

LOCAL GOVERNMENT FORUM

**SUBMISSION ON THE WELLINGTON CITY
COUNCIL'S DRAFT COUNCIL PLAN 2003/04**

MAY 2003

WELLINGTON CITY COUNCIL'S DRAFT COUNCIL PLAN 2003/2004

1 Introduction

- 1.1 This submission on the Wellington City Council's *Draft Council Plan 2003/2004* (the draft Plan) is made by the Local Government Forum (the Forum). The Forum comprises business organisations (listed in Appendix I) that have a vital interest in local government. Its members are among the Wellington City Council's largest ratepayers. We have appreciated the effort the Council has made to meet and discuss issues with the Forum over the past year. We have been encouraged by this constructive engagement to make this submission on the Council's 2003/04 draft Plan.
- 1.2 In past submissions we have called on the Wellington City Council (the Council) to focus on its core business of providing local public goods and undertaking regulatory functions conferred on it by central government. We have urged it to exit from commercial activities and review its provision of and/or funding of club goods such as the libraries, the zoo and swimming pools.
- 1.3 By focusing on its core activities the Council could cut expenditure and rates, which we believe is an essential step towards making Wellington a more attractive place for business. In turn a strong business sector can underpin and sustain the general welfare of the community.
- 1.4 The latest draft Plan suggests the Council may be making some progress in extricating itself from private commercial activities. On the other hand, the Council appears to be expanding other activities where it does not have a comparative advantage. Overall, the Forum believes the Council is not doing enough to reduce its spending below the growth rate of the economy and make room for the expansion of the private sector.

2 The comparative advantage of local government

- 2.1 The Council will only succeed at reducing expenditure and rates if it focuses on activities where it has a comparative advantage relative to households, private firms and the voluntary sector.

- 2.2 Local government's comparative advantage is in the provision of local public goods¹ that might be under-provided by the private sector, as well as the performance of regulatory functions conferred on it by the government. Local public goods should only be funded when the benefits of supply exceed the costs. Even where there is a case for council funding, such local public goods should be produced by the most efficient supplier, whether that is the Council or the private sector (including the voluntary sector). In many cases, contracting out supply to the private sector would be efficient.
- 2.3 The Council states in the Plan that its 'vision for Wellington' is to "promote the well-being of Wellington's economy, culture, environment and communities". While the statement is general and unobjectionable, it does not define the Council's role relative to that of individuals, firms and voluntary organisations. In fact, most social, economic, environmental and cultural outcomes are best achieved through private rather than political means. Voting is not a good way for people to obtain most of the goods and services they want – individual commercial and non-commercial transactions are better. An over-extension of the Council's role is likely to crowd out more efficient private efforts and undermine alternative voluntary cooperation.
- 2.4 The Forum does not support the Council's proposal (in defining its 'vision') of "fostering technological, economic, cultural and artistic creativity and innovation" and "encouraging smart, creative businesses and investing in growing numbers of jobs in the creative sector". We have submitted on a number of occasions that the Council should not be in the business of 'picking winners'. We do not believe that the Council can identify sectors that are somehow preferable to others and therefore deserving of special treatment ('business clusters', 'smart creative businesses'). Comparative advantage is impossible to spot in advance. It is discovered by trial and error by

¹ A public good has the following characteristics:

- Non-rivalry in consumption. A good is 'non-rival' when an individual can consume a unit of it without detracting from the consumption opportunities available to other people. Examples of non-rival goods are atmospheric quality and disease eradication programmes; and
- Non-excludability of benefits. Goods or services generate non-excludable benefits if it is too costly to prevent access to their benefits by people who do not pay. Examples are defence, flood control and cleaner air arising from pollution control devices.

A brief non-technical description of public goods is attached as Appendix II.

entrepreneurs, not by governments or councils. Taxing all businesses to selectively to benefit some will not increase economic activity in Wellington. Competing firms will be unfairly disadvantaged and others will lose resources (skilled labour etc) that the privileged firms will be able to bid away from them. As a result, local growth will be weaker.

- 2.5 Both economic analysis and empirical evidence indicate that such interventions are welfare-destroying. Support for such policies can only be ideological or politically driven. The Wellington City Council's policies are inducing other councils to follow suit – the Auckland City Council, for example, is now proposing to subsidise film-making. Beggar-thy-neighbour policies by councils are not in the country's interests. Naturally, some firms will seek hand-outs and some organisations will continue to lobby the Council on behalf of their members. Many cities in New Zealand and around the world yield to such 'rent-seeking' behaviour. Doing so, however, gives privileges to favoured businesses but harms other businesses and the community at large.
- 2.6 The Forum has submitted over a number of years that the Council's focus should be on the general business environment, not the interests of a few favoured firms or industries. We have said that such discriminatory spending and other Council policies are, at the margin, contributing to an exodus of head offices from Wellington and making Wellington a slow-growing economy. The Council has maintained and expanded these policies despite our criticism. We think the evidence is clear that we have been correct in our judgment, and we fear a continuing loss of business from the region if the Council continues to ignore it. As a business location the main competitor to Wellington is Auckland, and although we are critical of some of the Auckland City Council's decisions, it has accepted a framework consistent with our proposed approach and is now much more focused on its core business than Wellington. We have no difficulty with the idea of the Council providing information and promoting Wellington as a place to do business. More importantly, it should also seek to attract business by minimising rates and regulatory costs, and by ensuring the provision of good quality infrastructure. But it should not target particular industries or subsidise particular firms.

- 2.7 For these reasons we do not support the proposed expenditure of around \$370,000 on 'creative Wellington' initiatives. We continue to believe that the Council should scrap the proposed allocations to the Wellington tourism agency of \$3.6 million and the Wellington business agency of \$1.9 million. Firms that benefit from such activities should pay for them.

3 Exiting from commercial activities

- 3.1 We were pleased that the Council initiated a strategic review of its continued involvement in commercial activities last year. We believe the Council should exit from its involvement in commercial activities.
- 3.2 We strongly endorse the proposed sale of the Council's off-street parking facilities. We note that off-street parking is a private good that could be provided more satisfactorily by the private sector. There is no public good element to off-street parking that would justify the Council's continued ownership of such facilities.
- 3.3 We urge the Council to use the proceeds of any sale to repay debt, and that proposals to reinvest money to support the 'new Creative Wellington – Innovative Capital strategic' be subjected to careful cost benefit analysis and confined to the provision of local public goods.
- 3.4 The Forum was encouraged to hear that a scoping study of the Council's continued ownership of airport shares had been conducted. We are sure that any competent financial advisor would recommend that the Council divest its shareholding in the airport. The Auckland City Council has moved in this direction. We are disappointed with the slow progress the Council appears to be making on this issue, and the lack of any discussion of it in the Plan. The Council does not have control of the airport as an investor, the description of it as a 'strategic asset' is purely rhetorical, and a sale would strengthen the Council's balance sheet and allow it to devote more attention to its core business.
- 3.5 We are gravely concerned about the proposal that the Council and Housing New Zealand form a partnership to provide additional social housing in Wellington. The Plan proposes that \$1.179 million of new investment be jointly funded by the Council and Housing New Zealand. This is simply not an

appropriate local government activity and is a clear illustration in our view of the Council's lack of focus on its core business.

- 3.6 We believe that far from expanding its involvement in housing, the Council should divest the bulk of its housing stock. Auckland City recently sold its rental housing stock; its decision was a strong signal that it was determined to focus on promoting business and economic growth rather than income redistribution. The private market is able to supply accommodation for most people, including low-income individuals. Concerns about the affordability of housing are better addressed through income supplements or other housing policies which are a responsibility of central government rather than through the provision of subsidised housing by councils. The provision of emergency housing would be the main exception to this view.
- 3.7 We were pleased to observe that after years of discussing options for its water business, the Council has agreed with Hutt City to establish a jointly owned company to manage the two cities' water services. It appears that this proposal could achieve worthwhile cost savings.
- 3.8 While the proposed rationalisation of the councils' water businesses is positive, the shareholders will need to pay careful attention to the governance of the company given that it will be a non-profit operation. The difficulties of providing incentives and monitoring performance in a non-profit organisation are substantial. Forms of private participation should be explored within the constraints imposed by the Local Government Act 2002.

4 Limiting its involvement in club goods

- 4.1 We have noted before our belief that the Council should not, in general, be involved in providing or funding club goods. Unlike a public good, people who do not pay can be excluded from obtaining a club good. Thus, as long as the community values the services by more than the costs of providing them, club goods can be produced without Council involvement.
- 4.2 The Council should consider options for divesting club-good services, or at a minimum move to a substantial level of user charges since users of the services are clearly the main beneficiaries. People who use swimming pools and libraries clearly benefit more from them than those who do not. It is neither fair

nor efficient to expect non-users to fund such activities to any significant extent. We support the Council's proposal to set up the zoo as a trust, in the interests of facilitating an expansion of its services and attracting private sponsorship.

- 4.3 The Forum's view (on the basis of the limited information provided) is that the proposal to partially fund a community recreation centre at Tawa College should not be supported given the club good nature of the services that would be produced.
- 4.4 The Council's libraries are a significant cost, and options for increasing user charges should be reviewed. Around 90 percent of the funding for libraries comes from ratepayers' money. The Forum believes that the Council cannot credibly argue that 90 percent of the benefits of library use go to ratepayers other than the users. There are a number of options that could be explored for increasing user funding of the libraries within the constraints of the Local Government Act 2002 and/or for reducing costs. The library should also exit services provided in competition to the private sector such as DVD and video rental.

5 Core services

- 5.1 Roading is a core Council activity. We are pleased at the Council's commitment to maintaining a cost-effective, efficient road network maintained in good order, and its support for ensuring that the transport infrastructure in Wellington is sufficient to meet the region's needs. An efficient road network is likely to make a major contribution to the attractiveness of Wellington for businesses and residents. The current Land Transport Management Bill is not a satisfactory step forward. With economic growth Wellington could face increasing transport problems. We urge the Council to press more actively for improvements to central government transport policies and would be happy to lend our support.
- 5.2 The provision of open spaces including the waterfront areas and parks is core Council business. Projects such as the Oriental Bay beach upgrading, the proposed redevelopment of Cog Park and the creation of the coastal reserve at Evans Bay are public good outputs which are properly the responsibility of the Council. However, the provision of such amenities must be supported by

careful cost benefit analysis to ensure the wise expenditure of ratepayers' money.

- 5.3 The case for the Council providing increased funding to 'events' as proposed in the Plan rests on the possible public good nature of such activities.
- 5.4 Events held, for example, at the stadium would not have public good characteristics. Given that non-payers can be excluded from such events, there is little case for Council funding. Nebulous arguments about the 'feel good' factor produced by hosting events in Wellington should be treated with scepticism.
- 5.5 The arguments that there are spill-over economic benefits or 'multiplier effects' from funding events have been largely discredited in the economics literature.² The supposed spill-over gains are largely expenditure switching from one sector to another (eg the stadium gains but people have less disposable income to spend in cinemas, restaurants and retail outlets). If there are benefits at a local level, these are at the expense of some other part of the country so that there is no net gain at a national level.
- 5.6 The \$2 million of subsidies provided to Te Papa cannot be justified on the grounds that economic benefits arise from encouraging tourists to visit Wellington. Continued subsidisation by the Council effectively facilitates free riding by the users of the museum on the payments by ratepayers and taxpayers.
- 5.7 On the other hand, an event held in a public space, such as the Cuba Street Carnival, has public good characteristics and Council funding might be justified. Even so, the Council needs to ensure that the benefits of providing funding outweigh the costs and that Council involvement does not crowd out alternative funding options, such as private sector sponsorship.
- 5.8 The Forum notes that it has no way of judging whether the proposed allocation of \$1.15 million to an Events Development Fund (increasing total funding for events to \$2.6 million) might be reasonable, given the lack of any justification for that quantum in the draft Plan.

² See, for example, New Zealand Business Roundtable, *Should Governments Subsidise Stadiums and Events?*, New Zealand Business Roundtable, June 1999.

6 Funding the Council's activities

- 6.1 We remain concerned that the overall level of the Council's spending and its rates burden are far too high. In this year's Plan, net operating expenditure is forecast to increase by around 5 percent and the Council's net operating deficit will be around \$9 million. By contrast, Auckland City Council spending is forecast to increase by only 8 percent over the next 10 years in real terms, an increase of around 0.8 percent a year and lower than was projected last year. Wellington City's rates are proposed to increase by 2.7 percent this year. Although this may be a modest improvement on past performance, net operating expenditure growth will still exceed the rate of inflation (even allowing for population growth) and the Council's equity will reduce. Our view is that the Council's expenditure and rates need to shrink.
- 6.2 The Forum is pleased at the continued progress towards reducing the differential rating of commercial and residential ratepayers. However, we remain of the view that the rate of progress is too slow, and that there is no justification for a differential remaining at the end of the adjustment period. An acceleration of the programme would be a strong signal that the Council wants to be more pro-business and pro-economic development.
- 6.3 We note also that the funding of depreciation places an important constraint on the Council and is therefore desirable. We are therefore concerned at the proposal to continue to under-fund the depreciation of some of the Council's assets.

7 Benchmarking performance

- 7.1 The Forum's analysis suggests that Wellington is a high spending council by New Zealand standards. We note, however, the limited information available to ensure that 'like with like' comparisons with other councils are made in reaching this conclusion. Nevertheless, we believe the Council should, in the interests of its own management as well as the interests of its ratepayers, be making a greater effort to obtain and make publicly available benchmarking information. Comparative information can help councils to assess where their performance might be lacking and allow them to identify opportunities for improvement. Benchmarking would ensure ratepayers were better informed as

to the performance of councils. At our last discussion it was agreed that the Council would provide us with comparative information which it regarded as reliable. We understand this is still being prepared.

- 7.2 We have also been urging councils to publish more detailed itemised rating assessments in the interests of greater accountability and transparency. Although the Rating Act provides for such assessments on a voluntary basis, councils have been slow to provide them. A number of the small to medium-sized councils have been able to provide the relevant material, so it should not be unduly costly or difficult for the Council to do so.

8 Significance policy, policy on partnership with the private sector, and community outcomes

- 8.1 The Forum doubts that the requirement in the Local Government Act 2002 for councils to consult on matters deemed to be 'significant' will place effective constraints on their activities.

- 8.2 However, in the absence of any other effective constraints under the current legislation we suggest that the Council's significance policy be used to help confine the Council to activities where it has a comparative advantage. The Forum suggests, therefore, that a decision should be considered significant if:

- the proposal does not involve the supply of a local public good or provision of regulatory services required by central government.

- 8.3 The Forum notes also the vulnerability of councils to special interest group lobbying where parties attempt to secure benefits to themselves that are paid for by others. It therefore suggests that a decision also be considered significant if:

- the costs of a proposal are not borne largely by those parties who will benefit from it.

- 8.4 The Forum notes that a financial significance threshold, as proposed by the Council, might provide a useful constraint. However, it is unclear whether the proposed \$10 million threshold relates to the impact of a proposal in a single year or over time, and whether this is a gross or net figure. The Council could instead define the threshold in terms of the net present value impact of a proposal over the ten-year planning period. A threshold of \$10 million might

be acceptable for a ten-year horizon but would be too high if it related to a single year.

- 8.5 In relation to the policy on partnership with the private sector, the Forum notes the difficulty of defining meaningful general principles at an abstract level. Given that caveat, the broad principles proposed by the Council appear reasonable. Where an actual public private partnership proposal was being considered (and it was significant), the Forum would expect, as suggested in the introductory comments to the policy, that the Council would undertake "a detailed analysis of structure, risks, and management provisions" before proceeding.
- 8.6 The Forum notes the requirement in the Local Government Act 2002 (s91) for councils to undertake a process to identify "community outcomes" for the region and would be interested to know the Council's proposed timetable for this work. The Forum is concerned to ensure that the business community, which pays around half of the Council's rates, is fairly represented in the process the Council adopts for this purpose. We note the importance of ensuring that the chosen outcomes promote efficiency and economic growth, and that the Council's role in achieving any desired outcomes is confined to the provision of local public goods.

9 Conclusion

- 9.1 We remain of the view that the Council needs to make a much bigger effort to restrict itself to activities where it has a comparative advantage, ie providing local public goods and regulatory functions conferred on it by central government. It should exit from the provision of private goods and review its involvement in the provision of club goods. By focusing on its core activities, the Council could cut expenditure and rates, which we believe is an essential step towards making Wellington an attractive place for business, and for the wider community.

The Local Government Forum

The Local Government Forum was established in 1994 to promote greater efficiency in the local government sector and to contribute to debate on policy issues affecting the sector.

The Forum comprises business organisations that have a vital interest in the activities of local government. Member organisations include:

- Business New Zealand
- Federated Farmers of New Zealand
- New Zealand Business Roundtable
- New Zealand Forest Owners' Association
- Property Council of New Zealand
- Retail Merchants Association of New Zealand

Appendix II

A SIMPLE DESCRIPTION OF PUBLIC GOODS

There is much confusion about the term 'public goods'. Yet a clear understanding of it is important for deciding what things we need governments – central and local – to be involved in.

As the name suggests, the job of the public sector is essentially to provide public goods that people can't provide for themselves (in the case of central government, it is also to provide some level of welfare and social services). The job of the private sector is to provide private goods.

Clearly a public good is not just something that is 'good' for us. Food, gymnasiums and dental care are all 'good' for us but they don't need to be provided by the public sector.

Also many services called public are not public goods – they are simply services supplied to the public. Public transport is a case in point – bus, train and taxi services can be provided by private businesses.

A first approximation of a public good is something that can't be charged for. If private firms can sell goods and services to customers for a price, they are trading in private goods. Fares meet the cost of taxi services.

An example of a genuine public good – for which private supply is not feasible – is national defence. Individual beneficiaries can't be charged for it. Defence expenditures must be funded from taxation.

Streetlighting and stormwater are examples of local government public goods.

More rigorously, public goods have two distinct aspects. First, non-payers can't be excluded from the benefits of the good or service so there is a 'free-rider' problem (think national defence). Second, one person's use of them does not limit their availability to others (think streetlighting).

Such goods may be supplied inadequately through private initiatives – commercial or otherwise.

Markets can overcome some of these problems. Free-to-air broadcasting does not have to be financed from taxation: advertising is a source of revenue. Cable television services can exclude non-subscribers.

Also there are indirect means of covering costs: shopping malls provide lighting and parking but recover costs through rentals.

Some items are partly public and partly private goods. Patents provide private returns to inventors but on their expiry the invention becomes a public good.

With advancing technologies, what were once public goods (eg basic science) are sometimes capable of being produced privately – Celera's private human genome project is an example. Also people can come together voluntarily – eg in environmental and cultural organisations – and provide a tolerably efficient level of public goods.

The fact that market or voluntary solutions may not be perfect does not mean that government solutions will be better – inadequate information and special interest politics bedevil government solutions.

Finally, governments don't need to provide all public goods themselves. Often they can contract out their provision.

The number of genuine public goods is quite small. Central and local governments have expanded far beyond their core roles to undertake things that would be better left to firms or the voluntary sector.