Stage 2 Cost Recovery Impact Statement

Proposal to increase the transitional levy for Fire and Emergency New Zealand

Agency Disclosure Statement

The Department of Internal Affairs (the Department) has prepared this Cost Recovery Impact Statement (CRIS) to analyse options that enable Fire and Emergency New Zealand (Fire and Emergency) to meet increased costs as a result of settling a new Collective Employment Agreement with the New Zealand Professional Firefighters Union (NZPFU) in December 2022.

The Department faced several constraints when developing options for assessment

Fire and Emergency are responsible for consulting with those affected by any changes to the levy and therefore, what options are consulted on. Fire and Emergency focused on reviewing the existing levy rates in the *Fire and Emergency New Zealand (Levy Rates and Information Requirements in Transitional Period) Regulations 2017*. They consider increasing the transitional levy is the only feasible option to meet the costs of settlement and continue operating in the short term (two years). Cabinet agreed to a repayable Crown loan of $75.4 million to ensure Fire and Emergency can maintain sufficient cash reserves temporarily until the rates of the transitional levy could be increased. In line with this Cabinet decision, and Fire and Emergency's preferred option, our analysis focused on an increase to the transitional levy.

For Fire and Emergency to maintain a sustainable financial position without reducing services, any increase in revenue must come into effect by 1 July 2024. Because the insurance sector requires a long time to implement any change (approximately 12 months), our timeframes for seeking Cabinet's decisions have been constrained. This has limited the time available for analysis to the period between the settlement in December 2022 and completion of a Cabinet paper by June 2023 for policy decisions.

The Department has relied on financial information provided by Fire and Emergency to inform the analysis in this CRIS. The Department has relied on the information provided without additional scrutiny. However, we consider both the three-year forecasts established in Fire and Emergency's Statement of Performance Expectation document and the longer term forecasts established in its 20-year modelling have had robust scrutiny.[1]

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[1] Fire and Emergency's Statement of Performance Expectation provides assurance that its prospective financial statements have been prepared in accordance with the Crown Entities Act 2004 (see pp. 48 of *Statement of Performance Expectations 2022-2023 [Amended March 2023]* – available at https://www.fireandemergency.nz/about-us/key-documents/. As a Crown entity, these Statement of Performance Expectations are subject to auditing. Fire and Emergency's 20-year financial model (which provides the basis for forecasts from 2025/26 onwards in this CRIS) was reviewed by its Audit Review Committee as well as PwC in August 2022.

Options not considered in this document and related assumptions

This document does not discuss existing costs and how they are cost-recovered. Broader engagement in Fire and Emergency's long-term funding requirements will be considered when setting Part 3 levy rates (proposed to come into effect 1 July 2026). The Part 3 model will replace the existing funding model for Fire and Emergency. Any financial modelling extending into the 2026/27 financial year assumes that the Part 3 levy will provide the same level of total revenue as the transitional levy. Final decisions on the Part 3 levy and the distribution of the levy among policyholders will be made through a separate process.

This document has not included an option for different increases for different policy holder groups. This is due to limited time for analysis and the longer time required for implementation under this type of change.

When Cabinet approved the loan to meet the short-term costs of the settlement, it noted that there would need to be an increase to the transitional levy. While the analysis in this CRIS independently confirms our recommendation that there should be an increase to the transitional levy, Cabinet's previous decision has strengthened this recommendation.

The Crown's contribution to Fire and Emergency remains as $10 million per annum. Several submitters highlighted that this level of contribution is too low to cover the 'public good' element of the Fire and Emergency's services.

Cabinet has invited the Minister of Internal Affairs to report back on the appropriate level of Crown contribution to inform consideration of a potential future Budget bid [CAB-22-MIN-0520]. However, the processes required would not allow enough time for it to occur by 1 July 2024, so it has been discounted as an option.

We considered alternative options such as an increase to the Crown loan. While an increase to the loan would enable Fire and Emergency to meet the costs of settlement in the short term, a levy increase would still be required to repay the loan at a later stage. The added costs of repaying the loan would likely result in a substantial increase to the levy in 2026, when the Part 3 levy comes into force. This would also not align with previous Cabinet decisions, which noted that an increase to the levy would be needed to address the costs of the settlement. An increase to the loan has not been explored in this CRIS.

Modelling of the levy assumes a 2.7 per cent increase in levy growth per annum (increase in insured values due to inflation, or because the amount of property insured has increased in line with growth). In the current inflationary environment, insurance inflation may be higher. We note that the assumed 2.7 per cent increase is higher than the assumed 2 per cent increase which was presented in the Interim CRIS.

In consultation we tested whether an increase to the transitional levy could lead to lower levels of insurance coverage. While submitters indicated that this could be the case, there is not a clear view of the degree to which this might occur and whether reductions in insurance coverage may be driven more by other factors, such as higher premiums due to recent weather-related events.

Limitations on consultation

Fire and Emergency received 19 submissions on its proposal to increase the transitional levy. Of these, five came from individuals, two from local Councils, four from individual companies (two insurance and two forestry) and eight from industry associations (representing the insurance industry and business groups). The limited number of individual submissions in particular means we have a limited understanding of whether the community supports the increase to ensure Fire and Emergency can maintain current levels of service.

We consider that due to the minor difference in costs proposed for residential, personal property, and motor vehicle policyholders, most members of the community would not oppose the increase in levy. However, the cost increases for business owners will be higher due to the levy on non-residential property being uncapped. Receiving submissions from more individual business owners may have made the impacts of the increase in the transitional levy clearer.

This CRIS presents an alternative 9 per cent increase option. However, this was not provided as an option in consultation. We consider it may have added limited value to consult on the alternative 9 per cent increase. In line with the general opposition to a 12.8 per cent increase, we consider most arguments for a lesser increase would have focussed on whether Fire and Emergency should be more efficient. Submitters did not argue for a reduction in Fire and Emergency's service levels.

We also consider it may have been beneficial to proactively contact iwi or other Māori authorities about the consultation. Although timeframes for submitting were relatively short, proactive communication of this work may have brought forward submissions discussing the impacts of this change on Māori businesses, NGOs and marae.

Quality Assurance

The Department's Cost Recovery Impact Statement panel (the panel) has reviewed the Stage 2 Cost Recovery Impact Statement for the *Proposal to increase the transitional levy for Fire and Emergency New Zealand* (the CRIS) in accordance with the quality assurance criteria set out in the CabGuide. The panel considers that the information and analysis summarised in the CRIS **partially meets** the quality assurance criteria

The CRIS is complete and convincing. It clearly and concisely sets out the reasoning for the recommended increase to the transitional levy and why alternative approaches are not recommended. It also succinctly sets out the potential limitations with the consultation, which was open for a short period, included only a single option and could have been more proactively targeted towards Māori interests. We agree with the analysis in the CRIS that more effective consultation would be unlikely to change the recommendation and may not have revealed any further information to inform the decision, but we cannot be certain this is the case. The CRIS meets the quality assurance criteria except that it partially meets the consultation criterion.

7 July 2023

Suzanne Doig

General Manager

Policy Group, Department of Internal Affairs

Executive summary

1. Fire and Emergency deliver critical public services for communities. As well as fire related services, Fire and Emergency also have a role in hazardous substances, transport accidents, urban search and rescue, medical emergencies, natural hazard events, and other rescues.

2. Fire and Emergency are facing additional cost pressures following ratification of a new Collective Employment Agreement with the NZPFU in December 2022. The additional costs from the NZPFU settlement cannot be fully met through a reduction in Fire and Emergency's operational and capital spending without substantially impacting operations. Without change, Fire and Emergency's cash reserves will fall below the minimum level required to operate by the 2024/25 financial year.

3. Fire and Emergency receives 97 per cent of its revenue through a transitional levy on insurance contracts. Fire and Emergency have advised any reduction in expenditure will impact their ability to deliver critical services. To meet the costs of settlement and maintain sufficient cash reserves to operate, Fire and Emergency's revenue needs to increase. Therefore, the only practical way to increase revenue without impacting on Fire and Emergency's service delivery is to increase the levy rates.

4. We recommend a 12.8 per cent increase to the levy as the best option for addressing the costs of the settlement. Fire and Emergency's modelling suggests a 12.8 per cent increase to the levy is required to recover additional costs and maintain minimum levels of cash reserves without any impact to other spending and operations. This would increase levy costs by 12.8 per cent for levy payers. However, the impacts would be different for insurance policyholders who insure residential property, motor vehicles and non-residential property due to the way the levy system is currently designed.

5. Consultation revealed concerns about increases to the costs of insurance premiums – driven by weather-related events such as Cyclone Gabrielle and the recent increase in the EQC levy on residential buildings. Following this, we further considered a lesser increase of the transitional levy (a 9 per cent increase), which would require cuts to planned expenditure. However, we have concluded that this would present a significant risk to service delivery and we do not recommend this option.

6. Any changes will require an amendment to regulations. The insurance sector, which gathers the levy through premiums, will require time to implement any changes before 1 July 2024. Key stakeholders have indicated that they would expect to have 12 months to make this type of change. Our timeframes allow for just under 11 months for implementation.

Updates from Interim CRIS

7. The Department published an interim CRIS in March 2023 to support consultation.[2] Following consultation some aspects of this CRIS have been updated. Key updates include:

   - Updates to cost and revenue projections reflecting updated modelling:

     - Note that **budgeted** accounts of revenue and expenses refer to figures from, or that align with, Fire and Emergency's 2022/23 Statement of Performance Expectations (this is a version that was amended in March 2023)[3]. **Forecasted** accounts of revenue and expense refer to Fire and Emergency's current modelling of revenue and expenses;[4]

   - Further discussion of an option for a lesser increase to the transitional levy than the 12.8 per cent increase which is proposed; and

   - Additional discussion on impacts on the forestry and rural sectors as well as government agencies from an increase to the transitional levy.

Status quo

Fire and Emergency deliver critical public services that support community wellbeing

8. Fire and Emergency were established in 2017 under the Fire and Emergency New Zealand Act 2017 (the FENZ Act). The establishment of Fire and Emergency brought together rural and urban fire services into a single unified national organisation.

9. Fire and Emergency deliver critical public services that support community wellbeing. They provide services across the '4R's' of emergency management – reduction, readiness, response and recovery. The services Fire and Emergency provide help communities to minimise the impact of emergency and disaster events and recover more quickly after the event occurs.

10. Under the FENZ Act, Fire and Emergency's principal objectives are to:[5]

    - reduce the incidence of unwanted fire and the associated risk to life and property; and

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[2] The interim CRIS is available from the Treasury website at https://www.treasury.govt.nz/publications/risa/interim-cost-recovery-impact-statement-proposal-increase-transitional-levy-fire-and-emergency-new-zealand.

[3] The interim CRIS 'budgeted' numbers came from the original 2022/23 Statement of Performance Expectations published in June 2022.

[4] This forecasted data is also being used in the development of proposals for the levy settings for the Part 3 levy, which will be consulted on later in 2023. We use the same data to be consistent with the Interim CRIS for the Part 3 levy.

[5] Section 10 of the FENZ Act.

- protect and preserve life, prevent or limit injury, and prevent or limit damage to property, land, or the environment.

11. Fire and Emergency do more than fight fires. There are a broad range of functions under the FENZ Act that Fire and Emergency must carry out[6], including promoting fire safety, rescuing people in transport accidents and providing urban search and rescue services. A full list of the functions Fire and Emergency must fulfil is provided in **Appendix A**.

12. In addition, Fire and Emergency assist in other matters, should they have the capability and capacity to do so.[7] Some of these functions include responding to medical emergencies, responding to maritime incidents and responding to severe weather-related events. A full list of these other functions is also included in **Appendix A**.

Fire and Emergency respond quickly to incidents

13. Fire and Emergency generally perform well on incident response times in relation to their functions under the FENZ Act. The 2022/23 annual report shows that they meet, or are very close to meeting, their targets for response times as listed in **Table 1**.

Table 1: Fire and Emergency's performance measures[8]

Performance measure	Target	Actual	Met
Percentage of structure fires arrived at by career crews within 8 minutes.	80%	79%	✗
Percentage of structure fires arrived at by volunteer crews within 11 minutes.	85%	81%	✗
Percentage of vegetation fires arrived at within 30 minutes (anywhere in New Zealand).	90%	94%	✓
Percentage of Communications Centre events dispatched for all incidents in rural environments within 2 minutes of receiving the 111 call.	85%	90%	✓
Percentage of Communications Centre events dispatched for all incidents in urban environment, within 90 seconds of receiving the 111 call.	85%	89%	✓
Percentage of hazardous substances incidents arrived at by crews with specialist resources within 60 minutes.	85%	94%	✓
Percentage of motor vehicle accidents arrived at by crews with specialist resources within 30 minutes.	90%	97%	✓

[6] Section 11 of the FENZ Act.

[7] Section 12 of the FENZ Act.

[8] 2021/22 annual report

Percentage of career crews who respond to medical emergencies within eight minutes.	85%	82%	✗
Percentage of volunteer crews who respond to medical emergencies within 11 minutes.	80%	75%	✗

Overview of Fire and Emergency's finances

Fire and Emergency's revenue mostly comes from a levy on insurance contracts

14. A transitional levy has funded Fire and Emergency since 2017 and will continue to do so until a new levy system under the FENZ Act begins on 1 July 2026. The transitional levy is provided for in Schedule 1 of the FENZ Act. All contracts of insurance that provide cover for physical loss or damage from fire pay a levy to Fire and Emergency. The levy is set at a fixed rate per amount of insurance for most property. For motor vehicles, the levy is a set amount per motor vehicle per annum.

15. The transitional levy rates are set out in the *Fire and Emergency (Levy Rates and Information Requirements in Transitional Period) Regulations 2017*. These regulations came into force in May 2017 before Fire and Emergency was established. The transitional levy settings have not been reviewed or amended since then as the focus has been on establishing the new levy system in the FENZ Act. This new levy is referred to as the 'Part 3 levy', because it is set out in Part 3 of the FENZ Act.

16. The transitional levy treats some property types differently to others, as the transitional levy framework enables regulations to set differing levy rates for different types of property, as well as effectively cap the amount of levy paid for some property. This means the framework has created three different insurance 'policyholder' groups, whose treatment differs:

    - **Residential policyholders:** This includes residential home insurance and contents insurance.
    - **Motor vehicle policyholders:** This includes all motor vehicles under 3.5 tonnes.
    - **Non-residential policyholders:** This includes all other property not included above. Motor vehicles over 3.5 tonnes and non-residential property (including government and commercial buildings, farming property, factories, etc.) are all included in this policyholder group.

17. The key features of the transitional levy framework as it applies now are outlined in **Table 2** below:

Table 2: Current transitional levy framework[9]

Insurance policyholder group	Levy rate (exc. GST)	Maximum levy or cap (exc. GST)
Residential	10.6c per $100 insured.	Capped at $100,000 of home insurance and $20,000 of contents insurance. Means maximum levy of $106 for home insurance and $21.20 for contents.
Motor-vehicle (under 3.5t)	Flat amount of $8.45 per vehicle.	N/A
Non-residential	10.6c per $100 insured.	No maximum levy or cap applied.

18. The insurance sector plays a significant role in the levy system. Because the levy is calculated based on insurance contracts, insurance companies and brokers calculate and collect the levy on behalf of insurance policyholders. This is then paid to Fire and Emergency, who undertake analysis and audit to ensure that the correct amount of levy has been paid.

19. Fire and Emergency receives 97 per cent of its revenue from the transitional levy. The remaining revenue is made up of items such as interest revenue, charges for some services (for example, private fire alarm monitoring), recoveries for international deployments, and a Crown contribution for services provided by Fire and Emergency that are in the 'public good'. A breakdown of Fire and Emergency's budgeted revenue for the 2022/23 financial year is shown in **Table 3**:[10]

Table 3: Fire and Emergency's budgeted revenue for 2022/23 before the NZPFU settlement[11]

Revenue	Budget 2022/23 ($ m)
Levy	641.93
Interest revenue	1.92
Other income	7.39

[9] Fire and Emergency New Zealand (Levy Rates and Information Requirements in Transitional Period) Regulations 2017

[10] Statement of Performance Expectations, 2022/23 (amended version, March 2023).

[11] Ibid

Crown contribution	10.00
Total revenue	**661.24**

20. The transitional levy is inflexible to short-term changes that impact Fire and Emergency's revenue needs. The levy is charged at fixed rates per amount of insurance, set in regulations that take time to change. This means that the levy can and does grow over time as the value and number of insurance policies grows over time. Conversely, the levy can also decline. However, this is mostly connected to economic conditions and not to Fire and Emergency's expenditure needs. Fire and Emergency's costs also increase each year due to inflationary pressures and standard salary increases that increase operational costs.

Fire and Emergency incurs substantial costs to deliver services to New Zealand

21. Fire and Emergency incurs both operational and capital costs to deliver its mandated functions under the FENZ Act. A substantial amount of Fire and Emergency's costs are in relation to fire related functions. Operational costs can be broken down into output classes (the broad functions that Fire and Emergency delivers). Budgeted operational costs for the 2022/23 year are in Table 4 below:

Table 4: Fire and Emergency's budgeted costs for output classes in 2022/23[12]

Output class	Budgeted expenditure ($ m)
Fire prevention including promotion of fire safety, compliance, and enforcement.	72.20
Fire response and suppression.	447.93
Render safe hazardous substances and provide for safety at incidents.	10.43
Rescue as a result of transport accidents and urban search and rescue.	96.07
Responding to other emergencies, including medical, maritime, other rescues and natural hazard events.	86.37
Total	**713.00**

22. Fire and Emergency also have a substantial capital expenditure programme to maintain and upgrade their substantial asset base of approximately $1.5 billion.[13] This asset base spans both rural and urban assets, which had widely

[12] Statement of Performance Expectations, 2022/23 (Amended version, March 2023)

[13] Ibid

varying asset management practices before Fire and Emergency were established in 2017. This means that some assets require greater investment than anticipated in 2017 and, particularly for rural assets, cash reserves to make this investment were not passed on to Fire and Emergency (from previous fire service organisations).

23. Fire and Emergency's capital expenditure programme is funded through a combination of existing cash reserves and accumulated depreciation expense[14] (yearly depreciation expense is included in the costs in **Table 4** above).

24. The capital expenditure programme covers fleet (for example, fire trucks and other vehicles), property (for example, fire stations and corporate offices), Information Communication Technology (ICT), and equipment (for example, breathing apparatus and incident ground control radios). Budgeted capital spending for 2022/23 is shown in **Table 5** and results in a total yearly spend of $88.1 million.

Table 5: Fire and Emergency's budgeted capital spend for 2022/23[15]

Capital item	Budget 2022/23 ($ m)
Fleet	23.30
Property	38.00
ICT	12.00
Equipment	14.80
Total	**88.10**

25. Fire and Emergency's capital expenditure is fundamental to its ability to deliver services (for example, arriving at an event on time as outlined in **Table 1**). Ensuring that fire stations, fire appliances and other supporting assets are well maintained and performing well helps to ensure that Fire and Emergency can maintain and improve response times and other important performance measures.

Fire and Emergency need to sustain a minimum level of cash reserves to operate

26. Fire and Emergency's cash reserves enable them to maintain liquidity (pay for expenses incurred, such as payroll) and fund capital expenditure. Fire and Emergency's cash reserves are impacted by any surplus (revenue higher than

[14] Depreciation is the estimated reduction in the value of a fixed asset within a financial year. Fire and Emergency sets aside cash to fund the cost of depreciation.

[15] Information provided by Fire and Emergency

costs) or deficits (costs higher than revenue). Cash reserves are also reduced by:

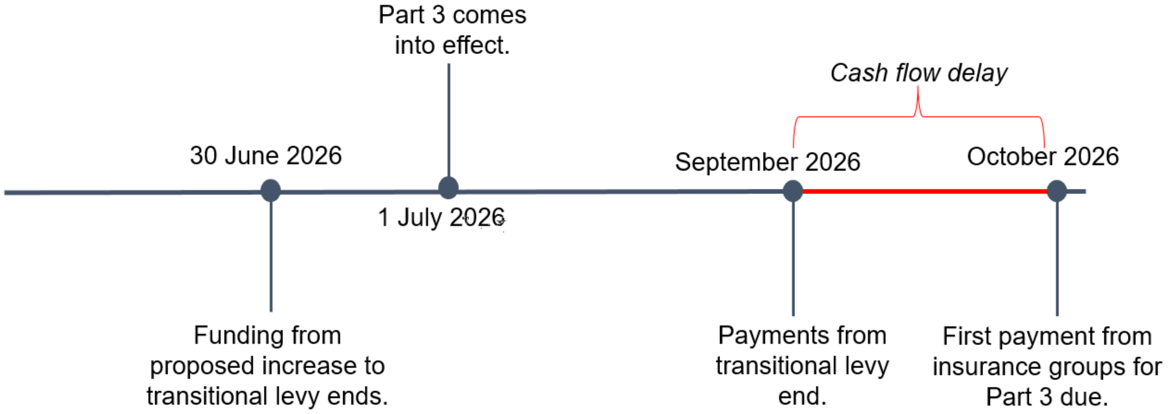
- additional capital expenditure required above the depreciation value on existing assets that is being charged to operating expenses;
- finance costs (repaying borrowings, with interest if applicable); and
- other minor balance sheet movements.

27. There are two factors that contribute to Fire and Emergency's minimum required level of cash reserves – standard business requirements and delayed income due to transitioning to the new Part 3 levy in 2026/27.

28. In terms of general business requirements, Fire and Emergency aim to hold a minimum of $50 million cash reserves to provide funding for:

- working capital (to fund day-to-day operations) of $25 million;
- liquidity buffer (to allow for delayed levy receipts and/or unexpected payments) of $10 million; and
- one significant adverse event[16] (for example, earthquake or major vegetation fire) of $15 million.[17]

29. In addition, Fire and Emergency will experience a one-month income delay in 2026/27. This will happen when the new Part 3 levy comes into effect, because this levy enables levy payments to be paid one month later than is currently allowed under the transitional levy.[18] A larger cash reserve is needed beforehand to cover costs for this month. The timeline below depicts the cash flow issue:



30. Fire and Emergency's cash reserve will never recover from the one month delay in income. Instead this delayed month of income will be represented in its

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[16] Fire and Emergency define a significant adverse event as an event that requires additional funding above and beyond normal budgeted costs to respond. The recent cyclone in February 2023 did not qualify as travel costs were the main expenditure and these are part of normal funding requirements.

[17] 2022/23 Annual Report.

[18] Under section 88 of the FENZ Act, the part 3 levy must be paid to FENZ no later than the 15th day of the third month after the end of the month in which the contract of insurance was entered into.

balance sheets by an increase to its *accounts receivable* (i.e. debt owed from insurers to Fire and Emergency) in perpetuity. In other words, the debt owed by insurers will increase from two months of levy payments (the current processing time for payments) to three months of levy payments on an ongoing basis. This increase in the debt owed will equal the decrease in cash that Fire and Emergency has in its reserves.

31. Fire and Emergency have forecast the transition to the Part 3 levy will incur a $69 million loss in revenue. This figure has been calculated by looking at both the forecast levy revenue for the 2026/27 financial year and historic proportions of levy revenue received in the month where no levy will be received.

32. This means that Fire and Emergency require cash reserves of $120 million (or close to this amount[19]) by the end of the 2025/26 financial year. Following that, cash reserves of $50 million are sufficient for business needs.

Fire and Emergency currently have a high level of cash reserves and yearly revenue and expenses broadly align

33. Fire and Emergency's existing cash reserves are high. At the start of the 2022/23 financial year reserves were $206 million. These high cash reserves are the result of greater than expected levy revenue growth and the fact that the transitional levy rates have not been reviewed or adjusted since 2017.[20]

34. Excluding the impact of the settlement with NZPFU, Fire and Emergency's forecast revenue and expenses are broadly aligned, as shown in **Table 6**.[21]

Table 6: Fire and Emergency's forecast revenue, expenses, and surplus/deficit excluding the NZPFU settlement impact

	2022/23 ($ m)	2023/24 ($ m)	2024/25 ($ m)	2025/26 ($ m)	2026/27 ($ m)
Revenue	696.02	704.40	718.76	735.65	755.14
Expenses	668.79	707.45	715.78	753.96	767.20
Net surplus/(deficit)	**27.23**	**(3.05)**	**2.98**	**(18.31)**	**(12.06)**

35. The alignment of revenue and expenses means that any substantial changes to costs will either need to be offset by increasing revenue, reducing costs elsewhere within the organisation, or reducing cash reserves (or a combination of all three).

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19 Fire and Emergency have indicated that if there is only $110 million in reserve at the end of 2025/26, cashflows can be managed in the following year to ensure there are sufficient cash reserves.

20 Fire and Emergency have budgeted for 2 per cent levy growth each year. Data since 2017/18 suggests the annual levy growth has been around 3 per cent.

21 Forecast data provided by Fire and Emergency

A recently agreed Collective Employment Agreement between Fire and Emergency and the New Zealand Professional Firefighters Union (NZPFU) has created significant additional costs for Fire and Emergency

36. Fire and Emergency and the NZPFU agreed on the terms of a new Collective Employment Agreement for professional firefighters in December 2022. The Collective Employment Agreement will raise professional firefighters' salaries in line with other similar jobs (for example, Department of Conservation firefighters) and provide medical benefits, such as early cancer screening, psychological support, and life insurance.

37. This agreement between Fire and Emergency and the NZPFU members will cost $406.7 million up till 2026/27 (this includes the increased costs of NZPFU wages and benefits). However, the true costs of the settlement for Fire and Emergency will be higher. Fire and Emergency are committed to retaining pay parity within the organisation. Fire and Emergency also need to apply some of the changes to non-NZPFU members as well. Furthermore, these additional costs will need to be embedded beyond the term of the existing Collective Employment Agreement, as these pay levels and employment benefits will continue to apply in the future.

38. Additional costs start to be incurred in the recently completed financial year (2022/23) and will cover both 2021/22 costs and those in 2022/23. The ongoing costs of the settlement are shown in **Table 7** below and broken down into salary increases for NZPFU members and non-NZPFU members, as well as increased job benefits (only for NZPFU members). The costs increase each year because the salary increases from the previous years must continue to be met in the next year, plus planned adjustments (either as agreed in the Collective Employment Agreement, or as planned salary increases due to the market).

Table 7: Annual costs incurred from NZPFU settlement[22]

	2021/22 ($ m)	2022/23 ($ m)	2023/24 ($ m)	2024/25 ($ m)	2025/26 ($ m)	2026/27 ($ m)
Salary increases NZPFU	28.90	43.00 *Previous year plus $14.1*	58.10 *Previous years plus $15.1*	67.40 *Previous years plus $9.3*	77.10 *Previous years plus $9.7*	87.20 *Previous years plus $10.1*
Benefits NZPFU	0.60	6.40	8.30	11.50	8.90	9.30
Salary increases non-NZPFU	0.00	5.90	12.10 *Previous year plus $6.2*	16.40 *Previous years plus $4.3*	21.00 *Previous years plus $4.4*	25.50 *Previous years plus $4.5*
Total cost of settlement	**-**	**84.80**	**78.50**	**95.30**	**107.00**	**122.00**

39. Fire and Emergency had already budgeted for additional costs resulting from settlement. Furthermore, there are costs to service a repayable Crown loan (discussed further in paragraphs 73 and 74). The existing budget and loan affect the total additional costs for Fire and Emergency and are shown in **Table** 8.

Table 8: Annual costs incurred from NZPFU settlement[23]

	2021/22 ($ m)	2022/23 ($ m)	2023/24 ($ m)	2024/25 ($ m)	2025/26 ($ m)	2026/27 ($ m)
Total cost of settlement	-	84.80	78.50	95.30	107.00	122.00
Provided for in Fire and Emergency budget	-	(30.18)	(30.47)	(40.89)	(53.06)	(62.00)
Cost of servicing Crown loan	-	0.79	2.22	3.81	4.20	3.70

[22] Information provided by Fire and Emergency. Costs for 2021/22 are paid in 2022/23 financial year.

[23] Information provided by Fire and Emergency. Costs for 2021/22 are paid in 2022/23 financial year.

Total impact on Fire and Emergency expenses	**-**	**55.41**	**50.25**	**58.22**	**58.14**	**63.70**

40. With these additional costs, Fire and Emergency's costs exceed their revenue. Forecast total costs compared to forecast revenue, after factoring in the additional costs of settlement are shown in **Table 9** below (note that 2021/22 costs above are paid in the 2022/23 financial year, along with 2022/23 costs). Orange highlighted boxes in **Table 9** show where figures have changed from what was provided in **Table 6**.

Table 9: Fire and Emergency's forecast revenue, expenses and surplus/deficit with additional NZPFU costs[24]

	2022/23 ($m)	2023/24 ($m)	2024/25 ($m)	2025/26 ($m)	2026/27 ($m)
Revenue	696.02	704.40	718.76	735.65	755.14
Expenses	724.20	757.70	774.00	812.10	830.90
Net surplus/(deficit)	**(28.18)**	**(53.30)**	**(55.24)**	**(76.45)**	**(75.76)**

41. Additional cost pressures resulting from the NZPFU settlement mean that expenses now exceed Fire and Emergency's revenue, resulting in ongoing deficits.

Without change, the costs of the settlement will quickly deplete Fire and Emergency's cash reserves and move it into an unsustainable financial position

42. From 2022/23 – 2026/27 the average annual cost of the settlement will be $97.5 million (refer to the top line in **Table 8**). As noted in **Table 6**, without the costs of the settlement, Fire and Emergency's projected expenses are aligned with its revenue. Fire and Emergency's modelling indicates that without any intervention, these costs, combined with the $69 million loss in revenue for the transition to the Part 3 levy, will deplete the $206 million cash reserve (from 2021/22) and will move Fire and Emergency into $234.2 million of debt by the end of 2026/27 (refer to **Table 9** below). Prior to the shift to the Part 3 levy, at the end of 2025/26, the debt would be at $56.8 million.

43. Waiting for the introduction of the Part 3 levy in July 2026 to address the settlement cost is not tenable. Fire and Emergency need to have a $50 million cash reserve for general business needs, as outlined in paragraph 28. The longer the delay in addressing the costs of the settlement, the more severe the

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[24] Information provided by Fire and Emergency

intervention would need to be to ensure Fire and Emergency can achieve a minimum cash reserve through to 2026/27.

44. The modelling accounts for a repayable capital loan provided by the Crown to Fire and Emergency [CAB-22-MIN-0520]. This loan was provided by the Crown to support a sustainable cash position for Fire and Emergency until further revenue could be found. This loan is worth $75.4 million and can be drawn down in instalments from 1 December 2022 to 30 June 2025. It will be repaid in full, with interest, no later than 2032/33.

45. Fire and Emergency's modelling is shown in **Table 10** below. Orange highlighted boxes show where Fire and Emergency's cash reserves fall below minimum required levels.

Table 10: Fire and Emergency's forecasted modelling of cash reserves[25]

($m)	2022/23	2023/24	2024/25	2025/26	2026/27
Opening cash balance	206.0	172.3	118.4	57.8	(56.8)
Receipts from Levy	663.4	679.2	700.0	718.5	667.5
Receipts from other revenue (incl. interest)	29.1	19.5	15.4	13.3	13.3
Operating expenses	(658.3)	(671.5)	(692.7)	(727.2)	(755.6)
Purchase of property, plant and equipment and intangible assets	(74.9)	(87.3)	(88.4)	(88.8)	(91.1)
Proceeds from capital injection	25.6	25.0	25.0	0.0	0.0
Repayments of capital injection	(12.7)	(12.6)	(13.2)	(20.5)	(8.3)
Other financing activities	(5.9)	(6.3)	(6.7)	(9.8)	(3.2)
Closing cash balance	172.3	118.4	57.8	**(56.8)**	**(234.2)**

46. We note that the significant increase in deficit between 2025/26 and 2026/27 is explained by the $69 million loss in revenue in the transition to the Part 3 levy (as discussed from paragraph 29).

25 Information provided by Fire and Emergency

Maintaining a minimum level of cash reserves is not possible solely through reducing costs

9(2)(f)(iv) [redacted]

47. To ensure Fire and Emergency have $50 million in cash reserve at the end of 2026/27, there would need to be $284.2 million in cash savings over four years. However, for this analysis we are assuming **$253.8 million** in savings would be needed – this would lead to a $19.5 million cash reserve.

48. Current forecasted costs are greater than was presumed in the Interim CRIS. This has led to an increase in the projected overdraft by the end of 2026/27:

    - the Interim CRIS indicated a closing cash balance of -$201.4 million; and
    - this CRIS indicates a closing cash balance of -$234.2 million.

49. 9(2)(f)(iv) [redacted]

Impacts of making up for deficits solely through cost savings

50. The analysis below shows the impact of reducing costs by $253.8 million through a 50/50 split reduction between operational expenditure and capital expenditure.

Reducing operational costs would likely significantly reduce Fire and Emergency's ability to deliver services

51. Fire and Emergency data shows that reducing operational spending to offset 50 per cent of the additional costs would require 140 full time equivalents (FTEs) to be made redundant, or 12 per cent of staff.[26] Staff reductions would need to be supplemented with a reduction in other operating costs of $13.5 million per year. This would mostly come from a reduction in professional fees, contractors and other funding required to implement initiatives as the loss of staff would slow these initiatives down.

52. This reduction would result in $126.9 million of savings over four years until 2026/27. The savings are shown in **Table 11**.

[26] Calculated using the average wage of staff groups and factoring in one-off redundancy costs that would be incurred.

Table 11: Forecast savings from operational expenditure reductions[27]

($m)	2023/24	2024/25	2025/26	2026/27	Total (four years)
Staff savings	18.9	18.9	18.9	18.9	75.7
One off redundancy	(2.9)				(2.9)
Additional operating costs	13.5	13.5	13.5	13.5	54.1
Total savings	**29.6**	**32.4**	**32.4**	**32.4**	**126.9**

53. The impact of losing 12 per cent of staff would be significant to how effectively Fire and Emergency can deliver services. Time constraints have limited the analysis that can be completed to understand the extent to which these redundancies would affect services. However, it is a reasonable assumption that a 12 per cent reduction in staff would have a significant impact.

54. Furthermore, trying to reduce costs would lead to delays in implementation of several important projects within Fire and Emergency because of a lack of staff and reduction in professional and contracting fees. This includes delays in health standards (investigating options to do health standard checks for staff to remain healthy and well while they undertake duties), carcinogen control (improving policies and procedures to reduce exposure to carcinogens and manage the consequences of exposure) and working safely in water (improving water training capability).

Reducing capital spending would likely lead to delays in necessary maintenance and upgrades and result in higher costs in the future

55. Fire and Emergency modelling indicates that offsetting 50 per cent of the costs of settlement through a reduction in capital spending only would require a 36 per cent reduction in yearly capital spend. This would result in $31.7 million of savings each year. Further information is provided in **Table 12** and **Table 13** below.

[27] Information provided by Fire and Emergency

Table 12: Forecast savings from capital spend reductions[28]

($m)	2023/24	2024/25	2025/26	2026/27	Total
Planned capital expenditure	87.3	88.4	88.8	91.1	355.6
Reduced capital expenditure	(31.7)	(31.7)	(31.7)	(31.7)	(126.9)
Revised capital expenditure	55.6	56.7	57.0	59.4	228.8

56. These reductions would be spread across fleet, property, equipment, and ICT spend and equate to the following savings:

Table 13: Breakdown of yearly capital spend reductions[29]

Capital spend	Savings ($m)	Impacts
Fleet	8.7	Equivalent to cost of 15 vehicles in total.
Property	15.8	Equates to 3 station rebuilds.
Equipment	3.5	Would delay equipment replacement programmes (for example, incident ground control radios, breathing apparatus).
ICT	3.7	Delay ICT programmes, including replacement of ICT equipment in stations, regional offices, and national headquarters.

57. The impact on service delivery of this reduction in capital spend could also be significant. Fire and Emergency owns a large amount of ageing assets with 27 per cent of fire appliances beyond their target asset life (of 20 to 25 years) and 27 per cent of fire stations more than 50 years old. The age of buildings does not necessarily determine their fitness for purpose, but the functionality of 36 per cent of Fire and Emergency's stations has been assessed as poor or very poor.[30]

58. Delaying these upgrades would mean some of these assets cannot perform to Fire and Emergency's required standards, maintenance costs would continue to increase over time and increased capital spending is required in the future to catch-up with deferred asset renewal.

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28 Information provided by Fire and Emergency

29 Ibid

30 Fire and Emergency's Briefing to the Incoming Minister, January 2023.

59. Furthermore, the recent bargaining with the NZPFU highlighted professional firefighters' concerns that the current working state of the fleet is poor and urgent attention is needed to upgrade these assets. Delaying this investment in particular is not a realistic option for Fire and Emergency in light of the new Collective Employment Agreement.

60. Time constraints have limited the analysis which could be completed to understand the full impact of reducing this capital spend. However, it is reasonable to assume that this level of reduced capital spending would result in significant risks to service delivery and is not a feasible option to meet the costs of settlement.

An increase in Fire and Emergency's revenue is needed to ensure it can retain a sustainable level of cash reserves

61. Fire and Emergency require an increase in revenue by the start of the 2024/25 financial year. Because the costs of settlement cannot be met by a reduction in spending alone, Fire and Emergency's revenue must increase to ensure services can continue to be delivered at the right level of quality and sustainable cash reserves are maintained. If this does not happen, Fire and Emergency will drop below its minimum required cash reserves by the end of the 2024/25 period and this position will continue to worsen over time (refer **Table 9**).[31]

62. Alternative methods for increasing revenue, either by an additional Crown loan or an increase to Crown contribution, are not feasible (further discussed below). This means that an adjustment to the transitional levy is necessary to provide sufficient revenue for Fire and Emergency to cover the ongoing costs of settlement with the NZPFU. The levy covers a significant majority (97 per cent) of Fire and Emergency's total revenue and is the only remaining revenue that can be adjusted.

63. Cabinet has not yet decided to increase the transitional levy. In November 2022, when approving the terms of the loan to enable Fire and Emergency to retain a sustainable cash position, Cabinet noted that Fire and Emergency's levies will need to increase on 1 July 2024 to enable the costs of settlement to be met and for the repayment of the Crown loan to start in the 2025/26 financial year [CAB-22-MIN-0520]. This CRIS is intended to inform Cabinet decisions to increase the transitional levy, and by how much.

Cost Recovery Principles and Objectives

64. The principles to guide this cost recovery proposal are:

- **Justifiability:** the transitional levy reasonably relates to services it is charged for;
- **Authority:** the transitional levy is charged within its statutory authority;

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[31] The situation would be partially mitigated by increased levy rates under the Part 3 Levy, coming into effect on 1 July 2026. However, a significant acute levy increase would be needed to recover the necessary cash reserves and would lead to an over-recovery for the remainder of the levy period (three years).

- **Sufficiency:** the transitional levy must provide sufficient funding for Fire and Emergency to deliver statutory functions at an appropriate quality level while maintaining minimum cash reserves;
- **Simplicity:** any changes to the transitional levy must be consistent with the existing transitional levy framework to avoid creating unnecessary complexity;
- **Transparency:** transitional levy payers have enough information to assess the transitional levy framework and provide meaningful feedback; and
- **Timeliness:** adjustment of the transitional levy system must be able to be implemented by 1 July 2024.

65. Selection of these principles assumed that the transitional levy will be increased and therefore apply to feasible options that meet this assumption.

66. The principles have been derived from Treasury and Office of the Auditor General guidance, as well as features of the Fire and Emergency levy. They have guided the development of options for Fire and Emergency's consultation. The principles also serve as the objectives of the cost-recovery proposal.

67. Inclusion of an equity principle was considered: that is, whether the transitional levy is set at a level that reflects the policyholders use of, or benefit from the potential use of Fire and Emergency's service. However, due to timing constraints and the need for a timely, simple option to address the shortfall, the decision was made to exclude equity from this analysis. This decision was made with the assumption that equity will be considered as part of the Part 3 levy work (set to come into force on 1 July 2026).

68. Inclusion of an efficiency principle was also considered: that is, a broader consideration of whether planned expenditure could be reduced while maintaining adequate service levels. Timing constraints have also meant that this assessment has not been made. The Part 3 levy work will allow for testing whether Fire and Emergency has adequately explored efficiencies and tested its proposed service levels against the community's ability and willingness to pay. Work on the Part 3 levy will consider Fire and Emergency's total finances (not just a specific cost pressure) and will run over a longer period to allow for more detailed engagement on those questions than was possible for the proposed changes to the transitional levy.

Policy rationale, level of proposed fee (cost recovery model) and impacts

Several options have been ruled out, as they are not considered feasible

69. As noted earlier in this CRIS, it is not feasible for Fire and Emergency to meet the additional costs solely through a reduction in operational and capital expenditure.

Differential increases for policyholder groups were not considered as feasible options

70. Options that resulted in differing increases across policyholder groups were considered but ruled out as not feasible. This would mean that certain policyholder groups would see a larger increase than others. These options require costs to be allocated according to property type, according to historic information in Fire and Emergency's incident response data (for example, motor vehicles, residential property or non-residential property). This information was not available when the existing transitional levy rates were set.

71. This would conflict with the principle of Simplicity. Because the existing rates are not allocated in this way, it would be overly complex and challenging to model what an appropriate increase should be to align the new costs appropriately. This complexity is unnecessary because the entire allocation of the levy model will be reconsidered when the Part 3 levy is developed and will be based off response data.

72. This also conflicts with the Timeliness principle. The insurance sector has indicated that more complicated changes would likely take an additional six months to implement. It is not feasible to incorporate this additional implementation time and to achieve the 1 July 2024 implementation date.

An additional Crown loan would lead to greater long term costs

73. We do not recommend increasing the Crown loan to meet the ongoing costs of the settlement. While it may provide a short-term solution to meet the costs of settlement, the loan would still need to be repaid and borrowing a larger amount would increase the accrued interest. This would likely result in a significant increase to levy rates in 2026 when Part 3 comes into effect. Ongoing reliance on Crown loans would also be inconsistent with Fire and Emergency being an organisation primarily funded through a levy.

74. Increasing the loan would place an unfair financial burden on policy holders who would face a significant increase to their existing levy rate in 2026 and ultimately pay more to enable Fire and Emergency to recover the additional interest costs. Increasing the levy in 2024 is more affordable than a significant increase two years later in 2026.

An increase to the Crown contribution is not feasible because of tight timeframes

75. Several submitters highlighted that the Crown contribution of $10 million is too low to cover the 'public good' aspect of Fire and Emergency's services. We note that for 2022/23 the Crown contribution is projected to make up 1.7 per cent of Fire and Emergency's revenue.

76. This CRIS assumes an increase to the Crown's contribution of $10 million to Fire and Emergency is not being considered, due to the uncertainty of whether such funding would be available by 1 July 2024. Cabinet has invited the Minister of Internal Affairs to report back on the appropriate level of the Crown contribution to inform consideration of a potential future Budget bid [CAB-22-MIN-0520]. These processes could not be completed in time to be incorporated

into an increase by the 2024/25 financial year but will inform future levy setting processes.

Fire and Emergency have proposed a 12.8 per cent increase to the transitional levy to recover the additional costs of settlement

An increase to the levy will incur different costs between policyholder groups

77. Fire and Emergency consulted on its proposal for a 12.8 per cent increase to all levy rates or annual amounts under the transitional levy. This increase would mean the following levy framework would apply in **Table 14**:

Table 14: Difference in the transitional levy framework under a 12.8 per cent increase

Policyholder group	Levy element	Current rate	New rate	Difference (per annum)
Residential home	*Rate*	10.6c per $100 insured	11.95c per $100 insured	12.8 % increase
	Cap	$100,000	$100,000	No change
	Maximum (exc. GST)	$106	$119.53	$13.53 increase
Residential contents	*Rate*	10.6c per $100 insured	11.95c per $100 insured	12.8 % increase
	Cap	$20,000	$20,000	No change
	Maximum (exc. GST)	$21.20	$23.91	$2.71 increase
Non-residential	*Rate*	10.6c per $100 insured	11.95c per $100 insured	12.8 % increase
	Cap	No cap	No cap	No change
	Examples (exc. GST)	$1 million insurance: $1,060 levy (per annum) $5 million insurance: $5,300 levy	$1 million insurance: $1,195 levy (per annum) $5 million insurance: $5,975 levy	$1 million insurance: $135 increase (per annum) $5 million insurance: $675 increase
Motor vehicle *(under 3.5 tonnes)*	*Flat amount (exc. GST)*	$8.45	$9.53	12.8 % increase $1.07 increase

78. Insurance policyholders would face a 12.8 per cent increase in their levy costs. This will ultimately increase their insurance costs, as the levy is calculated and paid at the same time that an insurance policy is taken out.

79. A 12.8 per cent increase in the levy would create different impacts for different policyholder groups. For example, residential home levies would increase by $13.50 per year (exc. GST), residential contents by $2.70 (exc. GST) and motor vehicles by just over $1.00 (exc. GST). Because the cap for residential home and contents are set at a relatively low amount, most levy payers will pay the maximum levy and the impact is relatively easy to understand. The same is true of motor vehicles because of the flat amount paid per year.

80. Understanding the impacts for non-residential policyholders is more challenging. Because there is no cap, the amount of levy depends on how much insurance a non-residential policyholder has. The specific impacts within the non-residential policyholder group are also difficult to model (i.e. how the costs are distributed), because the commercial sensitivity of insurance information means we have little information about the insurance within this group. However, we do know that a non-residential policyholder with $1 million in insurance can expect a $135 increase in levy per year, one with $5 million can expect a $675 increase.

81. The above changes would mean that each policyholder group contributes more to the levy annually than previously. These changes as forecast for the 2024/25 year are shown in **Table 15**.

Table 15: Change in policyholder group contributions to total levy revenue[32]

Policyholder group	2024/25 (existing levy rate) ($m)	2024/25 (12.8 per cent increase) ($m)	Difference ($m)
Residential home and contents	229.5	258.9	29.4
Non-residential	424.3	478.6	54.3
Motor vehicle *(under 3.5 tonnes)*	49.6	55.9	6.3
Total	**703.4**	**793.4**	**90.0**

A 12.8 per cent increase will support Fire and Emergency to have a sufficient cash reserve in 2026/27

82. Under this approach, Fire and Emergency would have enough additional revenue to operate a necessary surplus from 2024/25 to ensure minimum cash reserves are in place by 2026/27.[33] This would fully recover the additional costs of settlement, meaning that Fire and Emergency do not need to reduce operational or capital expenditure elsewhere. This meets the Sufficiency

[32] Information provided by Fire and Emergency

[33] This assumes a 2.7 per cent increase in the insurance base per annum. The increase in insurance values may be higher than this within the current inflationary environment.

principle – as Fire and Emergency will have enough revenue to deliver statutory functions at their existing levels.

83. Forecast revenue and expenses under this option are shown in **Table 16**. Orange highlighted boxes show where Fire and Emergency returns to a surplus, as compared with **Table 9** (Fire and Emergency's forecast revenue, expenses and surplus/deficit with additional NZPFU costs).

Table 16: Fire and Emergency's forecast revenue, expenses, and surplus/deficits under a 12.8 per cent levy increase[34]

	2022/23 ($m)	2023/24 ($m)	2024/25 ($m)	2025/26 ($m)	2026/27 ($m)
Total revenue	696.02	704.40	809.66	830.98	851.66
Total expenses	724.23	757.70	774.00	812.13	830.89
Net surplus/(deficit)	(28.21)	(53.30)	**35.66**	**18.85**	**20.77**

84. The return to a surplus would have a corresponding impact on Fire and Emergency's cash reserves. Fire and Emergency's modelling of the impact to cash reserves is shown below.

85. The modelling in **Table 17** below shows that the return to a surplus in 2024/25 enables Fire and Emergency to build and sustain the required minimum level of cash reserves (for general business needs, the transition to Part 3 levy, and to repay Crown loans). This would result in a $19.5 million cash reserve in 2026/27, after a loss of $69 million in cash after moving to the Part 3 levy but with no rate increase. The orange highlighted boxes can be compared with **Table 10** (Fire and Emergency's forecasted modelling of cash reserves with no increase to the transitional levy) to show the change in levy revenue and cash reserves.

86. 9(2)(f)(iv) [redacted]

[34] Information provided by Fire and Emergency

Table 17: Fire and Emergency's modelled cash reserves under a 12.8 percent increase to the levy[35]

($m)	2022/23	2023/24	2024/25	2025/26	2026/27
Opening cash balance	206.0	172.3	118.4	129.7	110.0
Receipts from Levy	663.4	679.2	771.0	810.4	752.9
Receipts from other revenue (incl. interest)	29.1	19.5	16.2	16.1	14.8
Operating expenses	(658.3)	(671.5)	(692.7)	(727.2)	(755.6)
Purchase of property, plant and equipment and intangible assets	(74.9)	(87.3)	(88.4)	(88.8)	(91.1)
Proceeds from capital injection	25.6	25.0	25.0	0.0	0.0
Repayments of capital injection	(12.7)	(12.6)	(13.2)	(20.5)	(8.3)
Other financing activities	(5.9)	(6.3)	(6.7)	(9.8)	(3.2)
Closing cash balance	172.3	118.4	129.7	110.0	19.5

87. These changes to Fire and Emergency's revenue and minimum cash reserves would occur without any financial impact elsewhere in the organisation. This reduces any risk that service levels will be impacted to meet these additional costs, as Fire and Emergency will not need to offset the costs from expenditure elsewhere within the organisation.

This approach will meet the cost recovery principles and objectives

88. This approach replicates the existing framework of the transitional levy, where different rates of levy continue to apply to different policyholder groups. The proportions of levy paid by each policyholder group also remains the same. This means that the principles of Justifiability and Authority are met. It also means the principle of Simplicity is met as additional complexity is not introduced to the transitional levy framework for two years before the new Part 3 levy takes effect.

89. The principle of Transparency is met through this impact assessment and consultation process being followed. The principle of Timeliness is met as these changes can be implemented by 1 July 2024. The principle of Sufficiency is met as the 12.8 per cent increase in the transitional levy will cover the costs of the settlement between Fire and Emergency and the NZPFU.

[35] Information provided by Fire and Emergency

A partial cost recovery is not recommended due to the uncertainty of impacts on service delivery

90. Following consultation, we have considered an option to increase the transitional levy by 9 per cent. Fire and Emergency suggested the 9 per cent increase as an alternative option to consider. We agree that this is a reasonable alternative option, as it could make a meaningful difference in cost impacts for non-residential levy payers, while potentially providing sufficient funding for Fire and Emergency's services. It also effectively demonstrates the general trade-offs of a partial cost recovery between the impacts on service delivery and cost savings for levy payers.

Benefits of a lesser increase to levy payers

91. We consider that the difference between these options for insurance policy holders of residential property, personal property and motor vehicles to be minor. This is due to the low flat levy rate for motor vehicles and the caps on the sum insured that is levied for residential property (up to $100,000 of the insured value is levied) and for personal property (up to $20,000 insured value is levied). The difference in costs between a 9 per cent increase and a 12.8 per cent increase for the annual cost of insurance for a household with full cover of their home, contents and two motor vehicles would be $5.54 per annum (excluding GST).

92. The benefits would be primarily felt by policy holders of non-residential property, as the insurance value that is levied is uncapped. This is particularly impactful for those with high property asset holdings, but relatively low annual revenue. See examples of differences in costs for policyholders of non-residential property in **Table 18**:

Table 18: Differences between options for policyholders of non-residential property

Levy increase	$1 million insurance value	$5 million insurance value
Current levy (exc. GST)	*$1,060.00*	*$5,300.00*
Cost from 9 per cent increase (exc. GST)	$1,155.00	$5,777.00
Cost from 12.8 per cent increase (exc. GST)	$1,195.00	$5,978.00
Difference between 9 and 12.8 per cent change (exc. GST)	$40	$201

A lesser increase would require significant cuts to planned spending

93. However, a 9 per cent increase to the transitional levy would still require significant cuts to planned spending. Fire and Emergency estimate that it would need to find $76.4m in cost savings between 2023/24 and 2026/27 ($19.1m per annum), in order to have a cash reserve of $19.5m at the end of 2026/27 (the same cash position as under a 12.8 per cent increase).

94. We consider these cuts to expenditure could have an impact on Fire and Emergency's operations. However, Fire and Emergency would need to do further work to identify where the cost savings could come from to identify the level of impact on services. We provide an example of a 50/50 split in cost savings between capital expenditure and operational expenditure, and its potential impacts, below:[36]

Table 19: Operational expenditure savings per annum for 9 per cent increase[37]

($m)	2023/24	2024/25	2025/26	2026/27	Total
Staff savings	5.4	5.4	5.4	5.4	21.6
One off redundancy	(0.8)	0.0	0.0	0.0	(0.8)
Additional operating costs	4.3	4.3	4.3	4.3	17.4
Total savings	**8.9**	**9.7**	**9.7**	**9.7**	**38.2**

95. Savings in operational expenditure would require a reduction of approximately 40 full time staff. These reductions would likely come from non-operational staff, some of whom provide direct support to operational staff to enable them to respond to emergencies. Savings to other operating costs are most likely to affect initiatives to improve organisational capability by either slowing down or ceasing these programmes.

Table 20: Capital expenditure savings per annum for 9 per cent increase

Capital spend	Savings ($m)	Impacts
Fleet	1.7	Equivalent to cost of 3 vehicles in total.
Property	5.2	Equates to cost of 1 station rebuild.
Equipment	1.3	Would delay equipment replacement programmes (for example, incident ground control radios, breathing apparatus).
ICT	1.3	Delay ICT programmes, including replacement of ICT equipment in stations, regional offices, and national headquarters.

96. We consider that these levels of cuts would create some risk that services would deteriorate. Given the critical nature of Fire and Emergency's functions, we do not recommend taking on this risk. A fuller review of Fire and Emergency's financing and services will be undertaken for the introduction of the Part 3 levy in July 2026. This will provide a better opportunity to consider

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[36] The proportions of savings with in the operational and capital spends are the same as outlined further above for no increase to the transitional levy.

[37] The cost savings for operational expenditure incorporate a one-off redundancy cost of $2.82m.

cost efficiencies, while not risking a deterioration of Fire and Emergency's services.

Impact Analysis

Potential impacts on levy payers

97. We have limited information on whether these changes will have any wider impacts for stakeholders (for example, reduced insurance cover), or different impacts on different groups. Submitters from the insurance sector indicated that increasing costs to premiums are likely to lead to reduced coverage. They note that other factors, such as high levels of insurance pay-outs for weather-related events, high inflation and changes to the EQC levy are also contributing to increasing insurance costs, which are influencing decisions to reduce levels of insurance coverage.

98. Time constraints have limited our ability to gather further evidence through consultation to understand how significant the impacts of the increase to the transitional levy could be. A longer timeframe could have enabled us to gather more evidence on the potential impacts across different sectors. However, even with more time, we do not know if it would be possible to develop any robust quantitative measurements of the impact of the levy increase. Impacts are difficult to assess because there are likely factors other than increasing premiums that are affecting people's insurance decisions (e.g., general inflation).

99. The impacts of this levy increase will not be large for most households. The yearly increase in levy costs for a household with full cover of their home, contents and for two motor vehicles would be $17.30 per year (exc. GST).

100. The impacts may be greater for levy payers with a high level of non-residential property insured. Submitters from the forestry sector[38] have emphasised the high cost of insurance of forestry. They indicated that increasing the transitional levy could lead to more forestry owners choosing to self-insure (and not contribute to the levy).[39] Submitters from the rural sector also noted there was a risk that an increase to the transitional levy would contribute to decisions to reduce insurance coverage.

Impacts on Government agencies

101. Additional annual costs for some Government agencies with large property portfolios are outlined below:

- Te Whatu Ora: $170,000 (excluding GST)
- Kāinga Ora: $102,000-$112,000 (excluding GST)

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[38] Forestry sector submitters included the New Zealand Institute of Forestry, the New Zealand Forest Owners Association, Juken Ltd and Wenita Forest Products Limited.

[39] The transitional levy does not apply to insurance on standing forest or bush, however it would apply to buildings and equipment used by the forestry sector.

- Department of Internal Affairs: $33,000 (excluding GST)
- Corrections: $50,000 (excluding GST)

102. Fire and Emergency have provided figures on the levy paid by central and local government in the financial year 2022/23. **Table 21** below shows the impact a 12.8 per cent increase to the transitional levy would have had on these figures (assuming the same levels of insurance coverage).

Table 21: Indicative impact of 12.8 per cent increase on 2022/23 levy revenue from central and local government

Savings ($m)	Actual figure 2022/23 (exc. GST)	With 12.8 per cent increase (exc. GST)	Difference (exc GST)
Crown Entities	7.88	8.89	1.01
Central Government Departments and Agencies	5.41	6.10	0.69
Local Government	11.79	13.30	1.51
Total	**25.09**	**28.30**	**3.21**

103. We assume there are no GST impacts as additional GST gathered through the levy payments will be offset by reduced GST elsewhere in the economy through reduced spending.

These changes are not expected to affect the demand for Fire and Emergency services

104. Changes to the levy are unlikely to affect demand for Fire and Emergency services. When Fire and Emergency services are requested, there is no charge to the requestor.

Consultation

105. Fire and Emergency consulted on a 12.8 per cent increase to the transitional levy. Fire and Emergency accepted written submissions on a discussion document over a four-week period between 5 April and 2 May 2023. Fire and Emergency published the discussion document on their website and publicised the consultation through their social media channels. They also proactively informed stakeholders that have engaged with the broader Fire and Emergency funding review since 2019. This included stakeholders from the following sectors: local government, insurance, energy, forestry, rural, supermarkets, property, aviation, museums and galleries, and business, as well as the NZPFU. We also met with key stakeholders to further discuss the implementation needs of the insurance sector.

106. Fire and Emergency provided an analysis of submissions which was used to inform the analysis in this CRIS. However, we also had access to the individual submissions which we have reviewed to inform our analysis.

107. Fire and Emergency received 19 submissions – 14 were opposed, four were supportive and one was undecided. Submitters raised the following key issues:

- Fire and Emergency had not considered opportunities to be more efficient in its spending. Submitters noted that the 40 per cent increase in funding from 2017 has not led to discernible improvements in Fire and Emergency's services.
- An increase in the transitional levy will add to other factors increasing insurance premiums, including weather-related events and the increase in the EQC levy. This will likely lead to more people opting for less insurance coverage.
- The $10 million Crown contribution to Fire and Emergency is insufficient to cover the 'public good' services it provides.
- The insurance sector would expect to have 12 months to implement a new levy rate. A shorter period increases the risk that mistakes will be made in calculating the levy charge for customers, which may lead to insurers being subject to penalties from Fire and Emergency or from the Financial Markets Authority.
- The assumption of two per cent annual growth of the levy (through inflation and growth in insurance policies) does not align with the historical trend of close to three per cent growth.

108. Following submissions we considered a lesser increase to the transitional levy, with cuts made to other expenditure (as discussed above). However, we considered that the risks of reduced service quality were significant. As noted above, there has not been time to consider an increase to the Crown contribution. The projections of revenue have been updated to incorporate a 2.7 per cent annual growth in the levy to better align with the historical trend of close to three per cent growth (an increase from the previously assumed 2 per cent annual growth in the levy).

109. We consider it may have added limited value to consult on the alternative 9 per cent increase. In line with the general opposition to a 12.8 per cent increase, we consider most arguments for a lesser increase would have focussed on whether Fire and Emergency should be more efficient. Submitters did not argue that a reduction in Fire and Emergency's service levels would be justified by a lesser increase in costs for levy payers.

110. We also consider it may have been beneficial to proactively contact iwi or other Māori authorities about the consultation. Although timeframes for submitting were relatively short, proactive communication of this work may have brought forward submissions discussing the impacts of this change on Māori businesses, NGOs and marae.

Conclusions and recommendations

111. To enable Fire and Emergency to meet increased costs as a result of settling a new Collective Employment Agreement with the NZPFU, increasing the transitional levy by 12.8 per cent is recommended.

Implementation plan

112. Changes to the transitional levy will require an amendment to the *Fire and Emergency New Zealand (Levy Rates and Information Requirements in the Transitional Period) Regulations 2017.* This will occur through the regulation amendment process.

113. Any change to the transitional levy requires system changes for both Fire and Emergency and the insurance sector (the insurance sector calculates and collect the levy on behalf of insurance policyholders). It is critical that the organisations involved have enough time to carry out necessary updates to their systems to enable the new levy amounts to be collected.

114. Fire and Emergency will update and provide new guidance on the new transitional levy rates to support stakeholders to understand the change. Given the changes to the system relate to the amount of transitional levy paid only (as opposed to process and information requirements), it should be relatively simple for stakeholders to adapt to the new approach.

115. To provide certainty for the sector to begin implementation, the policy decisions and regulations will be considered by Cabinet at the same time. Timeframes have been tightened to allow for close to 11 months for implementation. A later implementation date would have significantly affected Fire and Emergency's financial position.

Monitoring and evaluation

116. Existing monitoring and evaluation will be used to monitor and evaluate this change. Fire and Emergency provide regular performance updates to the Department which will provide information as to whether the intended effects of this change are occurring. These performance updates include:

- Quarterly financial reports
- Statement of Performance Expectations
- Annual report, including performance measures (for example, response times, speed to process fire permits, other organisational milestones)

117. We note that Fire and Emergency has historically underestimated annual levy growth, which has led to significant surpluses since 2017. The more recent

projections of levy growth will be evaluated and will inform the first review of the Part 3 levy (likely to begin in three years' time).[40]

A broader consideration of Fire and Emergency's costs will occur when the new Part 3 levy is designed

118. This change relates only to the increased ongoing costs as a result of settlement between Fire and Emergency and the NZPFU. These costs have already been agreed to and must be paid by the organisation.

119. The extent to which Fire and Emergency's existing costs before the NZPFU settlement are reasonable will be considered when the new Part 3 levy is being designed.

Review

120. No review is required as any change to the transitional levy will cease to take effect from 1 July 2026 when the new Part 3 levy takes effect. The design of the Part 3 levy is in effect a review of the transitional levy.

[40] Section 142 of the Fire and Emergency Act 2017 requires the Minister of Internal Affairs to review the levy settings at least once every three years (this applies to the Part 3 levy, not the transitional levy). Policy decisions for the initial Part 3 levy settings will occur next year, so data on levy growth can only be effectively evaluated when the review of these initial levy settings occurs.

Appendix A: Full list of Fire and Emergency's functions

1. In addition to fighting fires, Fire and Emergency must carry out the following functions:[41]

   - promote fire safety, including providing guidance on the safe use of fire as a land management tool;
   - provide fire prevention, response and suppression services;
   - stabilise or render safe incidents that involve hazardous substances;
   - provide for the safety of persons and property endangered by incidents involving hazardous substances;
   - rescue persons who are trapped as a result of transport accidents or other incidents;
   - provide urban search and rescue services; and
   - efficiently administer the FENZ Act.

2. In addition, Fire and Emergency assist in the following matters, should it have the capability and capacity to do so, including:[42]

   - responding to medical emergencies;
   - responding to maritime incidents;
   - performing rescues, including high angle line rescues, rescues from collapsed buildings, rescues from confined spaces, rescues from unrespirable and explosive atmospheres, swift water rescues and animal rescues;
   - providing assistance at transport accidents;
   - responding to severe weather-related events, natural hazard events, and disasters;
   - responding to incidents in which a substance other than a hazardous substance presents a risk to people, property, or the environment;
   - promoting safe handling, labelling, signage, storage, and transportation of hazardous substances; and
   - responding to any other situation if Fire and Emergency has the capability to assist.

[41] Section 11 of the FENZ Act.

[42] Section 12 of the FENZ Act.