Regulatory Impact Statement

Auckland Council's Request for Additional Rates Transition Management Tools

Agency Disclosure Statement

This Regulatory Impact Statement (RIS) has been prepared by the Department of Internal Affairs (the Department). It provides an analysis of:

- the Auckland Council's request for transitional regulations under the Local Government (Auckland Transitional Provisions) Act 2010 (Transition Act) to provide additional tools to manage the transition to a single rating system for Auckland;
- the reasons for the Council's request; and
- timing considerations for providing the Council with additional rates transition management tools.

The RIS does not consider in detail the relative merits of various options for managing the transition to a single rating system for Auckland, as the decision about which tools to apply is for the Council to make, not the Government. The RIS does, however, outline the options considered by the Council, as evidence of the inadequacy of the existing rates transition toolbox.

The RIS concludes that:

- there would be benefits in providing the Auckland Council with additional flexibility to manage the transition to a single rating system for Auckland;
- providing the Council with additional rates transition management tools would be consistent with the Government's underlying policy objective to enable the Council to protect ratepayers (particularly those on low and fixed incomes, and small businesses) from sudden and significant increases in rates liability [CAB Min (09) 39/6A refers];
- the Council has generally had valid reasons for discounting the existing rating tools that have been ruled out; and
- the Council would remain accountable for how it chooses to manage the rates transition.

The Department supports the proposed transitional regulations under the Transition Act.

Treasury's Regulatory Impact Analysis Team (RIAT) has advised that the proposed transitional regulations are not likely to have any significant impact or risk.

Paul James, Chair, Regulatory Impact Assessment Panel

16 April 2012

Status quo and problem definition

Summary of problem definition

1. The Auckland Council has requested greater flexibility to manage the transition to a single rating system across Auckland. The existing rates transition toolbox available to the Council is inadequate to smooth the impact of the transition on individual ratepayer liability. This is due to the complexity of the factors driving changes in rating levels in Auckland.

2. The Council considers that additional tools are required to enable it to give full effect to the Government's underlying policy objective to enable the Council to protect ratepayers (particularly those on low and fixed incomes, and small businesses) from sudden and significant increases in rates liability [CAB Min (09) 39/6A refers].

3. The Council has provided the Department of Internal Affairs (the Department) with detailed information about the existing rating tools it has considered, and discounted, to manage the rates transition. The decision about which rating tool or tools to use is for the Council to make, not the Government. However, the information about the options considered by the Council provides evidence of the limitations of the existing rates transition toolbox.

Single rating system for Auckland

4. The Auckland Council is required to introduce a single rating system across Auckland from 1 July 2012. The Council has the same rating options as other local authorities, except that it:

   - must use the capital valuation basis for general rates in 2012/13;[1]
   - has access to special rates transition management powers in the Local Government (Auckland Transitional Provisions) Act 2010 (Transition Act), in addition to general powers; and
   - may be constrained in terms of the availability or cost of some options by reliance on the computer rating systems of the seven former territorial authorities.

5. The move to a single rating system will lead to substantial changes in the distribution of rates, due to the significant differences in the rating policies of the former councils. Some ratepayers will face significant levels of change. The effects of property revaluations (following a period of volatility in property markets) on top of the standardised rating regime mean that there are significant variations in impact within most categories of ratepayers.

6. The following table, provided by the Council, sets out the number of ratepayers facing increases or decreases at various percentage levels under the single rating policy (with no transition policy):

[1] Local Government (Auckland Transitional Provisions) Act 2010, section 38. It was necessary to legislate to enable the creation of an Auckland wide valuation roll based on one valuation system before the Council existed. The Council will subsequently be able to change to an annual or land value based system

Table 1 – Number of ratepayers facing rates change by percentage level

Change in rates	<-10%	-10% to 0%	0% to 10%	10% to 15%	>15%
2012/13	111,863	80,522	122,806	79,368	112,239

7. The Council has decided a transitional approach is needed to smooth the impact of the 2012/13 increases/decreases over a three year period.

Existing tools to manage rates transition

8. Existing tools in the Local Government (Rating) Act 2002 (Rating Act) and the Transition Act provide the Council with significant flexibility to manage the transition to a single rating system. Generic rating tools in the Rating Act include uniform annual general charges, differential general rates, targeted rates, rates remissions and postponement of rates. These are summarised in Appendix A. The tools are flexible and are not mutually exclusive, but can be combined.

9. The Transition Act empowers the Council (uniquely) to adopt and implement a rates transition management policy to help manage the impact on individual ratepayers of implementing its rating system over a three year period (1 July 2012 to 30 June 2015). The underlying policy objective was to enable the Council to protect ratepayers (particularly those on low and fixed incomes, and small businesses) from sudden and significant increases in rates liability [CAB Min (09) 39/6A refers].

10. The Transition Act provisions allow the Council to set limits (in dollar and/or percentage terms) on the amount a ratepayer's rates can increase or decrease in any of the three years of transition. Different change limits can be set for increases and decreases, but only to achieve a net neutral outcome (i.e. so that foregone increases are funded by foregone decreases). The provisions do not enable the Council to set different limits for different categories of ratepayer, such as residential or business properties.

Auckland Council's request for additional tools

11. The Auckland Council wishes to adopt a rates transition management policy under the Transition Act. However, it has advised that the complexity of the factors driving changes in rating levels in Auckland has resulted in major variations between properties within the same rating category and between properties within the same area. This has made it difficult for the Council to use the existing tools to moderate the extent of changes to individual ratepayer liability, or to accurately target rates relief.

12. The Council has therefore requested that the rates transition options be extended to:

    - enable different change limits to be set for different categories of property, such as business, residential and farm/lifestyle;
    - enable a phased approach, whereby the annual change is a proportion of the difference from the previous year's rates; and
    - enable the exclusion of specified rates, such as targeted rates, from the calculation.

The desired outcomes and objectives

13. The desired outcome is for the Auckland Council to have access to the tools it needs to give effect to its objectives for the rates transition. Decisions about which tools, or combinations of tools, are most appropriate to apply are for the Council to make, not the Government. The Council is accountable for these decisions to its voters and ratepayers.

14. The Council's primary objectives for its rates transition management policy are to:

- ensure the rate of change is affordable for ratepayers;
- ensure the transitional approach is cost neutral. Any relief from rates increases is to be fully funded by reduced rates decreases;
- minimise change impacts. This includes shifting the cost of rates transition to ratepayers who would otherwise face a decrease in rates (if there was no transition policy), rather than to ratepayers who would otherwise face little or no change;
- avoid cross-subsidisation between sectors. As some of the largest rates increases are faced by large utilities previously rated on land value, significant costs would transfer to other categories of ratepayer if business ratepayers are not ring-fenced; and
- exclude "voluntary" targeted rates (such as rates to repay home insulation loans) from the transition policy so they are not subsidised by other ratepayers.

Regulatory impact analysis

Range of options considered by Auckland Council

15. The Auckland Council comprehensively considered a range of existing rating tools to achieve its objectives for its rates transition management policy. The options considered by the Council are set out in Appendix B. The Council discussed the options with the Department on several occasions and considered further combinations of options at the Department's request.

16. The Council's draft 2012/22 long-term plan seeks feedback on two options (discussed below).

Council's proposed remission option (no law change required)

17. The Council's proposed transitional remission option in the draft long-term plan involves a differential remission policy under which those facing the largest increase in each category (business or residential/farm/lifestyle) are entitled to a remission funded by other ratepayers in that category. This option does not require any law change.

18. The proposal is to remit rates as follows:

- residential ratepayers - remission of rates above an increase of 15 per cent or $300 (whichever is higher);
- farm and lifestyle ratepayers - remission of rates above an increase of 15 per cent or $500 (whichever is higher); and
- business ratepayers - remission of rates above an increase of 20 per cent or $1000 (whichever is higher), with a maximum remission of $6000.

19. The key disadvantages of the remission option, identified by the Council, are: the 15 per cent maximum annual increase for residential ratepayers is higher than desirable in terms of affordability; and it would result in a large number of ratepayers with increases just below the maximum limit. Further detail about the advantages and disadvantages of the remission option is provided in Appendix B.

Council's preferred combination option (law change required)

20. The Council's preferred combination option in the draft long-term plan, which would require legislative change, involves capping increases and decreases for residential/farm/lifestyle ratepayers and a separate phased approach for business ratepayers:

- for non-business ratepayers, limit rates increases by a 10 per cent cap each year, and limit decreases by caps of 5.6 per cent (year one), 3.8 per cent (year two), and 3.7 per cent (year three); and
- for business ratepayers, spread the impact of both increases and decreases over three years by requiring ratepayers to pay/sacrifice (approximately) one-third of the projected change to their rates each year.

21. The key advantages of the combination option, identified by the Council, are: it would minimise the amount of change; and it would be more affordable for most residential ratepayers, with the exception of those ratepayers who would otherwise face decreases (with no transition policy). Further detail about the advantages of this option, compared with the remission option, is provided in Appendix B.

Comment on Council's consideration of options

22. The Auckland Council has had considerable flexibility in the design of its proposed single rating system, with the ability to consider and reflect the transition implications of different options. The Council has decided on its preferred rating system and transition management policy objectives after considering trade-offs between different objectives. The Council is seeking transitional regulations to enable it to implement a preferred approach that reflects decisions about its objectives for rates transition.

23. It is not the Department's role to review the merits of the Council's particular trade-offs and judgements in arriving at those decisions. However, the Department requested information about the options considered by the Council to ensure sufficient evidence of the inadequacy of the existing rates transition toolbox.

24. The Department is satisfied that the Council has considered all options, and many potential combinations of options, currently at its disposal to manage the rates transition. The Council has had valid reasons for discounting the options that have been ruled out.

25. The complexity of the factors driving changes in rating levels has resulted in major variations between properties within the same rating category and between properties within the same area. This has made it difficult for the Council to use differential or targeted rating mechanisms to moderate or manage the extent of underlying change.

26. The Department considers there would be benefits in providing the Council with greater flexibility to manage the transition to a single rating system for Auckland. Expanding the Council's toolbox would be consistent with the underlying policy objective for rates transition (referred to in paragraph 2).

Consultation

27. This RIS has been prepared by the Department, which administers the Transition Act and the Rating Act. The Parliamentary Counsel Office, Crown Law Office and the Auckland Council have been consulted in the development of this RIS. The Department of the Prime Minister and Cabinet and Treasury have been informed of the content of this RIS.

Conclusions and recommendations

28. The Department's view is that there are no technical or policy disadvantages in providing the additional flexibility sought by the Auckland Council. The additional flexibility will enable a broader range of transition objectives to be met in circumstances that are more varied and complex than anticipated when the Transition Act was developed. Had these features been proposed at that time, it is likely they would have been supported by the Department.

29. Making such changes now, to allow a specific proposal to proceed, does however raise different considerations:

   - agreeing to regulations to enable the Council to proceed with its specific proposal may result in a public perception that the Government is effectively endorsing the Council's rating policy;

   - agreeing to regulations may be seen, by the Auckland Council, and by other councils particularly in the context of future voluntary reorganisations, as a precedent for requests for regulations or legislative amendments; but

   - not agreeing to the Council's request carries the risk that the Government may be perceived as being responsible for both the problem (requiring a single capital value rating system) and the lack of a better solution to the affordability of rates increases as the result of transition to a new rating system.

30. While the sensitivity of rates and the technical complexity of the causes of rating changes in Auckland pose challenges to successful management of such issues, this could be achieved by clear communications about the changes. For example, a decision to provide the Council with additional tools must emphasise that the Government is only providing the Auckland Council with greater flexibility, and that the Council is solely responsible and accountable for decisions about how the rates transition is managed.

31. The Department suggests transitional regulations to provide the Auckland Council with additional tools to manage the transition to a single rating policy for Auckland. As requested by the Council, the additional tools should:

   - enable different change limits to be set for different categories of property, such as business, residential and farm/lifestyle;
   - enable a phased approach, whereby the annual change is a proportion of the difference from the previous year's rates; and
   - enable the exclusion of specified rates, such as targeted rates, from the calculation.

Implementation

32. The Auckland Council is required to adopt its rates transition management policy when it adopts its 2012/22 long-term plan in June 2012. Councillors need to make a decision on the Council's approach to rates transition on 23 May in order to meet this timeframe.

33. The requested changes to the legislative framework could only be achieved within this timeframe with transitional regulations by Order in Council under section 5 of the Transition Act.

34. The authority for such regulations, and any such regulations themselves, expire on 31 October 2013. However, if the Council lawfully adopts its rates transition management policy before then, that policy can be applied for the full three years of transition (2012/13, 2013/14, 2014/15), notwithstanding the expiry of aspects of the legal authority for the policy.

35. To enable transitional regulations to be in force by the Council's deadline of 23 May 2012, policy agreement to the regulations would be required in April 2012.

Monitoring, evaluation and review

36. There would be no need to monitor and evaluate the effectiveness of transitional regulations to provide the Auckland Council with additional rates transition management tools. The Government is simply providing the Council with additional flexibility to manage the transition to a single rating policy for Auckland. It is for the Council to decide which tools (or combinations of tools) to apply, and to be accountable for that decision.

Appendix A

Generic rating tools under the Local Government (Rating) Act 2002

1. In addition to the unique rating tools in the Local Government (Auckland Transitional Provisions) Act 2010, the Auckland Council also has at its disposal existing generic rating tools under the Local Government (Rating) Act 2002. The tools, described below, can be combined.

2. A local authority's rates may include:
   - a general rate;
   - a uniform annual general charge; and
   - one or more targeted rates.

3. The general rate can:
   - be a uniform rate per dollar of capital value; or
   - be differential so that different amounts per dollar of capital value apply to different categories of property (determined by property use, zoning, location, services provided or available, etc).

4. A uniform annual general charge may be:
   - a fixed amount per property; or
   - a fixed amount per separately used or inhabited part of a property.

5. A targeted rate is specific to one or more activities and may be set:
   - on all properties in the district or only on specified categories of property (determined by property use, zoning, location, services provided or available, etc);
   - calculated on the basis of valuation, area, a fixed amount per property or separately used part, service provided etc; and
   - on a uniform or differential basis on the categories of property to which it applies.

6. Rates can be remitted (in full or in part) in accordance with a remissions policy adopted using the special consultative procedure. There are no restrictions on the criteria for remissions that can be included in a policy. Remitted rates must be accounted for as if paid by the local authority on behalf of the ratepayer (i.e. as expenditure rather than as foregone revenue). There is no constraint on how the cost of remissions must be funded by the local authority.

7. Liability for rates can be postponed (in full or in part) in accordance with a postponement policy adopted using the special consultative procedure. There are no restrictions on the criteria for postponement that can be included in a policy, or on when the policy can provide for postponed rates to become payable. The policy can provide for a fee to cover the net cost of the postponement to be added to the amount owing.

Appendix B

Auckland Council's consideration of existing rating tools

1. The existing rating tools, and combinations of tools, considered by the Auckland Council include:
    - setting the uniform annual charge at various amounts;
    - using different proportions of targeted and general rates;
    - varying business and rural differentials;
    - a range of rates remission and postponement policies;
    - a generic capping option, with a cap on both increases and decreases (the cap on decreases being calculated to fully fund the cap on increases);
    - combining differential remissions and caps, or having two layers of remissions;
    - a phased option that requires ratepayers to pay one-third of their projected rates change (increase or decrease) each year. This option was considered to be legally possible but not technically feasible to implement without a law change; and
    - spreading the transition over four or more years.
2. The Council's draft 2012/22 long-term plan seeks feedback on two options (discussed below).

Council's proposed remission option (no law change required)

3. The Auckland Council's proposed transitional remission option in the draft long-term plan involves a differential remission policy under which those facing the largest increase in each category (business or residential/farm/lifestyle) are entitled to a remission funded by other ratepayers in that category. This option does not require any law change.
4. The proposal is to remit rates as follows:
    - residential ratepayers - remission of rates above an increase of 15 per cent or $300 (whichever is higher);
    - farm and lifestyle ratepayers - remission of rates above an increase of 15 per cent or $500 (whichever is higher); and
    - business ratepayers - remission of rates above an increase of 20 per cent or $1000 (whichever is higher), with a maximum remission of $6000.

Key advantages and disadvantages of remission option (as identified by Council)

5. The key advantages of the remission option identified by the Council are that:
    - it achieves the Council's objectives of avoiding cross subsidisation between sectors and allows exclusion of voluntary targeted rates; and
    - it is administratively and technically simple to implement.
6. The key disadvantages of this option, identified by the Council, are that:
    - the 15 per cent maximum annual increase for residential ratepayers is higher than desirable in terms of affordability;
    - it results in a significant amount of change for many ratepayers as the costs of remissions are funded by rate increases to all other ratepayers. This results in a large number of ratepayers with increases just below the maximum limit; and
    - there would be a significant number of ratepayers with rates increases above 15 per cent, including ratepayers with increases below the dollar limits, business

ratepayers with increases between 15 and 20 per cent, and business ratepayers whose increases significantly exceed the $6000 maximum remission.

Council's preferred combination option (law change required)

7. The Auckland Council's preferred combination option in the draft Long-term plan, which would require legislative change, involves capping increases and decreases for residential/farm/lifestyle ratepayers and a separate phased approach for business ratepayers:

   - for non-business ratepayers, limit rates increases by a 10 per cent cap each year, and limit decreases by caps of 5.6 per cent (year one), 3.8 per cent (year two), and 3.7 per cent (year three); and
   - for business ratepayers, spread the impact of both increases and decreases over three years by requiring ratepayers to pay one-third of the projected change to their rates each year.

Key advantages of combination option (identified by Council)

8. The key advantages of the preferred combination option, identified by the Council, are:

   - it is cost neutral (limits on increases are fully funded by limits on decreases);
   - it would achieve the Council's objective of minimising the extent of change for ratepayers, as it would have minimal impact on ratepayers who would otherwise face little or no change (if there was no transition policy);
   - it would be more affordable for most residential ratepayers, with the exception of those ratepayers who would otherwise face decreases (with no transition policy);
   - the proportion of rates paid by business is maintained. There is no cross-sector subsidisation; and
   - there is no need to ring-fence large businesses to keep the transition affordable for other ratepayers.

Transitional regulations required

9. The Auckland Council's preferred option requires transitional regulations under section 5 of the Transition Act. This is because the capping mechanisms authorised by the Transition Act do not provide for a differentiated approach for business and non-business ratepayers, or the exclusion of specified rates from the calculations.

10. In addition, the Council has advised that the combination option's phased approach for business ratepayers would only be technically feasible to implement if the Transition Act is changed to allow the Council to set transition rates as a proportion of the difference between the previous year's and this year's rates. This is due to constraints with the legacy computer rating systems the Council is using.