

Submission

by

Business|NZ

to the

Local Government and Environment Select Committee

on the

Local Government (Rating) Bill

26 September 2001

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LOCAL GOVERNMENT (RATING) BILL
SUBMISSION BY BUSINESS NEW ZEALAND
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1. Introduction

- 1.1 This submission is made on behalf of Business New Zealand, incorporating regional employers' and manufacturers' organisations. The regional organisations consist of the Employers and Manufacturers Association (Northern), Employers and Manufacturers' Federation (Central), Canterbury Manufacturers' Association, Canterbury Employers' Chambers of Commerce, and the Otago-Southland Employers' Association. Business New Zealand represents business and employer interests in all matters affecting those sectors.
- 1.2 One of Business New Zealand's key goals is to see the implementation of policies that would see New Zealand retain a first world national income and to regain a place in the top ten of the OECD in per capita GDP terms. This is a goal that is shared by the Government. It is widely acknowledged that consistent, sustainable growth in real GDP per capita of well in excess of 4% per annum (and probably closer to 7-8%) would be required to achieve this goal. Continued growth of around 2% (our long-run average) would only continue New Zealand's relative decline.
- 1.3 The health of the economy also influences the ability of a nation to deliver on the desirable social and environmental outcomes that we all want. First class social services and a clean and healthy environment are possible only in prosperous, first world economies.
- 1.4 The local government sector's performance and its decisions on activities and funding impact significantly on the country's overall economic performance and our ability to move back into the top 10 of the OECD. For the year ended June 2000, total operating income for local authorities was \$3,739 million, nearly 4% of GDP, and of that amount, over half (\$1,977 million) was from

general rates. The assets of the sector (net of debt) amount to around \$42 billion, which is considerably more than the net asset value of all companies listed on the New Zealand Stock Exchange (around \$27 billion).

- 1.5 Business New Zealand therefore appreciates the opportunity to make a submission on the Local Government (Rating) Bill. The local government sector impacts upon all citizens and ratepayers, be they residents or businesses, so we welcome a thorough and principled review of the activities, funding, and powers of local authorities.
- 1.6 However, Business New Zealand has significant concerns about the process of reviewing local government legislation as well as reservations with a number of the specific proposals set out in the Bill. These are set out in the remainder of this submission.
- 1.7 Business New Zealand is also a member of the Local Government Forum, which has also made a comprehensive submission on this Bill. We fully endorse the points made in the Forum's submission.

2. Concerns with the Reviews of Local Government Legislation

- 2.1 Business New Zealand notes that the Government has been undertaking a series of major reviews into local government, most notably into the Local Government Act 1974, the Rating Powers Act 1988, and the Local Elections and Polls Act 1976. While we support the need for a comprehensive review of the activities, funding, and powers of local government, we are disappointed that these important and inter-related reviews have been carried out separately and on different timeframes.
- 2.2 It is particularly inappropriate that this Bill was introduced into the House before submissions closed on the Review of the Local Government Act. The Minister announced, in her first reading speech, that the Rating Bill is to be passed even before legislation to implement the outcome of the Review is introduced. Separate, but inextricably related, reviews on the powers of local

government and the funding of local government's activities should not have proceeded on different timeframes and should not be considered by Parliament in isolation. As we have yet to be informed of any credible rationale for this approach, speculation that the reviews were deliberately separated to minimise the impacts of extensive reform proposals is inevitable.

- 2.3 Business New Zealand has fundamental concerns with the Review of the Local Government Act and we made a comprehensive submission to the Department of Internal Affairs. In particular, we expressed grave reservations about the proposal for local authorities to be given a broad power of general competence combined with a proposed purpose statement that would encourage councils to actively promote social, cultural, environmental, and economic well being.
- 2.4 Instead, we believe that the Government should have undertaken a single first-principles review on the activities, funding, and powers of local government and it should have involved ratepayers and businesses in the development of the proposals as well as the local government sector.
- 2.5 In the light of our concerns about process and doubts about many of the specific proposals contained in the discussion document, our submission recommended that an experts group (including representatives of the business sector) be tasked with considering submissions and making recommendations to the Government on how best to progress the Review.
- 2.6 Similarly, we recommend that consideration of this Bill should be held over and merged with the Review of the Local Government Act. The experts group mentioned in paragraph 2.5 above should also examine the rating powers of local authorities.

3. Local Government (Rating) Bill

- 3.1 At present, local authorities' decisions on funding are constrained by the Rating Powers Act 1988. The previous Government commenced a review of

this Act in 1998. While it was initially intended to be an ambitious, first-principles review of the funding of the local government sector, we understand that over time it was scaled down to become a more narrow review of rating powers. The outcome of this review is the Bill now being considered, which is intended to replace the Rating Powers Act 1988.

- 3.2 The Government states that this Bill updates and simplifies the existing law. This may be true, but we believe that while many existing provisions are largely carried over from the existing legislation, the Bill does not go far enough in addressing some fundamental problems with local authority rating practices. At the same time, some of the proposed changes are significant and are in the wrong direction (most notably, the repeal of the requirement for councils to seek a Special Order for rating differentials).
- 3.3 On balance, as it is currently written, Business New Zealand recommends that the Bill should not proceed. As discussed in paragraph 2.6 above, we believe that the Bill should be held over and merged with the Review of the Local Government Act.
- 3.4 Specific concerns with the Bill are discussed in the following section. The individual recommendations are made without prejudice to Business New Zealand's primary recommendation that the Bill should not proceed in its current form.

4. Specific Concerns with the Local Government (Rating) Bill

Exemptions (Clauses 7-9 and Schedule 1)

- 4.1 At present there is a long list of rates-exempted properties and it is proposed in the Bill that this status quo will be maintained.
- 4.2 There are many categories of exemptions listed in Schedule 1 and we believe that anomalies are likely to exist in such a large list. We believe that there should be as few exemptions as possible and that a first-principles review of exemptions should have taken place. This does not appear to have occurred.

- 4.3 We believe that the existing rating base is unduly narrow and that substantial exemptions confer hidden subsidies on certain activities. The principles of neutrality, transparency, and accountability, which are a cornerstone in the context of central government taxation (where there are very few concessions and exemptions – GST being a particularly relevant example), should be equally applied to rates.
- 4.4 Business New Zealand believes that the tax base should be broadened, by removing exemptions except where there is a valid efficiency reason for not doing so. If councils wish to subsidise particular activities they should do so transparently by way of grants.
- 4.5 However, any broadening of the tax base must be accompanied by a reduction in the level of rates and not an increase in council spending, so that the overall effect is revenue neutral.
- 4.6 We would therefore prefer a reduction in the number of exemptions, providing that there is a mechanism to ensure that rates are reduced by a corresponding amount.

Owner vs. Occupier Liability for Rates (Clauses 10-12 and Clause 60)

- 4.7 The Bill clarifies that the unit liability for rates will generally be based on the concept of title. That is, owners rather than long-term occupiers would become primarily liable for the payment of rates. This could have implications for a shopping centre with many separately leased shops, for example, and would have the potential to become unnecessarily complex and expensive in terms of professional advice.
- 4.8 We also note that it could also penalise organisations that are currently exempt from rates if they do not own the building they occupy (e.g., a church leasing space in a commercial building), which might have to pay a higher rent

or lease if the building owner is liable for the full amount of rates due on the building.

General Rates (Clause 13)

- 4.9 While user charges are the most efficient method to recover costs for private goods and services, local (property-based) taxation is probably the most efficient way to fund local public goods. While we would support the continuation of general rates as a significant source of revenue for councils, this proposition must be assessed on a case-by-case basis as many goods, which are often regarded as 'public', can be better provided privately or at least funded by user charges.
- 4.10 In practice, however, it would seem that few councils have made such assessments, despite the provisions of the Local Government Amendment Act (No.3) 1996 which supported the recognition of economic efficiency and transparency. Unfortunately, many local authorities have instead sought to justify existing activities and funding policies rather than conduct first principles examinations of such arrangements.
- 4.11 Business New Zealand recommends that councils should be required to more robustly assess their activities and the most efficient way these should be funded and provided. We also recommend that councils should be encouraged to maximise the outsourcing of goods and services and make greater use of user charges.

Rates Differentials (Clause 14 and Schedule 2)

- 4.12 It is of fundamental concern that local authorities would, in practice, find it easier under the new legislation to impose rating differentials. At present, local authorities wishing to charge certain types of ratepayers more than the uniform rate must first seek a Special Order. This Bill, however, would give them *discretion* to strike rates differentials. Councils would be able to charge commercial, retail and industrial ratepayers more (or certain groups less) than

the general rate, and all that would be required is for the rating policy to be set out in the council's annual plan.

- 4.13 Business ratepayers already face a disproportionately high rates burden through rates differentials. For example, Manukau City Council charges businesses four times more in rates than residences for a property of equivalent value and Wellington City Council six times more. The result is that businesses pay over 50% of total rates on a nationwide basis. Rates differentials are grossly inequitable considering the beneficiaries of most council services (such as libraries, swimming pools etc) tend to be residents rather than businesses.
- 4.14 Business New Zealand strongly disputes the assertions made by some local authorities that businesses are rated more due to a greater 'ability to pay'. The vast majority of New Zealand businesses are very small (around 85% employ fewer than five people) and most have very low taxable incomes. Statistics from Inland Revenue indicate that 77% of companies have no assessable income at all, while another 15% earn less than the average wage. Rates differentials are therefore an onerous burden on the business sector. Unfortunately, however, it seems that businesses are an easy target from which to raise revenue, simply because there are far more residential ratepayers (i.e., voters) for councils to be concerned about.
- 4.15 Rates differentials are also unfair on businesses competing with those operating as home-based businesses. This is a widespread problem, but a specific example that has been brought to our attention is in the accommodation sector. While bona fide motel and hotel operators are subject to commercial rates, we understand that many 'bed and breakfast' establishments more often than not pay residential rates, despite operating as businesses and being registered for GST. It would be far more equitable to simply abolish rates differentials.
- 4.16 While local authorities should be able to tax a clearly identified set of ratepayers who largely benefit from particular public goods or services

(through targeted rates), safeguards need to be in place against the abuse of powers to discriminate against classes of ratepayers. Rates differentials have enabled councils to impose oppressive costs on businesses and we believe that these differentials should be abolished.

- 4.17 We therefore recommend that the provisions that allow for rates differentials should be repealed. At the very least, the existing provisions in the Rating Powers Act that require local authorities to seek a Special Order before setting rating differentials should be retained.

Targeted Rates (Clauses 16-20 and Schedule 3)

- 4.18 Benefits from certain local public goods may clearly accrue to a particular group of ratepayers. Therefore, it may be desirable to confront people who want a local authority to supply such goods with the true cost of supply, which is where targeted rates would come into play.
- 4.19 However, there is a risk that targeted taxation may also be used by a council to force a minority to pay for benefits enjoyed by others, in much the same way as rating differentials do at present. This concern is real – there is little historical evidence for believing that local authorities would use any power to tax on a discriminatory basis in a disciplined manner. We would be particularly concerned were targeted rates to be used in this manner for the promotion social, cultural, environmental, or economic “well being”. We therefore believe that targeted rating should only be permitted where a clearly identified community is provided with a distinctly different level of service from that of other ratepayers. In this case the targeted rate should reflect the difference in service level.
- 4.20 We also believe that there should be recourse (other than through the Annual Plan process) for ratepayers to dispute what a local authority considers to be the “true cost of supply”. Such recourse should be prompt, transparent, and inexpensive.

- 4.21 Therefore, while we support the principle of targeted rates, in practice we recommend that there should be a high threshold for their implementation.

30% Limit of Revenue from Uniform Annual General Charges (Clause 21)

- 4.22 Uniform Annual General Charges are fair in that they ensure that all ratepayers contribute a minimum 'flat' amount for the provision of public goods enjoyed by all. Economic theory holds that 'flat' broad based taxes (such as a Uniform Annual General Charge) are also more economically efficient than those that are narrowly based and 'progressive' (such as differential-based property taxes).
- 4.23 Removing the 30% cap could assist in reducing the relative burden faced by business ratepayers, who generally pay a disproportionately high amount of rates relative to residents.
- 4.24 We therefore recommend the removal of the 30% limit of revenue from Uniform Annual General Charges.

Rates Assessments and Invoices (Clauses 44 and 45)

- 4.25 A critical funding issue for ratepayers is transparency in rating procedures and we predict that this would become even more important if the proposals contained in the Local Government Act Review discussion document were to be adopted. Local authorities must be able to demonstrate where the burden and benefits for services will lie. Although some have made voluntary progress in this area, we believe that all councils must be required to provide clearly and easily understandable itemised assessments and invoices to all ratepayers so that they would be in a position to adequately judge whether their council is delivering value for money.
- 4.26 Itemised assessments and invoices should provide individual ratepayers with a breakdown of the amount they contribute to the following categories of council services:

- Civil defence;
- Community safety;
- Community sponsorship;
- Economic development;
- Environmental planning;
- Governance and strategy;
- Libraries, art galleries and museums;
- Parks and reserves;
- Regulation and inspection;
- Reticulation of storm/waste water;
- Roading; and
- Solid waste removal;

4.27 However, clauses 44 (regarding rates assessments) and 45 (regarding rates invoices) continue to leave it up to individual councils to decide whether or not to provide more detailed information to ratepayers along the lines suggested above. This is inadequate when such transparency would be easily enabled by modern information technology.

4.28 Business New Zealand recommends that all councils should be required to provide itemised rating assessments and invoices providing information on the amounts the ratepayer is contributing to various council services and activities.

Rates Remissions and Postponements (Clauses 84-89)

4.29 A concession to one ratepayer requires additional tax to be imposed on other ratepayers. Councils are not well placed to judge the ability of individual ratepayers to pay. Problems with the present rating system could be better addressed through other means (for example, by reducing spending or removing discriminatory taxes and differential rating).

4.30 Councils should have the power to postpone or remit rates in cases of extreme hardship, but these provisions need to be tightly framed so that councils do not unduly subsidise failing businesses and imprudent ratepayers

at the expense of other ratepayers. Nor should councils be permitted to postpone or remit rates simply on the grounds of promoting social or cultural “well being”. The Bill, however, proposes that rates may be remitted or postponed if the criteria and conditions of the local authority’s policies on these issues are met. This would not be sufficient in practice if the council were to choose to adopt a ‘soft’ policy.

- 4.31 We recommend that powers to remit or postpone rates should be more tightly framed.

Rating of Maori Land (Clauses 90-116)

- 4.32 There are nearly thirty clauses in this Bill making separate provisions for the rating of Maori land, continuing the status quo in the Rating Powers Act 1988. These separate provisions add considerable complexity to the legislation.

- 4.33 We recommend that all land, including Maori land, should be treated on a similar basis unless there are valid efficiency grounds for not doing so.

5. Recommendations

5.1 Business New Zealand recommends that:

- (a) Consideration of the Local Government (Rating) Bill should be held over and merged with the Review of the Local Government Act.

5.2 The following recommendations on specific aspects of the Bill are made without prejudice to recommendation 5.1(a):

- (b) The scope of rating exemptions should be reduced, providing that rates are reduced by a corresponding amount;
- (c) Councils should be required to more robustly assess their activities and the most efficient way they should be funded and provided;
- (d) Councils should be encouraged to maximise the outsourcing of goods and services and make greater use of user charges;
- (e) The provisions in the Rating Powers Act 1988 that allow for rates differentials should be repealed;
- (f) Targeted rates should be permitted, but that there should be a high threshold for their implementation;
- (g) Ratepayers should have recourse (in addition to the Annual Plan process) for disputing Council assessments of the true cost of supply;
- (h) The 30% limit of revenue from Uniform Annual General Charges should be repealed;
- (i) All councils should be required to provide itemised rating assessments and invoices;
- (j) Powers to remit or postpone rates should be more tightly framed; and
- (k) All land, including Maori land, should be treated on a similar basis unless there are valid efficiency grounds for not doing so.