Submission by

BusinessNZ

GROWING PROSPERITY AND POTENTIAL

to the

Department of Internal Affairs

on the

Fire and Emergency New Zealand Funding Review

Consultation Document

February 2020

**FIRE AND EMERGENCY NEW ZEALAND FUNDING REVIEW
CONSULTATION DOCUMENT
SUBMISSION BY BUSINESSNZ[1]**

1.0 SUMMARY

1.1 BusinessNZ welcomes the opportunity to comment on the Fire and Emergency New Zealand Funding Review Consultation Document ("the Consultation Document").

1.2 First, BusinessNZ would like to acknowledge that the Government is endeavouring to address the deficiencies of the previous Government's decisions on the future funding of Fire and Emergency New Zealand (FENZ). However, rather than implementing the changes proposed in the current discussion document, BusinessNZ recommends the Government moves towards a risk-based approach to funding the FENZ.

1.3 Given transitional funding arrangements (largely based on the status quo) are already in place, there is no need to rush funding changes. It is important to ensure that what is finally put in place largely meets the funding principles set out in the Fire and Emergency Act 2017.

1.4 To be clear, BusinessNZ strongly supports the Fire and Emergency New Zealand (FENZ) Act 2017 funding principles as they are consistent with those in the Treasury *"Guidelines for Setting Charges in the Public Sector* (April 2017). From BusinessNZ's perspective (and backed up by other independent commentators and researchers), the fundamental problem is with the Act's proposed regime which on several fronts fails to comply with the funding principles.

1.5 For clarity, this submission is in several sections, not necessarily in any order of importance as all are important in their own right.

1.6 Section A deals with the funding principles which should underpin a desirable funding regime based on risk (cost) rather than the current system of levies based on insurance coverage.

1.7 Section B looks at a potential model of funding more closely related to risk.

[1] Background information on BusinessNZ is attached as Appendix 1.

1.8 Section C looks at other issues in addition to risk-funding (outlined in Section B), including:

- the potential for experience-rating and other incentive mechanisms to reduce costs, including discounts for users who undertake significant investment in fire minimisation initiatives (e.g. sprinklers).
- the potential for partial user-charges.
- how to deal with the possible exemptions' issue e.g. where industrial sites and large enterprises have their own fire protection systems on standby or where it would be impractical for the FENZ even to provide services (e.g. to the underground power station at Manapouri, owned by Meridian Energy).
- the potential for large businesses to enter into separate supply agreements with FENZ with costs set accordingly.
- whether there should be caps on levies.

1.9 Section D looks more specifically at potential levy collection mechanisms.

1.10 BusinessNZ is ready to discuss our submission with Internal Affairs officials if this would be considered useful. As mentioned earlier, BusinessNZ would encourage officials not to rush this process, but ensure any funding regime is fit for purpose for the foreseeable future with funding better aligned to the risk (cost) imposed on FENZ.

Recommendations

BusinessNZ **recommends** that:

In order to significantly improve the allocation of the costs of FENZ service provision, the Department of Internal Affairs (DIA) clearly identifies the types of services provided, estimates the costs of each main service and better aligns these with user service charges (based on actual risk).

BusinessNZ **recommends** that:

The Government (in collaboration with private sector expertise) investigates a system of funding whereby the costs are sheeted home more appropriately to those who utilise the fire service (a risk-based approach). A possible model is outlined in Section B of this submission as a discussion starting point. The model strongly meets the principles of a good funding system outlined in the Fire and Emergency New Zealand (FENZ) Act 2017.

2.0 SECTION A: FUNDING PRINCIPLES

2.1 Developing a rigorous approach to funding first involves determining the nature of fire and rescue services. Public goods (which by definition include non-rivalry in consumption and non-excludability), are generally best funded out of general taxation but clearly with private goods (where the benefits and costs are largely of a private nature, with few externalities or spillovers), the costs should be funded as much as possible via user charges. User charges encourage individuals and businesses to undertake effective and efficient risk minimisation strategies based on known risks.

2.2 If individuals can effectively free-ride off third parties they will likely reduce the amount of effort (time and money) spent in trying to minimise damage to property.

2.3 Many desired outcomes and outputs of fire and rescue services involve the protection of the wider public interest of the New Zealand economy, its citizens and the environment. The benefit is to *all* New Zealanders, not just selective (private) groups or particular sectors of the economy but to New Zealand Inc. Fire and rescue activities are therefore, at least partially, a public good.

2.4 On the other hand, fire and rescue activities have a significant private good aspect which requires giving serious consideration to basing a large part of the funding on the risk or cost of services provided by FENZ to service users, with provision for at least partial user-charges.

2.5 The above concept is not necessarily unique or new but is widely practised in many overseas jurisdictions (as outlined in the Appendix to the Consultation Document along with other more in-depth papers reviewing overseas fire funding regimes).[2]

2.6 Significant improvements to both the current (transitional) and proposed funding regimes outlined in the Discussion Document could be made by clearly identifying the types of services provided by FENZ, estimating the costs of each of the main services and aligning these better with the charges imposed on the beneficiaries (users) of such services.

2.7 The above exercise would, to a much greater extent, allow charging for FENZ's services to be based on the expected risk and level of use.

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[2] See for example a comprehensive report prepared for the Property Council of New Zealand by TDB Advisory entitled *"Funding Regime for Fire & Emergency New Zealand – A Best-Practice Review" (5 October 2017.)*

2.8 Notwithstanding the above, BusinessNZ notes the Consultation Document's statement on p.6 that funding FENZ predominantly through general taxation is not on the agenda. BusinessNZ would hope this does not mean the Government will not provide appropriate funding for FENZ's public good aspects of FENZ activities. For example, it is noted that currently NZ firefighters are engaged in helping fight significant bushfires in Australia and their efforts have been much appreciated by both the Australian Government and the Australian public in general. Clearly funding for such activities should be via general taxation not a burden on insurance holders in NZ.

2.9 BusinessNZ is concerned the previous Government, in BusinessNZ's opinion wrongly, from a public policy point of view, effectively excluded general taxation as a viable funding mechanism, making only very minor payments (around $10 million per annum) in relation to the public good aspect of FENZ.

2.10 The above comments are clearly reinforced by numerous previous discussion documents from government agencies stating that expectations of the Fire Service have changed and will continue to change. FENZ (and its predecessor) services have adapted to changing community expectations and needs by responding to non-fire emergencies, such as swift water rescue, storm damage, medical emergencies, and motor vehicle extrications. These services are now part of the fire service. There are also more international responses, such has the FENZ helping with International Urban Search and Rescue (USAR). The (previous) rural fire sector also joined in international responses to wildfires in places such as Australia, Canada and the United States of America. The consequence of these changed expectations is an increasing need for resources, training and ongoing support for non-fire service and international activities.

2.11 Notwithstanding the above, it is understood that under an International Arrangement, the cost of airfares, daily rate for wages, accommodation and food etc may be covered by the requesting overseas fire agency which is seeking support.

2.12 A further justification for a greater taxpayer contribution to FENZ funding is that there are significant risks attached to government service provision where levy payers have little or no say in how services are provided or, perhaps more importantly, in how much they are required to pay – irrespective of services consumed.

2.13 A significant issue, cutting across all government services/regulatory enforcement, is what an appropriate charging/levy regime might be where there is no contestability in service provision. In normal competitive markets, individuals will make trade-offs between price and quality of service, along with a host of other factors.

2.14 Where an agency seeks to recover some or all of the costs of service/regulatory provision from the users or direct beneficiaries of that service, the public or individuals paying for the service need to be assured charges set are not excessive in relation to costs incurred, and take proper account of efficiency and equity considerations.

2.15 The dangers with what are effectively monopoly rights in relation to fire service provision (and guaranteed funding) appear to be threefold.

2.16 First is the concern that the price of a service set by a private business or in this case, the fire service, will exceed what it would have been had service provision been contestable.

2.17 The second is the potential for the fire service to provide a sloppy service in the knowledge that there are effectively no other competitors in the market.

2.18 The third (the corollary of the second and more likely), is the potential for the fire service to provide a gold-plated service in the knowledge that any increased costs can be simply passed on to private sector businesses and individuals via the insurance levy.

3.0 SECTION B: FUNDING MODEL BASED ON RISK (COST)

3.1 A potential model more closely related to risk is set out below. Under this model, what the beneficiaries of fire service provision pay is more closely aligned to the actual costs associated with risk but within the confines of an insurance-based risk assessment (i.e. pooling similar risks within the same category). It should be noted that risk-rating is practised to varying degrees in several overseas jurisdictions.

Potential Risk (cost) model

Beneficiary Group?	Risk (Cost) Group?	Charging (Levy) Base?
Residential	Residential	Flat rate per dwelling unit?
Industrial, commercial and rural buildings	High risk	Rate per sqm metre of building?
Industrial, commercial and rural buildings	Medium risk	Rate per sqm metre of building?
Industrial, commercial and rural buildings	Low risk	Rate per sqm metre of building?
Rural vegetation	High risk	Rate per hectare?
Rural vegetation	Medium risk	Rate per hectare?
Rural vegetation	Low risk	Rate per hectare?
Motor vehicles	Small on-road vehicles (would need to be classified)	Flat rate per vehicle?
Motor vehicles	Large trucks/higher risk group depending on material being moved (would need to be classified)	Flat rate per vehicle type?
Public buildings/medical emergency/natural disasters (flooding etc) plus "other" e.g. search and rescue, overseas assistance etc	Public good (generally speaking), although it is accepted there are elements of private goods in here as well)	Possible lump sum via consolidated account?
"Other"	?????	Possible lump sum via consolidated fund and/or user charges where practicable?

3.2 Notwithstanding the above, it may be necessary to consider the inclusion of other categories such as structural property that does not neatly fit into the residential, industrial or rural categories e.g. schools, hospitals, civic buildings (community halls), churches and so on. And there is a question whether categories of non-structural assets should also be captured e.g. stock, house contents, forests etc, particularly as it is desirable to have as broad a levy base as practicable. The need for balance between equity and the transaction costs involved will have to be considered.

3.3 While the above is simply a back of the envelope approach to risk rating and would require further work, including allocating FENZ costs appropriately across different risk groups, it would largely meet the funding principles set out in the Fire and Emergency New Zealand (FENZ) Act 2017 and which the Consultation Document states will be retained as part of the current funding review (which BusinessNZ supports).

3.4 These principles are outlined on p.12 of the Consultation Document:

(a) a **stable** source of funding to support FENZ in the performance of its functions and duties and exercise of power under this Act:

(b) **universal,** ensuring FENZ's costs are generally shared among all who will benefit from their potential use:

(c) **equitable,** so policy holders generally pay a levy at a level commensurate with their use of, or benefit from the potential use of, FENZ's services and with the risks associated with the activities they carry out (but without the need to observe strict apportionment according to use, benefit, or risk):

(d) **predictable,** enabling policyholders and levy payers to predict the amounts they will need to pay, and FENZ to predict how much levy income it will receive:

(e) **flexible,** allowing the levy to adapt to:
- (i) changes in the use, benefit, or risk associated with those who will benefit from the potential use of FENZ's services; and
- (ii) variations in FENZ's costs; and
- (iii) changes to the expectations of the Crown and to FENZ's strategic needs.

3.5 The above risk-based model would not be unique in NZ. The Accident Compensation Corporation (ACC) already provides an excellent model of how individual businesses are risk-rated based on the costs associated with accidents within broad categories and levies set accordingly. On top of this there is potential for experience-rating where individual companies receive discounts and/or loadings on premiums depending on their accident costs over time.

3.6 Every employer is allocated a classification unit (CU) derived from the Australian and New Zealand Standard Industrial Classification (over 500 CUs) and these CUs aggregated with other similar risk groups (around 40).

3.7 Obviously it would be impracticable to have 40 or so risk classifications in respect to fire insurance; getting such granular information in order to make reasonable (statistically credible) risk (cost) assessments would be near impossible. However, classifications organised into 10-12 groupings (as outlined above) based on historical FENZ data on accident type and cost would seem feasible, accompanied by information from local councils on housing and building types. Possibly Land Information NZ (LINZ) could also assist.

3.8 It might be desirable (given transaction costs and the difficulty of getting enough data to make decisions on type of houses for example), to apply a flat standard levy to residential houses and/or motor vehicles (where FENZ can be involved in providing accident services such as jaws of life etc).

3.9 BusinessNZ does not have a firm view on the number of classifications needed but it is likely that when the costs of service provision are relatively low (and where user-charges are not practicable), a flat levy could be useful for administrative purposes, as in the case of motor vehicles. This could be derived from the annual Motor Vehicle Licensing regime which currently includes an ACC element together with a general fee for issuing the annual licence.

3.10 A separate section later in this submission deals with options for collecting costs (levies) as their collection could be controversial and would need to be discussed with the specific sectors and industries potentially required to collect such levies.

3.11 Finally, a number of overseas funding regimes can provide insights into what is practically feasible when determining risk. Some possibilities are size of property (square metres), hazard factors, the ability of FENZ to respond rapidly and so on.

3.12 It should be noted that risk factors applying overseas do not generally include the value of the property as the value of a house/building bears little, if any, relationship to the cost of putting out a fire. Obviously, size of building, materials etc will be relevant and should ideally be included in any risk-rating regime where practicable.

4.0 SECTION C: OTHER ISSUES REQUIRING CONSIDERATION

4.1 While the above section suggests a risk-based approach to funding the fire service (alongside general taxation for the public good aspects and miscellaneous costs), several issues are worth considering together with risk-based funding, aligning levies to actual risk and experience even more closely.

4.2 Many events involving fire service use cannot be pre-determined making some form of socialisation of costs (based on broad risks) appropriate (as outlined in Section D). There are several issues that might need to be considered if government is keen to progress beyond broad categories of risk.

4.3 Section C looks at the potential for experience-rating and other incentive mechanisms to reduce costs, including the potential for partial user-charges or discounts for users who undertake significant investment in fire minimisation initiatives (e.g. sprinklers), dealing with the desirability of exemptions for example, for those industrial sites and large enterprises with their own fire protection systems on standby or where it would be impractical for FENZ even to provide services (e.g. to the underground power station at Manapouri owned by Meridian Energy). Whether there should be caps on levies is also discussed, along with the potential for large businesses to enter into separate supply agreements with FENZ with costs set accordingly.

4.4 Some of these issues, in no particular order, are outlined below.

4.5 BusinessNZ does not necessarily have strong views on possible options particularly given they would likely involve issues with transaction costs. However, some members have raised them on previous occasions, so BusinessNZ feels duty-bound to at least offer them for consideration in relation to any future funding arrangements. It should be noted that such matters can be relevant irrespective of whatever funding mechanism is put in place (whether risk-based, insurance based (as at present) or largely funded via general taxation).

Experience-rating (discounts/loadings)

4.6 While the ACC system operates on the principle of allocating costs (levies) based on broad risk categories, there is also some experience-rating of premiums (discounts/loadings on premiums) as a means of sending a signal to employers about the costs of workplace accidents compared with their peers in similar risk categories. This could be an option for FENZ levy-funding but for practical reasons would probably be reasonably feasible only where there were very large industrial, commercial or agricultural land bases.

4.7 Whether discounts should be available in response to additional fire minimisation initiatives (such as a comprehensive sprinkler system etc.) or whether such initiatives should be taken into account in making assessments requires further consideration.

Part-charges (partial user-pays)

4.8 Similar to the above (experience-rating), it is noted that some New Zealand ambulance services include a call-out fee of around $100 (although on average the real costs of a call-out are estimated to be more likely around $700). The rationale for such part-charges is, apparently, that most ambulance services provided are not totally government (taxpayer) funded but rely on grants and donations from the public etc. to make up the balance. Obviously, therefore, ambulance service providers see merit in sheeting home at least some of the cost associated with the use of their services to service users.

4.9 The above approach could also apply to the funding of FENZ service provision, including to costs arising from false/malicious calls which tie up fire service resources.

4.10 However, the part-charges option would need to be balanced against the increased administrative (transaction) costs associated with collecting such levies and/or part-charges.

Possible exemptions (or partial) exemption from FENZ levies?

4.11 BusinessNZ considers the issue of levy exemptions presents difficulties. On the one hand, there are genuine and legitimate reasons why some industrial groups should be exempt or partially exempt from levy payments. On the other, the potential for gaming could be a problem unless exemptions are tightly controlled.

4.12 At least four potential reasons can be put forward for providing at least partial exemptions from FENZ funding.

4.13 First, while some large residential/commercial or agricultural enterprises pose extremely low risk (with therefore potentially little cost) and are highly unlikely ever to use FENZ services, given their size they could pay significant levies under a risk-based approach.

4.14 Second, some enterprises have assets which FENZ services could simply not protect. Probably the classic case is the underground Manapouri power station (owned and operated by Meridian Energy), where fire service provision by FENZ, or any other organisation, would be simply impractical.

4.15 Third, several major industrial sites have their own fire brigades, given the potential risk of fire and the need to have a very fast initial response team in place. Examples include airports which often have their own risk management teams ready to respond in the event of an emergency.

4.16 With such sites making their own emergency provision (including for fire responses), there appears to be an arguable case for justifying at least some discount on potential fire levies (based simply on risk). Arguably, having a ready-response unit on site should (at least in theory) reduce the risk of calling on FENZ services.

4.17 Fourth, in some cases, isolation may be a factor in determining whether FENZ can provide a timely response to some potential risks. Again, whether there should/could be some form of discount and/or a possible exemption from levy payments might need to be considered.

Self-insurance or contracts for services

4.18 Some members have raised the possibility of self-insurance or whether large organisations could enter into contracts for services with FENZ in respect to some sites.

4.19 While BusinessNZ accepts that the above proposal can be considered as akin to the ACC Accredited Employment Scheme (whereby some large employers are able to at least self-insure against potential ACC claims costs, with some cost-sharing arrangements with ACC built in), there could be a problem with service provision if the contracts for service provided a lower level of service to that FENZ would normally provide (presumably at a lower level of cost). This would be particularly so if a fire were to spread and consumed properties outside the contract for services model.

4.20 It could be argued that amalgamating the rural and urban fire services into the FENZ model, as New Zealand has now done, was at least partially targeted at providing a more consistent and universal service across the country, irrespective of where risks (and costs) eventuate.

4.21 While having merit, the pros and cons of the mechanisms referred to (and the potential for positive and/or negative externalities on other individuals and/or property) would need to be considered and managed appropriately if they were to proceed further.

Caps on levies?

4.22 The FENZ currently applies caps on fire insurance levies for residential housing, although no such caps apply in respect to commercial property.

4.23 One suspects the rationale for caps on residential property, but no caps on commercial property, has something to do with politics (similarly to the way local government rating differentials generally adversely impact on the business sector) given businesses do not have a comparable impact via voting in local government elections.

4.24 Alternatively, the rationale might have something to do with ability to pay, or hopefully, be based on some form of risk assessment, although basing levies on property value has little, if anything, to do with risk.

4.25 Notwithstanding the above, it would seem sensible to have the costs associated with residential properties capped, as residential property costs are likely to be particularly difficult to risk rate in any meaningful fashion. This suggests some averaging of residential property costs would likely be required.

4.26 But the question remains whether other industrial, commercial or rural buildings should also be subject to caps. Perhaps there is an arguable case that where the risks imposed on FENZ are difficult to assess and subject to significant fluctuation, a cap may be justified. However, further work on this would be required. A flat charge per property could hardly be considered a justifiable basis for determining risk, even taking account of other risk-related factors such as size, location, building materials etc.

5.0 SECTION D: COLLECTION OF LEVIES

5.1 It is a reasonable assumption that any funding regime for FENZ needs to consider how to collect any levies imposed on a reasonably transparent and cost-effective basis.

5.2 While a risk-based approach to funding FENZ is considered superior to the current "insurance-based" approach (with the deficiencies of the insurance-based approach outlined in the Consultation Document and also in this submission), how can levies be collected in a cost effective manner?

5.3 Several ways of dealing with motor vehicles, residential property and commercial property are outlined below.

5.4 First, as a starting point, it is useful to look at existing frameworks for collecting levies and the like.

5.5 In respect to motor vehicles, perhaps the logical starting point would be to look at funding through the annual motor vehicle licensing regime. According to the Consultation Document, around 98 percent of motor vehicles are licensed so a flat fee per vehicle would seem appropriate and relatively easy to administer, given that the licensing regime is already up and running.

5.6 In respect to residential, industrial and commercial buildings, local councils generally have reasonable information on building types in view of the broad base of information provided for local government funding (rating). Possibly, any risk-related information and (levies) on buildings to partially fund FENZ could simply be attached to current local government rating polices, provided of course the levy was clearly transparent and separate from the rate demand. This amount could be passed on to FENZ with a transaction fee provided to local councils for having to undertake this service.

5.7 An alternative, but likely more costly mechanism, would be for FENZ to collect from (directly bill) residential, commercial and industrial owners the actual levies they pay.

5.8 Another possibility would be levy collection through the Inland Revenue's tax collection system, since most people covered by a levy are taxpayers in one way or another.

5.9 Obviously, an insurance-based funding regime could continue to be used but lacking a relationship between insurance and the use of FENZ, BusinessNZ does not consider the status quo would be a reasonable option.

5.10 In deciding which option would be the most effective, government policy officials will need to be aware of the potential risks and costs of compliance as well as cognisant of the funding principles outlined in the FENZ Act.

5.11 While BusinessNZ would be loath to recommend any one option, using existing mechanisms such as the property-based rating recovery mechanism would seem the most sensible, once the pros and cons of other options have been looked at. However, if this option were considered feasible, it would be necessary to consult local councils, including their representatives at Local Government NZ, to uncover any potential fishhooks.

5.12 Pursuing some of the other issues outlined in Section D, including part-charging and the like, might require additional collection mechanisms and the costs and benefits of such more granular funding regimes would need thorough analysis. Trying to design funding collection regimes to deal with some of the issues contained within Section D might be quite expensive and result in levy leakage, particularly if compliance were not substantially followed up.

Appendix One - Background information on BusinessNZ

BusinessNZ is New Zealand's largest business advocacy body, representing:

- Regional business groups EMA, Business Central, Canterbury Employers' Chamber of Commerce, and Employers Otago Southland
- Major Companies Group of New Zealand's largest businesses
- Gold Group of medium sized businesses
- Affiliated Industries Group of national industry associations
- ExportNZ representing New Zealand exporting enterprises
- ManufacturingNZ representing New Zealand manufacturing enterprises
- Sustainable Business Council of enterprises leading sustainable business practice
- BusinessNZ Energy Council of enterprises leading sustainable energy production and use
- Buy NZ Made representing producers, retailers and consumers of New Zealand-made goods

BusinessNZ is able to tap into the views of over 76,000 employers and businesses, ranging from the smallest to the largest and reflecting the make-up of the New Zealand economy.

In addition to advocacy and services for enterprise, BusinessNZ contributes to Government, tripartite working parties and international bodies including the International Labour Organisation (ILO), the International Organisation of Employers (IOE) and the Business and Industry Advisory Council (BIAC) to the Organisation for Economic Cooperation and Development (OECD).