across the greater region of some of the functions that are currently undertaken by the GWRC. This could be achieved through an enhanced mayoral forum and through contracting and sharing of services.

Our least-favoured option is Option 3, the single unitary authority.

Option 3 has the following advantages:

- it facilitates better coordinated spatial and environmental planning;
- it may result in less duplication and fewer conflicting policies across the Wellington and Wairarapa regions;
- resource consents, planning and decision-making may become simpler and faster under a single governing body;
- efficiency gains are possible for some capital-intensive local government functions.

However, these potential advantages can largely be achieved through other means (greater use of shared services and other forms of co-operation where the benefits of such co-operation outweigh the costs) without incurring the costs and other disadvantages of a single unitary authority.

A single authority is likely to lead to a diminution of local democracy: the larger a council becomes, the more distanced it is likely to be from the individuals and communities of interest that it represents. This distance brings with it both a loss of accountability to individual ratepayers and a loss of approachability. Local boards can mitigate these effects to an extent. However, as noted above, if the local boards do not have rating powers or independent decision-making powers, their influence is limited.

Likewise, having a number of councils within the Wellington and Wairarapa regions allows for different preferences in different communities to be enacted by the councils that represent them. A single authority reduces the scope for differences in local preferences.

A single authority brings with it the potential for diseconomies of scale. Although we have identified some potential for cost savings, there is also the potential for cost increases as councils get larger as noted in sections 4 to 6 of this report. Such diseconomies of scale and

increased bureaucracy are especially likely to affect the labour-intensive services of the local councils.

Also importantly, the transition costs associated with the creation of a single authority are likely to be substantial. Establishing a single unitary authority in the Wellington and potentially Wairarapa regions would be costly and disruptive. International experience suggests these transition costs are often underestimated. We have not seen any compelling evidence that incurring these costs is warranted.

Finally we note that some proponents of a single unitary authority for the Wellington and Wairarapa regions argue that having a “single voice” for the area would be beneficial, in particular when it comes to dealing with central government. This single voice is useful to the extent that the regions need a coordinated communication with central government. In particular, in the case of land transport, where the region receives central government funding, a single voice would be useful. This is an argument for having a regional land transport authority as noted above. However, it is not obvious to us that the area needs a “single voice” when it comes to matters of local concern like the funding and services of libraries, swimming pools or other recreational services where the interface with central government is minimal. To the extent that a “single voice” is needed in these areas, it could be achieved through an enhanced mayoral forum. Finally we note that having a single voice is only robust if the preferences of the underlying community are aligned. If there are a variety of opinions, preferences and communities of interest within the region, a single voice may not be the most beneficial means through which to meet the needs of the community.

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## Annex 1: List of meetings held

This annex details the key meetings we undertook in preparing this report.

- Michael Bassett;
- Guy Beatson, Deputy Secretary, Ministry for the Environment;
- Dave Benham, CEO, Greater Wellington Regional Council;
- Jenny Chetwynd, Regional Director Central, NZTA;
- Jane Davis, Strategy and Community Engagement Group GM, Greater Wellington Regional Council;
- Pat Dougherty, CEO, Kapiti Coast District Council;
- Mike Hensen, NZIER;
- Amy Kearse, Principal Planning Adviser, NZTA;
- Kevin Lavery, CEO, Wellington City Council;
- Local Government Commission;
- Sir Geoffrey Palmer;
- John Shewan;
- Gary Simpson, CEO, Porirua City Council;
- Tony Stallinger, CEO, Hutt City Council; and
- Chris Upton, CEO Upper Hutt City Council.



## Annex 2: Local government statutory objectives

This annex provides further detail on the statutory objectives for local government as provided in the Local Government Act 2002.

“Section 10 defines the purpose of local government as having two parts as follows:

- (a) to enable democratic local decision-making and action by, and on behalf of, communities and
- (b) to meet the current and future needs of communities for good-quality local infrastructure, local public services and performance of regulatory functions in a way that is most cost-effective for households and businesses”.

‘Good quality’ is defined in subsection 10(2) as follows:

“In this Act, in relation to local infrastructure, local public services, and performance of regulatory functions, means infrastructure, services, and performance that are:

- (a) efficient and
- (b) effective and
- (c) appropriate to present and anticipated future circumstances”.

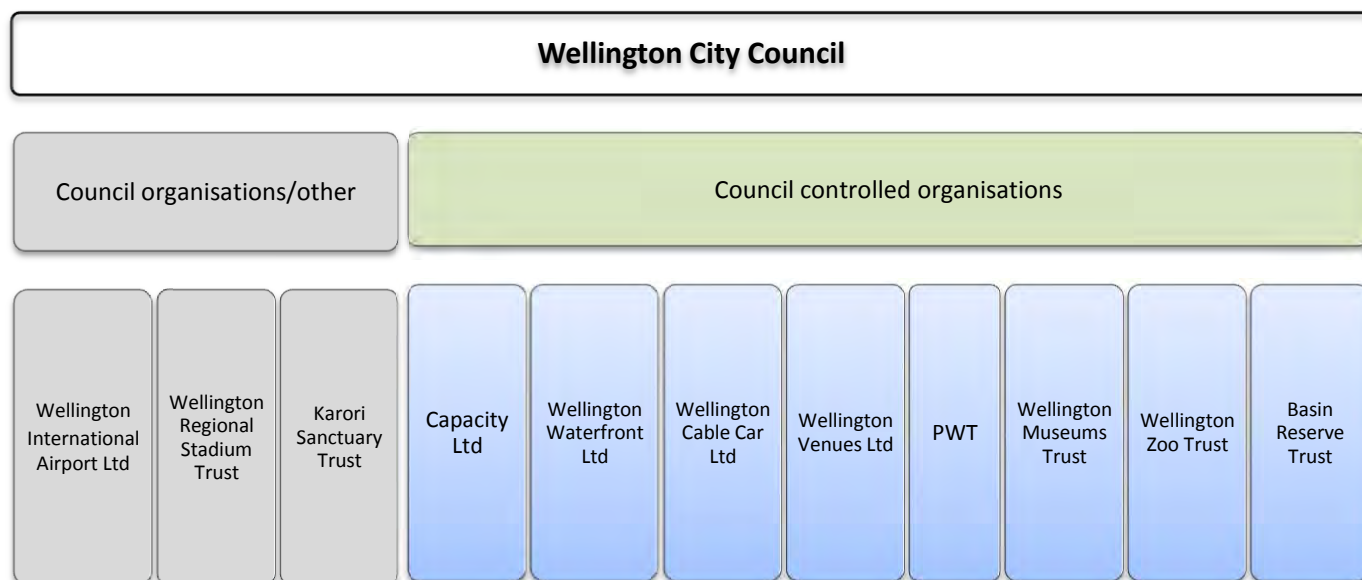
“Clause 12(b) of Schedule 3 identifies, without limitation, the following ways in which improved economic performance may be facilitated:

- (a) efficiencies and cost savings and
- (b) productivity improvements, both within the local authorities and for businesses and households that interact with those local authorities and
- (c) simplified planning processes within and across the affected area through, for example, the integration of statutory plans or a reduction in the number of plans to be prepared or approved by a local authority.”

“Clause 12(b) may be seen to be about changes that will lead to doing more with the same resources, or doing the same with less resources while also (where relevant) simplifying local government processes. Local authority service delivery should be appropriate to the area, the communities and their circumstances both in the present and for the future.”

## Annex 3: Summary of CCOs and non-CCOs

This annex summarises the council controlled organisations (CCOs) and non-CCOs within the Wellington region. The information has been sourced from *Future Wellington – Proud, Prosperous and Resilient*, Wellington Region Local Government Review Panel, October 2012.

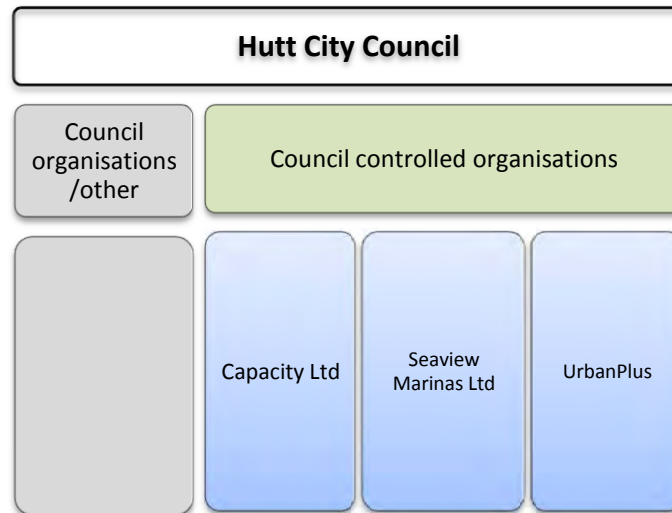


### Notes:

1. Wellington Regional Stadium Trust is not a CCO. It was established under its own empowering act.
  - a. It is jointly controlled (with Greater Wellington Regional Council) by means of board appointments
2. There are other minor organisations that are not substantive for the purposes of this review. These include:
  - a. Exempted CCOs – generally exempted due to their small size
  - b. Other council organisations
  - c. Subsidiaries e.g., Chaffers Marina
3. There are also joint committees and joint ventures (Spicer Landfill etc.)

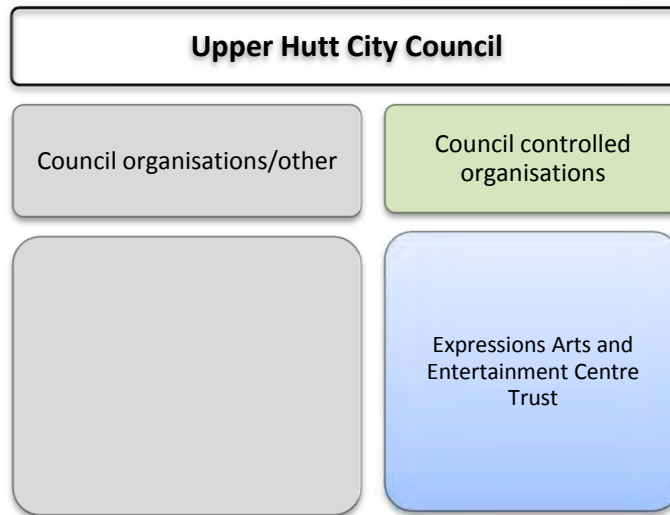
**Table 31: Wellington City Council CCOs**

CCOs	Form	Purpose	Governance/ ownership	Receives local operational funding?
Capacity Ltd (Est: 2003)	Company	Manages the provision of water services (water supply, stormwater and wastewater) to residents and businesses.	WCC and HCC have equal voting rights in this CCO, and between them appoint all of the board (made up of two councillors (one from each council) and four independent directors). WCC owns 63% of the shares, and HCC 37%. Each council continues to own its respective assets and determines the standard of services.	Revenue is received from councils for contracted services (Wellington City, Hutt City and Upper Hutt City councils).
Wellington Waterfront Ltd (Est: 1987)	Company	Implements the Waterfront Development Project.	WCC is 100% shareholder and appoints all directors (includes one Councillor).	Yes, management fee paid by WCC.
Wellington Cable Car Ltd (Est: 1991)	Company	Maintains and operates the cable car and trolley bus overhead wires.	WCC is 100% shareholder and appoints all directors.	Yes, WCC is purchaser (of services).
Wellington Venues Ltd (Est: 2011)	Company	Began trading on 1 Feb 2011, merging the operations of the St James Theatre Charitable Trust and the Wellington Convention Centre.	WCC is 100% shareholder. Directors appointed by the council (includes two councillors).	Yes, WCC is purchaser (of services).
Positively Wellington Tourism (Est: 1997)	Trust	Markets Wellington as a visitor destination nationally and internationally.	All trustees appointed by WCC (includes one councillor).	Yes, WCC is funder (operational grants) and minor purchaser (of services).
Wellington Museums Trust (Est: 1995)	Trust	Promotes and manages the City Gallery Wellington, the Museum of Wellington City & Sea, the Colonial Cottage Museum, Carter Observatory, Capital E, the Wellington Cable Car Museum, and the New Zealand Cricket Museum.	All trustees appointed by WCC (includes one councillor).	Yes, WCC is funder (operational grants) and minor purchaser (of services).
Wellington Zoo Trust (Est: 2003)	Trust	Manages the assets and operations of Wellington Zoo.	All trustees appointed by WCC (includes one councillor).	Yes, WCC is funder (operational grants) and minor purchaser (of services).
Basin Reserve Trust (Est: 2005)	Trust	Manages and operates the Basin Reserve.	The Trust was jointly established with Cricket Wellington. There are four trustees of whom two are appointed by WCC (including one councillor) and two by Cricket Wellington.	Yes, WCC is funder (operational grants).



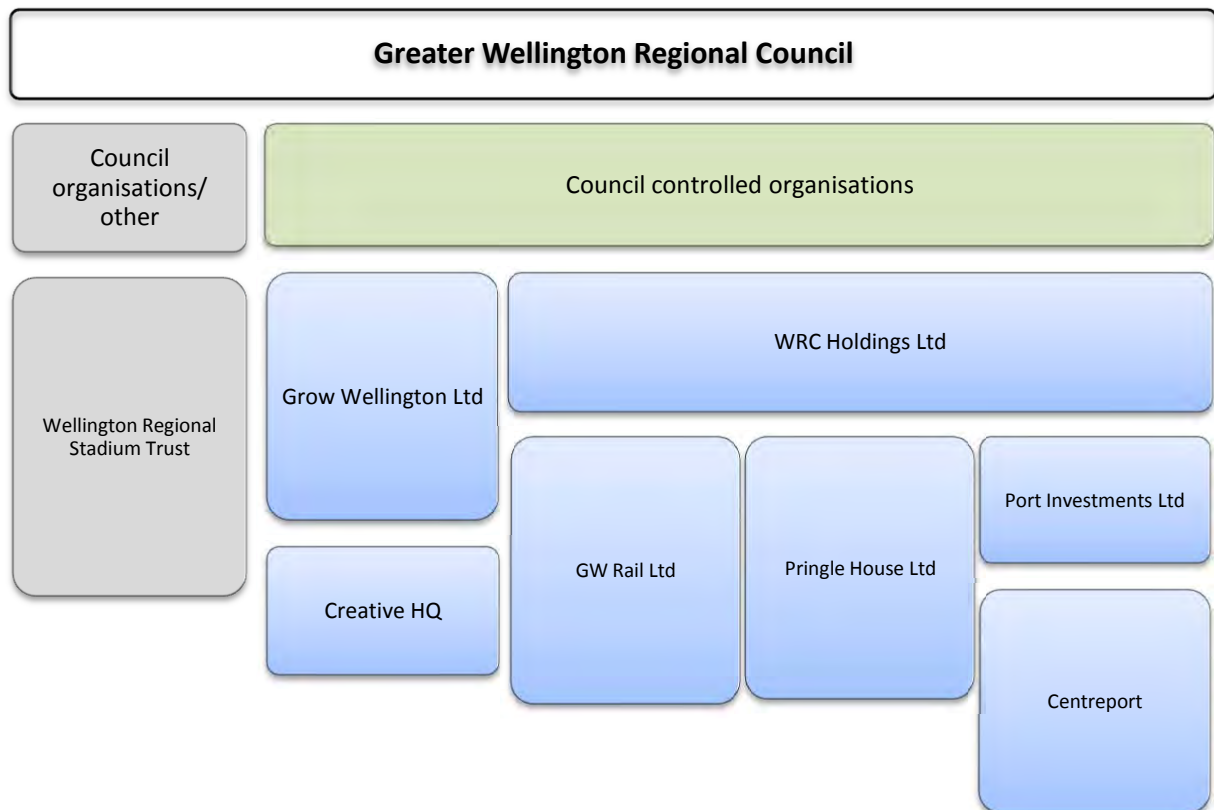
**Table 32: Hutt City Council CCOs**

CCOs	Form	Purpose	Governance/ ownership	Receives local operational funding?
Capacity Ltd (Est: 2003)	Company	Manages the provision of water services (water supply, stormwater and wastewater) to residents and businesses.	WCC and HCC have equal voting rights in this CCO, and between them appoint all of the board (made up of two councillors (one from each council) and four independent directors). WCC owns 63% of the shares, and HCC 37%. Each council continues to own its respective assets and determines the standard of services.	Revenue is received from councils for contracted services (Wellington City, Hutt City and Upper Hutt City councils).
Seaview Marinas Ltd (Est: 2004)	Company	Owns, operates and develops the marina.	HCC is 100% shareholder and appoints all directors.	No operational funding - loan from HCC to Seaview Marina.
Urban Plus Ltd (Est: 2007)	Company	Owns and operates a portfolio of rental housing, develops property in preparation for sale or lease and manages council property and building assets.	HCC is 100% shareholder and appoints all directors.	Yes, HCC is purchaser (of services).



**Table 33: Upper Hutt City Council CCO**

CCOs	Form	Purpose	Governance/ ownership	Receives local operational funding?
Expressions Arts and Entertainment Centre Trust (Est: 2003)	Trust	Manages the Expressions Arts and Entertainment Centre.	All trustees appointed by the council.	UHCC is funder (operational grants).



**Table 34: Greater Wellington Regional Council CCOs**

CCOs	Form	Purpose	Governance/ ownership	Receives local operational funding?
WRC Holdings Ltd (Est: 1987)	Company	Investment holding company.	100% owned by GWRC (appoint all directors, including 4 councillors).	GWRC is purchaser (of services) or shareholder / owner. No separate funding required.
GW Rail Ltd (Est: 2006)	Company	Owens investments in metro rail assets.	100% owned by WRC Holdings Ltd (appoint all directors, including 4 councillors).	Receives operational grants for rolling stock and station maintenance. Receives capital grants for rolling stock and station purchase and upgrades.
Pringle House Ltd (Est: 1985)	Company	Owens and operates the GWRC centre at Wakefield Street, Wellington.	100% owned by WRC Holdings Ltd (appoint all directors, including 4 councillors).	See WRC Holdings Ltd.
Port Investment Ltd (Est: 1991)	Company	Investment holding company - Owns 76.9% of CentrePort. Note that CentrePort is a commercial port company which is excluded from the CCO definition in the Local Government Act 2002.	100% owned by WRC Holdings Ltd (appoint all directors, including 4 councillors).	See WRC Holdings Ltd.
Grow Wellington Ltd (Est: 2007)	Company	Acts as an economic development agency to implement the regional strategy.	100% owned by GWRC.	Yes, GWRC is funder (operational grants).
Creative HQ Ltd (Est: 2009)	Company	Acts as an incubator to support growing companies.	100% owned by Grow Wellington Ltd (Grow Wellington Ltd appoint all directors).	See Grow Wellington Ltd.

**Table 35: Other significant (non-CCOs) within the Wellington region**

Non-CCOs	Form	Purpose	Relationship to local authority	Receives local operational funding?
Wellington International Airport Ltd	Company	Airport company.	WCC owns 34% shareholding (remaining 66% is owned by NZ Airports Ltd).	No.
CentrePort Ltd	Port company specifically excluded from definition of CCOs.	Port company.	GWRC owns 76.9% shareholding through WRC Holdings Ltd and Port Investment Ltd.	No.
Wellington Regional Stadium Trust	Trust specifically excluded from definition of CCOs.	Owns, operates and manages the Westpac Stadium.	Established by WCC and GWRC under Wellington Regional Council (Stadium Empowering) Act 1996. All trustees are jointly appointed by WCC and GWRC. The board includes one councillor from each council.	No. Loans of \$15 million from WCC and \$25 million from GWRC.
Karori Wildlife Sanctuary Trust	Trust	Manages Zealandia native wildlife sanctuary.	WCC appoints three of the seven trustees including the chair.	Small operational grant and interest free loan from WCC.



## Annex 4: Size and cost-effectiveness: the conceptual approach

This annex outlines the conceptual approach underpinning our analysis.

In economics the relationship between total costs of production as a function of total quantity produced is termed the “cost curve” or “cost function”.

We explore the evidence that is available on the cost of a constituent for local government entities. In the delivery of most products and services, cost is made up of both:

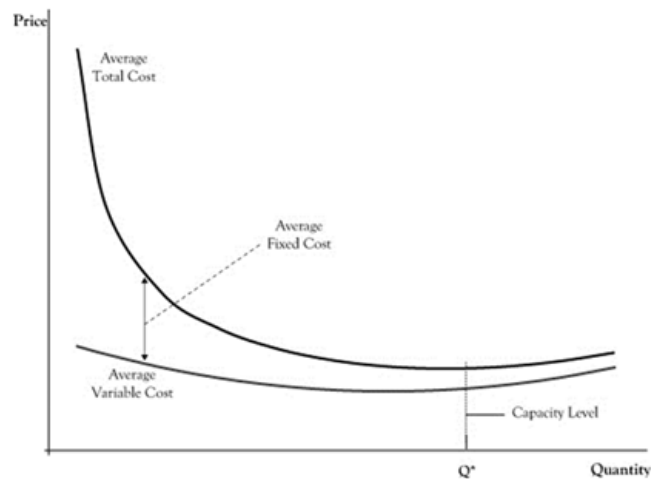
- fixed costs, that in the short term do not vary with the number of constituents served; and
- variable costs, that vary directly with number of constituents served.

This dissection leads to the observation that average costs per constituent initially tend to reduce as the number of constituents served by the same organisation rises and economies of scale are realised, but typically average costs then rise as diseconomies of scale take effect.

Some policymakers and some members of the public share a belief that larger councils should exhibit greater efficiency and cost-effectiveness. The belief that larger size should deliver more for every \$1 spent, or deliver services at a lesser cost, motivates a call for council amalgamation to cure the supposed inefficiencies of fragmented local public service provision. In a similar vein in the private sector, seeking an economy of scale has long been the underpinning theory for corporate behaviour from mass production to mergers and acquisitions, while diversification has been underpinned by the idea of an economy of scope. These ideas are derived from the field of managerial economics and are intuitive: if delivery of a service entails an element of fixed costs (that does not vary with service level) then the average costs of the service will decline with increases in provision until the limit of capacity is reached.

This relationship between service level and average cost of provision is illustrated in Figure 14 below. Average costs per customer tend to be lower when higher numbers of customers are served by the same organisation.

Figure 14: Average cost of delivering services at differing levels of production



What may be overlooked is the important qualification that once capacity is reached, average costs stop falling. To meet still further levels of service delivery, additional increments of fixed cost is required. The savings from spreading fixed costs over more production only applies until capacity is reached.

Economies of scale and scope can also have a dark side, called “diseconomies”, also recognised by managerial economics. The larger an organisation becomes in order to reap economies of scale and scope at an operational level, the more complex it has to be to manage and run itself. This complexity incurs a material cost, and eventually this cost may come to outweigh the savings gained from greater size. In other words, an economy of size does not necessarily apply forever. There is a qualitative difference that is also important: savings from combining service delivery tend to be identifiable and measureable at an operational level, while the diseconomy from size creeps up insidiously in the shape of policies, procedures, rigid organisational culture and additional management layers (i.e., increased bureaucracy).

Thus support for the supposed size and cost-effectiveness relationship is not a self-evident truth, and the belief in its existence provides little support for council amalgamation, except as warranted on a functional case-by-case basis.

## Annex 5: Letter from NZTA



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12 June 2013

Phil Barry  
TDB Advisory Ltd  
[phil.barry@tdb.co.nz](mailto:phil.barry@tdb.co.nz)

Dear Phil,

### Local Government Reorganisation in Wellington

To assist you in your work for Hutt City Council on governance options for the Wellington region, I thought it would be useful to outline the key principles that the NZTA considers relevant to any contemplation of local government reorganisation in Wellington. The selected local government governance model should:

- 1. Enable the development and implementation of a regionally strategic and integrated approach to land use and transport planning**  
The governance structure must foster a common and enduring regional identity and purpose that will support an integrated approach to land use and transport planning across the region. To be able to successfully implement that regional approach, decision makers need to be obliged to represent the interests of the region as a whole, rather than be limited by accountability and funding associated with specific territories within the region. Decisions on land use and transport planning need to be considered alongside each other to deliver on a common vision or regional strategy.
- 2. Support the development of a 'one network' systems approach**  
The governance structure must support a one network approach that integrates planning and operation of public transport, state highways, local roads, and walking and cycling and recognises the inter-relationship between the different activities that use that network. A one network approach takes a national, inter-regional, regional and local view of the transport network that is customer focused, with an emphasis on key routes and strategic connections rather than a project-specific funding approach. For example, in Wellington, it is important that the whole system that moves commuters to the Wellington CBD and other places of employment is considered in an integrated way rather than separate decisions being made by multiple authorities. To support the development of a 'one network' approach, it is preferable that a governance model streamlines interaction with the NZTA, and other key transport providers.
- 3. Provide a clear mandate and accountabilities for decisions on transport planning, funding, and delivery that encourage certainty**  
Any future governance framework must provide a clear mandate and the statutory authority to plan for, fund local share, and take the necessary actions to implement

current and future transport plans. Funding should reflect regional benefits and trade-offs, and avoid silo-ed responsibility for funding. To provide certainty, funds should also be sufficiently earmarked for transport over specific time periods rather than fluctuate and/or risk being reallocated away due to short-term changes in political priorities.

**4. Support a partnership approach and encourages collaboration in planning and delivery**

Any model also needs to provide a structure that will encourage collaboration with the private and public sectors. An open and effective process for central and local government engagement on transport and urban development issues is essential to ensure that the strategic direction adopted in the region is consistent with national policy objectives, and that investment between the different levels government is aligned. It is important that the role of the private sector as an investor in land use development and as a potential transport investor is also be recognised by any future governance model.

**5. Encourage efficient use of resources and value for money**

Looking forward, there will be a continuing emphasis on the efficient management of transport network and services. Any future governance structure must be capable of effectively and efficiently delivering maximum value within the available resources, in terms of cost, quality of service delivery, local democracy and community engagement. It should avoid duplication of processes, roles, and responsibilities and facilitate a best practice approach to the procurement of transport infrastructure, operations and maintenance.

**6. Build organisational capability and capacity**

The complexity of the transport system requires a range of skills from strategy development to the management and operation of transport system. Finding and retaining skilled staff is an ongoing concern across the transport sector. The Road Maintenance Task Force noted an ageing workforce, training and the number of people entering the industry was limiting the ability of local authorities to apply the advanced asset management practices needed to achieve better value for money. Small councils that are unable to provide a broad range of staff opportunities are particularly affected. This is a real concern given the long-term planning horizons that exist for most transport projects. Consolidating the development, management and operation of the transport system could help to address these capability and capacity issues and facilitate best practice and centres of excellence.

Yours sincerely



**Jenny Chetwynd**  
Regional Director

## Annex 6: Council surveys

Who commissioned?	Who conducted?	When conducted?	How conducted?	Who was surveyed?
Hutt City Council & Upper Hutt City Council	Colmar Brunton	Jun-13	Telephone survey	1,002 adults in the Hutt Valley (501 in Lower Hutt and 501 in Upper Hutt). The maximum margins of error are +/- 4.4% in both Council locations. The maximum margin of error for the total Hutt Valley sample is +/- 4%.
Kapiti Coast District Council	SIL Research	May-13	Telephone survey	1,500 residents across the four wards randomly selected and the scores weighted according to age and gender spread across the district. Poll results are reported at a 95% confidence level +/- 2.5%.
Eight territorial authorities (ex-GWRC)	Colmar Brunton	Jun-12	Telephone survey	3,300 adults were surveyed. The sample was designed so that it included 400 respondents in each district and 500 in Kapiti. Regional margin of error of +/- 2%.
Wairarapa Councils	Colmar Brunton	Jun-12	Telephone survey	1,200 adults were surveyed (400 Carterton; 400 Masterton; 400 Wairarapa).
Wellington City Council	Colmar Brunton	Apr-13	Online survey	Representative sample of 503 Wellington city residents. The sample includes both ratepayers (68%) and non-ratepayers (30%; a further 2% were unsure if someone in their residence paid rates). All subgroup differences mentioned in this report are statistically significant at the 95% confidence level.
Wellington City Council		May-12	Public Consultation / Submissions	Received 1,209 submissions.
Porirua City Council	Versus Research Limited	Jun-13	Telephone & Online survey	A random selection of 501 Porirua residents. The achieved sample delivers a margin of error of +/- 4.4% at the 95% confidence interval. The results are weighted to correct age skews.
Upper Hutt City Council		Jun/Jul 12	Public Consultation / Submissions	Received 1,409 submissions.
Hutt City Council		Sept/Oct 12	Public Consultation / Submissions	Received 973 submissions.

Who commissioned?	What was asked?
Hutt City Council & Upper Hutt City Council	Which option do you prefer? Option 1 (enhanced status quo), Option 2 (Hutt Valley unitary authority), Option 3 (Supercity), Don't know. How strongly do you feel (about your preference)? What is your second preference? (if first choice was not available)
Kapiti Coast District Council	"Firstly, there are two options: (status quo and single city options rotated). A SINGLE CITY OPTION: consisting of Hutt Valley, Wellington, Porirua and Kāpiti. This could be expanded to include the Wairarapa." Respondents were then asked which they preferred. An 'Other' option was added in the event a respondent couldn't or refused to choose between 'Single city' or 'Status quo'.  Those indicating a Single City option was preferred were then presented with the following question: "You mentioned you would prefer a single city. We are consulting on TWO possible structures; they are... (two tier and single tier council options rotated).  All respondents were then asked the following: "Is there another option not mentioned that you would prefer?"  Lastly, all respondents were asked the following question: "You may be aware that NEITHER single city option GUARANTEES community boards. In light of this, how important are community boards to you using this scale.
Eight territorial authorities (ex-GWRC)	"Do you think the way councils in the Greater Wellington region are organised should remain the same/change/don't know" Respondents were then asked their views of various options, including 1 council for the region, 2 councils (one for Wairarapa and one for the balance of the region and 3 councils. No details were provided for these options and there was no reference to a two-tier local board option.
Wairarapa Councils	Q: Wairarapa respondents were presented with the following options: No change to council boundaries but more shared services; A single district council (TA) for Wairarapa with a separate Regional Council; A single Wairarapa unitary council; One authority for the wider Wellington region that includes Wairarapa.
Wellington City Council	The questions in the survey were a replication of the Council's submission document and adapted for use as an online survey by Colmar Brunton. How much do you agree or disagree that the current local governance structure needs change? Which model do you prefer for local government in the Wellington region? (single-tier, two-tier, status quo, other). Further questions on awareness and Wairarapa.
Wellington City Council	Submitters were invited to state whether they wanted the current system to change or not. Submitters were asked for their views on four governance options for the Wellington region: Option 1: retain existing councils but with shared services; Option 2: merge all existing councils into three unitary councils; Option 3: merge all existing councils into two councils, a Wellington council and a Wairarapa Council; and Option 4: merge all councils into one council for the whole region.
Porirua City Council	Q: Which of the following best describes how you feel about a change in local government structure for the Wellington region and Porirua area? Are you...? (Strongly supportive, supportive, neutral, opposed, strongly opposed, unsure). Q: As per the information sheet we sent out there are three options: a single tier option, a two tier option and the status quo. Thinking about these option which one do you most prefer to see in place for the Wellington region and the Porirua area? Q: If local government HAD to change to one of the two options available which one would you most prefer to see in place for the Wellington region and the Porirua area? Q: If local government reform was to occur, how important do you think it is for Porirua to have a locally elected body to make decisions on Porirua community issues? Would you say it is...? (Very important, important, neutral, not important, not important at all). Q: Lastly, how would you rate the overall performance of Porirua City Council in the last 12 months? Would you say their performance has been? (Very good, good, average, poor, very poor, don't know).
Upper Hutt City Council	Submitters were invited to state whether they wanted the current system to change or not. Submitters were then asked that if change was inevitable, to select an option for change (or describe their own option). The options surveyed were the same as those used by Wellington City
Hutt City Council	The options surveyed were: a. Status quo with more shared services b. Three separate unitary authorities – Wairarapa, Hutt valley and rest of Wellington. c. A single unitary authority for Wellington region d. A different idea.



Who commissioned?	What was the response?
Hutt City Council & Upper Hutt City Council	<p><b>Which option do you prefer:</b> Total Hutt Valley (50% enhanced status quo; 28% Hutt Valley unitary authority; 18% Supercity; 4% Don't know).</p> <p><b>How strongly do you feel:</b> Most people feel strongly about their preferred option, but strength of feeling is strongest among those who support the status-quo.</p> <p><b>Second preference:</b> Three-quarters of those who support the status quo would prefer a united Hutt Valley if the status-quo was not an option. Seven in ten of those who support a united Hutt Valley would prefer the status-quo if a united Hutt Valley was not an option. Two-thirds of those who support a Supercity would prefer a united Hutt Valley if the Supercity was not an option.</p>
Kapiti Coast District Council	<p><b>Status quo vs. single city option:</b> 54.7% preferred the 'status quo' 42.9% the 'single city'</p> <p><b>Single city options</b> - of those respondents (42.9%) who preferred a 'single city option' 51% preferred a 'two-tier' council 44.5% preferred a 'single tier' council 4.5% stated 'other'</p> <p><b>Importance of community boards</b> - across all respondents 65.4% stated community boards are 'very or somewhat important'</p>
Eight territorial authorities (ex-GWRC)	<p><b>Change or no change:</b> 49% of respondents said "remain the same"; 41% of respondents said "change"; 9% said "don't know"</p> <p><b>First choice options:</b> 58% of all respondents wanted no changes to current local council boundaries; 31% wanted changed boundaries in some form (12% preferred Option 2 (3 councils for the whole region. These would be a) Wellington City, Porirua and Kapiti, b) Hutt and Upper Hutt, and c) Wairarapa); 9% preferred Option 3 (2 councils for the whole region. These would be a) Wellington City, Porirua, Kapiti, Hutt and Upper Hutt, and b) Wairarapa); 9% preferred Option 4 (1 authority for the whole Wellington region)); 2% preferred another option of their own which was not on the list of options; 10% were undecided.</p>
Wairarapa Councils	<p><b>Wairarapa as a whole:</b> 45% did not (initially) favour any boundary change (no change or more shared services); 41% wanted a single Wairarapa council; 5% wanted Wairarapa to be part of a single Wellington authority (super-city); 7% did not know.</p> <p><b>Wairarapa residents were asked to review three possible 'change' options (i.e. stay the same was not an option):</b> 28% preferred more shared services (without local council boundary changes); 60% preferred a single Wairarapa council; 8% preferred a single authority for the whole Wellington region; 3% said 'other/something else'; 1% said 'don't know'.</p>
Wellington City Council	<p><b>Need for change:</b> More than half of residents (52%) agree that the structure of local governance needs change (These residents hold this view because they think there are currently too many councils (33%) and an amalgamated Council could offer financial efficiencies (30%)), 15% disagreed it should change (residents fear a loss of 'local voice' or local perceptiveness (30%) or believe the current structure is working fine (29%) and 30% were neutral.</p> <p><b>Which model:</b> When asked if change was inevitable, 43% of respondents supported the single tier model, 37% supported the local board model, and 18% supported the status quo. When asked if change was inevitable and the status quo was not available, 50% supported a single tier model, 46% supported a local board model.</p> <p><b>Awareness:</b> Those who have some awareness of the models tend to prefer the Single-tier model (47%) over the Two-tier model (35%). Whereas, residents who are unaware of the models prefer the Two-tier model (42%) over the Single-tier model (34%).</p> <p><b>Wairarapa:</b> Almost one half (49%) of Wellington residents say they think the Wairarapa should be excluded from a reformed local government structure (only 29% say they think it should be included and 22% are unsure).</p>
Wellington City Council	<p><b>Want/don't want Change:</b> Of the 1,209 submitters, 1,092 (90%) responded to this question. Of those that responded, 23% (252) stated 'no change' and 77% (840) stated 'change'.</p> <p><b>Submitters were then invited to select an option for change (or tell us their own):</b> Of the approximately 1,000 submitters that voted for a change option - 252 voted for option 1 (all councils remain in place but with more shared services and collaboration (note that this is not the same 252 that stated 'no change', although there is some overlap of about 60 submitters)). 147 voted for option 2 (three unitary authorities). 296 voted for option 3 (unitary authorities for Wairarapa and Wellington). 234 voted for option 4 (a single unitary authority covering both Wairarapa and Wellington). 68 chose 'another option'.</p>
Porirua City Council	<p><b>Change in local government structure:</b> 51% supported change (supportive (38%) or strongly supportive (13%)); 24% were neutral; 19% opposed change (opposed (12%) or strongly opposed (7%)).</p> <p><b>Preferred option:</b> 41% supported two-tier; 31% supported single-tier; 22% supported status quo; 7% responded "don't know".</p> <p><b>Preferred option if local government HAD to change:</b> 63% chose two-tier; 15% chose single-tier; 22% responded "don't know".</p> <p><b>Importance of a locally elected body:</b> 87% supported this statement.</p>
Upper Hutt City Council	<p>Submissions showed that the public view was strongly in favour of remaining the same, with no structural change. <b>Change/No Change:</b> Of the 1,409 submitters, 1,383 (98.2%) responded to this question. Of those that responded, 75.8% (1049) chose 'remain the same' and 24.2% (334) chose 'change'.</p> <p><b>Preferred Option:</b> Of the 1,409 submitters, 1,397 (99.1%) responded to this question. 962 (68.8%) chose Option 1 (of the 962 responses for this option, 835 selected 'remain the same' and 127 selected 'change'); 277 (19.8%) chose Option 2 – three unitary authorities; 50 (3.5%) chose Option 3 – two unitary authorities; 33 (2.3%) chose Option 4 – the super-city option; 53 (3.7%) chose 'another option'; 22 (1.5%) selected 'did not know'; 12 (0.8%) respondents did not select an option (6 of the 12 chose 'remain the same').</p>
Hutt City Council	<p>Of the 973 submissions, 45% preferred modified status quo, 30% preferred three unitary authorities, 3% preferred a super-city, and 2.7% had an idea of their own to put forward.</p>



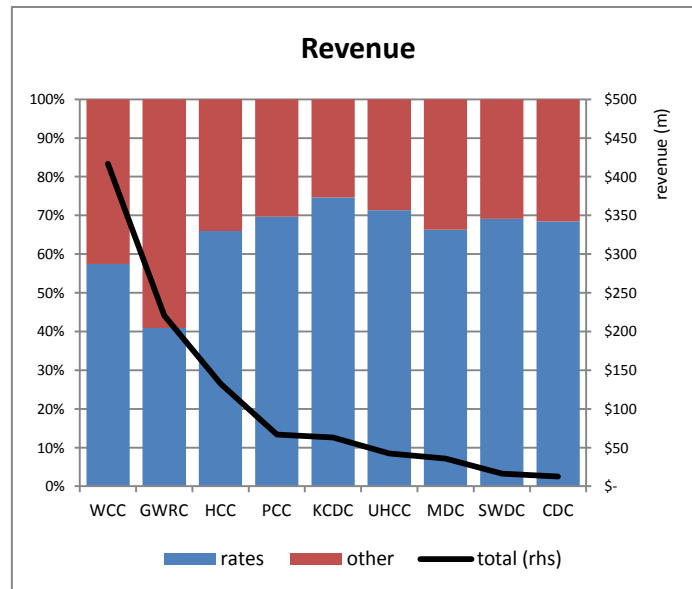
## Annex 7: Current financial positions of the local authorities

This annex provides further information on council rates and debt, supplementary to section 7 of the report.

### Rates

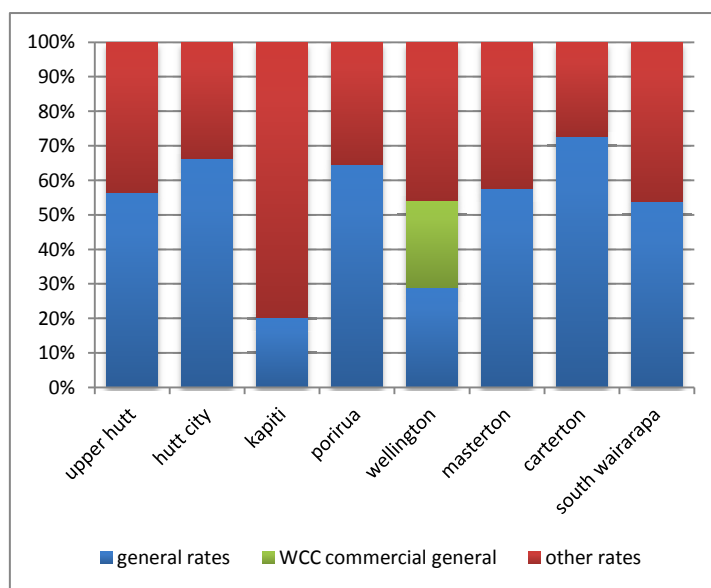
In the Wellington region, rates account for 58% of all revenue. Rates range from a low of 41% for GWRC to a high of 75% for Kapiti. In the case of GWRC, this is skewed to the low side by the large contribution from NZTA to the current rail upgrade programme – the purchase of rolling stock in particular. Figure 15 also shows the varying degrees to which councils generate other income – whether from user charges, grants or investments.

Figure 15: Proportion of rates versus other revenue by council



Looking at a breakdown of rates, Figure 16 shows that general rates are generally above 50% of total rates for all councils except Kapiti. Wellington’s commercial general rates are shown separately, given the significant contribution they make to the total.

Figure 16: General rates as % of total rates



With only 20% general rates, Kapiti is an outlier. This is because it has adopted a broad range of targeted rates. A number of these are calculated on capital value or are generally applied, and as such are not dissimilar to general rates. Aside from Kapiti, the range is from 54% to 73%.

General rates are applied based on capital value<sup>45</sup> (with differentials applied in some cases), and could be considered the “catch-all” basket, used when there is no more appropriate targeted method available. Our high level analysis of the impacts of change has also used capital value as the allocation basis. For two reasons this is considered appropriate for high level analysis:

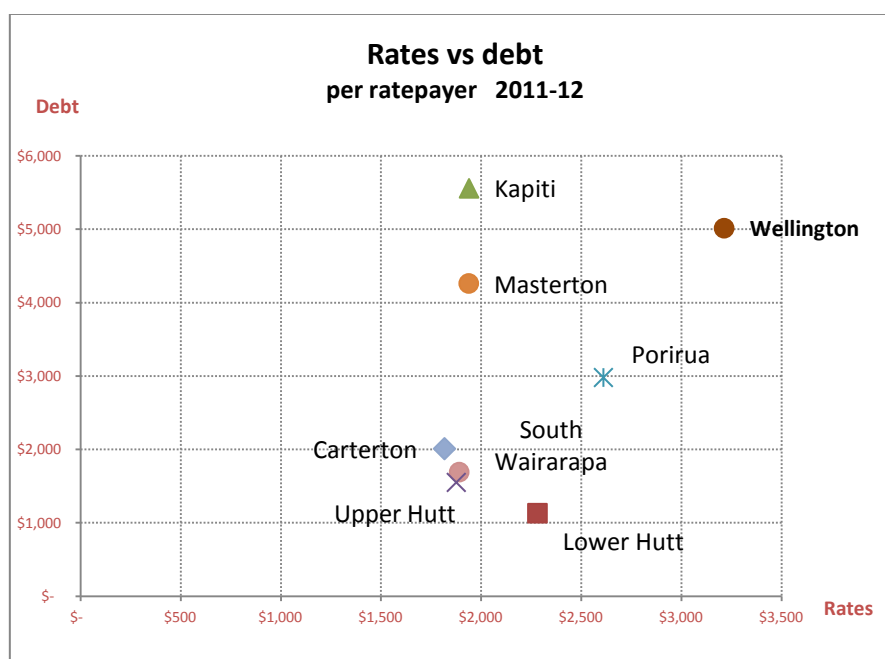
- it is a suitable proxy for the impacts of averaging change; and
- because changes will be applied against general rates as a default, when there is no better way to allocate them.

There is more discussion of this from a cost perspective in the next section. It is acknowledged that more detailed analysis will be appropriate if and when there is a specific reorganisation proposal to evaluate.

A final point of interest is to chart rates on a per household basis, against debt per household, for the councils of the region. Figure 17 shows that many councils have per household rates of just under \$2,000 per annum, but that debt levels vary widely. When rates are high, there is generally limited flexibility to increase rates in order to pay down debt. Wellington can be considered an outlier in this context, due mostly to the impact of the CBD on rates.

<sup>45</sup> Kapiti and South Wairarapa use land value.

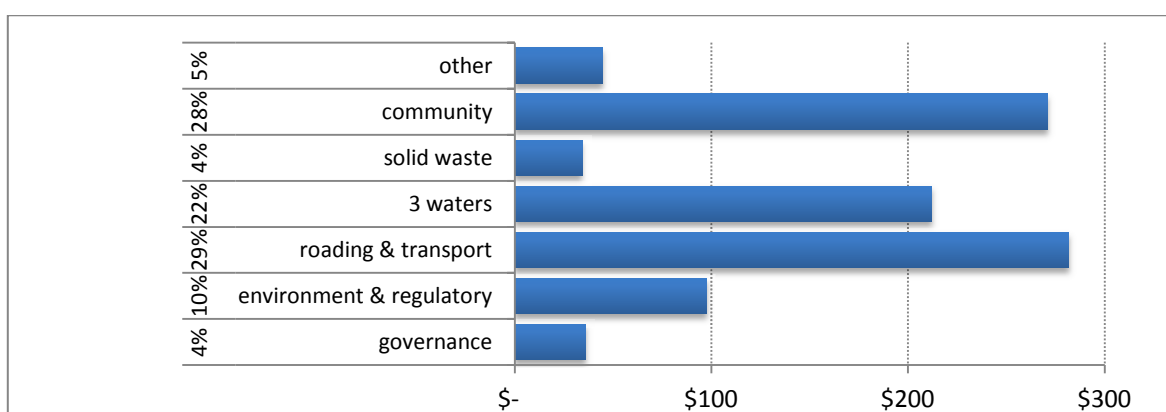
Figure 17: Rates and debt per ratepayer



### Expenditure

Activities that are often labelled “core infrastructure” make up 54% of council operating expenditure. These include roading and transport, three waters, and solid waste. They are also the basis of the capital-intensive activity analysis, discussed earlier in this report.

Figure 18: Breakdown of operating expenditure by activity group, 2012/13 (\$m)



A lot of the costs within the community group are also asset-based, such as libraries, parks and pools.

Roading expenditure provides a rich data set from which we can highlight the wide variation in expenditure across the region. Figure 19 shows the operating expenditure per kilometre of roads, by council. This excludes state highways, as these are maintained by NZTA. It is clear that expenditure in the urban areas is much higher than the predominantly rural areas.

Reasons will include the size and capacity of the roads, including the number of vehicles the roads are designed for, and the speed at which traffic will be travelling.

Figure 19: Roading expenditure per km by council

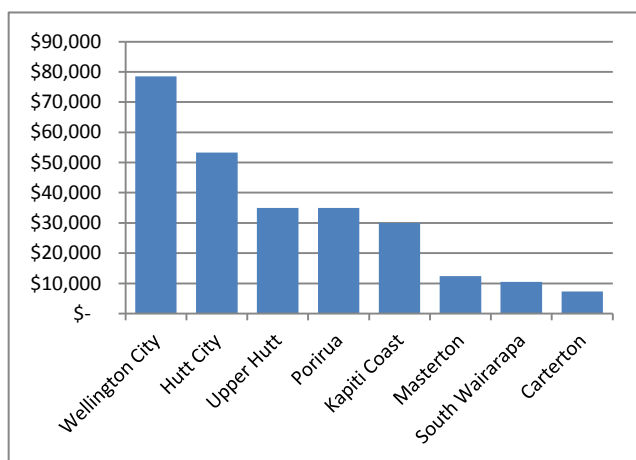
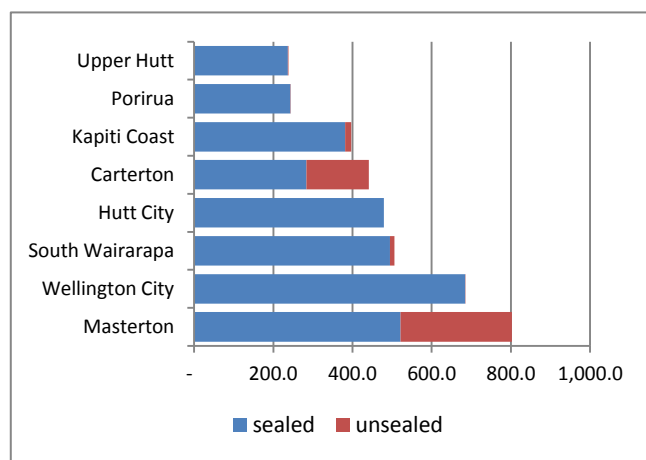


Figure 20: Length of roading network



Other factors will include the type, age and condition of roads – for example, unsealed roads are obviously cheaper to maintain. The point of this example is to suggest that, upon amalgamation, it is possible that these costs will be redistributed across all ratepayers within the new organisation(s). While the methodology may differ according to the activity, the effect in this instance would be to reduce costs for the higher-cost councils such as Wellington and Hutt City, and to increase them for the others. Similar changes will happen for the other major activity areas (even if the winners and losers differ in each case). In this respect, the impact will be broadly similar to that of the redistribution of general rates, and accordingly it is reasonable to use total rates and capital value as a high-level proxy allocation method.

### **Functional assessment**

As a way of testing the above high-level assumptions, we examine the possible savings opportunities within specific activities of the councils. This is the approach taken by Morrison Low<sup>46</sup> when estimating potential efficiency opportunities for a Hutt Valley unitary authority.

### **Governance**

Rationalising the number of councils, and the associated support costs, is likely to deliver savings in governance costs across the region, depending on the governance structure that is ultimately adopted. Within this activity group, it is also widely noted that executive management teams will be reduced in number. In both cases, savings could be partially offset as individual remuneration could rise in recognition of added responsibility.

<sup>46</sup> Morrison Low (2013).

There are some benchmarks available in the sector of the savings potential. All councils are required to report their key management costs – which are usually the costs of elected members and executive management. We can identify benchmark councils of similar size to the potential new unitary authorities. For example, merging the three Wairarapa councils would see the creation of a single organisation with a population of just over 40,000. This is close to the current Upper Hutt City Council, which can therefore be used as a benchmark. Combining the two Hutt councils would create a council with a resident population of approximately 145,000, which is not too dissimilar to Hamilton. Finally, there is not a close benchmark for the population of a combined Wellington-Porirua council, but Christchurch can be used as a conservative comparator. Table 36 shows the costs and savings opportunities.

**Table 36: Comparative remuneration for key personnel (\$m)**

Wairarapa		Hutt Valley		Wellington		Total
Upper Hutt	1.36	Hamilton	2.68	Christchurch	4.00	
Masterton	0.93	Hutt City	1.87	Wellington	4.01	
Carterton	0.37	Upper Hutt	1.36	Porirua	1.67	
South Wairarapa	0.41					
	<b>1.71</b>		<b>3.23</b>		<b>5.68</b>	
<b>Saving</b>	0.35		0.55		1.68	2.58

In addition, the remuneration for GWRC executive and elected members was \$2.96m. Combining the potential governance savings of \$2.58m from merging the councils, as estimated in the table above, with the \$2.96m savings from abolishing the GWRC would result in the potential savings from governance alone of around \$5.5m per annum. Savings could also be expected from support and administration costs, with fewer committees and councillors to provide services for.

While management costs are generally allocated across all activities, rather than kept within the governance grouping, \$5.5m is approximately 15% of the total expenditure on governance.

## Roading

Morrison Low has referred to findings of the Road Maintenance Task Force<sup>47</sup>, which suggests that collaboration and clustering of roading activity may yield efficiency gains of between 2% and 20% depending on the model chosen. There may be additional benefits from a “one network” approach around network optimisation. Savings towards the higher end seem quite extreme. However, on operating expenditure of approximately \$125m per annum, the lower estimate of 2% would equate to \$2.5m per annum in savings while the higher estimate of 20% would equate to \$25m per annum.

<sup>47</sup> Road Maintenance Task Force (2012).

### Three waters

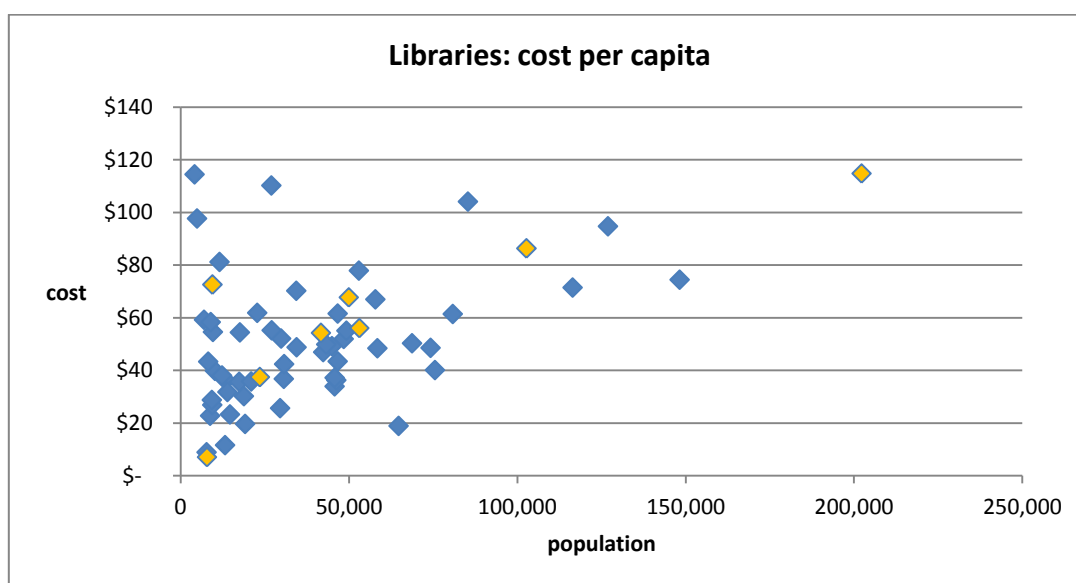
A report by PwC<sup>48</sup> suggests that creating a fully regional approach to the delivery of three water services could deliver up to \$5.1m in annual operating expenditure savings. This maximum requires that all council water-related activity, including the water supply activity of GWRC, is included. On total annual operating expenditure of around \$210m, this equates to a saving of 2.4%.

### Community

No specific examples have been provided for savings opportunities for community activities. Total expenditure is approximately \$270m per annum, which makes this one of the largest areas of council expenditure. There is some evidence that costs on community activities may increase with size.

For example, the following chart shows the cost per capita for library services across the country, related to population. The yellow points are the councils of the Wellington region. Both regionally and nationally there is some evidence of an increase in costs with population. According to the Public Library statistics data, compiled by the Library and Information Association of New Zealand, the cost of library services in the region is \$42m, with more than half attributable to Wellington City.

Figure 21: Libraries cost per capita, 2011/12



The weighted average cost of library services for all of New Zealand is \$60 per capita, while the average for the Wellington region is \$86. For context, the two largest councils (which are not shown on the chart above) have costs of \$79 for Christchurch and \$53 for Auckland.

This suggests that in part the difference in cost is attributable to service level choices – the number and size of branches, and the range of services offered. In part the differences reflect

<sup>48</sup> Delivering Water Services to the Wellington Region, February 2012.

higher costs for the larger city-based operations – floor space in Wellington central is more expensive than in Carterton.

The question posed in the earlier section about savings to be made from moving to better practice is the most relevant to this kind of activity. A cost reduction of \$5 per capita (thus closer to the cost for Christchurch on average) would equate to savings of \$2.4m per annum.

### **Regulatory and environment**

There should be economies of scale from merging consent teams together, and there may be savings from having fewer plans and policies. There are, however, no immediately available case studies for reference. Total expenditure is around \$97m per annum across the region.

### **Other**

There are a number of council functions to consider under the general “other” heading, with varying prospects of savings being achieved from amalgamations.

There is the potential for reducing the cost of borrowing of around \$1.1m per annum although the LGFA should be able to deliver much of this.

Debt sharing, while not having any net impact, would likely see a redistribution of the debt servicing costs, to the benefit of those (like Kapiti) with higher debt levels.

GWRC recovers its loan to the Stadium by way of a targeted rate. Wellington City, on the other hand, does not pay down the principal on its loans. It is possible that under both unitary options the Wellington City approach would prevail, reducing rates in the short term by \$2.6m per annum.

GWRC has corporate overhead allocations of \$9.1m stated in its funding impact statements for the LTP 2012/13 year. This includes approximately \$2m in executive management costs, which have been covered under the governance discussion above. However, under any unitary authority model, the majority of these corporate overheads could be expected to be saved.

### **Summary**

This functional view has provided an indication that possible savings are in the order of \$15.5m to \$38m per annum from a number of reported initiatives. Savings in the “Other” category opportunities could be as much as a further \$10m per annum. Assuming all the suggested savings above can be realised, then we have an indication that \$25.5m could be saved and as much as \$38m depending on the level of savings on roading activities.

It is important to note that the nature of the savings opportunities is such that they could be largely achieved under any structure, including the status quo. Given that our enhanced status quo involves the creation of land transport and water services CCOs, we expect any cost savings from roading or water services to be achieved under a single authority and the status quo. Removal of these two functions leaves us with possible savings of \$17.9m per annum.



The \$17.9m in cost savings may be slightly higher if further savings are achievable in areas not identified above or they may be somewhat lower if these savings do not come to fruition or the same savings are achievable under the enhanced status quo. Nevertheless, from this set of examples it is reasonable to infer that our savings assumption of around \$22m per annum may be achievable under a single authority, as suggested by our high-level assumption: cost savings are 3% of operating expenditure.

## **Debt**

### ***Gross debt or net debt?***

It is acknowledged that a number of contributions to the reorganisation debate have suggested that net debt is more an informative indicator, as it recognises the contribution to income from investments. These suggestions have also included looking at debt per resident (rather than ratepayer).

Most of this analysis is focused on the ratepayers' perspective, as they are the people who will have to pay. Analysis of debt therefore focuses on **gross** debt – because what ratepayers are most interested in is the impact on their pockets. This is mostly about the cost of debt servicing, but also needs to consider how the debt will be repaid (and specifically, what the impact will be on their rates). It does not make sense to consider investments, assuming they are making a positive contribution, as the investments would not be sold to repay debt. Therefore, debt repayments are going to be funded through other operating income, primarily through rates or further borrowing.

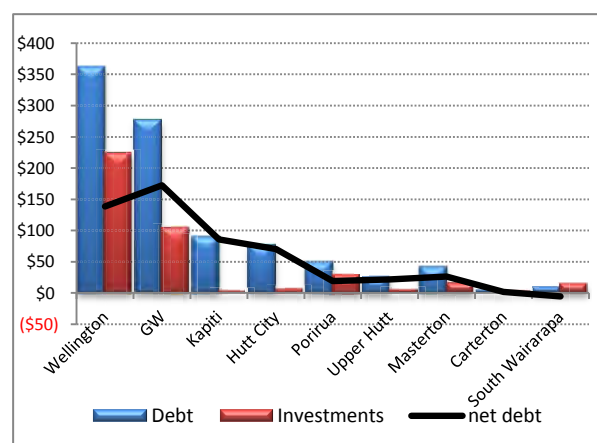
### ***Net debt: debt versus investments***

Wellington City has emphasised that, while it does have the highest debt levels in the region, debt has to be considered in the light of its investments. These investments earn income for the Council, and accordingly they contend that it is more appropriate to consider net debt. Figure 22 below shows debt and investments for each council, as at June 2012.

For this net debt position to be useful, the investments need to be earning a yield that is better than the cost of debt – or else the investments should arguably be sold to repay debt. Obviously there can be other strategic reasons for holding certain investments.

As an example, Wellington City has investment property with a value of \$200m and reported net income of \$11.4m in 2011/12, which suggests a yield of 5.7%. This yield appears to be lower than the effective borrowing cost (shown in Table 37) at 6.1%.

Figure 22: Debt and investments



However, as the Figure 22 above confirms, Wellington City’s net debt is considerably lower than its gross debt. Wellington City aside, Figure 22 shows that many of the councils in the region have very few investments.

### Effective interest rates

The Office of the Auditor General (OAG) has a series of measures that it is now using when reviewing the financial performance and position of councils<sup>49</sup>. These measures have been categorised as indicators of stability, resilience and sustainability. One such measure of financial sustainability is interest expense to debt. In its report, the OAG stated:

*“The interest expense to debt indicator shows the effective interest rate of debt. A higher result indicates a relatively higher cost of external funding that the local authority (and therefore the community) has to bear.”*

While the measure is simplistic, as it does not recognise any weighting of debt over the course of the financial year and does not look at long-term implications, it can be used here as a high-level indicator of the relative positions of the councils.

Table 37: Borrowings by council

2012–13 (LTP) \$m	Total	GWRC	KCDC	PCC	WCC	HCC	UHCC	Wairarapa
Current	187.2	26.7	13.9	22.4	92.1	28.7	1.2	2.2
Non-current	722.2	155.5	121.3	30.6	281.6	40.0	23.8	69.3
Total debt	909.4	182.2	135.2	53.0	373.7	68.7	25.0	71.5
Finance cost	52.25	8.17	8.47	3.33	22.65	4.00	1.46	4.16
Effective interest rate	5.7%	4.5%	6.3%	6.3%	6.1%	5.8%	5.8%	5.8%

The OAG noted that the average forecast for the sector in their long-term plans is 5.9%, which is near to the 2012/13 average for the Wellington region of 5.7% (above). It should be noted that the GWRC figures are an outlier, and as such are skewing the overall cost down

<sup>49</sup> Office of the Auditor General (2013).

slightly. This may in part be attributable to the difference between the council and the group for the GWRC, as the group includes significant extra debt. It can be observed that in the annual report for 2011/12, GWRC's actual effective interest rate was 5.7% for the Council, and 5.9% for the Group.

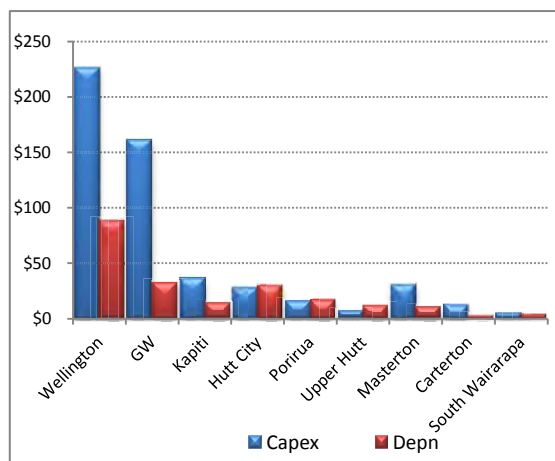
In theory there would be opportunities to generate lower borrowing costs, from having better credit ratings and from managing the cash flow and borrowing requirements across a larger organisation. If we were to assume this translated to a borrowing rate of 5.9% on the debt above (excluding GWRC), the potential savings are detailed in Table 38 below.

**Table 38: Potential savings in finance costs**

	Total	KCDC	PCC	WCC	HCC	UHCC	Wairarapa
Savings in finance costs	\$1.1m	\$0.5m	\$0.2m	\$0.6m	(\$0.1m)	\$nil	(\$0.1m)

However, the creation of the Local Government Financing Agency, or LGFA, should be generating most of those benefits for the sector already.

**Figure 23: Capex and depreciation**



### Capex versus depreciation

Debt is mainly being used to fund capital expenditure, particularly for new or upgraded assets. In simple terms (and in particular for the majority of councils, who do fund their depreciation), the excess of capex over depreciation has to be funded through debt.

Some councils are explicitly holding their capital expenditure levels at or under the level of depreciation. On the other hand, some councils have a number of significant investments at present, including Wellington, GWRC and Kapiti. There are differing

opinions being expressed about whether there is sufficient expenditure on asset maintenance and renewal, with some suggesting there is an infrastructure deficit, while others say that there is not.

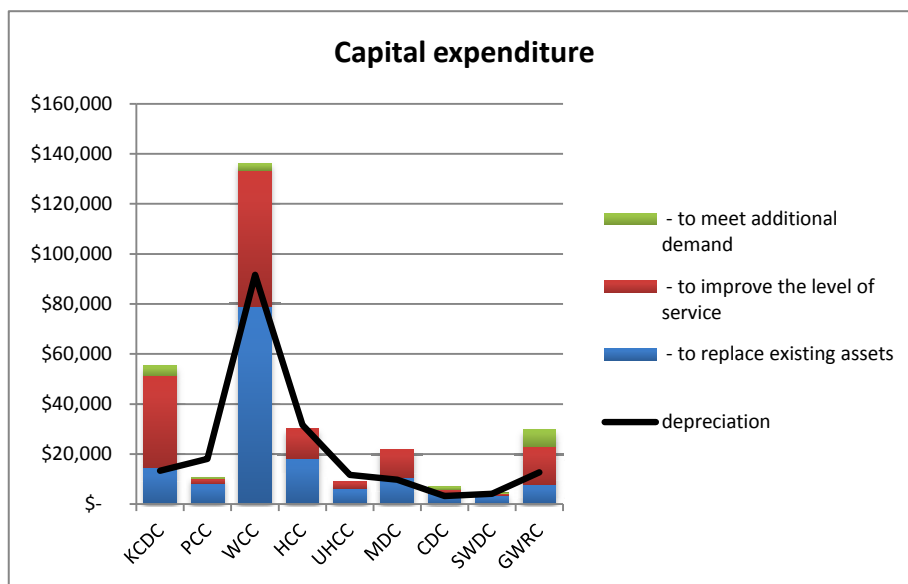
In their review of 2011/12 annual reports, the Office of the Auditor General has suggested that:

*“A consistently low percentage could call into question the ability to maintain assets in the long term or suggest a need for a significant rise in capital expenditure in the future.”*

Figure 24 below shows the breakdown of capital expenditure by council, per their funding impact statements. There is a reasonable correlation between expenditure to replace existing

assets (renewals) and depreciation, which is what we would expect. From that snapshot, asset maintenance (capex) is at appropriate levels – but as with much of this analysis, certainty would only come from much more detailed investigation. This chart highlights those councils that are investing in improved service levels, or for additional demand. These are the areas of capital expenditure that are going to be debt funded.

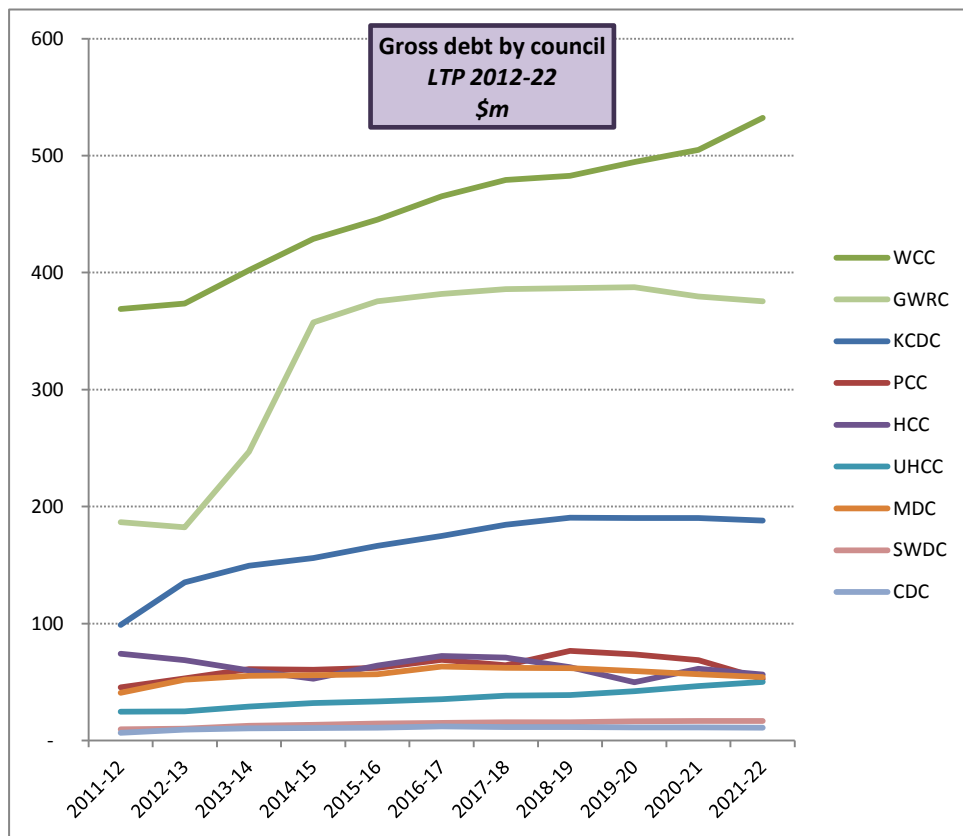
**Figure 24: Breakdown of capital expenditure – 2012/13**



***Debt over ten years (long-term plan)***

The long-term trend reflects the differences between the councils across the region. Figure 25 below shows the budgeted gross debt by council over the ten years of the long-term plan.

Figure 25: Gross debt – 10 years



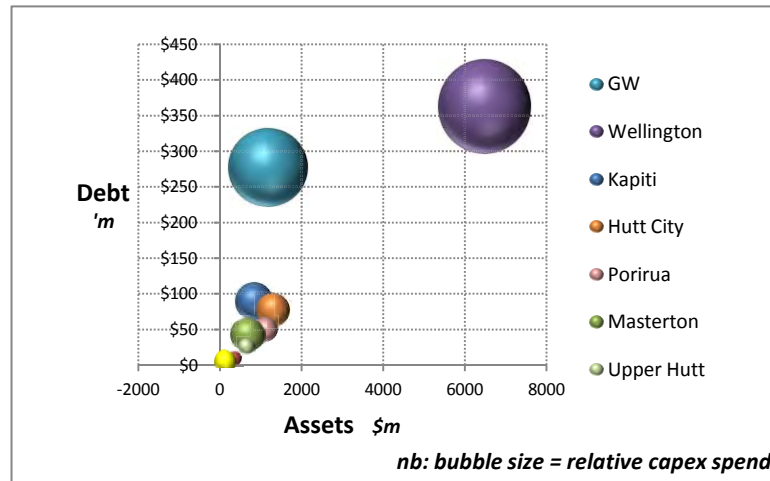
There are widely varying levels of capital expenditure, and there are quite different approaches to debt within the respective financial strategies. For example, GWRC is planning to repay debt over appropriate periods relative to the expected lives of the assets. On the other hand, Wellington City has no debt repayment planned over the current long-term plan. These two organisations have by far the majority of the capital expenditure and debt over the course of the long-term plan. Across the region there are differences in the approach to funding of depreciation, and as has been noted, there are also differences in investments held by councils, and accordingly the net debt position.

What a combined organisation would decide, in terms of its financial strategy, is therefore difficult to anticipate. What is apparent is that some councils are pursuing a strategy of low debt, while others are investing in future growth, and this investment is largely debt funded. This is acknowledged as one point of contention between the organisations when considering merging.

### *Debt versus assets*

As the debt is for investment in assets, Figure 26 shows the current level of debt in relation to the underlying value of fixed assets (property, plant and equipment) for each council. The size of the bubble represents the relative capital expenditure – the numbers in this case are for 2011/12.

**Figure 26: Debt – assets – capex**



The differing scale of asset base and expenditure stands out. Figure 26 suggests that, excepting the current rail investment by GWRC, only Wellington City is going to materially impact on the region's debt levels. Wellington has 42% of the debt and 51% of the assets within the region – more or less as much as everyone else combined.