Regulatory Impact Statement: Local Government Water Services (Transitional Provisions) Bill

Coversheet

Purpose of Document	
Decision sought:	Agree to final policy proposals to support the second stage of Local Water Done Well via the Local Government Water Services (Transitional Provisions) Bill.
Advising agencies	Department of Internal Affairs
Proposing Ministers:	Hon Simeon Brown, Minister of Local Government
Date finalised:	14 March 2024

Problem Definition

Under the current settings, council ownership and delivery of water services is financially unsustainable and not meeting minimum quality standards for communities. Analysis indicates that there is a deficit of at least $120 billion needed to improve New Zealand's water services. Five key root causes have been identified:

- **Institutional barriers to more efficient delivery of water services:** The fragmented and dispersed manner in which water services are delivered across 67 local authorities of varying sizes and capabilities has an impact on their overall quality and efficiency.
- **Poor incentives on councils to adequately invest in and fund water services:** Councils and their executives have to prioritise investments and make trade-offs across a portfolio of activities, often in the context of a three-year political cycle.
- **Varied decision-making quality:** Water services are capital intensive and complex. Those involved in decisions may not have the skills and capabilities needed to provide effective asset management and delivery of water services or to ask the right questions of those that manage water services, which leads to overall lower quality decision-making.
- **Funding constraints:** Poor past management and investment decisions have left many councils with water services that have not been adequately maintained or renewed.
- **Incomplete regulatory and stewardship oversight and monitoring:** Since the establishment of Taumata Arowai, the regulation of drinking water has improved significantly but New Zealand does not have economic regulation to ensure the efficient financial management and delivery of services by councils and protect the interests of consumers.

Executive Summary

Local authorities (councils) provide drinking water, wastewater and stormwater services to most New Zealanders. There are currently 67 councils that own, operate and provide water services to around 85 percent of New Zealanders – the remainder of water services are provided by smaller private and community-based schemes. Councils are responsible and accountable under the Local Government Act 2002 (LGA) to their ratepayers through the local democratic system for the delivery of water services to their communities. There are varying delivery models for water.

There have been issues with New Zealand's water services for a considerable period, and these were highlighted during the outbreak of gastroenteritis in August 2016 in Havelock North. In response to the findings of an inquiry into the Havelock North contamination event instigated by the previous National-led government, the previous Labour led government undertook the Three Waters Reform (also known as Affordable Water Programme), a centralised response where ownership of water services assets shifted to multi-regional entities with greater borrowing capacity.

Local Water Done Well

The Coalition Government did not support the Three Waters Reform but recognises that water services delivery must be improved urgently. As an alternative to the previous government's centralised approach to reform, the Government's 100-Point Economic Plan and National Party's Local Water Done Well (LWDW) manifesto prioritises localism and flexibility, while balancing high standards for water quality and investment in infrastructure. There are three key stages to implement LWDW:

- Water Services Act Repeal Act 2024 (Bill One) repealed the Water Services Entities Act 2022 in February 2024 to end the previous government's 10-entity model and to restore powers and responsibilities for water services delivery to local authorities.
- Local Government Water Services (Transitional Provision) Bill (Bill Two), which is covered in this Regulatory Impact Statement (RIS) and will set out the framework and initial operating environment for the replacement regime. This omnibus bill will make relevant amendments to the LGA02 and Local Government (Auckland Council) Act 2009 (LGACA). It will:
    - establish foundational information disclosure requirements to support the design and implementation of a new economic regulatory regime;
    - require councils to prepare water service delivery plans to be submitted within 12 months of the Bill's enactment that will set out a council's approach for delivering their water services in ways that are financially sustainable and meet regulatory compliance and service standards;
    - remove barriers and streamline requirements for establishing council-controlled organisations (CCOs) under the LGA to make it easier for councils to shift the delivery of water services into more financially sustainable organisational structures; and
    - explore options for the financial separation of Watercare from Auckland Council.
- The Local Government Water Services Bill (Bill Three), which will provide the settings for economic regulation.

As a package, all three stages of LWDW must be implemented – without each component, it is likely that water services investment will continue to be underfunded and financially unsustainable. This RIS focuses on the transitional provisions to be provided for in the second Bill.

Strategic options to address the problem

There are four broad approaches, known as strategic options, available to the Government as it considers how councils can own and deliver water services that are financially sustainable and meet minimum regulated quality standards in the long-term. The four strategic options are:

- Strategic Option One: Status quo, being reliance on the current provisions of the LGA to provide for council accountability in financial management and delivery of water services, and current regulatory settings;
- Strategic Option Two: Transitional provisions to focus councils on the sustainable financial delivery of their water services, inform development and implementation of economic regulation and prepare councils for full economic regulation;
- Strategic Option Three: Economic regulation without transitional provisions; or
- Strategic Option Four: Economic regulation coupled with stronger direction from central government to councils on how to manage and organise their delivery of water services.

Strategic Option Two is the Department's recommended approach, as it aligns with LWDW and provides the necessary incentives and support for councils to improve delivery of their water services in the lead up to full economic regulation in Bill Three. These proposals ensure retained council ownership and control over water services, prioritise ring-fenced funding for water infrastructure, and support transitional provisions for economic regulation to provide greater accountability to consumers and communities.

Four key proposals in RIS to support Strategic Option Two

There are four key proposals within the RIS as part of Strategic Option Two. Proposals One to Three are a package, and Proposal Four is a discrete option specifically to fast-track options for improvements for Auckland Council and Watercare.

Proposal One: Foundational information disclosure to inform the regulatory regime

- Option One: No information disclosure is required (status quo);
- Option Two: A two phase, gradual approach to foundational information disclosure (Department recommended);
- Option Three: Comprehensive information disclosure led by the Commerce Commission modelled on the Commerce Act 1986.

Option Two will require councils to collect more comprehensive information regarding their assets to inform future investment of water services delivery and support proposals for future economic regulation. Councils are likely to prefer this option as it will be easier to implement and aligns with the requirements for Proposal Two.

Proposal Two: Systems are set up to focus councils on achieving the financially sustainable delivery of their water services that meet regulatory standards

- Option One: No Water Service Delivery Plans are required (status quo);
- Option Two: Council water services providers must submit Water Service Delivery Plans to be accepted by the Department of Internal Affairs (the Department) as compliant with statutory plan requirements within 12 months of enactment of Bill Two (Department recommended);
- Option Three: Water services providers submit a Water Services Delivery Plan (WSDP) to be assessed and approved by the Department as providing a sound basis for sustainable delivery of water services, within 12 months of enactment of Bill Two.

Option Two will improve councils' transparency and assurance to local communities, regulators, and the Government that each council has a 'plan' for delivering high-quality water services in a financially sustainable manner. It will also support a smoother transition to economic regulation. The role of the Department in checking that WSDPs meet statutory requirements means that councils are responsible for the content and proposals of their WSDPs, which aligns with LWDW. By contrast, Option Three would involve an assessment of the council's proposals by the Department and potential directions to councils from central government on how they should organise delivery of their water services, with a shifting of accountability from councils to the centre for the content of plans.

Proposal Three: Transitional arrangements to streamline the process for establishing new water services council-controlled organisations (CCOs)

- Option One: No legislative amendments are made (status quo);
- Option Two: Targeted amendments to clarify councils' ability to jointly consult on proposal to establish a joint water services CCOs;
- Option Three: Bespoke arrangements for establishing water services CCOs under current LGA settings (Department recommended).

Option Three creates an optional mechanism for councils to enable streamlined processes for establishing water services CCOs (for potential use by any council considering a CCO under LGA settings – sole or joint). It also reduces the analytical and consultation burdens on individual councils by providing for joint consultation run by a joint committee, and for minimum consultation and information requirements. Consultation is still largely bound by the requirements of the LGA and utilises the joint committee mechanism in the LGA to ensure ease of implementation (where joint CCOs are being considered).

Proposal Four: Explore options for the financial separation for Watercare

- Option One: No change (status quo);
- Option Two: Enhanced status quo with Crown support (Auckland Council's preferred option);
- Option Three: Independent Council-owned organisation (Watercare 2.0);
- Option Four: Mixed council and consumer ownership (Department recommended).

The Department recommends Option Four because it is most likely to achieve financial separation and ringfencing of Watercare from Auckland Council. 9(2)(ba)(i), 9(2)(g)(i) [redacted] If financial separation is achieved, both Watercare and Auckland Councill will likely be able to take on more debt than they would without separation. This will improve Watercare's capacity to invest in upgrades to existing infrastructure, deliver new infrastructure to enable growth and reduce costs to communities. It will also improve Auckland Council's capacity to take on more debt to invest in transport and other priorities. Auckland Council's initial preferred option is Option Two.

Population impacts of proposals

The Department recognises that given the importance of water for all New Zealanders and the wider economy these proposals are likely to have an impact across the country. The impacts of the water services crisis differ regionally, as some councils are in worse off situations than others. Enabling councils to retain ownership and leadership of their water services will ensure that locally-based decisions in the proposals are prioritised.

All population groups are expected to benefit over the long term, though in the short term an increased focus on ensuring the financial sustainability of services could result in increased changes for some.

In recognition of the Crown obligations under Te Tiriti o Waitangi, the LGA requires local authorities to facilitate Māori participation in local government decision-making processes. Māori have been critical of local authority responses to this obligation. The proposals do not seek to address implementation issues of the LGA with regards to Māori participation

Limitations and Constraints on Analysis

There are several limitations and assumptions associated with the analysis of the proposals contained in the RIS. These are detailed below.

Limitations with problem definitions and analysis

- The Department has assumed that if central government intervention is not progressed, under-investment in water services delivery will continue and the problem will continue to worsen. All three stages of LWDW need to be implemented, otherwise under the status quo council owned water services will continue to degrade due to inconsistent management and under-funding.
- The analysis of these policy options was completed at pace to meet the required legislative timelines set by the Minister for Local Government to implement the transitional provisions and build the regulatory environment to support Bill Three.
- Some analysis relies on work completed as part of the previous government's Three Waters Reform (including the Affordable Waters Programme). Some significant step changes have occurred within the water services delivery system since the previous RIS were drafted, such as the establishment of Taumata Arowai. The previous Three Waters Reform included a significant amount of consultation – both at the exploratory problem definition phase during the Three Waters Review and during the design of the reform. Where relevant, the Department has considered feedback collected during these work programmes for the problem definition.
- The evidence highlighted in the problem definition is collected from a range of councils across New Zealand. A detailed comparison or analysis of all councils have not been included as part of this problem definition. As described previously, it is important to note that each council is different, so some situations described may not apply to all.
- The economic context for each council's 2021-2031 long-term plans (LTPs) may present an overly optimistic view of council finances. Council finances will have been significantly affected by unforeseen events (such as extreme weather events) and optimistic planning assumptions (now impacted by higher levels of inflation and interest rates). It is expected that the new LTPs (2024-2034), which are currently being drafted and consulted on, will show deteriorating financial positions for the water services operated by most councils.
- The Department has also relied heavily on evidence that has been collected from media reports due to time constraints. The Department did not have sufficient time to validify the statements made in media articles with the affected councils.
- The Department has used various Annual Performance Reports conducted by Water New Zealand. While these provide a comprehensive picture of the water services across New Zealand, they are voluntary and therefore do not have information from all suppliers.

Limitations of Strategic Options

- As discussed, LWDW is the counterproposal to the previous government's Three Waters Reform and the Affordable Water Programme. The key parameters of LWDW prioritise council ownership of their water services assets and delivery, greater accountability to local communities, financial sustainability, and a move to economic regulation. As a result, the proposed Strategic Options (Section 2) are informed by, and limited to, the government's policy. This prioritisation has meant that other potential strategic options or delivery models have not been included for consideration (for example, the centralised delivery model proposed as part of the reform) and short- to medium-term objectives are prioritised over long-term impacts.

Limitations with development of policy proposals

- While this RIS was drafted, local councils were in the process of drafting their LTPs prior to public consultation. This meant that there was limited time to engage and test these proposals with councils. As a result, there are no views of consulted stakeholders in this RIS.
- However, the Department has been guided by the Technical Advisory Group (TAG), which includes several experienced council and infrastructure experts. The TAG provided input into the proposals included in this RIS but the feedback on the proposals is not included (as this was not the role of the TAG).
- Auckland Council has led the policy programme on options for Watercare and been supported by the Department. Other agencies involved in this co-design process include Crown Infrastructure Partners and the Treasury. No external consultation has been done on these proposals.
- A small number of select councils were engaged on the LGA amendments and their feedback on the perceived barriers to the LGA were considered in the policy design of the option. They were not consulted on the proposed policy options.
- Due to timeframes, it was not possible for the Department to complete a full analysis of the costs and benefits of the four proposals beyond qualitative estimates. They should be considered as indicative only.
- 9(2)(ba)(i), 9(2)(g)(i) [redacted]

Responsible Manager(s) (completed by relevant manager)

Bex Sullivan

Deputy Executive Director Water Services Policy

Local Government Branch

Quality Assurance (completed by QA panel)

Reviewing Agency:	Department of Internal Affairs
Panel Assessment & Comment:	The panel considers that the information and analysis summarised in the RIA *partially meets* the quality assurance criteria. The RIA provides a clear description of the problem and its root causes. It identifies the scope and timing constraints resulting from government policy direction in this area and within these clearly identifies strategic and detailed options going forward and uses an appropriate framework to assess these. The timeframe constraints have meant there has been no opportunity for sufficient consultation on the proposed options, as required by the Cabinet criteria. The timeframes have also meant that there have been limitations on analysis; most notably there is no quantitative information in the RIA on the effects of various options on each proposal. 9(2)(ba)(i), 9(2)(g)(i) [redacted] The panel's assessment was also limited by timeframe constraints and the assessment took a truncated process. The panel provided a final set of comments on the revised draft of the RIA but did not see the final version. The panel were however of the view that this would not alter its overall assessment.

Glossary

A&A Board	Appointment and Accountability Board
CCO	Council-controlled organisation
the Department	the Department of Internal Affairs
LGA	Local Government Act 2002
LGACA	Local Government (Auckland Council) Act 2009
LGFA	Local Government Funding Agency
LGNZ	Local Government New Zealand
LTP	Long-term plan
LWDW	Local Water Done Well
NPS-FM	National Policy Statement for Freshwater Management
9(2)(b)(i) [redacted]	[redacted]
TAG	Technical Advisory Group
WICS	Water Industry Commission of Scotland
WSDP	Water Services Delivery Plans

Introduction

1. The Coalition Agreements provide for the repeal of the Water Services Entities Act 2022, which happened in February 2024. The Government had campaigned on a clear direction for water services, which included a detailed policy document setting out features of their desired system arrangements and a commitment to repeal the legislation that established water services entities.

2. The National Party manifesto, Local Water Done Well (LWDW), described three key components of the policy.

   a) A voluntary regime, where councils could choose their preferred model for water services delivery, provided they could demonstrate that it met financial sustainability requirements and regulatory standards.

   b) A strengthened regulatory regime, involving both quality and economic regulation. A focus on financial sustainability, including revenue sufficiency for water services, ring fencing, and funding for growth.

   c) New classes of council-controlled organisations (CCOs), that are financially independent of their owner councils, to enable greater levels of debt to be taken on to fund water services.

3. Upon its formation, the Government committed to repeal water services entities legislation within 100 days. This included the Water Services Entities Act 2022 and the Water Services Economic Efficiency and Consumer Protection Act 2023. Both Acts were repealed on 16 February 2024.

4. Government's stated approach to implementing its policy to improve council delivery of water services involves two stages following repeal of the Water Services Entities Act 2022. These following two stages involve:

   a) Transitional provisions to ensure immediate council focus on planning to achieve the financial sustainability of their water services, while also providing for information to inform the design and implementation of economic regulation. These transitional measures also include provisions to remove actual and perceived legislative obstacles to the reorganisation of water service by councils under the LGA, and to facilitate and fast track the reorganisation and economic regulation of Auckland Council's water services.

   b) Longer term provisions to expose all councils to the disciplines and incentives of economic regulation to improve the financial performance of council water services for consumers, and also to provide councils with new organisational options for their shared delivery of water services and to ringfence and increase investments in water services while also providing for more operational efficiencies in their delivery.

5. The policy objective is that local councils deliver water services that are financially sustainable and meet minimum regulated quality standards. The delivery of water services will be led by councils and recognises that each region requires an individual solution, as opposed to a one-size-fits-all centrally imposed approach.

6. The scope of this RIS is confined to evaluation of the stage two transitional policy proposals (stage one is already complete). It is intended however, that it will be added to provide evaluation of government's stage three proposals, and the context, problem definition and evaluation criteria have been written to provide for this.

Section 1: Diagnosing the policy problem

What is the context behind the policy problem?

Overview of the current water services delivery system in New Zealand

7. Drinking water, wastewater and stormwater infrastructure are critical to human wellbeing, and their provision is an essential enabler of residential and regional development, new housing provision and economic growth. Their provision and physical condition are also important to community resilience and is becoming more important because of climate change.

8. Local authorities (councils) provide drinking water, wastewater and stormwater services to most New Zealanders. There are currently 67 councils that own and operate water services across New Zealand. Around 85 percent of New Zealanders receive their drinking water and other water services from these councils, with the remainder provided by smaller private and community-based schemes.

9. The service delivery models employed by councils vary, and include in-house business units, CCOs, and a variety of contracting and sourcing arrangements to private operators and service delivery companies. Examples include,

   a) Auckland Council, whose drinking water and wastewater networks are owned and operated by Watercare, a 100 percent Auckland Council owned CCO. In owning and operating drinking water and wastewater networks, Watercare sets and charges its customers directly for its services, directly raises and manages debt to fund its services, and is governed by a competency-based board. Auckland's stormwater network is not operated by Watercare, and is directly owned, operated and funded by Auckland Council.

   b) Six councils from the greater Wellington region, who each own and fund their water services, but contract the operation and management of their water services from a CCO, Wellington Water. Wellington Water is owned by Wellington region local authorities and Greater Wellington Regional Council (which provides bulk water to councils in the region). It does not directly charge its customers, but instead contracts with each of the Wellington councils to operate and deliver their water services who in turn fund the costs of their water services through rates and debt.

   c) Most other councils directly own and manage their water services. These councils employ a variety of different approaches to their operation of water services including a variety of contracting and outsourcing arrangements for the operations, asset maintenance and renewal to third parties (for example, Ashburton and Nelson). A number of councils contract out aspects of their water services operation to CityCare, a Christchurch City Council owned CCO.

10. Regardless of the operating model, councils are responsible and accountable under the LGA to their ratepayers through the local democratic system for the delivery and of water services to their communities. To this end, council LTPs include provision for water services and for how each council intends to deliver and fund its water services.

The previous government proposed a centralised response to addressing problems associated with council owned water services in New Zealand

11. In June 2017, the National-led Government established the Three Waters Review to assess whether local government practices and system oversight relating to water services/infrastructure were 'fit for purpose'. In early 2018, the Labour-led Government continued this Review – informed by a set of initial key findings outlined by the Department and the issues and findings identified in the Stage Two report of the Government Inquiry into Havelock North Drinking Water. The aim of this work was to identify improvements to the regulation and service delivery arrangements for water services. It led to the enactment of the Taumata Arowai-the Water Services Regulator

Act 2020 and the Water Services Act 2021.

12. The Water Services Act 2021 provided for a strengthened approach to the regulation of drinking water suppliers, and some provisions relating to wastewater and stormwater, to protect health and to minimise negative environmental impacts. Taumata Arowai took over all responsibilities as drinking water regulator from the Ministry of Health Manatū Hauora in November 2021 and became responsible for certain aspects of the environmental performance of public wastewater and stormwater networks in October 2023 (regional councils remain the regulator of these networks, though).

13. In parallel with the regulatory reforms, the previous government commenced the Three Waters Reform Programme (the Reform Programme) in July 2020 in response to mounting evidence of financial and other problems with council provided waters service delivery. The Reform Programme had four key outcomes:

    a) safe, reliable drinking water;

    b) better environmental performance of wastewater and stormwater services;

    c) efficient, sustainable, resilient and accountable multi-regional water and sewage services; and

    d) making it affordable for future generations.

14. The Reform Programme proposed to shift ownership of water services assets and their delivery from councils to new multi-regional statutory entities that would have greater borrowing capacity than councils. It was initially proposed that water services would be transferred from 67 local councils to four water services entities, but this was changed to 10 entities under the second iteration, the Affordable Waters Programme. It was decided that each of the 10 water entities would be overseen through a joint oversight model made up of a group of representatives from local iwi and councils, proposed in part to help achieve financial separation of water services entities from councils.

15. This approach was politically divisive because it required the transfer of ownership and a loss of control over local water services from councils to multi-region water services entities, a joint oversight model to help ensure the financial separation of water services entities from councils, and to provide a role for mana whenua in the governance of local water services.

16. Local Government New Zealand Te Kāhui Kaunihera ō Aotearoa (LGNZ) stated at the time that "while councils have a range of views on the best model, there is near universal agreement that the status quo can't remain."[1]

The Coalition Government has committed to a locally led approach to improving water services in New Zealand

17. The Coalition Government did not support the Reform Programme / the Affordable Water Programme. The decision to repeal the Water Services Entities Act 2022 as outlined in the National Party manifesto document, LWDW, recognises the importance of putting council-owned water services onto financially sustainable footings. Ensuring New Zealanders have access to clean, quality water is a fundamental right and water services delivery must be improved urgently.

18. As part of the 100-Point Economic Plan the Coalition Government agreed to prioritise a policy programme to improve water services delivery in New Zealand through localism and flexibility, while balancing high standards for water quality and investment in infrastructure. Under the Coalition Government's policy, local councils will remain in control of their water services assets and delivery. They will be accountable to their

[1] Local Government New Zealand Te Kāhui Kaunihera ō Aotearoa (no date), *Water Services*, https://www.lgnz.co.nz/policy-advocacy/key-issues-for-councils/water-services/

local communities for local water services, and to regulators who will ensure that council services are delivered to minimum quality standards and that the interests of consumers are protected.

19. LWDW aims to ensure that New Zealand's water services are safe, resilient, reliable and customer-response, at least cost. The key parameters set out within LWDW are:

    a) councils will retain ownership and control of their water services assets and delivery;

    b) central government will have stronger oversight to ensure that the status quo does not continue;

    c) water services will be financially sustainable and councils will be required to ringfence assets and funds for water infrastructure; and

    d) there is greater transparency and accountability to consumers, communities and regulators.

20. The Coalition Government has announced that it will implement LWDW in three stages as part of its 100-point Economic Plan.[2]

    a) **The Water Services Act Repeal Bill** (Bill One), which has repealed the Water Services Entities Act 2022 to end the previous government's 10-entity model and to restore powers and responsibilities for water services delivery to local authorities. This was the first step to delivering a new system with stronger central government oversight, economic and quality regulation, and requirements for local authorities to use financially sustainable delivery models. Bill One received Royal assent on 16 February 2024.

    b) **The Local Government Water Services (Transitional Provisions) Bill** (Bill Two) to set out the framework and initial operating environment for the replacement regime. Bill Two is an omnibus bill that will make relevant amendments to the LGA and Local Government (Auckland Council) Act 2009 (LGACA). It will:

        i. establish foundational information disclosure requirements to support the long-term economic regulatory regime;

        ii. require councils to develop water service delivery plans to be submitted within 12 months of the enactment of Bill Two to demonstrate how water services will be organised and managed to ensure that they are financially sustainable and meet regulatory compliance and service standards;

        iii. remove barriers and streamline requirements on councils for establishing CCOs under the LGA, to make it easier for councils to reorganise their delivery of water services into more financially sustainable configurations; and

        iv. consider options for a fast-tracked approach for Watercare and Auckland Council to achieve the financial separation of water services and move to economic regulation ahead of other councils.

    The policy proposals providing for Bill Two are due to be considered by Cabinet in March 2024 in order to provide for legislation to commence drafting. It is intended that Bill Two will be introduced to Parliament in May and to come into effect by 30 June 2024.

    c) **The Local Government Water Services Bill** (Bill Three) will provide for the long-term regulatory settings for sustainable water service delivery. It will:

[2] National Party (2023), *Rebuilding the Economy Policy Document*, https://www.national.org.nz/rebuildingtheeconomy

i. include long-term requirements for financial sustainability, including establishing new classes of council water organisations to enable the financial ring-fencing, planning and reporting requirements of council water services from other areas of council operations;

ii. provide for a complete economic regulation regime (to be developed by the Minister of Commerce and Consumer Affairs);

iii. amend the legislation providing for Taumata Arowai's regulation of water services, which could include amendments to the threshold for regulated suppliers;

iv. establish a new regulatory backstop power to be utilised when councils are unwilling or unable to effectively deliver financially sustainable or safe water services; and

v. provide refinements to water service delivery system settings including requiring consistent industry standards, development contributions and powers for charging.

It is intended that Bill Three will be introduced in December 2024 and will come into effect in mid-2025.

21. All three stages of LWDW must be implemented, otherwise under the status quo council owned water services will continue to degrade due to inconsistent management and under-funding. LWDW will provide for councils to make decisions on the future organisation and management of their water services and ensure that water infrastructure is funded and invested in at appropriate levels where and when it is needed, and that water services are delivered using financially sustainable models and to minimum regulated quality standards.

What is the regulatory context of water services delivery?

There are a number of players involved in the current water services regulatory environment

22. Councils are already regulated in their delivery of water services. The current, high-level regulatory context for the provision and delivery of drinking water, wastewater and stormwater is summarised at Figure 1.

23. Key elements of the current regulatory environment include:

a) Local Government Act 2002, which includes:

i. Obligations on councils to assess community access to water services, and to continue provision of existing water services;

ii. Requirements for long term planning of council operations including water services CCOs.

b) Taumata Arowai-the Water Services Regulator Act 2020 and Water Services Act 2021, that provide for:

i. Drinking water quality standards and their enforcement;

ii. Waste and stormwater environmental network performance standards; and

iii. Taumata Arowai to administer and regulate council compliance with the above standards.

c) Resource Management Act 1991 which provides for:

i. Resource consent requirements and their monitoring; and

ii. Monitoring of discharges and abstraction points.

Figure 1: Water services regulatory landscape, as at February 2024

	Health outcomes	*Environmental outcomes*	*Infrastructure sustainability and resilience outcomes*	*Financial sustainability outcomes*
Department of Internal Affairs	Policy, stewardship, legislation - **local government** system / water services system Monitors **Taumata Arowai**			
Taumata Arowai	Drinking water regulation (under **Water Services Act 2021**) Oversight of performance of wastewater and stormwater networks Reviewing **source water risk management** & **drinking water safety** plans			
Ministry for the Environment	**NES – sources of human drinking water**	**Freshwater management** regulations (inc. NPS-FM) Administers **Environmental Reporting Act 2015** Policy/stewardship - resource management system	**National Adaptation** Plans **Emissions reduction** plans	
Regional Councils	Regulator – wastewater/stormwater networks (in region)	Regional plans		
Ministry of Health	Policy advice - **public health** matters relating to drinking water.			
National Emergency Management Agency			Administers **Civil Defense Emergency Management Act 2002**.	
Te Arawhiti	Policy lead on the Crown's Treaty of Waitangi obligations – including Treaty settlements			

24. The current regulatory system's focus is on drinking water quality and the environmental impacts of the water services operations. It does not include regulation of financial sustainability or economic regulation of water service operations or provide for customer rights and interests in water services.

What is the policy problem or opportunity and how is it expected to develop?

Without systemic change, council ownership and delivery of water services is financially unsustainable and is not always meeting the minimum quality standards

25. Council-supplied information on assets and planned capital expenditure indicates that at least $120 billion of investment[3] is needed in water services over the next 30 to 40 years to maintain, replace and upgrade existing assets and enable and provide for residential development, new housing and population growth.[4]

26. Councils across New Zealand are facing major financial challenges in their ownership and delivery of water services. The extent of these challenges varies across councils but is such that many councils are unable to adequately maintain their current services or upgrade services to meet minimum regulatory requirements or expand services to enable residential and economic growth without large increases to rates. The extent of this problem varies across councils.

27. This is resulting in a situation where many New Zealand communities are provided with

[3] Water Industry Commission Scotland (2021), *Economic analysis of water services aggregation, Phase 2*.

[4] Department of Internal Affairs Te Tari Taiwhenua (31 March 2021), *Local Government briefing: Three Waters Reform – Number and boundaries of proposed water service entities*.

subpar service delivery and provision of water services. The financial constraints faced by many councils in their delivery of water services, results in their water services not always meeting minimum quality standards and being a constraint on the supply of new housing, local economic growth and development, and resilience to unexpected events.

28. While Havelock North was a large-scale water contamination event with serious consequences for human life and health, this was not an isolated symptom of issues facing council owned water services. Additional events that demonstrate the increasing pressure on the provision of all water services are listed below.

    a) Lead in Dunedin's drinking water reported in February 2021;

    b) Ongoing wastewater leaks in Wellington's CBD;

    c) Ongoing pipe breaks in Wellington: as at mid-February 2024, Wellington City is losing around 45 percent of its drinking water to the leaks across the public network and on private properties.[5] As at 26 February 2024, there were 1,746 leaks in Wellington and an additional 1,732 in Wellington Water's jurisdiction in the greater region;

    d) Repeated burst pipes in Levin in February 2021;

    e) Issues with numerous unswimmable beaches due to high levels of faecal bacteria in Auckland since the summer of 2020;

    f) Ongoing water restrictions in Auckland City, Hamilton and Kaitaia; and

    g) Boil water notices in many areas, more recently including Frankton, Kelvin Heights, Queenstown, Akaroa and Carterton.

29. The Ministry of Health's Annual Report on Drinking Water Quality 2020-2021 found that every region apart from Auckland and Taranaki had some form of clean water failure over the 12-month period. In addition, numerous water suppliers across the country failed the bacterial standards with E. coli detected in their supplies and eight large suppliers failed the protozoal standards.[6]

Operating costs are increasing as some councils reach their debt limits

30. Councils already struggling to fund deferred maintenance and replacement of water services are also facing increasing costs in their operation of water services.

31. There are fixed costs associated with delivery of water services that are challenging for councils with very small populations to fund, as councils vary considerably in population size. For example, Auckland Council is the largest authority with 1.7 million people and is able to spread its fixed costs of providing water services across a large number of users, while the smallest Kaikōura District Council, has a population of just under 4,000 people. Councils are all responsible for the same core water services, which means the share of expenditure allocated to different services can vary significantly between councils.[7]

32. Some councils are less efficient than others in their management of water services

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[5] Wellington Water (10 November 2023), *Water shortage and water restrictions FAQs*, https://www.wellingtonwater.co.nz/assets/Reports-and-Publications/Water-Shortage-FAQs-Nov23.pdf

[6] Ministry of Health Manatū Hauora (2022), *Annual Report on Drinking-water Quality 2020-2021*, https://www.health.govt.nz/system/files/documents/publications/annual-report-on-drinking-water-quality-2020-2021-mar22.pdf

[7] New Zealand Productivity Commission Te Kōmihana Whai Hua o Aotearoa (November 2018), *Local government funding and financing,* https://www.productivity.govt.nz/assets/Documents/909fba8afd/Local-government-funding-and-financing-issues-paper.pdf

which means that some charge more than others for the same service.[8]

33. Water New Zealand's 2021-2022 National Performance Review of Water Services found variation in operating expenditure normalised on a per-property basis is large. Per-property water supply expenditure ranged from $168 to $994 dollars, from $191 to $685 for wastewater, and from $15 to $480 for stormwater.

34. There has been a steady increase in the operating cost of councils over the past 10 years[9, 10] and there is evidence that a key contributing factor of this increase in cost has come from the delivery of water and wastewater services.[11]

35. Water New Zealand's 2021-2022 National Performance Review of Water Services (Review) found that water services providers spent an average of 86 percent of the capital expenditure budgeted for water supply, wastewater, and stormwater services in the 2022 fiscal year. Service providers in the Review reported operating expenditure of $741 million. Average operating expenditure per property increased from the previous year by 11.5 percent for water supply, 6.7 percent for wastewater, and 13.9 percent for stormwater.

36. For example, Wellington Water accounted for the greatest increase in capital expenditure from the previous year, with capital works on water supply increasing from $49 million in 2021 to $76 million in the 2022 fiscal year, accounting for more than half of the increasing expenditure on water supply.[12] Across the same period, wastewater expenditure at Wellington Water increased from $43 million to $82 million, accounting for $39 million of the additional $102 million increase on previous years.[8]

37. Investment decisions are made by individual councils and are therefore subject to different revenue and debt constraints. For example, debt policies vary considerably across the country and while the Local Government Funding Agency (LGFA) sets a hard debt ceiling (at 290 percent of revenue), councils vary in their net debt to revenue ratios. This is shown at Figure 2.

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[8] Water New Zealand (2022), *National Performance Report 2021-2022*, https://www.waternz.org.nz/NationalPerformanceReview

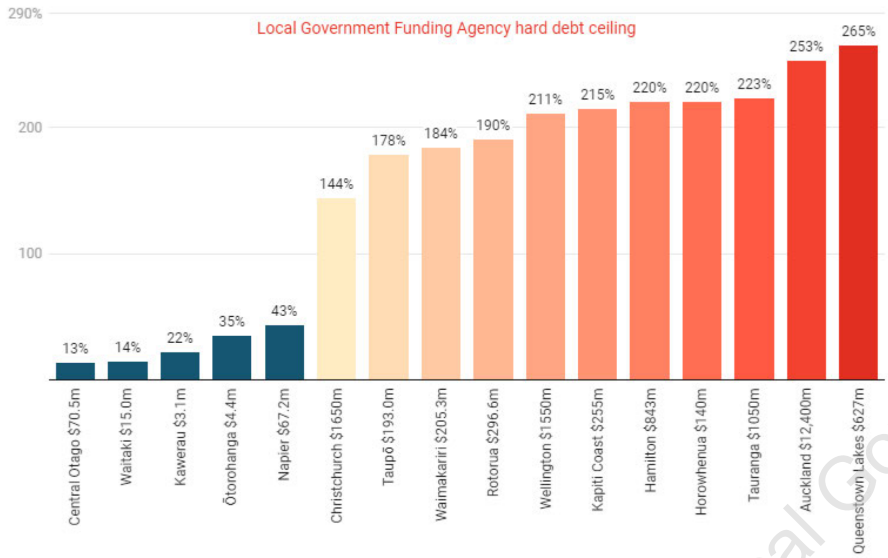
[9] Office of the Auditor General Tumuaki o te Mana Arotake (2020), Insights into local government: 2020, https://oag.parliament.nz/2021/local-govt/part1.htm

[10] Department of Internal Affairs Te Tari Taiwhenua (no date), Local government in New Zealand – Local Councils Operating expenditure, http://www.localcouncils.govt.nz/lgip.nsf/wpg_URL/Profiles-Local-Government-Statistical-Overview-Operating-Expenditure

[11] Department of Internal Affairs Te Tari Taiwhenua (July 2018), *Costs and funding of local government*, https://www.dia.govt.nz/diawebsite.nsf/Files/Central-Local-Government-Partnerships/$file/Costs-and-funding-of-local-government-Morrison-Low-report.docx

[12] Wellington Water provides services on behalf of six councils: Greater Wellington Regional Council (which owns bulk water assets), Porirua City Council, Wellington City Council, Hutt City Council, Upper Hutt City Council, and South Wairarapa District Council.

Figure 2: Councils' net debt to revenue ratios[13]



38. While councils have ownership over decisions around investing in water infrastructure, they face pressure to direct funding away from non-water-related investment priorities to meet the costs of improving their water networks or to reduce investment to restrict rate rises. Some councils may also need to increase their borrowing, which will affect credit ratings and cost of finance, and will limit financial flexibility for local authorities that are near their debt ceiling.

The five root causes of New Zealand's water crisis

39. The Department expects that without immediate action, it is highly likely that the water services delivery system will continue to degrade at an unsustainable rate with risks to health, environment and to future plans for urban growth and development. As ratepayers in some districts reach peak rates to fund this issue and as some councils realise debt constraints, the Crown will come under increased pressure to provide financial support to councils to resolve their issues if no other action is taken.

40. There are five root causes that contribute to the persistent systemic problems with the delivery of water infrastructure and services, which are discussed individually in more detail below. These root causes are:

    a) **institutional barriers to more efficient delivery of water services**;

    b) **poor incentives on councils to adequately invest in and fund water services**;

    c) **varied decision-making quality;**

    d) **funding constraints; and**

    e) **incomplete regulatory and stewardship oversight and monitoring**.

41. The evidence used to inform this problem definition comes from a range of sources, which are included as a bibliography at **Annex One**. The problems are also illustrated by council-specific case studies, which are attached at **Annex Two**.

42. The limitations and assumptions of the evidence used in this problem definition can be found from paragraphs 149 onwards.

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[13] Newsroom (30 October 2023), *Three Waters assets to move to new council-owned companies*, https://newsroom.co.nz/2023/10/30/three-waters-assets-to-be-moved-to-new-council-owned-companies/

Root cause one: Institutional barriers to more efficient delivery of water services

43. Councils operate a highly fragmented and dispersed system, in which services and infrastructure are managed, delivered, operated, and paid for by (or on behalf of) 67 councils. The level of service quality and efficiency differs between councils as does the size of each population base to spread the fixed costs of providing water services.

44. While there are potential efficiencies to be gained through joint and shared service arrangements and the sharing of fixed costs across larger populations, most councils continue to directly deliver services.

45. Potential areas for efficiency gains include more collaborative approaches to procurement and supply chain management, in collaborative approaches to workforce development (including attraction, training and retention) and utilisation of scarce expertise, in sharing the costs of specialist skills and expertise and expensive equipment, in investments in new technologies and information technology (IT) across councils, and in collaborative approaches to risk management and mutualised approaches to insurance.

46. The LGFA, provided for by government policy decisions and in legislation, is an exception and demonstrates the benefits available to councils through collaborative approaches to debt funding and management.

There are perceived process barriers under the LGA that inhibit councils from exploring and entering into shared service arrangements

47. Councils are obligated to consult with their communities in accordance with the consultation principles set out in section 82 of the LGA to set up a CCO.

48. In addition, any decision to significantly alter the intended service level for any significant activity (which includes water service delivery) or to transfer the ownership or control of a strategic asset to or from the council, cannot be made unless it is provided for in the council's LTP. Therefore, councils need to include the establishment of a water services CCO in their LTPs (via an LTP amendment, if out of cycle) and use the special consultative procedure provided for in the LGA when adopting the LTP.

49. For councils considering a joint CCO, it is likely to be more efficient and cost-effective for them to undertake joint consultation – potentially through a joint committee. There do not appear to be any legislative barriers to this. Schedule 7, clause 32 allows councils to delegate powers and responsibilities (with several exceptions named) to joint committees. Consultation powers are not named as an exception. However, recent engagement with a small number of council officials found that despite these provisions within the LGA, councils remain constrained by the time and resources required to undertake these consultations, particularly if multiple rounds of consultation are required.

50. Councils engaged with stated that these consultation processes, which could include an early consultation round on alternative options, and then another consultation round on the necessary LTP amendment associated with the final decision, could take several years – particularly if multiple councils are involved. Therefore, the current process is not optimal for those who are looking to swiftly set up a water services CCO to improve their water services provision.

Decision-making processes can be onerous, and councils are concerned about the risks of legal challenge

51. Councils must, when making decisions:

    a) seek to 'identify all reasonably practicable options for the achievement of the objective of a decision';

    b) review the cost-effectiveness of current arrangements for meeting the needs of communities within their district for good-quality local infrastructure and include consideration of at least six listed options for the governance, funding, and delivery of infrastructure, services, and regulatory functions (this includes the use of CCOs (both single and joint)); and

c) ensure prudent stewardship and effective and efficient use of its resources in the interests of its district.

52. Feedback from some councils and the TAG noted that the consideration of 'all reasonably practicable options' in relation to the establishment of a water services CCO can be unnecessarily onerous, as well as resource and time intensive.

53. Councils also indicated that a key barrier and disincentive to setting up a CCO is the possibility of judicial review. This mainly relates to the interpretation of what factors can be taken into consideration in a council's decision making – including that they may not have fully considered all of the reasonably practicable options.

The individualistic approaches to each water network makes it hard to create efficiencies

54. Due to the multiplicity of water service delivery models within New Zealand, partly as a result of the LGA, each council has a different asset base to manage. The table below highlights areas where councils may use individualistic approaches as part of their water services delivery, and as a result, cannot use the benefit of scale to improve their efficiencies.

Table 1: Key areas where water services could be more efficient

Key components	How is this linked to efficiency?	Evidence
Information and communication technology, and digital infrastructure procurement and management and other procurement, and supply chain management	The variation in councils' scale means that their ability to access and invest in new opportunities is limited. Smaller councils delivering the same services as larger struggle to have the resources. There is also limited market capacity to deliver large upgrades and expansions, which can result in councils competing with each other in their procurement. Improving procurement and supply chain coordination across water services entities would support efficiencies in supply chain management and cost savings.	There is a significant variance in the uptake of new technology by councils with some councils using manual treatment methods and not taking advantage of the benefits of technological advances and automation.[14] Higher performance tends to be found in mid- to large-sized local authorities and in single-purpose entities such as Watercare, which all have large, specialised three waters asset management teams and sophisticated technology and data systems. Councils may find themselves competing against their neighbouring regions for resources, contractors and contracts. This can have particularly negative effects for smaller councils with lower ratepayer bases or fewer staff, as they cannot easily achieve scaled benefits compared to larger councils or compete against larger councils in their procurement.
Risk management and insurance	This is necessary to ensure that all water services entities are able to access insurance for infrastructure	New Plymouth District Council experienced a 24 percent increase across the council's insurance programme which kicked in on July

[14] Water New Zealand (2018), *Draft Submission to Productivity Commission Issues Paper: Local government funding and financing inquiry*, https://www.waternz.org.nz/Folder?Action=View%20File&Folder_id=527&File=DRAFT%20for%20member%20feedback%20Water%20New%20%20Zealand%20Submission%20to%20the%20Productiv..._.pdf

Key components	How is this linked to efficiency?	Evidence
	at a reasonable cost, especially access to insurance for seismic and natural hazard related risks. Insurance premiums have risen due to inflation and increased asset values. Cost and availability of insurance is also coming under pressure as a result of climate change related weather and other events These will make it increasingly difficult and more expensive for some councils to insure their water service assets	1, raising the overall cost of cover to more than $2 million annually. Stratford District Council is expecting an overall insurance increase of up to 80 percent, which has been attributed to national and international disasters and a growth in the Stratford District Council's asset base from just below $60 million to more than $80 million. South Taranaki District Council confirmed the organisation was also facing insurance cost rises of between 15 and 20 percent.[15]
Workforce development and management	The total number of water staff varies greatly between providers. For example, Mackenzie District Council employs 4.5 full time equivalents (FTE) compared to 272 FTE at Wellington Water (noting that Wellington Water services five councils). Watercare employs over 1,000 staff.[8] The Office of the Auditor-General found that councils had "to varying degrees, issues with staff capability" linked to succession planning, recruitment, and retaining staff. There is potential for councils to explore the delivery of collaborative water services to reduce capability and capacity issues and improve efficiencies.[16]	A previous Water New Zealand report found that 40 percent of the water services workforce are employed as contractors. This can create issues where neighbouring councils invest in infrastructure projects simultaneously, therefore requiring the same skillsets through the procurement process and creating inefficiencies. Stakeholder feedback from LGNZ found that rural and remote councils were particularly concerned about accessing the necessary technical expertise of water services professionals, and that the previous government's reform could exacerbate these issues.[17] It is often difficult for smaller, rural, and provincial local authorities to develop the capabilities needed, and to access and retain people with specialist skills required for new technology. Smaller local authorities by nature have smaller teams, with wider and more general skills, rather than specialists.
Demand management tools	Councils take different and approaches to demand management (see Annex Three). Often their approach is based on the quality and abundance of their water supply, and balanced against other priorities for their region.	Water New Zealand states that water meters are installed at half of the residential properties and nearly three-quarters of non-residential properties in New Zealand. Water meters enable network operators to determine and manage loss, identify leaks more efficiently, and lower water usage when combined with volumetric charging. Water New Zealand's 2021-2022 Annual Performance Report found that all districts

[15] Stuff (24 July 2023), *Council insurance premiums to skyrocket in wake of weather related disasters*, https://www.stuff.co.nz/taranaki-daily-news/news/132589549/council-insurance-premiums-to-skyrocket-in-wake-of-weather-related-disasters

[16] Office of the Auditor-General Tumuaki o te Mana Arotake (2018), Managing the supply and demand for drinking water, https://oag.parliament.nz/2018/drinking-water/docs/drinking-water.pdf

[17] Local Government New Zealand Te Kāhui Kaunihera ō Aotearoa (September 2015), *Improving New Zealand's Water, Wastewater and Stormwater Sector*.

Key components	How is this linked to efficiency?	Evidence
		without residential water meters (excluding three) reported higher than average water usage than areas with water meters.[8]

55. More collaborative approaches and shared service arrangements have previously been recommended as critical to achieving efficiency gains in delivery of water services.[18]

56. These inefficiencies also flow through to central government. Te Waihanga, the Infrastructure Commission's recent report found that the multiplicity of suppliers across New Zealand complicates the government's ability to apply and enforce an effective regulatory framework and increases the cost of regulation. The report says that overseas models highlight "that optimal performance for water utilities operating in a monopolistic environment necessitates strong regulatory oversight and the consistent definition and enforcement of health, economic and environmental standards."[19]

Root cause two: Poor incentives on councils to adequately invest in and fund water services

57. Councils have a mix of purposes and functions as set out in the LGA. Section 10 of the LGA requires local authorities to "promote the social, economic, environmental, and cultural well-being of communities in the present and for the future." This broad remit requires councillors and their executives to prioritise investments and make trade-offs across a portfolio of activities (for instance, between investments in parks, libraries, conference centres and underground pipes).

58. These decisions are made in the context of a three-year political cycle. The incentives associated with this cycle, especially in an environment characterised by competing priorities and funding constraints tend to favour investment in shorter term and higher visibility and more populous initiatives. They are not conducive to the effective governance and funding of capital-intensive long-life infrastructure assets, and especially those that are not generally visible to the public until they fail.

59. There are many instances where councils have traded off maintenance and network renewals, and investments to improve resilience and quality against more short term and more visible competing investment priorities; with the costs of these trade-offs falling on future councils and generations of ratepayers.

60. This dynamic is accentuated by a lack of transparency and impartial information needed to enable local residents to judge council performance to support effective accountability.

61. The evidence of these poor incentives can be seen through:

    a) historic under investment of water services;

    b) large infrastructure deficits; and

    c) non-compliance with resource consents.

Historic underinvestment has led to a financial crisis for councils to deliver water

[18] Department of Internal Affairs Te Tari Taiwhenua (July 2023), *Water Services Entities Amendment Bill Departmental Report*, https://www.parliament.nz/resource/en-NZ/53SCGA_ADV_0075f255-c960-4ab6-a499-08db6df0cca0_GA26979/26f905e989f7d055467e40d318e9d2203f1bd229

[19] Infrastructure Commission Te Waihanga (no date), Sector state of play: Water, https://tewaihanga.govt.nz/our-work/research-insights/sector-state-of-play-water

services

62. It is estimated that there is approximately $54.6 billion of council-owned water assets across the country, with an estimated $8.1 billion worth of water-related debt.[20]

63. Debt financing is a sensible tool for investment in long-life assets. However, some councils have been unwilling to borrow to fund investment through debt, and instead rely on rates (and passing the costs onto ratepayers) to invest in their long-life assets. In many cases, councils choose to invest less because of concerns for rate increases.

64. In addition, costs have increased substantially over the last three years. Inflation has run at approximately double the rate of what was assumed by the sector when the 2021-2031 LTP Budgets were set.

65. The Office of the Auditor-General attributes this to a number of factors, including delays in consents, supply chain issues, the impact of COVID-19, capability and capacity issues, and uncertainty with large government reforms.[21]

66. In addition, councils face increasing pressure to lift rates, reduce spending or find alternatives forms of revenue due to:

    a) aging assets;

    b) asset revaluations;

    c) replacement values of infrastructure impacted by higher construction prices, meaning replacement values and by extension depreciation charges are significantly higher;

    d) capital price inflation;

    e) higher amounts of debt owed by councils, which limits the ability to use debt finance to fund increased expenditure;

    f) limitations for debt ceilings set by the LGFA in order to maintain current credit ratings;[22]

    g) higher likelihood of councils reaching their debt ceilings;

    h) stronger enforcement of regulatory requirements;

    i) climate-related events and resilience issues; and

    j) increased scrutiny by auditors.

Under current approaches to water service delivery, local authorities will continue to struggle to deliver their water services

67. There have been reports that due to financial constraints, councils will be unable to service the necessary infrastructure maintenance and investments. In some cases, this may lead to further deterioration, increasing costs to ratepayers, and inadequate investments in water services. A small sample of councils are listed below as evidence, but this is by no means an exhaustive list.

68. Unexpected cost pressures have increased Queenstown Lakes District Council's net

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9(2)(ba)(i) [redacted]

[21] Office of the Auditor-General Tumuaki o te Mana Arotake (2022), *Matters arising from our audits of the 2021-2031 long-term plans*, https://oag.parliament.nz/2022/ltps/part4.htm

[22] Infrastructure New Zealand (2023), *Position Paper: Water Infrastructure and Services*, https://infrastructure.org.nz/wp-content/uploads/2023/12/Infrastructure-NZ-Policy-Postions-Water-Infrastructure-002.pdf

debt to revenue ratio while capital expenditure for water was lower than forecast.

a) Since 2021, the council has faced several unexpected cost pressures, including a leaky building claim settlement that was not fully budgeted. In the 2022/23 financial year, the net debt to revenue ratio was 253.4 percent - significantly higher than the forecast level (189.5 percent). This is despite having increased rates by 6.5 percent (higher than the forecast increase of 5.87 percent) in response to inflationary pressures and increasing interest rates.

b) Debt increases for water supply and wastewater were much lower than forecast for 2022 and 2023. This appears to have come mostly at the expense of capital expenditure to meet additional demand and improve the level of service (spending on replacing existing assets was slightly higher than forecast for both years).[23] In response to these financial pressures, the Annual Report indicates that the council has deferred (or is looking to defer) the completion of several significant water infrastructure projects through the upcoming LTP process including the $52.4m Wanaka Water Treatment Plant.[23]

69. Whakatāne District Council does not have the financial capacity to deliver its water services over the next ten years.[24] At a LTP 2024-2034 public meeting in March 2024, Whakatāne District Council noted that the cost of keeping the district's three waters systems compliant with consents over the next 10 years was $440 million. These increased costs are a result of increased compliance standards, resilience in responding to climate change, and meeting demands for future growth. The council does not have the financial capacity to provide $440 million, and as a result, plans to reduce its wastewater services from year three onwards to reduce the overall cost to $170 million. Council staff have noted that this proposed reduction will mean the council accepts a higher element of risk.

70. Councils' cost pressures apply across the board to other infrastructure that councils also provide, such as transport.

Looking forward, local authorities across New Zealand face significant water infrastructure deficits

71. Water infrastructure comprises of the assets used to collect, store, transfer, treat and discharge the water services. The infrastructure is complex, expensive and much of it (around 80 percent) is underground.

72. The water services infrastructure deficit is challenging to quantify due to poor information on asset condition. Modelling to quantify the potential required investment in water infrastructure over the next three decades is complicated, and as a result, varies significantly.

a) A national analysis completed by the Water Industry Commission of Scotland (WICS), was used as the basis for the previous government's reform's policy programme. Estimates suggests that $120 - $185 billion was needed over the next three decades for water investment. This is equivalent to 30-47 percent of New Zealand's current GDP.[26]

b) However, a regionally focused model approximates the total funding to be much less and depends on each council. For example, case studies completed by Castalia highlights the following over-estimates between the WICS analysis and

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[23] Queenstown Lakes District Council (2023), *Annual Report Rīpoata ā-tau 2022-2023*, https://www.qldc.govt.nz/media/ogeh4xmz/qldc_annual-report_2022-2023_final-251023-adopted.pdf

[24] Radio New Zealand (8 March 2024), *Whakatāne council can't afford to deliver water upgrades*, https://www.rnz.co.nz/news/ldr/511186/whakatane-council-can-t-afford-to-deliver-water-upgrades

councils' own reporting:

i. Auckland Council's Watercare: 1.6 times more investment than needed;

ii. Waimakariri District Council: four times more investment than needed;

iii. Hastings District Council: more than 4.5 times more investment than needed.[25]

73. For the purposes of this RIS, the Department recognises that council-supplied information on assets and planned capital expenditure indicates at least $120 billion[26] of investment is required over 30 to 40 years to maintain, replace and upgrade existing assets and enable and provide for needed residential development, new housing and population growth.[27]

74. These deficits are a result of deferred maintenance and the renewal of infrastructure that has lasted beyond its economic and functional life and, in some cases, improper depreciation. As a result, many councils are facing financially challenging decisions concerning the need to upgrade existing infrastructure to meet minimum quality standards for human health and environmental impact, while also being challenged demands for investment in water service to improve its resilience to natural hazards and climate change and to enable residential development and economic growth.

75. Because water services are directly provided by councils, or CCOs that they own, debts associated with water services are consolidated on council balance sheets. This consolidation results in hard constraints on the amount of debt that can be raised for investment in water services. It also limits the amount of debt that councils can take on for roads or other investment priorities, and results in challenging decisions on which priorities to invest in and which to forego or put off.

76. In recent years, the Office of the Auditor General has raised concerns about the reliability of information available on water assets and repeatedly warned that council spending on asset maintenance and renewal is below depreciation.[9]

77. Levels of planned investments in water services are often insufficient to enable growth, to improve the resilience of water services networks to natural hazards and other risks, and to ensure that services meet minimum quality standards necessary to safeguard human health and to reduce the negative environmental impacts of wastewater and stormwater discharges and overflows. For example, Central Hawke's Bay District Council has said that debt repayments could lift rates by six percent "before we do anything else", with a total rate rise of 20-30 percent likely.[28]

Surveys suggest that some councils do not, or cannot, prioritise investment in stormwater or wastewater

78. Environmental regulation of wastewater and stormwater networks helps to ensure systems are operated in a manner that protects public health and the environment. In New Zealand, this is achieved by the issuing of consents for discharges from wastewater and stormwater networks.

79. On average, expenditure of stormwater networks is considerably lower than that for drinking water and wastewater. Water New Zealand's 2021-2022 Annual Performance

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[25] Castalia (July 2022), *Flaws in Water Service Entities Bill: Report to Communities 4 Local Democracy*.

[26] Water Industry Commission Scotland (2021), *Economic analysis of water services aggregation, Phase 2*.

[27] Department of Internal Affairs Te Tari Taiwhenua (31 March 2021), *Local Government briefing: Three Waters Reform – Number and boundaries of proposed water service entities*.

[28] Hawkes Bay App (21 December 2023), *Video: Central Hawke's Bay rates increase could be between 20 and 30 per cent, says mayor*, https://cdn.hbapp.co.nz/news/pijf/video-central-hawkes-bay-rates-increase-could-be-between-20-and-30-per-cent-says-mayor

Review found that expenditure for stormwater was 36 percent and 33 percent of the investment in drinking water and wastewater, respectively from surveyed councils.[8] The large variance between stormwater investment versus drinking and wastewater is not clear, but it almost certain that councils make trade-offs to invest more heavily in other areas of their remit.

80. Only seven of the 33 stormwater services providers in Water New Zealand's survey had all stormwater discharges covered by a resource consent. Such consents act as a driver for monitoring and management practices that improve the quality of stormwater discharges. Nonetheless, stormwater catchment management plans, and stormwater quality monitoring, have gradually become more prevalent. Three quarters of participants had stormwater catchment management plans in place, and 70 percent undertook monitoring.

81. Water New Zealand's survey found that while all wastewater plants had discharge consents, nearly 10 percent were expired. Water New Zealand states that the consent process is lengthy, which may impact on councils' ability to adequately invest time and resources to reobtain the consents.

82. Water New Zealand also states that while resource consents are in place, there is a long-running trend of little regulatory compliance action in response to non-conformance with consent conditions. In the 2022 fiscal year, 412 non-conformances with wastewater treatment plant consents where reported, however only 36 compliance actions were taken in response. For stormwater consents, 191 non-conformances were reported with only seven corresponding compliance actions.

Root cause three: Varied decision-making quality to adequately invest in and fund water services

83. Water services are capital intensive and complex, and decisions on their funding and delivery require expertise in asset and network management, finance and financial management of long-life assets, and risk management. The assets are expensive and long life and require consistent approaches over many years to their management, maintenance and renewal if they are to operate effectively.

84. Water services delivery across most councils is governed by directly council and council sub-committees formed from locally elected councillors. Auckland Council's Watercare is an exception, with a competency-based board and independent chair. It includes professional directors with expertise in infrastructure and asset management, finance and economics, risk and insurance and technology.

85. As governors of water services, councillors are often required to make decisions based on incomplete information and analysis and subsequently cannot act in the best interests of their communities. Those involved in decisions may not have the skills and capabilities needed to provide effective governance over a council's asset management and delivery of water services. They may not, for instance, understand the implications of complex financial information or have the knowledge and experience required to ask appropriate questions of the executives they govern.

86. As a result, they may not always act in the best interests of their communities. This leads to overall lower quality decision-making, which can have long-lasting effects when coupled with the management of crucial infrastructure assets.

87. Evidence of this can be seen in the politicisation of decision-making and the impact of external shocks.

The politicisation of decision-making can have a negative impact on infrastructure management and investment

88. As noted above, decisions on water infrastructure can have input from council management, staff, and councillors. Several recent reports have highlighted that the interplay between politics and water services delivery is complex. For example:

a) The Report of the Havelock North Drinking Water Inquiry: Stage Two found that political accountability via elected members was ineffectual, as "most large and medium water suppliers are district or city councils which can be subjected to significant political and fiscal pressures from their communities. These pressures can result in councils deciding not to spend money on drinking water infrastructure improvements".[29]

b) Other evidence collected by the Report of the Havelock North Drinking Water Inquiry: Stage Two also found that in the South Island, an elected member overrode the decisions of the Medical Officer of Health's recommendation to chlorinate the supply. It was stated that political pressure should not be prioritised in the decision-making process and that in a private company, directors or senior managers would not be able to override similar such decisions.

c) Te Waihanga, the New Zealand Infrastructure Commission found that the role of elected members (known as the politicisation of decisions) in compliance, monitoring and enforcement activities within water services has raised concerns.[19]

d) Research by Motu found that policy tools used in the management of water services in New Zealand are "highly political and value laden", which can inhibit councils from having the confidence to make decisions or changes to their water policies.[30]

e) LGNZ's submission to the Productivity Commission highlighted that the distribution of infrastructure costs between current and future decisions can be viewed as a "political argument that must be won in each district." Councils' decisions to improve the management of infrastructure assets and efficiency of services can be influenced by the political preferences of the majority of councillors.[31]

89. More broadly, the Review into the Future of Local Government found that elected members needed more support to make "good long-term decisions for communities in an increasingly complex operating environment" and that there was a "case for significant change in offering elected members training and development to increase their capability and confidence in making effective decisions".[32]

In addition, external shocks and resilience planning can impact how councils make investment decisions

90. Long-term planning requires councils to outline key actions, activities, good or services provided by a council, and specific funding and financial management policies and information. However, LTPs can be overridden when councils are faced with external shocks that require urgent funding or support.

91. While this is not a criticism of previous council decisions where funding had to be reallocated urgently to meet other pressing community needs, it is important to

[29] Government Inquiry into Havelock North Drinking Water (December 2017), *Report of the Havelock North Drinking Water Inquiry: Stage 2,* https://www.dia.govt.nz/diawebsite.nsf/Files/Report-Havelock-North-Water-Inquiry-Stage-2/$file/Report-Havelock-North-Water-Inquiry-Stage-2.pdf

[30] Motu (2020), *Motu Working Paper 20-10: Review of policy instruments for freshwater management*, https://motu-www.motu.org.nz/wpapers/20_10.pdf

[31] Local Government New Zealand Te Kāhui Kaunihera ō Aotearoa (February 2019), *Review of local government funding and financing: LGNZ's submission to the Productivity Commission,* https://www.productivity.govt.nz/assets/Submission-Documents/020e6fee3a/Sub-112-Local-Government-New-Zealand.pdf

[32] Review into the Future of Local Government Te Arotake I te Anamata mō Ngā Kaunihera (2023), *He piki tūranga, he piki kotuku*, https://www.dia.govt.nz/diawebsite.nsf/Files/Future-for-Local-Government/$file/Te-Arotake_Final-report.pdf

consider that with finite financial resources, councils can be required to prioritise urgent spending to the detriment of planned renewals and maintenance for infrastructure.

92. For example, Auckland Council spent an additional $45 million supporting the urgent response and recovery following severe weather events in January and February 2023. This resulted in an excess of $25 million for the council's operating costs. The Department recognises that this funding was urgently needed to support Auckland Council's communities and does not critique this decision but notes that it came at a cost through deferred infrastructure delivery. Their 2023 Annual Report states that $50 million of the operational budget for projects were postponed to offset recovery costs.[33]

93. Furthermore, councils are experiencing additional, and in some cases unplanned, costs associated with climate. For example, cyclone Gabrielle damaged water infrastructure in Gisborne and Central Hawke's Bay, causing significant service disruptions.

94. Underperformance of the urban stormwater systems in Napier and Auckland have highlighted the need for investment to strength councils' resilience.

Root cause four: Funding constraints

95. The funding constraints of local government are well known and understood. Poor past management and investment decisions have left many councils with water services that have not been adequately maintained or renewed.

96. Some councils, including New Zealand's larger urban councils are constrained in the amount of money they can borrow to invest in water services as they reach debt caps. Other councils are overly reliant on rates to fund the costs of investments for long life assets that might be better funded through debt and paid back over the economic life of assets. In many councils, these two issues are resulting in substantial pressures on rates, with some councils indicating general rate increases in the order of 20 percent.

97. In addition, many councils are facing pressures to upgrade networks to meet minimum standards, to improve their resilience to external shocks, and to expand their coverage to enable population and residential growth.

98. The root causes include growing debt ratios and caps, an increasing number of councils receiving credit downgrades, and a reliance on rates or user charges to increase the revenue required to support their networks.

9(2)(ba)(i) [redacted]

99. 9(2)(ba)(i) [redacted]

100. 9(2)(ba)(i) [redacted]

33 Auckland Council Te Kaunihera o Tāmaki Makaurau (2023), *Annual Report 2022/2023 Hui ā-Tau 2022/2023*, (2023), https://www.aucklandcouncil.govt.nz/plans-projects-policies-reports-bylaws/our-annual-reports/Pages/current-annual-report.aspx

9(2)(b [redacted]

9(2)(ba)(i) [redacted]

101. 9(2)(ba)(i) [redacted]

102. 9(2)(ba)(i) [redacted]

9(2)(ba)(i) [redacted]

9(2)(ba)(i) [redacted]

103. 9(2)(ba)(i) [redacted]

Councils are being forced to increase their expenditure and raise rates to address funding challenges

104. In the 2021-2031 LTPs, councils planned to spend $2.7 billion to maintain and upgrade their water infrastructure. This represents an increase of 80 percent compared to the 2018-2028 LTPs.

105. However, in practice, most councils do not keep pace with planned investment and the actual capital expenditure falls short of the planned investment which resulted on increased pressure for investment in future years.

106. Some councils are increasing their planned capital expenditure in the 2024-2034 LTPs to repair, renew or upgrade existing infrastructure. For example:

[35] Newsroom (20 February 2024), *Councils placed on negative credit watch due to three waters repeal*, https://newsroom.co.nz/2024/02/20/councils-placed-on-negative-credit-watch-due-to-three-waters-repeal/

a) Dunedin City Council has signalled that capital spending of $2 billion could be needed across the next decade, which is an increase of $500 million from what was in their 2021-2031 LTP;

b) Hutt City Council has announced that it will cost $1.5 billion over the next decade to fix their pipes and other water infrastructure;[36]

c) Wellington City Council has announced it may spend $2.5 billion over water infrastructure over the next decade, which includes $1.1 billion of capital expenditure. This capital expenditure on water would represent an increase of 65 percent compared to the 2021-2031 LTP;[37]

d) Central Otago District Council will spend $389 million over the next ten years (including $100 million in the first three years) on water services.[38]

107. Capital requirements for councils over the next three years are likely to be driven by three major factors:

a) planning for population growth driving urban expansion and intensification;

b) addressing deferred maintenance of existing infrastructure, as renewals and replacements because infrastructure built in the post-war period is starting to fail; and

c) meeting higher compliance standards as part of the resource consent process and drinking water standards when councils renew or replace infrastructure (as it is 50+ years old).

108. A recent scan of potential or planned future rates rises linked to the rapidly rising bills for water infrastructure are detailed in Table 2 below. It is worth noting that these rates rises are proposed and have not been confirmed in LTPs. This is not an exhaustive list of all proposed rates rises and represents a scan of available media articles as at February 2024.

Table 2: Comparison of proposed rates rises linked to water infrastructure costs

Council	Proposed rates rise	Justification
Ashburton District Council	11.5%	“Three waters, drinking, waste and storm water, work will continue to impact the budgets over the next 10 years as the council works to reach mandatory compliance standards.”[39]
Auckland Council (Watercare)	~25%, followed by 14.6% and 10%	Watercare says “that to maintain its infrastructure programme it must increase the water price paid by ratepayers by 25.8% from 1 July this year – an increase in $29 a month for the average

[36] Wellington Scoop (12 December 2023), *Hutt City plans $15.9% rates increase, but ‘life is difficult for many ratepayers’*, https://wellington.scoop.co.nz/?p=157149

[37] New Zealand Herald (31 January 2024), *Wellington residents face 15.4% rates increase as water shortage bites’*, https://www.nzherald.co.nz/nz/wellington-water-shortage-council-looks-at-budget-cuts-and-rates-rises-to-fix-pipes/KM4CZEFMXRGYRMVUD43PPXOFXY/

[38] Radio New Zealand (7 February 2024), *‘Unprecedented financial hardship’ – Southern mayors call for rates rise answers*, https://www.rnz.co.nz/news/national/508554/unprecedented-financial-hardship-southern-mayors-call-for-rates-rise-answers

[39] Radio New Zealand (22 December 2023), *Ashburton signals 11.5 percent rates rise looming*, https://www.rnz.co.nz/news/ldr/505393/ashburton-signals-11-point-5-percent-rates-rise-looming

		household."[40]
Buller District Council	31.8%	"Last year, Buller District Council Mayor Jamie Cleine warned a 31.8% rates rise could be on the cards, in large part due to the need to upgrade the water network."[41]
Clutha District Council	20% for one year	"If it was not for Three Waters upgrades, rates would be rising about four percent this year instead of 20%."[38]
Gisborne District Council	11.4%	Revenue collected through higher rates will be spent on resilient water services, roads, and wood debris management.
Hamilton City Council	25.5%, followed by 14.1% for four years	Hamilton Mayor Paula Southgate "said water services made up around 30% of their operating costs and capital investment." "The council can borrow more to fund the infrastructure investment needed, but needed to increase revenue, largely from rates, to remain within the limits set by the agency."[42]
Hutt City Council	16.9%	"The draft long-term plan will prioritise spending $1.5 billion over 10 years in a move to safeguard drinking water, storm water and waste water."[43]
Wellington City Council	13.8-15.4%	Wellington Water has recommended spending of $2.5 billion on water infrastructure over the next decade.[44] Wellington City Council staff recommended that councillors "invest $1.1 billion over the next 10 years to fix the city's thousands of leaky pipes."[45]

Councils are experiencing higher costs to meet regulatory standards

109. The stronger enforcement of regulatory requirements by Taumata Arowai and regional councils are also expected to increase costs for councils. For example, Taumata Arowai:

   a) recently instructed councils to take action to comply with the drinking water regulatory requirements. 27 council suppliers (covering 84 drinking water supplies and servicing over 310,000 people) have been identified where the drinking water treatment plants are operating without the required protozoa barriers. These councils are expected to have confirmed and funded plans in place to address this issue by 30 June 2024, and protozoa barriers must be installed and operational by 31 December 2024 (for surface water sources) and 31 December 2025 (for bore

[40] The Post (20 February 2024), *Aucklanders face 25% increase in water rates in coming year, after Three Waters repeal*, https://www.thepost.co.nz/politics/350185533/aucklanders-face-25-increase-water-rates-coming-year-after-three-waters-repeal

[41] Radio New Zealand (22 January 2024), *'Tipping point' for several councils as double-digit rates rises loom'*, https://www.rnz.co.nz/national/programmes/ninetonoon/audio/2018922883/tipping-point-for-several-councils-as-double-digit-rates-rises-loom

[42] New Zealand Herald(8 February 2024), *Three Waters: Hamilton City Council says adding water services costs back in to budget will affect rates*, https://www.nzherald.co.nz/waikato-news/news/three-waters-hamilton-city-council-says-adding-water-services-costs-back-in-to-budget-will-affect-rates/R2VJDITP3NDRDOZWZIFS2UG7UU/

[43] Radio New Zealand (20 February 2024), *'Lower Hutt rates could increase by 17% in bid to curb water leaks,* https://www.rnz.co.nz/news/national/509687/lower-hutt-rates-could-increase-by-17-percent-in-bid-to-curb-water-leaks

[44] New Zealand Herald (30 January 2024), *Wellington Water suggests $2.5b to fix city's pipes*, https://www.nzherald.co.nz/nz/wellington-water-suggests-25b-to-fix-citys-pipes/P6I6N64AKZALPJUSQYB4RGWY3E/

[45] Newshub (15 February 2024), *Wellington City Council to finalise rates increase, plans to better fund water issues,* https://www.newshub.co.nz/home/new-zealand/2024/02/wellington-city-council-to-finalise-rates-increase-plans-to-better-fund-water-issues.html

water sources).

b) estimates that 300 council supplies are likely to face bacterial treatment and residual disinfection issues.[46]

Auckland Council is already taking significant steps to separate itself from Watercare

110. Auckland Council's proposed LTP includes a proposal to increase water charges by 25 percent from 1 July 2024, with further increases of between 14 percent and 11 percent in subsequent years. The proposed LTP will be consulted on publicly soon.

111. The extent of price increases is a function of Watercare's intended investment programme ($1.2 billion in 2024/25) and its inability to increase its debt to revenue ratio above the 340 percent currently permitted by Auckland Council.

112. Auckland Council is approaching the limits of its debt headroom while remaining within its existing borrowing covenants and is exploring a range of short-term and more enduring options to increase debt headroom. Without balance sheet separation, Auckland Council and Watercare will be unable to borrow further debt to finance needed investments in infrastructure.

113. As a result, the Department and Crown Infrastructure Partners Limited are supporting Auckland Council to develop options to undertake a fast-tracked separation of Watercare to achieve greater financial flexibility.

Root cause five: Incomplete regulatory and stewardship oversight and monitoring

114. The level of regulation across water services is incomplete. For example, as a result of the Havelock North drinking water contamination, Parliament passed legislation to provide for new drinking water regulation by Taumata Arowai. This has resulted in considerably more transparency and focus on water quality issues across New Zealand. As a result, there is relatively comprehensive regulation to ensure drinking water quality.

115. However, a trusted and independent body is missing to monitor and regulate councils in their management of water services to ensure that services are being delivered at reasonable cost to consumers. While missing in New Zealand, economic regulation of water is common in other countries.

116. The incomplete regulatory and stewardship oversight and monitoring can be seen through quality issues, increased compliance costs and a lack of accountability to customers.

Financial challenges have led to quality issues

117. A survey of more than 23,000 people by the Infrastructure Commission found that access to safe drinking water is the number one infrastructure issue of concern to New Zealanders.[47]

118. Poor financial performance is contributing to poor quality services and negative health and environmental outcomes. A symptom of this was the contamination of the public drinking water supply in Havelock North in 2016. While not entirely the result of financial factors, this event led to more than 5,000 people becoming ill and contributing to the deaths of four people in a town of 15,000 people.

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[46] Taumata Arowai (5 October 2023), *Taumata Arowai releases list of supplies without protozoa barriers and next steps*, https://www.taumataarowai.govt.nz/news/articles/taumata-arowai-releases-list-of-council-suppliers-without-protozoa-barriers-and-next-steps/

[47] Infrastructure Commission Te Waihanga (2021), Aotearoa 2050.

119. The Havelock North Drinking Water Inquiry was a catalyst for the significant reform in how drinking water is provided, and failures have been identified across all parts of the system: regulation, service provision and source protection of drinking water.

120. 9(2)(ba)(i) [redacted]

9(2)(ba)(i) [redacted]

121. As discussed in root cause two, the operating environment for wastewater continues to highlight further inefficiencies and quality issues with nearly 10 percent of operators relying on expired consents.

The existing mechanisms within the current regulatory framework fails to provide economic regulation

122. Economic regulation is a framework to encourage efficient pricing and expenditure while providing greater transparency to regulators and customers about the performance of water services delivery. Many jurisdictions deliver water services within a strong economic regulatory environment which requires greater accountability, both to customers and central agencies. As shown in Table 3 below, there are a number of different economic regulatory approaches that can be implemented.

Table 3: Approaches to economic regulation of water services[48]

Level of provision	Jurisdiction	Economic regulation
National	Scotland	Water Industry Commission for Scotland
	Ireland	Commission for Regulation of Utilities
State	Tasmania	Office of the Tasmanian Economic Regulator
Regional	England and Wales	Water Services Regulation Authority (Ofwat)
	Victoria	Essential Services Commission
Regional and local	New South Wales	Independent Pricing and Regulatory Tribunal
Municipal/local	Florida	Florida Public Services Commission
	Colombia	Potable Water and Basic Sanitation Regulatory

[48] Castalia (January 2024), *Meeting key objectives of Local Water Done Well: Draft report on policy objectives and proposed process.*

		Commission
	Philippines	Local government units

123. In comparison, there is limited economic regulation of water services beyond the Department and Office of the Auditor-General within New Zealand. Furthermore, in the absence of a dedicated economic regulator, there is a lack of regulatory and system stewardship to protect consumer interests in councils' delivery of water services.

124. The Infrastructure Commission notes that economic regulation of water has become more common internationally. As a system, it provides for cost savings for consumers and reduces inefficiencies across water delivery. For example, the establishment of the economic regulator in England and Wales led to a 30 percent reduction in water leakages across the network.[19]

125. The role of economic regulation is discussed further in Section Two.

Who is affected by the water services crisis?

126. As such, all New Zealanders continue to be affected by the water services crisis as consumers of council provided drinking water, wastewater and stormwater services.

    a) In the immediate term, all New Zealanders are affected if water services do not meet regulatory or environmental standards. Consumers in some parts of the country are facing water shortages due to council under investment, while others are facing large rates increases.

    b) In the medium term, New Zealand ratepayers will be placed under additional financial pressure through increased rates or user charges for consecutive years to fund the historic backlog of investments in water services and new investments to enable residential development and growth, and compliance of existing services with regulated minimum standards. Short term decisions to defer rates increases or user charges will be to the cost of future rate payers.

127. Generally, the increasing costs of providing water services is also a limit on the capacity of most councils to invest in other high priority public services, such as local roads and parks.

128. However, the impacts of the water services crisis differ regionally, as some councils are in worse off situations than others. For example, Wellington residents are waiting 17 times longer than other cities to get the leaks on their streets and properties fixed.[49] Enabling councils to retain ownership and leadership of their water services will ensure that locally based decisions in the proposals are prioritised.

129. Regardless, given the importance of water for all New Zealanders and the wider economy, these proposals should tangentially improve the water service delivery for all New Zealanders. Achieving this should result in better and more cost-efficient services over the long term, though it may result in increased costs to consumers over the short to medium term as councils invest more and better fund their water services to get them financially sustainable.

130. The Department expects that Bill Two will not create any issues regarding human rights or constitutional issues.

What objectives are sought in relation to the policy problem?

131. The root causes identified above are, together inhibiting councils in their efforts to put delivery of their water services onto financially sustainable tracks and to provide

[49] Stuff (10 March 2024), *Wellington leaks taking 17 times longer to fix than other cities*, https://www.stuff.co.nz/nz-news/350202089/wellington-leaks-taking-17-times-longer-fix-other-cities

assurance to their communities that these services are meeting minimum regulatory requirements for drinking water safety and to reduce harmful environmental impacts associated with delivery of water services.

132. The Department's proposed approach to solving the policy problem is linked to the key features of LWDW (noting that components of this will be features of Bills Two and Three). **The policy objective is that local councils deliver water services that are financially sustainable and meet minimum regulated quality standards for communities.**

133. Putting water services onto a financially sustainable footing, with adequate investment and funding is critical if services are to meet community expectations of quality including drinking water safety and provide for local and regional growth and development.

134. Under LWDW:

a) financial sustainability means demonstrating:

i. revenue sufficiency – water services earn enough lifetime revenue from rates or water pricing to cover costs;

ii. ringfencing – water services revenue is ringfenced to enable borrowing against that revenue and protect funding for other council services; and

iii. funding for growth – water services can access finance for growth whenever there are users willing to pay the cost of services.

b) regulatory quality standards means:

i. water quality standards set by Taumata Arowai and regional councils; and

ii. water infrastructure standards, plus disclosure regime and price regulation set by the Commerce Commission.

135. Within this, the delivery of water services will be led by councils and recognises that each region requires an individual solution, as opposed to a one-size-fits-all approach. The approach will empower communities, improve decision-making quality and set rules for quality and investment.

Enabling Māori participation in decision-making

Engagement with mana whenua

136. The LWDW policy recognises that iwi have rights and interests in water. This Bill does not have specific objectives in relation to the role of iwi/Māori decision-making for water services. Nevertheless, the Department considers the proposals should be consistent with the current LGA requirements, and do not reduce Māori participation in decision-making regarding water services.

137. The Crown requires local authorities to facilitate Māori participation in local government decision-making processes, to give effect to the Crown's Te Tiriti o Waitangi/Treaty of Waitangi obligations. Sections 4, 60A and 77 of the LGA acknowledges the Crown's responsibility to take appropriate account of the principles of the Treaty of Waitangi and to maintain and improve opportunities for Māori to contribute to local government decision-making processes. Parts 2 and 6 of the LGA provide principles and requirements for local authorities that are intended to facilitate participation by Māori in local authority decision-making processes.

138. In addition, section 60A of the LGA requires that before a CCO makes a decision that may significantly affect land or a body of water, it must take into account the

relationship of Māori and their culture and traditions with their ancestral land, water, sites, wāhi tapu, valued flora and fauna, and other taonga.

139. Māori have been critical of local authorities' responses to these LGA requirements. The proposals do not seek to address implementation issues of the LGA with regards to Māori participation.

140. In an affidavit for the Crown in *New Zealand Māori Council v The Attorney-General* [2013], Deputy Prime Minister English summarised the Crown position was that it "acknowledges that Māori have "rights and interests in water and geothermal resources".[50] A water body may be a taonga of significance and importance to Māori, and the Crown has a duty to protect iwi/Māori rights and interests under the Treaty of Waitangi/Te Tiriti o Waitangi.[50]

141. Because the relationships, rights and interests that Māori have with water are often very geographically or catchment specific, these are often recognised at the local level, in agreements between mana whenua and councils, such as Iwi Management Plans or relationship agreements. In these contexts, meeting Treaty responsibilities will usually be focused on ensuring that mana whenua are engaged appropriately in decision-making processes that are relevant to their rights and interests.

142. The Crown requires local authorities to facilitate Māori participation in local government decision-making processes, to give effect to the Crown's Tiriti/Treaty obligations. Section 4 of the LGA gives explicit recognition to the Crown's obligations for local authorities in this respect. In 1993 the Waitangi Tribunal commented that, where the Crown has delegated functions to local authorities, it must still ensure that the Crown's obligations of active protection under Ko te Tuarua/Article 2 of te Tiriti/the Treaty must be fulfilled.[51]

143. The Crown has obligations under te Tiriti o Waitangi/the Treaty of Waitangi to respect the right of Māori to make decisions in relation to their lands and taonga, within the context of the Crown's right to govern. Te Tiriti/the Treaty also affirms that the Crown's obligations to New Zealand citizens are owed equally to Māori.

Te Mana o te Wai

144. Based on consultation undertaken as part of the previous reform, a clear concern from iwi/Māori is that any proposal needs to uphold, align, and integrate with Te Mana o te Wai and freshwater management. Te Mana o te Wai is a concept developed with Iwi as a way of describing the importance of freshwater within a Te Ao Māori framework. As Sir Mark Solomon and Donna Flavell explained: Upholding Te Mana o Te Wai acknowledges and protects the mauri of the water, and supports Te Hauora o Te Taiao (health of the environment), Te Hauora o Te Wai (health of the waterbody) and Te Hauora o Te Tangata (the health of the people).[52]

145. The recognition of Te Mana o Te Wai through the National Policy Statement of Freshwater (NPSFM) is intended to establish a framework which ensures that the health and wellbeing of freshwater bodies is at the forefront of decision-making. It was derived in part from the principles and values expressed in the Ngā Mātāpono ki te Wai

[50] Courts of New Zealand Ngā Kōti o Aotearoa (27 February 2013), *The New Zealand Māori Council v The Attorney-General – [2013] NZSC 6,* https://www.courtsofnz.govt.nz/cases/the-new-zealand-maori-council-v-the-attorney-general-2

[51] Waitangi Tribunal (1993), *The Ngawha Geothermal Resource Report 1993*, page 153 https://forms.justice.govt.nz/search/Documents/WT/wt_DOC_68348162/Ngawha%20Geothermal%20Resources%201993.pdf

[52] New Zealand Government (2017), *National Policy Statement for Freshwater Management 2014 (Updated August 2017)*, https://environment.govt.nz/assets/Publications/Files/nps-freshwater-ameneded-2017_0.pdf

developed through the Freshwater Iwi Chairs in 2017 and was included in the NPSFM. The NPSFM provides councils with a direction on how to manage freshwater under the Resource Management Act 1991, local authorities are required to give effect to Te Mana o Te Wai by engaging with hapū and iwi as part of their Regional Plan making.

146. While the Waitangi Tribunal in Wai 2358 praised the development of the latest formulation of Te Mana o te Wai, it found that the NPSFW "is still not compliant with Treaty principles, and Māori continue to be prejudiced by the weakness of mechanisms for the inclusion of their values and interests in freshwater management."[53]

147. However, legislation has been enacted that further implements the principles of Te Mana o Te Wai in relation to the provision of water services. The Water Services Act 2021 requires that all persons performing a function, power, or duty under this Act, must give effect to Te Mana o te Wai (to the extent that it applies to the function, power, or duty) as set out in the NPSFM.

148. The Bill does not make amendments to these mechanisms set out in the Water Services Act 2021 which uphold the principles of the Te Tiriti o Waitangi/the Treaty.

What are the limitations and assumptions of this Regulatory Impact Statement?

149. There are many limitations and assumptions within this policy proposal, detailed below.

Limitations with problem definitions and analysis

150. The Department recognises that the problem definition uses evidence collected from a range of councils across New Zealand. A detailed comparison or analysis of all councils has not been included as part of this problem definition and it is important to note that each council is different, so some situations described may not apply to all councils.

151. The Department has assumed that if central government intervention is not progressed, under-investment in water services delivery will continue and the problem will continue to worsen. All three stages of LWDW need to be implemented, otherwise under the status quo, council-owned water services will continue to degrade due to inconsistent management and under-funding.

152. The analysis of these policy options was completed at pace to meet the required legislative timelines set by the Minister for Local Government to implement the transitional provisions and build the regulatory environment to support Bill Three.

153. Some analysis relies on work completed as part of the previous government's reform (including the Affordable Waters Programme). The Department recognises that some significant step changes have occurred within the water services delivery system since the previous RIS were drafted, such as the establishment of Taumata Arowai and the repeal of the Water Services Entities Act 2022.

    a) As such, any limitations within evidence used in the problem definition and/or options analysis are highlighted.

    b) However, the previous reform included a significant amount of consultation – both at the exploratory problem definition phase during the Three Waters Review and during the design of the reform. Where relevant, the Department has considered feedback collected during these work programmes for the problem definition.

[53] Waitangi Tribunal Te Rōpū Whakamana i te Tiriti o Waitangi (2012), *Inquiries: National Fresh Water and Geothermal (Wai 2358)*, https://www.waitangitribunal.govt.nz/inquiries/kaupapa-inquiries/national-fresh-water-and-geothermal-resources-inquiry/

154. The Department has tried to concentrate on locally focused, at place data via information shared by councils through previous LTPs and annual reports. LTPs do provide the best available financial outlook for councils, but as discussed earlier, the economic context for the 2021-2031 LTPs presented an overly optimistic view of council finances. Council finances have been significantly affected by unforeseen events (such as extreme weather events) and optimistic planning assumptions (now impacted by higher levels of inflation and interest rates). It is expected that these LTPs will show deteriorating financial positions for the water services operated by most councils.

155. The Department has also relied heavily on evidence has been collected from media reports due to time constraints. The Department did not have sufficient time to validify the statements made in media articles with the affected councils.

156. The Department has used various Annual Performance Reports conducted by Water New Zealand. While these provide a comprehensive picture of the water services across New Zealand, they are voluntary and therefore do not have information from all suppliers. The 2021-2022 Annual Performance Report provides information from 33 water services providers who participated in the survey. However, in other years, there have been as many as 62 out of 64 providers supplying information. The data presented from Water New Zealand should be considered a snapshot as opposed to a complete analysis of the entire sector.

Limitations of Strategic Options

157. As noted in Section 1, the Coalition Government has repealed the previous government's reform (including the secondary Affordable Waters Programme) in place of an alternative approach where councils will retain direct responsibility for delivery of local water services while being held accountable for doing so in a financially sustainable manner and complying with minimum quality standards. The LWDW policy was a key manifesto commitment of the National Party, and the repeal of the previous government's Water Services Entities Act 2022 features in the Coalition Government's 100-point Economic Plan (numbers 67-69). Therefore, the scope of policy options that are explored within the RIS are somewhat limited by the Coalition Government's position on the previous reform, their manifesto commitments and coalition agreements.

158. As a result, the proposed strategic options (Section 2) are informed by, and limited to, the Government's policy. This prioritisation has meant that other potential strategic options or delivery models have not been included for consideration (for example, the centralised delivery model proposed as part of the reform).

159. The four components within Bill Two need to be implemented quickly to set up the transitional framework for the third stage of LWDW. Two components within Bill Two (Proposal Three: Watercare's financial separation and Proposal Four: Legislative amendments are made to support economic regulation for Watercare) need to be implemented as soon as possible, as the status quo remains unsustainable and would lead to continued deterioration of water services delivery, performance and cost. As such, the scope of options to be considered are limited.

160. As noted, most councils face pressure to lift water investment due to asset revaluations, inflation, population growth and regulation. The Department has considered that there is a non-regulatory option for the Crown to fill the revenue gap for water services delivery of an estimated $120 billion or more. This option is discounted for a number of reasons.

   a) Under the current fiscal environment, it is highly unlikely that the Treasury would be able to provide the required funding to ensure councils can deliver their water services to a minimum regulated standard.

   b) Providing the necessary funding would be highly unlikely to drive or encourage councils to make any performance improvements within their water services delivery, which is likely to lead to similar systemic issues in future years.

Limitations with development of policy proposals

161. The analysis of the four proposals in Strategic Option Two favours short- and medium-term outcomes (as opposed to long-term outcomes), given Bill Two's role to set up transitional provisions.

162. Similarly, due to the legislative timelines for Bill Two, there has been a relatively small amount of consultation with stakeholders during the overall policy design process. In addition, local councils are currently under pressure to draft and consult on their LTPs. However, officials have been able to rely on:

    a) evidence and insights collected through the public consultation from the previous policy programme (including select committee processes);

    b) the Government's newly established TAG which provided policy design input into the proposals included in this RIS (their specific feedback is not included in the RIS); and

    c) targeted, select engagement with key councils about the problems associated with LGA for the current proposals to understand their perceived barriers under current legislative requirements.

163. While this RIS was drafted, local councils were also in the process of drafting their LTPs prior to public consultation. This meant that there was limited time to engage and test these proposals with councils. There are no views of councils included in this RIS.

164. Auckland Council has led the policy programme on options for Watercare and been supported by the Department. Other agencies involved in this co-design process include Crown Infrastructure Partners and the Treasury. Auckland Council has yet to complete external consultation on the proposed options.

165. A small number of select councils were engaged on the LGA amendments, and their feedback on the perceived barriers to the LGA were considered in the policy design of the options. These councils did not provide any feedback on the policy options.

166. The Department also had access to submissions made to Parliamentary select committees in their consideration of the previous government's various bills to provide for its water services reforms.

167. Due to timeframes, it was not possible for the Department to complete a full analysis of the costs and benefits of the four proposals beyond qualitative estimates. They should be considered as indicative only.

168. 9(2)(ba)(i) [redacted]

Section 2: Deciding upon an option to address the policy problem

What strategic options could the Government explore?

169. There are four broad approaches (Strategic Options), available to the Government as it considers what it can do to enable and support local councils to deliver water services that are financially sustainable and meet minimum regulated quality standards.

170. The four Strategic Options are:

    a) **Strategic Option One: Status quo** is described in Section 1 as the status quo following the repeal of the Water Services Entities Act 2022. Under the status quo, councils will be regulated in their delivery of water services under the Resource Management Act 1991 and the Water Services Act 2021 to ensure their compliance with minimum regulatory quality standards in their delivery of water services. Councils will continue to have obligations to provide and assess the adequacy of water services and to include provision for water services in LTPs under the provisions of the LGA. In cases of serious non-performance, the Government will also have powers to intervene in the operation of councils under the LGA.

    b) **Strategic Option Two: Transitional provisions** to enable council reorganisation of water services in the lead up to economic regulation. A combination of four key proposals to ensure council focus on what is needed to put their water services onto sustainable financial footings as a basis for their transition to full economic regulation in the future. They will focus councils on the sustainable financial delivery of their water services and inform the development and implementation of economic regulation. The four proposals are greater information disclosure to inform the regulatory regime; systems to ensure councils deliver financially sustainable water services that meet regulatory standards; legislative amendments to streamline the establishment of new water services CCOs; and explore options for the financial separation for Watercare.

    c) **Strategic Option Three: Economic regulation without transition provisions** requires full economic regulation of water services with immediate effect. More information on the implementation of economic regulation is provided below.

    d) **Strategic Option Four: Economic regulation with stronger central government direction** is the same as Strategic Option Three <u>and</u> in addition, there will be stronger powers for central government to direct councils in how they are to manage and organise the delivery of water services, and less flexibility for councils to determine which service delivery model can be used.

171. The four Strategic Options are assessed against the following criteria (see below) in Table 5. The analysis of the Strategic Options favours short- and medium-term outcomes (as opposed to long-term outcomes) given Bill Two's role in providing for transitional provisions in the lead up to full economic regulation.

What criteria will be used to compare options to the status quo?

172. The following criteria have been chosen to compare the Strategic Options against the status quo and each of the subsequent policy proposals. These criteria are generic enough to provide a robust analysis within this RIS of both the Strategic Options and proposals without presupposing any decisions, but still fit within the Government's policy parameters of LWDW.

173. As shown in Table 4, the criteria provide a link between policy options and the Government's reform objectives, and a basis to indicate the extent to which each option will result in changes to councils' delivery of water services to improve their

financially sustainability in order to better meet community quality expectations of those services.

Table 4: Criteria descriptions

Criteria	Description	Relevance to objectives and root causes
Improved incentives, efficiency and accountability for sustainable performance	The extent to which an option supports a more transparent, efficient, and accountable system that drives better decision making and improved performance. This includes accountability to communities and regulators.	Incentives and accountability are critical to the success of a locally led approach to delivery. The problem definition concludes that current incentives on council management of water services are not well aligned to achieving the sustainable financial management of long-life water services assets. It also concludes that communities do not have access to transparent and reliable information to hold councils to account for their performance in delivering water services, as they deserve high quality water delivery. The problem definition also points to how a lack of economic regulation contributes to weak incentives and accountability. Institutional barriers to exploring and implementing more efficient organisational approaches to water services delivery are compounded by incentives on councils to be risk averse.
Improved evidence-base to inform delivery decisions	The extent to which an option supports faster and more sustainable investment from water services providers in water services infrastructure.	Water services networks and infrastructure are complex and expensive long-life assets. Good information and capable decision making and governance are supported by strong evidence, which is critical to sustainable financial management. The problem definition concludes that management of water services is not always informed by good evidence and that councils may not always have the capabilities they need to provide effective governance.
Provides a financially sustainable approach for local council delivery of water services	The extent to which an option addresses the ability of water services providers to use a range of tools to fund and finance new investment.	This criterion aligns to the overarching objective and is intended to provide for an overall assessment of the effectiveness of an option in providing for improved financially sustainable delivery of water services. The problem definition identifies funding constraints as being critical to financial sustainability and meeting minimum quality standards for communities, and this criterion will include consideration of the extent to which each option addresses these constraints.
Enables of improved quality, resilience, and residential growth	The extent to which an option supports future resilience and quality of water services delivery whereby growth is	This criterion also aligns to the overarching objective and is intended to provide for an overall assessment of the effectiveness of an option in providing for improved quality

Criteria	Description	Relevance to objectives and root causes
	not inhibited.	outcomes in local provision of water services.
Provides a practical path for implementation	The extent to which an option allows for a smooth transition to a new system, including reorganisation of water services across multiple regions. The options should explore practical implementation for councils and central government.	This criterion has been included to assess the practicality of each option as a basis for its successful implementation.
Enables Māori participation in decision-making	The extent to which an option enables Māori participation in decision-making that reflects the nature of their rights and interests in freshwater management and provision of water services to communities.	This criterion has been included because of the significance of water to Māori and in recognition of the Crown's Treaty obligations to Māori. It allows for an assessment of the compatibility of each option with the Crown's obligations.

174. When using these criteria for analysis, they favour short- and medium-term outcomes (as opposed to long-term outcomes) given Bill Two's role to set up transitional provision.

Table 5: Comparison of Strategic Options against Status Quo

Policy criteria	Strategic Option One: Status quo	Strategic Option Two: Transitional provisions to support economic regulation	Strategic Option Three: Economic regulation	Strategic Option Four: Economic regulation with stronger central government intervention and less water service delivery flexibility
Improved incentives and accountability for efficient, sustainable financial performance of water services	0 • Councils are likely to continue to deliver water services in a relatively fragmented and dispersed manner. It remains difficult for councils to reorganise their delivery of water services to achieve more efficient approaches to their delivery and funding of water services, which may mean performance continues to be average. • Access to technology, procurement, workforce capability and capacity and insurance may continue to be tackled by councils individually. • Councils are likely to perceive that barriers to joint service delivery models outweigh possible benefits. The process via the LGA to improve efficiencies through joint services may continue to be seen as risky. • Additional interest in improvement of water services from the media and communities may encourage councils to focus on improved performance. • The highly fragmented water services delivery system	++ • Requirements for councils to transparently provide information that demonstrates how they will deliver water services in a sustainable way should provide a roadmap for improvements. • The increased expectations of information disclosure and specific planning should flow through to increased accountability. This information will be publicly available to local communities and regulators and will hold councils accountable for performance in their delivery of water services. • The transitional nature of the information provided will be used to inform the design of economic regulation, while Taumata Arowai remains the water quality regulator. • Proposed amendments to streamline the establishment of new water services CCOs may reduce barriers to exploring joint services with other councils. This could reduce direct council control over the delivery of water but is likely to result in improved incentives and efficiencies.	+ • The pathway to economic regulation can take a long time (sometimes up to three years to implement the first version of the regime). Councils are likely to operate as per the status quo during the first three years of implementation (whereby water is delivered in a fragmented and relatively inefficient manner). • Councils may have a steeper learning curve moving directly to economic regulation without any transitional supports. This burden is likely to be higher for councils with lower workforce capability and capacity. • However, moving straight to full economic regulation is likely to force councils to make significant improvements to their supplies quickly. This may result in improved performance for some councils. • Central government may not have the necessary information to the support the design and implementation of economic regulation at the start. This could impact on	0 • Councils may have a steeper learning curve moving directly to economic regulation without any transitional supports. This burden is likely to be higher for councils with lower workforce capability and capacity. This burden may increase if councils are required to use a delivery model mandated by central government. • However, moving straight to full economic regulation is likely to force councils to make significant improvements to their supplies quickly. This may result in improved performance for some councils. • Central government may not have the necessary information to the support the design and implementation of economic regulation at the start. This could impact on how efficient the first iteration of the regulatory scheme is. • Regulation (both for Taumata Arowai and the economic regulator) is likely to be more efficient, as there will be fewer delivery models to regulate.

Policy criteria	Strategic Option One: Status quo	Strategic Option Two: Transitional provisions to support economic regulation	Strategic Option Three: Economic regulation	Strategic Option Four: Economic regulation with stronger central government intervention and less water service delivery flexibility
	makes regulation inefficient. • Regulation continues to focus on drinking water quality and compliance with environmental standards. An ongoing lack of economic regulation means there is no assurance to consumers that water services are prudently managed and that costs to consumers are reasonable.	• The financial separation of Watercare utilises a well-known delivery model that should increase overall accountability to consumers.	how efficient the first iteration of the regulatory scheme is. • Moving to full economic regulation may be less efficient for central government while there are many water services providers. Taumata Arowai will remain an effective water quality regulator. • Economic regulation will support significantly better outcomes for customers.	This should improve the quality of comparable information and lift performance. • The increased role of central government intervention may have mixed impacts for councils. Some may find the increased intervention a motivation to increase their performance. Others may find this increased intervention leads to a perception that they do have control over their supplies. • Overall, economic regulation should support significantly better outcomes for customers. However, it is not known if the prescription of delivery models will impact this.
Improved evidence-base to inform delivery decisions	0 • Councils will continue to have varying levels of water services infrastructure asset management. • They will continue to rely on LTPs and 30-year infrastructure strategies to inform their investment and asset management decisions and accountability. • The increased financial pressures to invest in and maintain water infrastructure may mean that councils are	++ • Requirements for councils to provide information that demonstrates how they will deliver water services should build capacity for infrastructure asset management. It can be used to support decision-making through a focused roadmap or plan. • The information collected during this phase will also increase the evidence-base for delivery decisions when	++ • Moving directly to economic regulation may require councils to improve their decision-making as quickly as possible. It is likely they will make considerable efforts to improve their evidence-base to support this. The resource that this may take (both in terms of time, cost and resource required) will depend on each individual council and the state of their water services.	+ • Moving directly to economic regulation may require councils to improve their decision-making as quickly as possible. It is likely they will make considerable efforts to improve their evidence-base to support this. The resource that this may take (both in terms of time, cost and resource required) will depend on each individual council and the state of their water services.

Policy criteria	Strategic Option One: Status quo	Strategic Option Two: Transitional provisions to support economic regulation	Strategic Option Three: Economic regulation	Strategic Option Four: Economic regulation with stronger central government intervention and less water service delivery flexibility
	making trade-offs between other services or projects. • Councils are likely to focus on water infrastructure delivery as the system reaches crisis levels. Councils may need to invest in their infrastructure reactively to meet these pressing needs, while deferring community projects to make savings needed for water investment. • There may be a stronger reliance on council management and councillors relying on expert staff within councils for better quality decision-making	designing the economic regulatory regime. • Clearer investment plans will allow communities to hold their councils to account, as they have more transparent information. • Councils may also use plans as a roadmap to explore and secure alternate revenue models such as greater use of variable pricing and direct cost recovery through user charges rather than rates. • Councils would have a clearer statutory process to explore water services CCOs, which should reduce the barriers (perceived or real) associated with potential for judicial review. Accountability and decision-making through LTP amendments and consultation is still required via the LGA. • The financial separation of Watercare should remove barriers associated with the political cycle as authority remains with a board that should have diverse skills.	• There will be a higher expectation that councils and council staff make better informed, more robust decisions as part of economic regulation. This may be difficult in the short-term as councils focus on improving the information and planning of their assets. • This option should ensure water services reach the desired operating models quicker and councils will continue to have the flexibility to choose their delivery model (as opposed to it being mandated). • This should result in better outcomes for communities sooner (as opposed to remaining in the status quo option) – but benefits to communities are not likely to occur until economic regulation has been embedded for a period (for example, in the medium- to longer-term following the initial design phase).	• There will be a higher expectation that councils and council staff make better informed, more robust decisions as part of economic regulation. This may be difficult in the short-term as councils focus on improving the information and planning of their assets. The increased role of central government could place additional pressure on councils. • Mandating delivery models may allow councils to share information to understand their asset bases better, but given that all supplies are different, the impact of this may be negligible. • This should result in better outcomes for communities sooner (as opposed to remaining in the status quo option) – but benefits to communities are not likely to occur until economic regulation has been embedded for a period (for example, in the medium- to longer-term following the initial design phase).
Provides a financially sustainable approach for local council	0 • Persistence of large variations across councils on their performance • The gap for funding needed to	+ • Information disclosure should support greater insights to improve overall management of infrastructure, which can be	0 • Without transitional provisions, councils are likely to continue to reach debt caps as interest rates remain high, limiting	- • Without transitional provisions, councils are likely to continue to reach debt caps as interest rates remain high,

Policy criteria	Strategic Option One: Status quo	Strategic Option Two: Transitional provisions to support economic regulation	Strategic Option Three: Economic regulation	Strategic Option Four: Economic regulation with stronger central government intervention and less water service delivery flexibility
delivery of water services	invest in water services (at least $120 billion) will continue to grow unsustainably. • Some councils (particularly large urban councils) are likely to reach their debt caps as interest rates remain high. There is a risk that their credit ratings are downgraded, which will increase the cost of their debt repayments. • Some councils may rely on increased rates and user charges to fund water infrastructure – either because they have reached their debt limit, or they do not wish to take on more debt. In this case, ratepayers and communities will continue to fund water services infrastructure. For example, Watercare's water charges are expected to go up by more than 25% if the company cannot be removed from Auckland Council's balance.	used as justification to finance future investments. It will explicitly require councils to identify how they will address the financial sustainability of their water services delivery. • There will be compliance costs for councils to complete the necessary financial disclosure and planning. • Legislative amendments to support the establishment of joint CCOs may reduce the overall consultation costs (time and resources) on individual councils, as it enables a more efficient and cost-effective method. • Joint or shared arrangements may encourage use of demand management and pricing tools to diversify revenue beyond rates. • Councils may also use plans as a roadmap to explore and secure alternate revenue models such as greater use of variable pricing and direct cost recovery through user charges rather than rates. • There will be compliance costs for councils to complete the necessary financial disclosure and planning. The financial separation of Watercare should improve the sustainable delivery of water	their ability for balance sheet separation. • Without financial support from the Crown or alternative funding or financing tools, it is very likely that rates and user charges will continue to rise to fund water investment. • There will be compliance costs for councils to complete the necessary financial disclosure and planning as part of the economic regulation regime. However, councils could use this information to explore and secure alternate revenue models and are likely to use demand management and pricing tools.	limiting their ability for balance sheet separation. • Without financial support from the Crown or alternative funding or financing tools, it is very likely that rates and user charges will continue to rise to fund water investment. • There is a chance that councils expect increased financial support from the Crown if they are required to change their delivery model to a mandated one, or there is more central government intervention over their delivery. • There will be compliance costs for councils to complete the necessary financial disclosure and planning as part of the economic regulation regime. However, councils could use this information to explore and secure alternate revenue models and are likely to use demand management and pricing tools.

Policy criteria	Strategic Option One: Status quo	Strategic Option Two: Transitional provisions to support economic regulation	Strategic Option Three: Economic regulation	Strategic Option Four: Economic regulation with stronger central government intervention and less water service delivery flexibility
		services, as it will allow increased borrowing for long-life assets and reduce the proposed costs of water charges.		
Enables of improved quality, resilience, and residential growth	0 • Due to financial constraints, councils may be limited as to how much funding they can put towards improving the proactive and reactive resilience of their infrastructure (e.g. for both growth and emergencies). The increased costs of this (for example via increased insurance) may fall on consumers and communities.	+ • Information requirements should encourage councils to take a more strategic and long-term approach to their assets and future investments. • The planning requirements will provide transparency for how planned investments in water services will provide for planned or foreseeable growth. • It is expected that legislative amendments to support joint CCOs will not have a measurable positive or negative impact on enabling growth or improving resilience.	+ • Any information disclosure requirements and increased accountability to communities that are included as part of economic regulation should encourage councils to strategically consider the growth and resilience of their assets and future investments.	0 • Any information disclosure requirements and increased accountability to communities that are included as part of economic regulation should encourage councils to strategically consider the growth and resilience of their assets and future investments. However, this resilience and growth may be limited by central government-mandated models of service delivery.
Provides a practical path for implementation	0 • No change.	+ • Implementation for councils will depend on their maturity levels and the complexity of their water services supplies. It is likely that more mature councils may find the implementation of increased information requirements easier to adopt than smaller councils with less capability. Overall, councils should have a lot of the information required as part of their	0 • Some councils may struggle with the increased reporting required of them, particularly if it models regimes set up under Part 4 of the Commerce Act 1986, without a transitional period. It is likely that more mature councils may find the implementation of increased information requirements easier to adopt than smaller councils with less capability.	0 • Some councils may struggle with the increased reporting required of them, particularly if it models regimes set up under Part 4 of the Commerce Act 1986, without a transitional period. • Full economic regulation is resource intensive to set up for central government. • The Commerce Commission does not currently have a strong relationship with water

Policy criteria	Strategic Option One: Status quo	Strategic Option Two: Transitional provisions to support economic regulation	Strategic Option Three: Economic regulation	Strategic Option Four: Economic regulation with stronger central government intervention and less water service delivery flexibility
		regular planning processes. • There may be increased compliance costs for councils to fulfil the requirements. • The transitional nature of these proposals will be used to inform the design of economic regulation, which is likely to be an easier stepping stone for councils (rather than moving directly to economic regulation). • The streamlined process for joint water CCOs should support easy implementation (both for central government to amend the legislation and for councils to engage with and follow). Utilising joint committee mechanisms supports practicable implementation for councils. • Implementation for central government agencies depends on their role, but a transitional approach is likely to be easier for most agencies to adopt.	• Full economic regulation is resource intensive to set up for central government. • It may be more costly for councils to allocate resource sooner to meet the requirements. • The Commerce Commission does not currently have a strong relationship with water services providers. This may inhibit a smooth transition to economic regulation, but this may be discounted given they are best placed to support economic regulation. • Consistent information disclosure and planning will make it easier for regulators to compare water services delivery across New Zealand. • The stewardship and monitoring of economic regulation may be more inefficient when monitoring multiple service providers.	services providers. This may inhibit a smooth transition to economic regulation, but this may be discounted given they are best placed to support economic regulation. • Stronger central government involvement in the models of service delivery is likely to increase the costs to the Crown to support this. • It may be more costly for councils to allocate resource sooner to meet the requirements, particularly if they are required to move to a central government-mandated model of service delivery.
Enables Māori participation in decision-making	0 • No change as discussed in Section 1: LGA ensures that councils facilitate Māori participation in local government decision-making processes to give effect to the Crown's Tiriti/Treaty obligations (section 4).	0 • No change compared to status quo. • Watercare will remain a local council organisation under s124 of the LGA. It will therefore be obligated to accord with Auckland Council's LTP and related	0 • No change compared to status quo.	0 • Each individual council will need to consider if any Treaty settlements would be impacted by the central government-mandated water services delivery models. They would need to act in partnership with iwi and hapū

Policy criteria	Strategic Option One: Status quo	Strategic Option Two: Transitional provisions to support economic regulation	Strategic Option Three: Economic regulation	Strategic Option Four: Economic regulation with stronger central government intervention and less water service delivery flexibility
	• Te Mana o te Wai must be upheld through councils' management of freshwater under the Resource Management Act 1991 and Water Services Act 2021. • Watercare's obligations to mana whenua will continue to lie with Auckland Council.	plans that mana whenua feed into.		accordingly to ensure their obligations are upheld.

Key:

- Green ++: Much better than doing nothing/status quo
- Green +: Better than doing nothing/status quo
- Orange 0: About the same as doing nothing/status quo
- Red -: Worse than doing nothing/the status quo
- Red --: Much worse than doing nothing/the status quo

Overall assessment of the Strategic Options

175. As noted earlier, the key parameters of LWDW prioritise specific components of water services delivery and ownership. This has influenced the Department's analysis of the Strategic Options.

176. **Strategic Option Three** is not recommended as it does not meet the criteria as effectively as other options. Furthermore, it will be less favoured by councils compared to Strategic Option Two. This is because there are no transitional provisions to support the move to economic regulation, which may be a significant burden for some councils. The Department recognises that Strategic Option Three is likely to be easier for central government to implement. However, priority for implementation needs to be given to local councils first given that they need certainty about the future of water services in New Zealand following a number of significant work programmes over recent years.

177. **Strategic Option Four** is not recommended because it scores unfavourably against the criteria. It does not align with these key parameters or the Coalition Government's intent for the future of water services delivery.

   a) It reduces the flexibility for councils to choose a locally led approach to their water services delivery by limiting the types of models that can be used. This approach assumes a one-size-fits-all model and discounts that councils have varying levels of maturity with regards to their asset maintenance, investment and delivery.

   b) While Strategic Option Four includes the use of stronger central government intervention, which is a key component of LWDW, there is a risk that this reduces incentives for councils to improve their performance when coupled with the delivery model prescription.

   c) There may also be an expectation that significant Crown funding is provided to each council if there is stronger central government intervention and less flexibility for delivery models.

178. **The Department recommends Strategic Option Two: Transitional provisions to support economic regulation.** It features a combination of four key proposals that set the foundations within the water services delivery sector to transition to full economic regulation in the future.

179. Further information about the Department's judgements within the analysis of the Strategic Options and the exploration of non-regulatory options is included below.

Other key judgements of Strategic Options

180. Further information about the Department's judgements within the analysis of the Strategic Options, and its subsequent recommendation of Strategic Option Two, is included below.

Economic regulation promotes positive outcomes for customers but requires a long implementation process

181. Part 4 of the Commerce Act 1986 provides for the regulation of the price and quality of goods and services in markets where there is little or no competition and little or no likelihood of a substantial increase in competition. Electricity lines, gas pipelines and certain airports are currently regulated under Part 4.

182. As stated in section 52A of the Commerce Act, economic regulation promotes outcomes produced in competitive markets by ensuring that suppliers:

   a) "Have incentives to innovate and to invest, including in replacement, upgraded, and assets; and

   b) Have incentives to improve efficiency and provide services at a quality that reflects consumer demands; and

c) Share with consumers the benefits of gains in the supply of the regulated goods or services, including through lower prices; and

d) Are limited in their ability to extract excessive profits."

183. Due its complexity, economic regulation can take a reasonable length of time to implement and is set for long periods. Economic regulation is commonly applied in periods that tend to be between four and six years in length.

184. Under the previous government's reform, it was recommended that there was a "pre-regulatory period (2023-2026) in which the economic regulator would work with the water sector to build its understanding of how to comply with economic regulation, before determining the rules required for the first regulatory period [CAB-22-MIN-0207 refers]." As part of this pre-regulatory period, suppliers would be required to provide basic information and there would be a focus on providing quality-only regulation.

185. The establishment of an economic regulator also takes time and resource. Central government will need to communicate with and educate councils on the regulatory requirements and develop of input methodologies on which to base price-quality regulation.

Transitional provisions are likely to be beneficial for councils in the move towards economic regulation

186. Given the demands of economic regulation on councils and the significant time period that economic regulation will take to implement, Strategic Option Two will create the necessary environment for councils as they move towards full economic regulation that is planned for in Bill Three.

187. The Department expects that Strategic Option Two will be more beneficial than Strategic Option Three, as it will support all councils, regardless of their capability to prepare for economic regulation. For example, it should support suppliers that are ready to move to a stronger regulatory environment (such as Auckland City's Watercare) and suppliers that will need to gradually shift their mode of delivery to clearer planning through a roadmap and provide greater accountability to their communities.

188. It will also ensure that all councils are focussed on what they need to do and change to put their water services onto financially sustainable footing in the years prior to the full implementation of economic regulation.

Analysis of Strategic Option Two: Transitional provisions

189. Based on the analysis above, the remainder of this RIS focuses on the four key proposals in Strategic Option Two. The four proposals are:

a) greater information disclosure to inform the regulatory regime;

b) systems are set up to focus councils on achieving the financially sustainable delivery of their water services that meet regulatory standards;

c) legislative amendments to streamline the establishment of new water services CCOs; and

d) explore options for the financial separation of Watercare (which is a discrete proposal separate from the first three proposals).

190. As shown in each of the four proposals' analysis tables in the following section, short- and medium-term outcomes are weighted higher than long-term outcomes given Bill Two's role to set up transitional provisions.

Proposal One: Foundational information disclosure to inform the regulatory regime

191. Three options are explored below:

a) **Option One: No information disclosure is required (status quo)**

b) **Option Two: A two phase, gradual approach to foundational information disclosure (Department recommended)**

c) **Option Three: Comprehensive information disclosure led by the Commerce Commission modelled on the Commerce Act 1986.**

Option One: Status quo

192. Under Option One, information on water services will continue to be collected by a number of different agencies including:

a) Taumata Arowai;

b) regional councils; and

c) Water New Zealand (using data from territorial authorities for their National Performance Review dashboard).

193. In addition, the LGA provides some information gathering powers. For example, councils are required to provide water-specific performance measures to the Department. However, information gathering powers in the LGA are either too narrow or have a prescribed statutory process which includes extensive consultation with councils which is unrealistic for this stage.

194. Taumata Arowai collects data for the purpose of ensuring water services providers are meeting drinking water standards. Taumata Arowai also collects limited information on stormwater and wastewater services. For example, Taumata Arowai collects information on pipes and other assets, but for the purpose of ensuring that suppliers are complying with drinking water standards.

Option Two: A two phase, gradual approach to foundational informational disclosure

195. A foundational information disclosure regime will come into force with the enactment of Bill Two in mid-2024. Foundational information disclosure is a transitional step towards the comprehensive economic regulation regime that will be supported through the enactment of Bill Three in mid-2025.

196. Foundational information disclosure, through the WSDPs, will help to build up a more detailed understanding of the sector's current state. This will be a two phased approach, as taking a graduated approach will build the capability of councils and the

Commerce Commission ahead of the full economic regulatory regime. The two phases involve the following:

a) Phase 1: Councils will prepare WSDPs that include baseline information about the current state of their operations, assets, revenue, expenditure, pricing, and capital. This process will be overseen by the Department. It will not be a regulatory information gathering exercise as such, but will include collection of information that will be relevant for future regulatory purposes. The Commerce Commission will work alongside the Department in this respect.

b) Phase 2: In addition, some councils (and potentially CCOs) may be subject to a more detailed information disclosure regime led by the Commerce Commission. This would build on the high-level information being collected through Phase 1 – and reflect that some councils are more advanced in their asset/financial management practices then others.

Who is required to disclose information

197. All councils that have water service delivery responsibilities (provided either directly or through other arrangements, such as CCOs) will be subject to foundational information requirements – through the preparation of WSDPs. Under Phase 1, all councils will prepare the information as part of their WSDPs. Under Phase 2, some additional councils, and CCOs, may be subject to a more detailed information disclosure regime.

198. Under Option Two, foundational information disclosure should be achievable across most water services providers, under either Phase 1 or Phase 2.

199. These two phases will ensure that all water service providers are subject to the interim regime, including councils who intend to move early and may establish a new water services delivery organisation before the full economic regulation regime comes into force under Bill Three. It will build capacity on and infrastructure knowledge across all water services providers on a consistent and comparable basis to inform investment priorities, and promote public transparency of providers' plans.

200. Small community suppliers, private schemes and self-suppliers will be excluded from the interim regime as the focus is to lift the quality of councils who deliver water services, regardless of their chosen delivery model. A designation regime could enable the Commerce Commission to bring small community providers into the regulatory regime in the future, if they believe the benefits are likely to outweigh the costs.

201. Councils can decide whether to include stormwater in their service delivery model and WSDPs. If they do, it would be subject to foundational information disclosure. While the inclusion of stormwater in water services delivery is voluntary, the Department recommends provision is included for it in Bill Two, regardless of whether stormwater has been included in the WSDPs or not.

Key components of Phase 1

202. The baseline information required during Phase 1, to make up part of the WSDPs (see Proposal Two), could include:

a) Financial information, including expenditure, revenues and financing;

b) Asset information, including asset type, condition, lifespan, average life, and estimate value, asset management plans and replacement policies;

c) Pricing practices, including metering or plans for metering;

d) Financial and non-financial performance measures, including number of customers and connections and current governance processes;

e) Quality performance measures and statistics, including leaks and water use and complaints processes; and

f) Assumptions, policies, and methodologies.

Key components of Phase 2

203. Some councils are more advanced and may establish new water services delivery organisations in the near term, and some water services providers have more mature asset management practices than others. These providers could be subject to more detailed information disclosure prior to Bill Three being enacted.

204. The more detailed information required during Phase 2 would build on the baseline information provided in WSDPs to be collected during Phase 1. Councils that reach desired maturity will move to an earlier more detailed information disclosure regime led by the Commerce Commission, and before the full economic regulation regime is enacted through Bill Three in mid-2025.

205. The Department is not yet able to confirm with the Commerce Commission the cost estimates to inform an assessment of funding requirements.

Delegated powers and disclosure requirements

206. It is proposed the legislation will provide for the Minister of Local Government and the Minister of Commerce and Consumer Affairs to determine which councils (if any) would be subject to the additional ‘Phase 2’ requirements. These decisions would be based on the advice of the Secretary for Local Government and Commerce Commission. The specific decisions and requirements would be given effect through Order in Council.

207. Other matters could be provided for in secondary legislation (including through Gazette notices), as relevant:

   a) the baseline information to be disclosed through WSDPs (led by the Department); and

   b) the additional information to be disclosed during Phase 2 (led/determined by the Commerce Commission).

208. We expect there will be a consultation period on Phase 1 foundational information requirements following the passing of Bill Two in July 2024. The consultation period would likely be from the beginning of October to mid-November 2024. Consultation with councils and other stakeholders will ensure that the information requested is fit for purpose and achievable.

Key roles to administer the regime

209. The Department will lead Phase 1, collecting information from councils through the WSDPs.

210. The Commerce Commission will lead Phase 2 information collecting for those providers who are graduated to this Phase.

Option Three: Comprehensive information disclosure led by the Commerce Commission modelled on the Commerce Act 1986

211. Under Option Three, a comprehensive information disclosure regime would be led by the Commerce Commission and modelled on similar regimes under Part 4 of the Commerce Act 1986. The comprehensive information disclosure regime would apply to all water services delivery models. This includes water services provided directly by councils, as well as separate but related providers, such as Wellington Water (where the council is a shareholder).[54]

212. The Commerce Commission has extensive experience in economic regulation and currently regulates New Zealand’s electricity lines services, gas pipeline services and

[54] Auckland Council’s water service provider Watercare will require bespoke arrangements, which are covered in Option Three.

certain airports (see section 52B of the Commerce Act 1986).

213. The Department expects that Option Three would help drive efficiency and provide better informed oversight of the water services sector under Bill Two to support the transition to full economic regulation provided for in Bill Three.

214. However, the information disclosure regimes set by the Commerce Commission are more refined and substantially more detailed than what may be necessary for a transitional regime. This may place undue burden on councils to comply.

Who is required to disclose information

215. Under Option Three, the comprehensive information regime would apply to existing council supplies and any new water services delivery models that councils choose to establish under LWDW, such as financially independent CCOs or regional CCOs. This will ensure that all water services providers are subject to the interim regime, including councils who intend to move early and may establish a new water services delivery organisations before the full economic regulation regime comes into force under Bill Three.

216. Small community suppliers, private schemes and self-suppliers will not be also included in the comprehensive disclosure regime. However, a designation regime could enable the Commerce Commission to bring small community providers into the full regulatory regime in the future, if they believe the benefits are likely to outweigh the costs.

217. As per Option Two, councils can decide whether or not to include stormwater in their service delivery model and WSDPs – and, if they do, it would be subject to foundational information disclosure.

Key components of information disclosure

218. Disclosure requirements are likely to align with information collected through WSDP (see Proposal Two) and will include:

a) Financial information, including expenditure, revenues and financing;

b) Asset information, including asset type, condition, lifespan, average life, and estimate value, asset management plans and replacement policies;

c) Pricing practices, including metering or plans for metering;

d) Financial and non-financial performance measures, including number of customers and connections and current governance processes;

e) Quality performance measures and statistics, including leaks and water use and complaints processes; and

f) Assumptions, policies, and methodologies.

Delegated powers and disclosure requirements

219. As also discussed above under Option Two, under Option Three Bill Two will include a delegated power to set the disclosure requirements in secondary legislation, consistent with other information disclosure regimes under the Commerce Act 1986, or through statutory notice to reflect the need for flexibility in the foundational regime.

220. The Department recommends that this power would include the ability to require an independent audit which will help lift the quality of the information; and compliance powers that will help to ensure providers comply with the disclosure.

221. However, there will be a consultation period on foundational information requirements following the passing of Bill Two in July 2024. The consultation period would likely be from the beginning of October to mid-November 2024. Consultation with local authorities and other stakeholders will ensure that the information requested is fit for purpose and achievable.

Key roles to administer the regime

222. While the Commerce Commission does not currently have strong relationships with water services providers, leading the foundational information disclosure regime will contribute to continue building their expertise and enable them to start building relationships.

223. Under Option Three, the Department would provide the Commerce Commission with support in building relationships with water providers including councils. The Commerce Commission would also work closely with the Department in ensuring the information disclosed supplements other elements such as the WSDPs.

224. Further, the Commerce Commission's current regulation of essential monopoly sectors under Part 4 of the Commerce Act mainly involves regulating corporate entities (some of which are council- or community trust-owned) rather than councils. The Commerce Commission does not have existing relationships with councils or expertise or experience in working with local government. Although over the past couple of years the Commerce Commission has built capability on the water sector in anticipation of a new regulatory regime, it does not have expertise in leading advice on sustainability of the plans and structure of the water sector.

225. As per Option Two, Option Three will include an independent audit to help lift the quality of information received.

How do the options compare to the status quo?

	Option One – Status quo	Option Two – A two phase, gradual approach to foundational informational disclosure (Department recommended)	Option Three – Comprehensive information disclosure led by the Commerce Commission modelled on the Commerce Act
Improved incentives, efficiency and accountability for sustainable performance	0 Incentives to improve performance align solely with LTPs, council strategies and general accountability to communities via LGA.	++ A more consistent approach to information disclosure will be more efficient for regulators. Likely to promote accountability to communities. This phased approach will be faster to implement for councils, so likely to see improved incentives and accountability sooner. Given that this is transitional, we expect to see the effect of this in the more immediate term.	+ A more consistent approach to information disclosure will be more efficient for regulators. Likely to promote accountability to communities. This approach will take time to implement, so there may be a delay in seeing any improved incentives or accountability. This approach would see benefits realised in the longer term, given the slower start to implementation through this option.
Improved evidence-base to inform delivery decisions	0 Evidence base comes from LTPs and council strategies, including 30-year infrastructure strategies. This will continue to provide a low-quality information base that does not support effective decision-making or strong accountability.	++ Information disclosure should build capacity in infrastructure asset management, leading to better quality decision-making. It will be used to inform councils' future direction and economic regulation. This phased approach will be faster to implement for councils, as baseline information is easier to pull together in this foundational scheme so likely to see better decision-making sooner. It will build the capability of councils (and the Commerce Commission) to transition into the comprehensive economic regulation regime provided for in Bill Three that will commence in mid-2025.	+ Information disclosure should build capacity in infrastructure asset management, leading to better quality decision-making. This approach will take longer to implement, so likely to be a delay in seeing better decision-making as a result of improved evidence-base. The speed of implementation is important as it may increase how long councils need to rely on borrowing for.

	Option One – Status quo	Option Two – A two phase, gradual approach to foundational informational disclosure (Department recommended)	Option Three – Comprehensive information disclosure led by the Commerce Commission modelled on the Commerce Act
Provides a financially sustainable approach for local council delivery of water services	0 Councils have incentive to provide water services in financially sustainable way but limited tools or levers to achieve this.	+ Information disclosure should support greater insights to improve overall management of infrastructure, which can be used as justification to finance future investments. The speed of implementation is important as it may reduce the long-term reliance of councils on debt. This model supports councils better, as it is less rigid and will require less of a learning curve or resource (particularly as it starts with the Department and then moves to the Commerce Commission).	+ Information disclosure should support greater insights to improve overall management of infrastructure, which can be used as justification to finance future investments. This option may see long-term results of improved financial sustainability sooner, as it supports the move to economic regulation quicker. This is a more rigid approach that may be more difficult for councils as there are no transitional phases.
Enables of improved quality, resilience, and residential growth	0 Councils' obligations for improved quality, resilience and residential growth remain focused on their obligations through the LGA.	+ Information disclosure should encourage councils to think more strategically and long-term about their assets as they consider investment. This should include consideration to future growth and resilience. The stepped approach to disclosure will provide early information to inform the development of proposals for economic regulation and its implementation.	+ Information disclosure should encourage councils to think more strategically and long-term about their assets as they consider investment. This should include consideration of future growth and resilience.
Provides a practical, implementable path for implementation	0 No implementation required.	++ Implementation is phased depending on councils' maturity levels, so likely to be overall easier for councils to adopt. Phase One will inform WSDPs (Proposal Two) to support practicable implementation. Varying levels of practical implementation from a central government perspective, as the Department and Commerce Commission need to work on different timeframes.	0 The Commerce Commission is best placed to support this implementation. However, regimes set up under Part 4 of the Commerce Act 1986 are more refined and substantially more detailed than transitional approaches and without any kind of staged approach, it may place undue burden on councils. This option does not align with the timelines for WSDPs (Proposal Two). This may increase compliance costs for councils and require them to allocate more resource sooner to complete this work.

	Option One – Status quo	Option Two – A two phase, gradual approach to foundational informational disclosure (Department recommended)	Option Three – Comprehensive information disclosure led by the Commerce Commission modelled on the Commerce Act
Enables Māori participation in decision-making	0 Does not require any additional work by councils.	0 Captures status quo– does not amend local authorities' responsibilities to ensure Māori can participate in decision-making.	0 Captures status quo – does not amend local authorities' responsibilities to ensure Māori can participate in decision-making.
Overall assessment	0 Does not require any additional resource or work for councils beyond meeting their existing obligations. However, no measurable impact will occur to improve councils' delivery of water services.	++ **Department recommended option** Above measures will require councils to collect more comprehensive information regarding their assets. This information will be used to inform future investment in water services delivery and support proposals for future economic regulation. Councils are likely to prefer this option as it will be easier to implement and aligns with the requirements for Proposal Two.	+ Above measures will require councils to collect more comprehensive information regarding their assets. This information will be used to inform future investment in water services delivery and support proposals for future economic regulation. This proposal will require more information from councils so may place an undue burden on them to meet the requirements. Central government agencies are likely to prefer this option, as it moves water suppliers to economic regulation sooner.

What option is likely to best address the problem, meet the policy objectives, and deliver the highest net benefits?

226. The Department recommends that Option Two, a two phased foundational informational disclosure led by the Department, with the Commerce Commission imposing more detailed information disclosure regime for more advanced councils, is implemented. Option Two is recommended for numerous reasons.

   a) It provides a phased approach for councils with a key focus to inform the design of the future economic regulatory regime. This phased approach recognises that councils do not provide water services delivery in a homogenous way and each region is managed differently, which was identified as a key component of the policy objectives and LWDW.

   b) The Department expects that all councils will be able to meet the requirements for Phase 1 through foundational information disclosure.

   c) This option gives Ministers the flexibility to graduate early moving water service providers as needed, taking considerations such as size and sophistication into account.

   d) Foundational information disclosure will build capacity in infrastructure knowledge across all councils on a consistent and comparable basis to inform investment priorities, and promote public transparency of providers' plans.

   e) In addition, councils have different levels of maturity in their investment and asset management of the infrastructure. Option Two will support less mature councils to begin to implement informational disclosure, while enabling more mature councils to underrtake more sophisticated and detailed information disclosure when ready.

   f) Option Two leans on and utilises the Department's current relationships across the local government sector. In comparison, Option Three would require the Commerce Commission to establish key relationships at pace.

   g) The Department expects that Option Two will provide significant benefits compared to Option One, as councils will be more accountable to their communities through this information disclosure and the decisions they make using the improved information.

   h) Option Two will also inform the design of economic regulation, which should in turn result in a higher-quality economic regulatory regime to be set up through Bill Three.

227. The Department expects that the benefits of Option Two will be felt relatively quickly as councils collect this information to inform the future of their infrastructure management and investment. The continued information disclosure requirements will keep councils focused on financially sustainable delivery of water services and accountable to their local communities.

228. As part of the development of Proposal One, the Department has engaged with the TAG, Ministry of Business, Innovation and Employment (MBIE), and the Commerce Commision.

What are the marginal costs and benefits of the option?

229. Due to the time constraints, the Department has not been able to undertake any quantitative cost benefit analysis of its preferred option.

Affected groups	Comment	Impact	Evidence Certainty
Additional costs of the preferred option compared to taking no action			
Regulated groups	There will be an ongoing cost to councils in preparing the	Low to	Medium: Councils are already providing this

	information requested through the WSDPs. However, the Department expects information will be relatively easy to collect, as it is largely already required as part of their other planning documents such as long-term plans.	medium	information through other channels, so it is expected to be a low burden on most councils to disclose it in their WSDPs. While some councils may be required to provide more information than others, it is not expected to impose a high burden on them.
Regulators	There will be a one-off cost to both the Department, through Phase 1, and to the Commerce Commission, and MBIE, through Phase 2, to resource the support required to carry out each of these phases. Implementing Phase 2 by the Commerce Commission is a step towards the full economic regulation.	Low	Medium: The Department is not certain of the costs at this stage, or resource required, though it is expected to be low impact.
Others (eg, wider government, consumers, etc.)	There are no expected costs for consumers.	Low	High: We are confident there are no ongoing costs to consumers through information disclosure.
Total monetised costs	Time constraints have not allowed for quantitative analysis to be undertaken.		
Non-monetised costs		Low	Medium
Additional benefits of the preferred option compared to taking no action			
Regulated groups	There will be an ongoing benefit to councils in preparing this information, as it will lift their information base, enabling them to better make decisions in the future and provide greater transparency to their consumer base.	Medium	Medium
Regulators	There is an ongoing benefit to the Department, MBIE and the Commerce Commission as the disclosure of information will help lift the information base which will help to inform the development of the future economic regime.	Medium	High: The Department is confident that building an information base will help to inform the development of the future economic regulatory regime.
Others (eg, wider government, consumers, etc.)	We expect there to be an ongoing benefit to consumers as a result of the uplift in the quantity and quality of information provided through foundational information disclosure. There will be	Medium	Medium

	greater transparency in the delivery of water services.		
Total monetised benefits	Time constraints have not allowed for quantitative analysis to be undertaken.		
Non-monetised benefits		Medium	Medium

Proposal Two: Systems are set up to focus councils on achieving the financially sustainable delivery of their water services that meet regulatory standards

230. Three options are explored below:

a) **Option One: No WSDPs are required (status quo)**

b) **Option Two: Water service providers submit a WSDP to be accepted by the Department as compliant with Statutory plan requirements within 12 months of the legislation (Bill Two) being enacted (Department recommended)**

c) **Option Three: Water service providers submit a WSDP to be assessed and approved by the Department as providing a sound basis for sustainable delivery of water services, within 12 months of the legislation (Bill Two) being enacted.**

Option One: Status quo

231. Under option one there would be no requirement on councils to develop standalone WSDPs. Instead, plans for water services would continue to be contained within LTPs.

Options Two and Three: Key components of Water Services Delivery Plans

232. The same overall aims and purpose of the WSDPs are used in Options Two and Three, however, the operational components of the WSDPs and legislation required to support these options differ. As such, they are described and compared below.

233. The WSDPs will provide for councils – individually or jointly – to publicly demonstrate how they intend to deliver water services in ways that are financially sustainable, meet regulatory quality standards for network infrastructure and water quality, and (where relevant), unlock housing growth.

234. The general intent of the WSDPs is to:

a) ensure that each council is focused on what it needs to do to transition delivery of their water services onto a financially sustainable footing;

b) make publicly transparent council plans for water services delivery so that local communities are better able to hold their councils to account for performance; and

c) inform the design and implementation of economic regulation and the administration of water quality standards by Taumata Arowai, regional councils and the Commerce Commission.

235. The WSDPs will broadly cover:

a) council priorities and proposals to achieve financially sustainable delivery of water services – including the proposed organisational delivery model (on an individual basis or joint with other councils);

b) asset management, the planned approach to network maintenance and renewal, upgrades to achieve regulated quality standards, and investments needed to enable economic growth and development;

c) funding and pricing, the planned approach to funding water services – including details of user charges, borrowing and approaches to debt management (including any plans to increase debt headroom through financial separation from councils); and

d) approach to organising delivery of water services, including ringfencing of financial management and delivery of water services from other council activities.

236. It is anticipated detailed content requirements would be set out in secondary legislation and/or guidance – and would relate to the following categories:

a) description of the water services, levels of service, growth and service targets and service areas ('current state');

b) description of compliance with regulatory requirements, standards, and service targets;

c) the capital and operational expenditure requirement required to deliver water services, comply with regulatory requirements/standards, and achieve service targets;

d) operating projections (operating costs and revenues to comply with regulatory requirements/standards and meet service targets);

e) an assessment of the current condition, lifespan, and value of water services assets;

f) a description of the asset management approach, including capital, maintenance and operational programmes for delivery of water services;

g) financing plan – illustrating how revenue to deliver water services is funded and financed;

h) issues, constraints and risks that impact on delivery to water services standards / regulatory requirements;

i) proposed delivery model, including any proposed arrangements for joint approaches with other councils; and

j) for joint arrangements, information on the corporate form of the proposed delivery model (including the indicative ownership and governance structure, control and financial rights of each council), as well as any major contracting that is planned, and an indicative implementation plan and timeline (if the proposals are sufficiently advanced to include these details).

237. Secondary legislation may also include requirements that the WSDPs are reviewed by an independent engineer.

238. The WSDPs are transitional (one-off) in nature and must be delivered within 12 months following enactment (though in limited circumstances the Minister will have the ability to consider extensions, on a case-by-case basis). This may affect what can be feasibly covered in the WSDPs, but it should support each council to focus on what it needs to do to transition delivery of its water services onto a financially sustainable footing ahead of economic regulation. As part of these policy proposals, there is also a recommendation to streamline the consultation and decision-making processes for councils to explore and establish CCOs under current legislative settings (see Proposal Three).

239. There are likely to be three scenarios for the WSDPs:

a) councils propose to continue to deliver water individually and the WSDPs are focused solely on a council's own district;

b) councils want to explore joint service arrangement but can only signal an intention to do this within the timeframes, as an arrangement cannot be completed by the WSDPs' deadlines; and

c) councils are able to submit a WSDP proposing a joint arrangement, collectively.

240. Bill Two will include a legislative framework for the WSDPs to ensure a sound and consistent approach across councils to their planning. The WSDPs will need to comply with the following general requirements:

a) include material on council owned water services – drinking water and wastewater are mandatory, but stormwater is optional;

b) cover a similar period to councils' 2024-34 long-term plan, with a particular focus on what will be delivered over the first three years to put water services on a financially sustainable footing;

c) enable the growth identified in a council's 2024 long-term plan (or other council planning documents);

d) be grounded on achieving compliance with current regulatory requirements;

e) identify the public consultation undertaken in the development of the proposals in the WSDP; and

f) include a declaration that the WSDP is compliant with statutory requirements and that the information it contains can be relied upon.

241. The option for a group of councils to develop a joint WSDP also provides an incentive for councils to collaborate to achieve scale and more efficient approaches to delivering water services.

242. The WSDPs will require councils to identify the following components related to their financial sustainability.

a) Their approach to capital investment, and the sufficiency of proposed investment to address deferred maintenance and renewals, to enable existing infrastructure to meet minimum regulatory standards, and to expand infrastructure to enable residential and economic growth.

b) Their approach to funding operational costs and investments in water services, in order to put financial management of water services onto a financially sustainable track.

c) Their approach to organising their management and delivery of water services including shared service arrangements with other council to achieve scale and efficiency benefits, and to ringfencing management and delivery of water service from other council activities to improve transparency and debt headroom.

243. It is proposed the legislation will provide for Ministerial powers of assistance and intervention in relation to these WSDPs, to ensure councils are incentivised to prepare a WSDP and there are appropriate Ministerial powers to act if problems arise (e.g. if WSDPs are not provided by statutory deadlines, do not meet statutory content and other requirements, or are not provided at all).

244. This is proposed to be done through provisions that to enable the Minister of Local Government to appoint a 'Crown Facilitator for Water Services Delivery Plans'. This is an option that could be used to help bring about the successful submission of a compliant and acceptable WSDP and might be associated with requests for extensions. It would be considered in situations where councils are in need of more than just the informal support available through guidance and access to technical assistance – particularly if they are seeking to establish joint arrangements.

245. The Crown Facilitator would be a flexible option, whereby a person or team of people could be appointed to do one or more of the following:

a) assist, advise, and if necessary direct, a council on how to prepare a WSDP;

b) work across a group of councils to facilitate or negotiate a joint WSDP/proposals for a joint arrangement – if those councils would benefit from someone external to help 'broker' and coordinate this;

c) if requested and agreed by a group of councils – provide an 'arbitration' role to resolve matters being debated during the process for forming proposals for a joint arrangement; and

d) anything else that may be necessary or desirable to help a council (or group of councils) to achieve the purpose of the WSDPs and LWDW.

246. In addition, as a last resort (backstop) measure, it is proposed the Minister would have the power to appoint a separate person or team who would prepare a WSDP on a council's behalf and, if necessary, direct the council to adopt and submit that WSDP. These powers would be considered if a council has failed to meet the statutory 12-month deadline and/or other requirements, despite having reasonable opportunities to do so (and where extensions have not been agreed). They could also be recommended in a report by a Crown Facilitator.

247. These powers would be in addition to, and separate from, the Ministerial powers of assistance and intervention in Part 10 of the LGA. Consistent with these standard provisions, councils would be required in the legislation to cooperate with the Crown Facilitator and any other Ministerial appointees, and to comply with any directions issued.

248. The WSDPs would be submitted to the Department (via the Secretary for Local Government) within 12 months of Bill Two coming into effect. Review and acceptance by the Department is likely to be completed in August 2025.

Key differences between Options Two and Three

249. The point of difference between Options Two and Three is the role of government in administering the requirements.

a) Under Option Two, the role of government is to review the WSDPs to check that councils have complied with statutory requirements. This is, that WSDPs have been developed and that WSDPs contain the required information.

b) Under Option Three, the role of government is also to review the content of WSDPs and to determine whether each council's WSDP provides a sustainable basis for its delivery of water services.

250. This is described in further detail below.

<u>Role of central government reviewing the WSDPs in Option Two</u>

251. Under Option Two, the Department would not endorse or sign off the WSDPs but would be reviewed by the Department. The Department does not recommend that a formal review process is undertaken by technical experts, but this does not preclude the Department from drawing on expertise as required prior to after the acceptance of WSDPs. This could be done on an 'as needed' basis and would not require legislation.

252. Councils will continue to have sole responsibility to deliver water services in a financially sustainable way. The WSDPs reinforce council roles in the management and delivery of water services, and accountabilities of councils to local communities for the services delivered.

253. While the Minister will be enabled to provide extensions, this would be in limited circumstances only, and on a case-by-case basis (with requests informed by evidence that councils are making progress with their WSDPs and have been taking reasonable steps to meet requirements). It is important that councils are required by the legislation to submit a WSDP on time, and there are 'regulatory backstop' powers to address this should they fail to do so (as suggested above). It is possible that this may be

contentious for some councils who may seek more time to provide the information, particularly if they are a smaller authority with less capability.

254. The legislation would be sufficiently flexible to ensure discretion can be exercised in exceptional circumstances where a WSDP cannot be delivered on time (for example, a natural disaster).

255. The legislative framework for the WSDPs will be included in Bill Two to ensure that they encourage a consistent approach to planning and management across councils. Bill Two would set out the key requirements and obligations for the WSDPs.

256. The WSDPs will be submitted to, and accepted by, the Department (via the Secretary for Local Government) within 12 months coming into effect. This schedule will support timely assurance to:

a) the Minister and Department that councils are meeting their responsibilities under the LGA; and

b) local communities and regulators that councils have a clear approach to deliver services in a safe and sustainable manner.[55]

257. This timeframe would mean the accepted final WSDPs can be returned to the council for publication before the pre-election period.

258. There is still a risk that the proposals in the WSDPs could become an election issue – though public consultation and getting community 'buy-in' to the proposals before the final WSDP is submitted could help minimise this.

259. The Department can still seek input from regulators (Taumata Arowai and the economic regulator) as required.

<u>Role of central government accepting the WSDPs in Option Three</u>

260. Option Three would require significant resource within the Department to review and approve up to 67 WSDPs at the same time, due to the increased role of central government to determine if the WSDPs provide a sustainable basis for the delivery of water services. This resource will need to have skills in engineering, financial modelling, water services and/or infrastructure investment and management.

261. Furthermore, the role of the Department in accepting the WSDPs may increase tension between central and local government, as councils may feel a lower degree of 'ownership' of the proposals. It also goes against the premise of LWDW whereby councils retain full control over their water services infrastructure and delivery.

[55] Note: the Plans are not a replacement for ongoing regulation by the economic regulator or Taumata Arowai.

How do the options compare to the status quo?

	Option One – Status quo	Option Two - Councils submit WSDP to be accepted by DIA as compliant with statutory requirements within 12 months of the legislation (Bill 2) being enacted	Option Three - Councils submit a WSDP to be assessed and approved by DIA as providing a sound basis for sustainable delivery of water services, within 12 months of the legislation (Bill 2) being enacted
Improved incentives, efficiency and accountability for sustainable performance	0 Continued focus from communities and media on water infrastructure issues (for certain councils) may increase councils' incentives to improve their performance, however, any improved performance may continue to be hindered by financial constraints.	++ Expectation that councils prepare and own their WSDPs, which should create a higher level of accountability for councils to improve their water services delivery. Requirements for WSDPs will result in improved information from councils on how they intend to deliver water services. This information will be publicly available to local communities (and government and regulators) and will help communities to hold councils accountable for performance in their delivery of water services. The requirement to include content such as a planned approach to network maintenance and renewal, and upgrades to achieve regulated quality standards increases incentives to improve economic efficiency. In addition, the provision for councils to submit a joint WSDP provides an opportunity for them to make efficiency gains by combining resources. This option aligns with LWDW as it recognises that the Crown will not step in to provide financial support to councils. Ministerial powers of assistance and intervention would help to ensure councils are incentivised to prepare their WSDPs, with sufficient Ministerial powers to act if assistance is needed or problems arise.	+ Councils will prepare the WSDPs, but the increased role for the Department to approve them may result in councils feeling like they do not 'own' their WSDPs, therefore reducing their accountability and the incentives to improve. Department review and feedback on WSDPs will contribute to their robustness but may increase expectations of central government involvement in council decision making and delivery of water services at the expense of local responsibility and accountability. This may make the relationship between the Department and councils murky. The requirement to include content such as a planned approach to network maintenance and renewal, and upgrades to achieve regulated quality standards increases incentives to improve economic efficiency. In addition, the provision for councils to submit a joint WSDP provides an opportunity for them to make efficiency gains by combining resources. Ministerial powers of assistance and intervention would help to ensure councils are incentivised to prepare their WSDPs, with sufficient Ministerial powers to act if assistance is needed or problems arise.
Improved evidence-base to inform delivery decisions	0 Councils will continue to rely on their LTPs and 30-year infrastructure strategies as an evidence-base for infrastructure	+ The WSDPs will produce useful content for councils to manage their water services more effectively. It will also generate better quality information for regulators. While WSDPs are transitional in nature, they should	++ The WSDPs will produce useful content for councils to manage their water services more effectively. It will also generate better quality information for regulators. The additional role for the Department to review and

	Option One – Status quo	Option Two - Councils submit WSDP to be accepted by DIA as compliant with statutory requirements within 12 months of the legislation (Bill 2) being enacted	Option Three - Councils submit a WSDP to be assessed and approved by DIA as providing a sound basis for sustainable delivery of water services, within 12 months of the legislation (Bill 2) being enacted
	investment.	provide councils with the necessary focus to take the steps needed to ensure their water services can be delivered in a financially sustainable way ahead of economic regulation.	accept the WSDPs may increase the quality of information collected, as it results in more detailed interrogation. This may be particularly beneficial for smaller councils with limited expertise.
Provides a financially sustainable approach for local council delivery of water services	0 Councils will continue to rely on their LTPs and 30-year infrastructure strategies as an evidence-base for infrastructure investment. The limited information that they collect is not likely to support financially sustainable approaches to water delivery.	++ The required content includes how council will address financial sustainability. This process is likely to be faster than Option Three, as it does not require the Department to assess and approve the WSDPs or consider the extent to which they provide a sound basis for the sustainable delivery of water services. It is likely to increase accountability to incentivise delivery against infrastructure planning. Council WSDPs will need to address two key questions: what needs to be invested to deliver water services to minimum regulated standards and to provide for growth, and how will operating costs and investment be funded.	+ The required content includes how councils will address financial sustainability. The role of the Department in assessing and approving these WSDPs is likely to slow down this process. Additional feedback may be provided to councils that can improve their approach for financial stability, but this approach is less well aligned with the principles of LWDW. Council WSDPs will need to address two key questions: what needs to be invested to deliver water services to minimum regulated standards and to provide for growth, and how will operating costs and investment be funded.
Enables of improved quality, resilience, and residential growth	0 Councils have varying skills to plan for and manage growth and resilience.	+ The submission of a WSDP will increase the transparency and accountability of council decision-making, incentivising improved performance with a focus on current <u>and</u> future delivery. WSDPs will need to provide transparency for how planned investments in water services will provide for planned or foreseeable growth.	+ The submission of a WSDP will increase the transparency and accountability of council decision-making, incentivising improved performance with a focus on current <u>and</u> future delivery. WSDPs will need to provide transparency for how planned investments in water services will provide for planned or foreseeable growth. The role of the Department in approving the WSDPs could have an unintended impact on how councils plan for growth.

	Option One – Status quo	Option Two - Councils submit WSDP to be accepted by DIA as compliant with statutory requirements within 12 months of the legislation (Bill 2) being enacted	Option Three - Councils submit a WSDP to be assessed and approved by DIA as providing a sound basis for sustainable delivery of water services, within 12 months of the legislation (Bill 2) being enacted
Provides a practical path for implementation	0 Councils will continue to deliver their water services and requires little to few implementation changes. Central government retains role as regulator for implementation.	0 Increased workload for councils to deliver the WSDP but this information should be readily available through their current documents (LTPs and 30-year infrastructure strategies). This burden may differ depending on the council (for example, smaller rural councils may require more assistance than larger suppliers). Councils that explore joint service arrangements will only need to submit one WSDP, which may lessen the overall burden. Councils will have access to some 'light touch' support during the WSDP preparation process, provided by or via the Department. This would be in the form of guidance material, templates and – if requested – access to technical assistance. Appointment of a Crown Facilitator may also support the preparation of WSDPs for some councils – and, in particular, help to facilitate joint arrangements. The requirement to complete WSDPs will also increase compliance costs for local government. WSDPs will provide a consistent approach to delivery, which should improve the regulators' efficiency when assessing the WSDPs and supplies.	-- The broader (assessment and approval) remit and higher threshold for acceptance requires more work for councils to achieve an acceptable WSDP. This increases the cost and time of staff required to review and assess up to 67 WSDPs within a specific timeframe for the Department. It is expected the cost would be significant. There is the potential to create tension between central and local government if disagreements regarding the WSDPs arise. Councils will have access to some 'light touch' support during the WSDP preparation process, provided by or via the Department. This would be in the form of guidance material, templates and – if requested – access to technical assistance. Appointment of a Crown Facilitator may also support the preparation of WSDPs for some councils – and, in particular, help to facilitate joint arrangements.
Enables Māori participation in decision-making	0 Councils will continue to be responsible for facilitating Māori/iwi participation in decision-making, including mechanisms prescribed in settlement legislation.	0 The LGA will continue to require councils to facilitate Māori participation in decision making.	0 The LGA will continue to require councils to facilitate Māori participation in decision making.

	Option One – Status quo	Option Two - Councils submit WSDP to be accepted by DIA as compliant with statutory requirements within 12 months of the legislation (Bill 2) being enacted	Option Three - Councils submit a WSDP to be assessed and approved by DIA as providing a sound basis for sustainable delivery of water services, within 12 months of the legislation (Bill 2) being enacted
Overall assessment	0 Councils to continue to use varying approaches to manage and plan for their water infrastructure. Accountability to communities and regulators may be low in some regions and performance remains sub-par.	++ **Department recommended option** WSDPs will provide a stronger focus from councils regarding their service delivery and funding arrangements, greater transparency about the 'current state' (of assets, etc.) and improve accountability to communities. This approach will also support a smoother transition to economic regulation. The overall responsibility remains with councils to own and deliver these WSDPs, which aligns with LWDW.	+ WSDPs will provide a stronger focus from councils regarding their service delivery and funding arrangements, greater transparency about the 'current state', and improve accountability communities. This approach will also support a smoother transition to economic regulation. The role of the Department may reduce councils' incentives to own and deliver these WSDPs, which does not align with LWDW.

What option is likely to best address the problem, meet the policy objectives, and deliver the highest net benefits?

262. The Department recommends the implementation of Option Two, councils submit WSDPs to be accepted by DIA as compliant with statutory plan requirements within 12 months. Option Two is recommended for numerous reasons.

   a) It ensures that councils continue to own and manage their water services using a model that best suits them, and provides clear proposals for service delivery arrangements and financial sustainabilty (including ringfencing. It also recognises that a one-size-fits-all approach does not work, which aligns with the principles of LWDW.

   b) The WSDPs should not require significant resource for most councils to pull together (although it may be more resource intensive for smaller councils with less capacity and capability), as the information is held in current documents.

   c) Consumers and communities can use the WSDPs to hold councils to account. It is expected that this should improve councils' incentives to lift the performance of their water services delivery.

   d) New Ministerial powers of assistance and intervention (including a 'regulatory backstop') will help ensure councils are incentivised to prepare the WSDPs to sufficient quality – and provide fit-for-purpose mechanisms for providing bespoke assistance and addressing problems (should this be needed).

   e) The information collected through the WSDPs will support the move to economic regulation and is likely to be valuable for the regulator during the design phase.

263. The Department expects that the benefits of Option Two will be felt relatively quickly as councils collect the information from Proposal One for their WSDPs to inform the future of their infrastructure management and investment, and start thinking about proposed service delivery arrangements (including exploring and starting to implement joint models). The continued information disclosure requirements will keep councils focused on financially sustainable delivery of water services and accountable to their local communities.

264. As part of the development of Proposal Two, the Department has engaged with the TAG.

What are the marginal costs and benefits of the option?

265. Due to the time constraints, the Department has not been able to undertake any quantitative cost benefit analysis of its preferred option.

Affected groups	Comment	Impact.	Evidence Certainty
Additional costs of the preferred option compared to taking no action			
Regulated groups	It is proposed that a template for the WSDPs will be provided to councils to give direction on information requirements. The intention is that council officers will populate the WSDP using information that is already held by council. The level of effort and resource required will be dependent on the existing level of separation (ringfencing) of water services, and the size and scale of councils' water services. Where councils	Low: We have not undertaken any formal cost-benefit analysis but estimate that FTE requirements for the preparation of WSDPs and endorsement by council is in the order of: • For small council - one FTE for 40 hours • For medium council	Low: Detailed design of the WSDP content is still to be completed- and would be set in secondary legislation. We do not know the extent to which councils will outsource the

	are preparing joint WSDPs, this will increase complexity, but they could share costs across councils. The WSDPs will need to be "adopted" by each council, which will require preparation of internal material to support council resolution	- one FTE for 60 hours • For large council or joint WSDPs – 80-100 hours	plan preparation.
Regulators	Cost to the Department (via resource and time) as the regulator to review the WSDPs, and potentially ongoing costs for the Department (via resource and time) to support councils with lower capability and capacity to prepare their WSDPs. The focus on meeting statutory requirements will mean that processes supporting the review of WSDPs will be able to be standardised. The Department will need to engage technical and financial expertise to support the review process. This expertise may also need to be engaged to support councils to prepare the WSDPs and/or develop and agree new joint delivery models. This is dependent on council responses.	Low	Low: It is unknown how many councils may seek the Department's assistance to prepare WSDPs. The number of councils likely to submit joint WSDPs is not yet known.
Others (eg, wider govt, consumers, etc.)	NA		
Total monetised costs	Time constraints have not allowed for quantitative analysis to be undertaken.		
Non-monetised costs		Low	Low
Additional benefits of the preferred option compared to taking no action			
Regulated groups	LWDW emphasises councils should determine future delivery models for water services (provided that the delivery model is financially sustainable). The preparation and development of the WSDPs in particular the requirement to ringfence water services and test the financial sustainability of current or proposed delivery models is a "first step" to enable councils to consider alternative delivery models for water services. Supporting that WSDP development process through development of plan templates, guidance and technical support, benefits councils who would otherwise need to undertake this activity	Medium	Medium

	on their own.		
Regulators	Local Water Done Well emphasises that councils should determine future delivery models for water services (provided that the delivery model is financially sustainable).	Medium	Medium
Others (eg, wider govt, consumers, etc.)	NA		
Total monetised benefits	Time constraints have not allowed for quantitative analysis to be undertaken.		
Non-monetised benefits		Medium	Medium

Proposal Three: Transitional arrangements to streamline the process for establishing new water services CCOs

266. Three options are explored below:

    a) **Option One: Status quo;**

    b) **Option Two: Targeted amendments to clarify councils' ability to jointly consult on proposals to establish a joint water services CCO;**

    c) **Option Three: Bespoke arrangements for establishing water services CCOs (Department recommended).**

Option One: No legislative amendments are required

267. Under option one there would be no changes to the legislative requirements in the LGA. Instead, councils would still have to rely on the existing provisions in the LGA if they wanted to move early to a single or joint water services CCO.

Option Two: Targeted amendments to clarify councils' ability to jointly consult on proposals to establish a joint water services CCO

268. This option would make several amendments to the LGA to clarify the provisions regarding councils consulting jointly on a proposal. This option would amend the relevant provisions to explicitly provide that councils can, for the purposes of considering forming a joint water services CCO, use the existing joint committee provisions (Schedule 7, clauses 30-32) to undertake joint consultation on a joint proposal. This option would only be making clearer what is currently allowed within the LGA, to give councils more confidence that they are able to use a joint committee for consultation on a proposal that involves multiple councils.

269. A joint committee would still be required to follow the consultation principles in section 82 in the LGA but would have the flexibility to determine how it may satisfy the consultation requirements.

270. Some council officials have indicated it is prudent, for the purposes of considering establishing a joint CCO, that provisions explicitly provide for councils to use the existing joint committee mechanism to undertake joint consultation particularly because the provisions around consultation use the singular 'a local authority'.

271. A drawback of this approach is that it only addresses some of the identified issues with the consultation and decision-making requirements. It does not for instance, deal with the burden that councils face of having to, in their decision-making identify, analyse and consult on 'all reasonably practicable options' which can span over a dozen possible options in some cases. This can be incredibly time and resource intensive.

272. However, it is unlikely that it would substantially reduce the drain on time and resources that many councils face when attempting to engage on joint proposals. It would also be a more complicated solution to implement from a legislative drafting perspective.

Option Three: Bespoke arrangements for establishing water services CCOs

273. The overall intention for this option is to provide councils with a transitional, bespoke and streamlined process for consulting on and deciding to establish a water services CCO (under current LGA settings), whether on their own or jointly with other councils. A more enduring framework for establishing a range of council-owned water organisations, including water services CCOs, is intended to be put in place by subsequent legislation.

274. The process would provide that councils who are wanting to form a joint water services CCO can set up a joint committee under the relevant provisions in Schedule 7. The joint committee's scope could include analysis of options, recommending a preferred option/proposal to the participating councils, undertaking consultation on the proposal

(if approved by all councils) in a joint manner, and making final recommendations to the participating councils on whether to establish the joint CCO.

275. There would be clarity on the minimum requirements for consultation, modified information requirements and modified considerations in the decision-making process. The modified factors that the joint committee (if used) and councils could include in their decision making (as detailed below) would also serve to 'de-risk' the process for councils who are concerned about the possibility of judicial review if they are seen to, as part of the consultation and decision making process, consider for example, the wider impacts of a CCO rather than just their individual district.

276. Most of the arrangements in the bespoke mechanism could also apply where a single council wishes to establish a water services CCO.

277. This option provides a stand-alone process for setting up a single or joint water services CCO, with added streamlining. As such, it is anticipated that it would significantly lessen the burden on time and resources for participating council(s). This is unlike option two which only clarifies a number of existing provisions in the LGA and is less workable as a solution. Option two also only addresses some of the potential challenges around establishing a *joint* water services CCO, whereas option three is intended to also help to streamline the establishment of a *single* council owned CCO.

278. A bespoke arrangement will better support any councils that wish to 'go-early' in establishing a CCO for water services ahead of Bill Three.

Establishment of a joint committee

279. Under Schedule 7 of the LGA, councils can set up joint committees with other councils and delegate any of their responsibilities, duties or powers to the committee (with some specific powers that cannot be delegated). However, as indicated before, it is not entirely clear to councils if they can use a joint committee to consult jointly for the purposes of establishing a joint water services CCO.

280. The proposal would include a provision in the LGA clarifying that councils wishing to form a joint water services CCO can set up a joint committee under Schedule 7. The joint committee would be able to recommend a proposal to participating councils, undertake consultation (if approved by all councils) in a joint manner and make final recommendations to the councils on whether to form a joint CCO. That is, councils would effectively have two decision points: (1) approving the preferred option proposed by the committee for consultation; and (2) approving the final proposal to be implemented (following consultation).

Consultation Process

281. The current individual consultation process on significant proposals can involve multiple rounds of consultation with the district. The proposed bespoke arrangement would only require councils to undertake one round of consultation on the proposal. This consultation could be carried out by the joint committee, by other collective arrangements the councils choose, or individually.

282. This option would also streamline the consultation process by exempting councils from having to consult on any proposed LTP amendment resulting from a decision to form a water services CCO, provided that the councils are satisfied that based upon the earlier consultation, they understand the views and preferences of their communities on the proposal.

283. If a joint committee is responsible for leading consultation, it would have the flexibility to determine how it runs public hearings and manages the process (including whether to use the special consultative procedure), providing it adhered to the consultation principles set out in section 82(1) and the requirement to have processes in place for consulting with Māori in section 82(2).

284. Additionally, this option would be flexible enough to ensure that, if changes needed to be made to the proposed model after consultation, this would not generally require

another round of consultation - unless the changes were extensive or had significant implications.

Information requirements for consultation

285. As noted in Section 1, councils must undertake significant analysis of 'all reasonably practicable options' and consider (as part of a review required under section 17A of the LGA) at least six listed options for changes to infrastructure. Under Option Three, the bespoke arrangement would only require councils, or the joint committee if used, to analyse and provide information on two options at a minimum, one being the current arrangements for delivery of water services (the status quo) and the second the proposed water services CCO. The proposal for consultation would have to provide a clear rationale for the preferred option. Councils would be exempt from the requirements of sections 77, 82A and 17A.

286. This would not preclude councils or the joint committee from being able to consult on more than two options. However, it minimises the range of options they would be required to analyse and present to their communities - and clarifies this in the legislation.

287. The arrangements would also require that, for each of the options put forward for consultation, the proposal would have to provide sufficient details on the impacts (including financial) on each of the districts included in the proposed water services CCO. This requirement would enable more genuine engagement across the districts and would support the councils in any resulting LTP amendments resulting from the adoption of a proposal.

Decision-making

288. As stated above, a joint committee is able to make recommendations to the participating councils about whether a joint water services CCO should be established and the final decision would rest with the councils. This protects local autonomy and accountability and ensures that there is buy in from all councils involved.

289. In the decision-making process, both the joint-committee (if used) and the councils would be able to consider the collective impacts on the communities across the proposed CCO area, as well as their usual considerations. It would be up to the joint committee and the councils as to how they weighted all these considerations.

290. Councils considering whether to establish a joint water services CCO would be able to factor into their decision making the considerations of the other participating councils, and the views of people outside of their own district (that are within the new CCO area).

291. The above arrangement would serve to 'de-risk' the decision-making process and allay council concerns around judicial review.

292. There is the possibility that, at either the first or second council decisions on whether to proceed, that one or more councils will decide to not go further with the proposal. If a council does not agree to the proposal prior to consultation, the remaining councils could either still move on to the joint consultation stage (but with the necessary changes made to the proposal), or they could stop the process. If a council does not agree to the proposal after consultation, the other remaining councils could still decide to pursue the proposed CCO. However, if the council pulling out means there is a significant change to the proposal, the councils would likely need to consult again. Alternatively, the councils could decide that they no longer wish to go ahead.

293. This ability for councils to pull out during the process may be a disincentive for councils to start the establishment process; however, it preserves councils' autonomy and flexibility to determine their own water service delivery arrangements.

Long-term plan (LTP) amendments

294. The arrangements would still require councils to amend their LTPs to include their decision to establish a sole or joint water services CCO and reflect the implications this

will have. However, the consultation requirements on an LTP amendment would be waived.

295. In the case of councils considering establishing a joint water services CCO, the legislation would also explicitly enable the councils to conditionally approve their LTP amendments. This would ensure that if a participating council subsequently decides against joining the CCO and that decision impacts on one or more of the other councils' decisions to join, those councils can pull out of the proposed arrangement without needing to make another LTP amendment.

How do the options compare to the status quo?

	Option One – Status quo	Option Two – Targeted amendments to clarify councils' ability to jointly consult on proposal to establish a joint water services CCOs	Option Three - Bespoke arrangements for establishing water services CCOs
Improved incentives, efficiency and accountability for sustainable performance	0 No amendment to consultation requirements maintains accountability of councils to individual districts and their interests. Requirement to consult on 'all practicable options' critical barrier. The resource required, and the possibility of legal challenge in exploring a joint CCO likely to disincentivise councils to explore shared service delivery.	+ Clarification of councils' ability to jointly consult would reduce ambiguity and clarify the process of consulting under current requirements, the same accountability to individual districts still apply.	++ Bespoke arrangements are optional for councils. There is the potential to reduce direct individual council control, however it increases the incentive and ability to collaborate with other councils to form a joint water services CCO. Option could potentially reduce the level of engagement and consultation but should support better incentives and stronger accountability to multiple communities. If this leads to CCOs being set up more quickly and those CCOs are more efficient, then this would improve efficiency of delivery of water services.
Improved evidence-base to inform delivery decisions	0 No change to the current evidence base, councils would continue to make independent decisions. Requirement to consult on 'all practicable options' provides significant amount of evidence for policy options.	+ Clearer consultation requirements would support joint proposals, whilst still maintaining the current broad evidence base drawn from individual council districts.	+ Joint committee completing joint consultation reduces individual council control. However, the proposal would retain the requirement to seek submissions on consultation from all interested parties. This would provide for a broader evidence-base to inform the joint committee. There may be a reduced evidence-base if councils choose to consult on only two options as the minimum requirement. Providing a clear statutory process is likely to reduce the risk (perceived or real) associated with a potential for judicial review. Option still maintains local accountability and decision-making through requiring LTP amendments and consultation still required to follow section 82 of the LGA.

	Option One – Status quo	Option Two – Targeted amendments to clarify councils' ability to jointly consult on proposal to establish a joint water services CCOs	Option Three - Bespoke arrangements for establishing water services CCOs
Provides a financially sustainable approach for local council delivery of water services	0 Current consultation requirements can result in multiple rounds of consultation by each council involved in a joint proposal. This creates higher costs to run each consultation round.	0 Clarifying provisions on joint committees would maintain the current costs of consultation for individual councils.	++ Bespoke arrangements reduce consultation cost and burdens on individual councils. Provides a collective approach to support consultation on water services CCOs which could create cost efficiencies across a group of councils. Supports a faster process to allow implementation of joint services. The sooner this can happen, the sooner councils can implement more financially sustainable methods.
Enabling of improved quality, resilience, and residential growth	0 This option is neutral with regards to improved quality, resilience and residential growth.	0 This option is neutral with regards to improved quality, resilience and residential growth.	0 This option is neutral with regards to improved quality, resilience and residential growth.
Provides a practical path for implementation	0 The current provisions in the LGA have proven to be burdensome and create significant work for councils to try to navigate when trying to implement joint proposals.	+ Clarification of the process for consultation would make the existing tools in the LGA more accessible for councils and make it easier to engage in joint committees on joint proposals. However, the burden of potentially multiple rounds of consultation remains. The use of "to avoid doubt" provisions would be complex and difficult to administer under the legislation.	++ It creates a standalone process in the LGA for councils to follow, which should support easy implementation (both for central government to amend the legislation and for councils to engage with and follow). Bespoke arrangements significantly reduce the burden of consultation on individual councils. It is expected to reduce the time and resource burden on councils when preparing and consulting on a proposal to establish or join a water services CCO. Using an existing joint committee mechanism means the approach is accessible and should be a more practical solution to achieving implementation. This reduces the risks to councils that they do not meet their consultation requirements and provides more clarity on how to implement this as an option. The use of a separate and clearly defined set of provisions explicitly for the purposes of establishing a water services CCO would provide

	Option One – Status quo	Option Two – Targeted amendments to clarify councils' ability to jointly consult on proposal to establish a joint water services CCOs	Option Three - Bespoke arrangements for establishing water services CCOs
			legislative simplicity.
Enables Māori participation in decision-making	0 This option is neutral with regards to Māori participation in decision making. Councils are already required to facilitate this under the LGA.	0 This option is neutral with regards to Māori participation in decision making. Councils are already required to facilitate this under the LGA. No changes are proposed to this requirement.	0 This option is neutral with regards to Māori participation in decision making. Councils are already required to facilitate this under the LGA. No changes are proposed to this requirement. Care would need to be taken to preserve any mechanisms prescribed in settlement legislation.
Overall assessment	0 Status quo provisions in the LGA create a significant burden on individual councils when seeking consult on a joint proposal. The provisions themselves are ambiguous and councils have issues getting joint committees off the ground. This burden can be disincentivising and resource consuming, particularly for smaller councils.	+ Clarifying the existing provisions in the LGA would support councils' ability to utilise the joint committee provisions. There may still need to be multiple rounds of consultation and councils would still have to analyse potentially a large number of different practicable options, which is resource and time intensive. Therefore, the current identified problems would not be fully addressed.	++ **Department recommended option** A bespoke arrangement creates an optional mechanism for councils that enables a smoother process for establishing a water services CCO. It also reduces the consultation burden on individual councils by providing for joint consultation run by the joint committee. Consultation is still largely bound by the requirements of the LGA and utilises the joint committee mechanism in the LGA to ensure ease of implementation.

What option is likely to best address the problem, meet the policy objectives, and deliver the highest net benefits?

296. The Department recommends Option Three, Bespoke arrangements for establishing water services CCOs, is implemented. Option Three is recommended for numerous reasons.

a) It will achieve the objective of providing councils with a streamlined approach to consulting and deciding on whether to form a single or jointly owned water services CCO.

b) Option Three will streamline the process for setting up a water services CCO, reduce time and resources put into consultation and decision making, and provide certainty to councils in terms of what they are able to factor into their decision making. It would do this without undermining the importance of community consultation. It would 'de-risk' this process and reduce the risk of legal challenge by providing a clear set of provisions in the legislation designed for this purpose.

c) The arrangement under Option Three would be optional for councils to use, therefore, the risk of any perception of reduced individual council autonomy would be limited. There could still be a perception of less focus on the interests of individual districts however, this will be mitigated through giving councils' discretion as to how they weigh up various considerations in their decision making.

d) Finally, in our engagement while developing Option Three, it was supported as being the preferred option, and would lead to achieving the policy objective. Option Two for example, would not fully address the issues and challenges that have been identified with the status quo and would likely be more difficult to draft in legislation. On balance, Option Three would best address the problem.

297. As part of the development of Proposal Three, the Department has engaged with a small number of councils and the TAG.

What are the marginal costs and benefits of the option?

298. Due to the time constraints, the Department has not been able to undertake any quantitative cost benefit analysis of its preferred option.

Affected groups	Comment.	Impact	Evidence Certainty
Additional costs of the preferred option compared to taking no action			
Regulated groups	A cost (one-off or ongoing) to councils that explore or set up joint water services CCOs. However, this is expected to be a reduction in cost compared to if councils were to use the current arrangements.	Medium	Low
Regulators	One-off cost to the Crown to complete legislative amendments (approximately 1 FTEs for two weeks). Potential minor ongoing cost to the regulator to support councils understanding of changes.	Low Low	Medium High
Others (eg, wider govt, consumers, etc.)	Potential one-off or ongoing cost for ratepayers (cost of consultation, potential establishment, water user charges).	Medium	Low
Total monetised	Time constraints have not allowed for quantitative analysis to be		

costs	undertaken.		
Non-monetised costs		Low to medium	Low
Additional benefits of the preferred option compared to taking no action			
Regulated groups	An ongoing benefit as the councils are likely to save resources, (money, time, and FTEs) compared to if they were to use the current legislative settings, as they would not be required to undertake extensive options analysis work, consult on multiple options, and consult multiple times.	High	Low to medium
	Potential to cost share for consultation.	Medium	Low to medium
	De-risked process for councils to avoid judicial review.	Medium to high	Low to medium
Regulators	No clear benefits	NA	NA
Others (eg, wider govt, consumers, etc.)	Potential benefits to ratepayers if scale efficiencies are achieved and/or the potential for better governance and management via a joint water CCO.	Low to medium	Low
Total monetised benefits	Time constraints have not allowed for quantitative analysis to be undertaken.		
Non-monetised benefits		Medium	Low

Proposal Four: Explore options for the financial separation of Watercare

299. Auckland Council is leading a policy process to explore options for the financial separation of Watercare from Auckland Council. Its process is being supported by the Department and will require government agreement and legislation to provide for its implementation. Proposal Four is a distinct policy option separate to Proposals One-Three.

300. Four options are explored below:

a) **Option One: Status quo;**

b) **Option Two: Enhanced status quo with Crown support (Auckland Council's initial preferred option);**

c) **Option Three: Independent Council-owned organisation (Watercare 2.0); and**

d) **Option Four: Mixed council and consumer ownership (Department recommended).**

301. Under all options, Watercare would remain a not-for-profit organisation. The majority of its revenue will come from water charges and charging infrastructure costs to developers. It will have statutory authority to set and collect charges in relation to existing and new connections.

302. It would not be permitted to pay a dividend or distribute a surplus in any way to any owner or shareholder. Surpluses in excess of allowable margins would be rebated to water consumers under a proposed 'interim regulatory' approach.

303. What changes most from Option One to Option Four is the amount of control and influence that Auckland Council has over the governance and operation of Watercare, Watercare's financial proximity to Auckland Council and, as a result, the amount of debt that Watercare and Auckland Council can each take on and the cost of that debt.

304. 9(2)(ba)(i), 9(2)(g)(i) [redacted]

305. 9(2)(ba)(i), 9(2)(g)(i) [redacted]

Option One: Status quo

306. Under Option One, Watercare would continue to be fully owned by Auckland Council. There would be no change to its governance, management, or operational arrangements. Auckland Council is assessed by its financial auditors and credit rating agencies as having a high degree of control and influence over Watercare. It is assumed by auditors and credit agencies that in the case of financial distress of Watercare, that Auckland council will intervene. Because of this high degree of control and influence, Watercare's balance sheet is consolidated with that of Auckland Council. Because of this, Watercare is constrained in its ability to borrow money by Auckland

Council's overall financial performance and borrowing capacity and also by Auckland Council's financial policy, which limits borrowing by Watercare to 340 percent of revenue. Auckland Council is indirectly constrained in its ability to borrow money for other initiatives, such as roading and transport projects, by Watercare's borrowing requirements.

307. Watercare has proposed the following price pathway in Auckland Council's draft LTP 2024-2034 to fund its current investment programme.

Price increase	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
	25.8%	14.6%	10.0%	6.9%	7.5%	7.4%	7.5%	1.2%	0.0%	0.0%

Option Two: Enhanced status quo with Crown support

308. Under Option Two (Auckland Council's preferred option), Watercare would remain a CCO of Auckland Council and would continue to operate under the legislative framework provided by the LGACA. Auckland Council would continue to own 100 percent of Watercare, appoint its board of directors, approve its statement of intent, and have rights to water care assets upon its wind-up. Like option one, Auckland Council would be assessed as having a high degree of control and influence over Watercare, and Watercare's balance sheet would be consolidated with that of Auckland Council.

309. The main difference to the status quo is Auckland Council's proposed that the Crown would provide support in the form of a guarantee, indemnity, or liquidity facility. This support would enable Auckland Council to increase its borrowing without adversely impacting its credit rating (and cost of debt). This would in turn provide for increased investment by Watercare in its delivery of water services.

310. Option Two is not supported by the Ministers of Finance or Local Government, as it would create fiscal risk for the Crown that would need to be accounted for on the Crown's balance sheet. This option has been included in the RIS and analysis tables (following section) as it is understood to be Auckland Council's initial preferred option.

Financial support, balance sheet treatment and credit ratings

311. Auckland Council has proposed that, in return for the Crown's financial support, the Crown would be provided specific rights to protect its position. The detail of any specific rights was not finalised at the time of writing. The intent of the conditions would be to minimise the risk to the Crown that the facility is ever called upon. These rights could provide for changes to governance arrangements or other conditions that could limit Auckland Council's control and influence over Watercare.

312. 9(2)(ba)(i), 9(2)(g)(i) [redacted]

Regulation, legislation and statutory management

313. Watercare would be subject to economic regulation under Bill Three from 2027. This would provide independent oversight over pricing, investment and borrowing decisions by Watercare. In the interim, it is proposed that a Crown monitor be appointed to oversee an 'interim regulatory' approach for Watercare. These measures will ensure there is an appropriate level of discipline and external scrutiny on Watercare ahead of formal economic regulation applying.

314. Option Two can be implemented via approval from the Minister of Finance under the Public Finance Act 1989.

315. There would be no specific statutory management arrangements for insolvency. Any statutory management would rely on Crown intervention powers under the LGA.

Option Three: Independent Council-owned organisation (Watercare 2.0)

316. Option Three describes an independent council-owned organisation where Auckland Council would continue to own 100 percent of Watercare 2.0 but would substantially relinquish its control of and influence over Watercare.

317. Watercare 2.0 would have a new board appointed on merit by a new Appointment and Accountability (A&A) Board, which would be given effect through a Council-settled trust or statutory provisions. Membership of the A&A Board would comprise persons appointed by Auckland Council, consumers (through elections) and others (such as the Crown appointees if it provides financial support) or mana whenua.

318. A constitution would specify minimum board size, rights to appoint directors, process for appointing and removing Board members, prohibition on appointment of members or employees of Auckland Council, and any other requirements for Board members (i.e., requirements to appoint professional directors or members with suitable industry expertise).

319. In addition to appointing Watercare's Board, the A&A Board (rather than Auckland Council) would approve Watercare 2.0's Statement of Intent. Auckland Council would have the right to comment on the Statement of Intent but would not approve it as it currently does. This together with the composition of the A&A Board would substantially lessen Auckland Council's control of and influence over Watercare.

320. Under a new statutory accountability framework, existing CCO monitoring and reporting requirements under the LGA would be replaced by a bespoke framework, enabling Watercare 2.0 to be exempted under section 7 from the definition of a CCO in section 6 of the LGA.

321. There would be a requirement for Watercare 2.0 to deliver to its shareholders and publish publicly available half-year reports on the company's operations and an annual report, including auditor's reports and performance against targets and other measures.

Financial support, balance sheet treatment, credit ratings, existing debt and new borrowings

322. Auckland Council would not guarantee Watercare 2.0's debt and would be prevented from providing Watercare 2.0 with any financial support, including if it was in financial distress. Statutory limitations would include provisions that Auckland Council:

    a) has no right, title, or interest in the assets, security, debts, or liabilities of Watercare 2.0 (and the constitution cannot confer any such right, title, or interest);

    b) must not receive any equity return, directly or indirectly, from Watercare 2.0;

    c) must not give Watercare 2.0 any financial support or capital;

    d) must not lend money or provide credit to Watercare 2.0; and

    e) must not give any person any guarantee, indemnity, or security in relation to the performance of any obligation by Watercare 2.0.

323. Watercare 2.0's debt (likely to be around $3.4 billion by 30 June 2024) owed to Auckland Council on the separation date would remain in place on the current interest rate and terms. There would be an agreed repayment profile for existing debt, the term of which would not exceed five years from the separation date.

324. To support the new borrowing that would be required, Watercare 2.0 would borrow funds from banks, capital markets and/or the LGFA to refinance the debt owed to Auckland Council and raise new debt to meet the capital expenditure requirements.

325. 9(2)(ba)(i), 9(2)(g)(i) [redacted]

9(2)(ba)(i) [redacted]

Regulation, legislation and statutory management

326. Option Three can be implemented through new legislation, with that legislation providing for enabling functions and powers, and amending the LGA and LGACA.

327. Statutory management or reorganisation provisions would be in place.

Option Four: Mixed council and consumer ownership

328. Option Four is similar to Option Three but the key difference is that Watercare's majority owner would be a newly established Auckland Water Consumer Trust (60-70 percent ownership) and Auckland Council would be a minority owner (30-40 percent). This model is similar to the ownership structure of some electricity distribution businesses (for example, Vector in Auckland is 75 percent owned by Entrust). It would be set up as a limited liability company governed in accordance with a constitution and applicable law.

329. A charter would be drafted within its constitution to protect the interests of the community and consumers and provide for 'interim regulation'.

330. As per Option Three, Watercare would have a new Board appointed on merit by a new A&A Board, which would be given effect through a Council-settled trust or statutory board. Membership of the A&A Board would comprise of members appointed by Auckland Council and the new Consumer Trust.

331. Watercare's constitution would specify minimum board size, rights to appoint directors, the process for appointing and removing Board members, prohibition on appointment of members or employees of Auckland Council, and any other requirements for Board members (i.e., requirements to appoint professional directors or members with suitable industry expertise).

332. Like Option Four, the A&A Board would approve Watercare's Statement of Intent, the requirements for which would be set in legislation.

333. There would be a statutory requirement for Watercare to deliver to its shareholders and publish publicly available half-year reports on the company's operations and an annual report, including auditor's reports and performance against targets and other measures.

334. The Crown would not guarantee or indemnify Watercare.

Financial support, balance sheet treatment, credit ratings, existing debt and new borrowings

335. As per Option Three, Auckland Council would not guarantee Watercare's debt and would be prevented from providing Watercare with any financial support, including if it was in financial distress. Statutory limitations would include provisions that Auckland Council:

    a) has no right, title, or interest in the assets, security, debts, or liabilities of Watercare (and the constitution cannot confer any such right, title, or interest);
    b) must not receive any equity return, directly or indirectly, from Watercare;
    c) must not give Watercare any financial support or capital;
    d) must not lend money or provide credit to Watercare; and
    e) must not give any person any guarantee, indemnity, or security in relation to the performance of any obligation by Watercare.

336. As per Option Three, Watercare's debt (likely to be around $3.4 billion by 30 June 2024) owed to Auckland Council on the separation date would remain in place on the current interest rate and terms. There would be an agreed repayment profile for existing debt, the term of which would not exceed five years from separation date.

337. To support the new borrowing that would be required, Watercare would borrow funds from capital markets and/or the LGFA to refinance the debt owed to Auckland Council and raise new debt to meet the capital expenditure requirements.

338. 9(2)(ba)(i), 9(2)(g)(i) [redacted]

Regulation, legislation and statutory management

339. Option Four can be implemented through new legislation, with that legislation providing for enabling functions and powers, and amending the LGA and LGACA.

340. The Auckland Water Consumer Trust would be set out with a trust deed. The principal objective of the Trust would be to hold the shares in the new company and oversee and protect the interests of the beneficiaries as shareholders and customers.

How do the options compare to the status quo?

	Option One – Status quo	Option Two – Enhanced status quo with Crown Support	Option Three – Independent Council-owned organisation (Watercare 2.0)	Option Four – Mixed council and consumer ownership
Improved incentives, efficiency and accountability for sustainable performance	0 No change to Auckland Council or Watercare's incentives to deliver water services efficiently. Likely to continue to rely on increased water charges and rates. Requirement to publish reports on performance.	0 The availability of Crown support to Watercare may set a precedent that such support will be provided to other councils which could weaken incentives on councils more generally to take responsibility for the financially sustainable performance of their water services. Strengthened scrutiny of performance by the Crown Monitor could also provide stronger incentives for efficiency improvement.	+ Relatively unknown model (not used for other utility entities) so unclear the extent to which it will result in incentives for improved financial performance and accountability to consumers. Whether the option results in improved incentives will be sensitive to the role of the A&A Board, the quality of the Watercare 2.0 Board, and the effectiveness of the 'interim regulation' approach adopted by the Crown Monitor.	++ Well known model that is used with other utility entities. Increases accountability through transparency. Trust model empowers communities and increases overall accountability to consumers. Trustees will act on behalf of beneficiaries and consumers. Requirement to publish reports on performance.
Improved evidence-base to inform delivery decisions	0 Watercare continues to make decisions based on existing information collection methods.	0 Auckland Council would still approve Watercare's Statement of Intent (borrowing and investment plan), but limited evidence that there will be better information to inform these decisions. Auckland Council still appoints majority of Board. Evidence base likely to remain the same.	+ While evidence-base likely to remain the same, A&A Board to appoint Watercare's Board. Diverse skills and roles across Board likely to improve evidence base used to manage and govern infrastructure assets outside of council workforce. Model likely to lessen influence associated with political cycle or direction as councillors will devolve authority for Watercare's governance to the arms-length A&A Board.	++ While evidence base likely to remain the same, separation of ownership governance from Auckland Council should minimise influences associated with the three-year political cycle, and result in improved ongoing focus on Watercare's performance. Diverse skills and roles across Board likely to improve evidence base used to manage and govern infrastructure

	Option One – Status quo	Option Two – Enhanced status quo with Crown Support	Option Three – Independent Council-owned organisation (Watercare 2.0)	Option Four – Mixed council and consumer ownership
				assets outside of council workforce. Model likely to remove barriers associated with political cycle or direction as councillors will devolve authority to the Board.
Provides a financially sustainable approach for local council delivery of water services	0 Watercare likely to continue to operate within limits of borrowing and pressure to keep increases in water charges to a 'politically acceptable' level, so there is high likelihood that further investment to be postponed. Reliance on water charges and rates to continue, with borrowing to fund investment in long-lived assets constrained by Auckland Council Group's borrowing limits.	0 Crown support required to allow Auckland Council to borrow more without impacting credit rating. Crown support for Watercare may set a precedent for other councils. Additional debt headroom is not guaranteed. Not supported by the Ministers of Finance or Local Government as it would move Watercare to Crown's balance sheet. No expected change to credit rating. A delivery model that relies on Crown support is not financially sustainable.	0 Watercare 2.0 required to establish own Treasury function and insurance policies. Watercare 2.0 to borrow funds and raise new debt to meet capex requirements. 9(2)(ba)(i), 9(2)(g)(i) [redacted] Balance sheet outcome may be more susceptible to future changes to credit rating methodologies.	++ Most likely to achieve balance sheet separation from Auckland Council, as a Consumer Trust will become the majority owner of Watercare.
Enabling of improved quality, resilience, and residential growth	0 Watercare unlikely to be able to respond to growth unless via water charges or infrastructure growth charges.	+ Crown support will allow for Auckland Council and Watercare to take on more debt to fund growth-related investment.	+ If the option achieves balance sheet separation to the satisfaction of rating agencies, it will allow for both Watercare and Auckland Council to take on more debt. 9(2)(ba)(i), 9(2)(g)(i) [redacted]	++ Credit rating is expected to increase, allowing Watercare to borrow more money to invest in future growth and improved resilience.

	Option One – Status quo	Option Two – Enhanced status quo with Crown Support	Option Three – Independent Council-owned organisation (Watercare 2.0)	Option Four – Mixed council and consumer ownership
			9(2)(ba)(i), 9(2)(g)(i) [redacted]	
Provides a practical, implementable path for implementation	0 No implementation required.	-- Can be implemented via approval from the Minister of Finance under the Public Finance Act 1989. Auckland Council's preferred option for implementation as easiest. Crown's least preferred option as further financial support not approved by Ministers.	+ Implementation will require new legislation, with that legislation providing for enabling functions and powers, and amending the LGA and LGACA. The Department has less clarity around how easy this option would be to implement for Auckland Council and the Crown.	+ Implementation will require new legislation, with that legislation providing for enabling functions and powers, and amending the LGA and LGACA.
Enables Māori participation in decision-making	0 Obligations to local mana whenua continue to lie with Auckland Council.	0 No change to status quo.	0 Watercare will remain a local council organisation under s124 of the LGA. It will therefore be obligated to accord with Auckland's LTP and related plans that mana whenua contribute to.	0 Watercare will remain a local council organisation under s124 of the LGA. It will therefore be obligated to accord with Auckland's LTP and related plans that mana whenua contribute to.
Overall assessment	0 Watercare continues existing operations but is unable to invest in further infrastructure due to balance sheet constraints and debt cap limits.	0 **Auckland Council recommended option** As enhanced status quo, it provides marginal benefits. However, the success or feasibility of this option relies predominantly on financial support from the Crown that is not guaranteed. This option is favoured by Auckland Council but Ministers do not wish to provide liquidity support, so not able to be implemented. It also risks setting a	+ Above measures would need to be sufficient for credit rating agencies to achieve balance sheet separation 9(2)(ba)(i) [redacted]	++ **Department recommended option** Provides cleanest way to financially separate Watercare and the Council. Greater accountability to consumers through trust model. 9(2)(g)(i) [redacted] This is Auckland Council's least preferred option.

	Option One – Status quo	Option Two – Enhanced status quo with Crown Support	Option Three – Independent Council-owned organisation (Watercare 2.0)	Option Four – Mixed council and consumer ownership
		precedent that other councils expect financial support from the Crown.		

What option is likely to best address the problem, meet the policy objectives, and deliver the highest net benefits?

341. As noted above, Auckland Council prefers that Option Two, Enhanced status quo with Crown support, is chosen because it is the easiest to implement. The Department notes that while the final policy decision lies with Auckland Council and Ministers, the Government's position is that it does not wish to support Option Two or provide any kind of Crown support for Watercare as this is not considered to meet LWDW's definition of financially sustainable.

342. The Department recommends Option Four. Option Four is most likely to achieve financial separation and ringfencing of Watercare from Auckland Council. This option is the most certain to result in balance sheet separation in the eyes of credit rating agencies. Both Watercare and Auckland Councill would be able to take on more debt than they would without separation. This will improve Watercare's capacity to invest in upgrades to existing infrastructure and to deliver new infrastructure to enable growth. It will also improve Auckland Council's capacity to take on more debt to invest in transport and other priorities.

343. It is noted that Option Four is Auckland Council's least preferred option, because it results in a substantial loss of influence and control over delivery of water services by Auckland Council. This loss of influence and control is, however, critical to achieving the benefits of financial separation between Watercare and Auckland Council.

344. 9(2)(ba)(i), 9(2)(g)(i) [redacted]

345. The development of Options Three and Four has been led by Auckland Council and supported by the Department, Treasury and Crown Infrastructure Partners. The Department notes that Auckland Council has not yet undertaken any public consultation about this option, which would likely be a subsequent stage in the consideration of this option. It is expected any legislative amendments would set out consultation requirements for Auckland Council.

What are the marginal costs and benefits of the option?

346. Due to the time constraints, the Department has not been able to undertake any quantitative cost benefit analysis of Option Four.

Affected groups	Comment	Impact	Evidence Certainty
Additional costs of the preferred option compared to taking no action			
Regulated groups	Auckland Council and Watercare will face some restructuring and implementation costs. These will include the cost of establishing the Appointment and Accountability Board.	Not enough information to assess, but expected to be relatively modest	High
Regulators	Watercare will continue to be regulated under the Resource Management Act 1991 and the Water Services Act 2021 with no or very minor administrative implications for regulators. Cost of proposed economic regulation will be unaffected. There will be costs associated with implementing the 'interim regulatory'	Insignificant. Minor administrative costs to existing regulatory systems. Medium one-off costs to the Crown associated with implementing the 'interim regulatory'	High

	approach (same across options 2-4).	approach.	
Others (eg, wider govt, consumers, etc.)			
Total monetised costs	Time constraints have not allowed for quantitative analysis to be undertaken.		
Non-monetised costs		NA	High
Additional benefits of the preferred option compared to taking no action			
Regulated groups	Watercare will continue to be regulated under the Resource Management Act 1991 and Water Services Act 2021. Increased access to debt and improved governance focus should over time improve Watercare's capability and capacity to meet regulatory requirements.	Insufficient information to quantify benefits	Medium
	Watercare debt/revenue increases to 500% (compared to the 340% limit imposed by Auckland Council).	High	High
Regulators	Improved governance and greater debt headroom should result in improved performance and compliance with regulatory requirements	Insufficient information to quantify benefits	Medium
Others (for example, wider government , consumers, and so on.)	Improved access to debt and improved governance should improve Watercare's capacity and capability to maintain and improve its services to customers (including to enable urban growth). The additional costs of increased debt and changes to financing rates are expected to offset over time by improvements in asset management and operational efficiencies from economic regulation. Price pathway for 2025-2034 expected to be significantly less than proposed in LTP (e.g. average price increase is 7.2% for water charges compared to 16.8% for 2025-2027), and possibly lower subject to efficiency gains. Over the long term, the efficiency gains from economic regulation coupled with improved asset management should result in more stable price paths and costs to consumers relative to what they would have paid under option 1.	Insufficient information to quantify benefits	Medium
Total monetised benefits	Time constraints have not allowed for quantitative analysis to be undertaken.		

Non-monetised benefits	Improvements to service quality though more debt headroom and improved governance resulting in improved financial performance.	NA	High

Section 3: Delivering an option

How will the new arrangements be implemented?

347. As noted previously, LWDW was a National Party manifesto document as part of the 2023 General Election. The arrangements that are discussed in the RIS are signalled in the 100-point Economic Plan and were announced by the Government in February 2024. As a result, councils are aware of the upcoming changes.

Proposal One: Foundational information disclosure to inform the regulatory regime

348. Phase 1 of Option Two (the preferred option) will be implemented by councils through the WSDPs, with Crown support for those with capability and capacity constraints. The first foundational disclosures will be required within 12 months of the Bill being passed.

349. There will be a consultation period (likely in Quarter 4 2024) with councils and other stakeholders to ensure that the information requests are practicable and fit for purpose.

350. Under Phase 2 of Option Two, the Commerce Commission would lead the implementation of the more detailed information disclosure. Primary legislation (Bill Two) would enable some matters to be provided for in secondary legislation, including the development of the additional information to be disclosed under Phase 2.

351. Councils subject to these regulations would still be required to provide information by 30 June 2025, prior to when Bill Three is intended to come into effect.

352. No Crown support will be available for these councils, as only those providers with sufficient asset management maturity and an acceptable plan for how they will deliver water services will be subject to these information disclosure requirements.

353. It is unlikely that many councils will complete their WSDPs and transform their water services much earlier than 1 July 2025 when Bill Three is intended to be enacted. If some councils are able to move quickly, the period that information disclosure would need to last beyond 1 July 2025 would be very short (months). This option gives Ministers the flexibility to graduate early moving water services providers as needed and taking considerations such as size and sophistication into account.

354. Option Three would provide similar benefits that will be achieved through Option Two. However, as discussed in the above analysis, the Commerce Commission is not experienced regulating such a sector. In addition, the information required under Part 4 would be harder for councils to comply with, so there is a risk that disclosure under this option would be harder for councils and the Commerce Commission to implement.

Proposal Two: Systems are set up to focus Councils on achieving the financially sustainable delivery of their water services that meet regulatory standards

355. Councils will be responsible for developing their own WSDPs (either individually or jointly), within 12 months of the Bill being passed.

356. For those councils with existing capacity and capability constraints, the Crown intends to provide an assistance package. This will be focused on technical support and will include the following components.

    a) Guidance (including a template) to clearly articulate what information councils must provide to meet the statutory requirements.

    b) Ensuring that the information that is requested is can be accessed by reference to councils' existing planning documents and reports and that any relevant information currently held by the Department (National Transition Unit) can be accessed by councils.

    c) For councils that need "hands on" assistance, we are purposing that we engage a small number of people with the appropriate expertise to support councils with technical assistance on:

i. sources of information or analysis that may be required to complete statutory requirements; and

ii. the robustness of the information to support councils' self-assessment of their confidence in the information that has been provided.

357. The Department is working with Crown Infrastructure Partners to identify how we can provide the appropriate expertise to enable that support at a level that is sustainable for the Department.

Proposal Three: Legislative amendments to support establishment of new CCOs

358. Under Option Three (the preferred option), the LGA will be amended to provide councils with a new, bespoke process for establishing water services CCOs. This process will be optional for councils.

359. Should councils choose to use this process, they will be entirely responsible for meeting the requirements under the amended legislation, including amending their LTPs to include their decision to establish a sole or joint water CCO and reflect the implications this will have.

360. If Option Two was chosen, the LGA would be amended to make the relevant clarifications about councils being able to use a joint committee for the purposes of consulting on the proposal of a joint water services CCO. As above, councils would be responsible for meeting the requirements of the LGA.

361. The Department will consider whether it would be beneficial to provide the sector with any guidance on the new provisions to help them understand what the amendments are intended to enable.

362. Implementation risks include the amendments being more complicated to draft than initially intended, and councils not using the new provisions.

Proposal Four: Financial separation for Watercare

363. Decisions on the financial separation of Watercare are subject to the outcome of ongoing discussions with Auckland Council. The outcome of these discussions will inform the detail of the preferred option with implications for what will be involved in implementation.

364. The Department's recommended option will require legislation to implement. Once legislation is enacted it will require the following.

a) Establishment of an A&A Board to appoint the Board of Watercare 2.0 and to oversee and to monitor its performance. This will involve:

   i. development of a constitution;

   ii. appointment of Board members; and

   iii. providing secretariate support to the Board, that would likely be funded by Watercare.

b) Consequent changes to Auckland Council and associated governance and administrative processes and systems to reflect its new role as a minority owner of Watercare.

c) 9(2)(b)(i), 9(2)(g)(i) [redacted]

365. Any changes would require public consultation first. It is expected these requirements will be set out in the legislation.

How will the new arrangements be monitored, evaluated, and reviewed?

366. Bill Two is focused on establishing transitional provisions to enable, support and oversee councils in delivering well-functioning and financially sustainable water services, ahead of a fully developed economic regulation regime outlined in Bill Three.

367. Overall, monitoring and evaluation for the four proposals will be focused on the degree to which each option is achieving its objectives.

368. Therefore, the effectiveness of these transitional proposals will be evaluated largely based on the extent to which they generate high quality evidence to inform further policy development.

369. In addition, each of the transitional provisions have specific characteristics that allow us to evaluate how (and how well) they can inform the development of further economic regulation.

Proposal One: Foundational Information disclosure

370. In the two-phase approach that is recommended, the Department (for Phase 1) and the Commerce Commission (for Phase 2) will be responsible for overseeing information disclosures, and assessing the information provided.

371. During the 12-month preparation process for the WSDPs, the Department will engage with councils and peak bodies as needed to obtain progress updates. This will help to ensure councils fully understand the requirements and are on track in collecting the required information. It will also help to identify situations where assistance may be required and/or extensions may be sought.

372. Success will be evident when councils begin to develop and provide necessary information, thereby fostering a more transparent regime and offering data and evidence to support future decision making. The Department will consider how the exercise is supporting the Commerce Commission and councils to develop the capability and capacity needed for the upcoming economic regulation (under Bill Three).

373. As part of the review of the submitted Plans, the Department will consult – as necessary – with the Ministry of Business, Innovation and Employment, the Commerce Commission, Taumata Arowai, and Crown Infrastructure Partners.

374. Foundational information disclosure will help to inform the development of future information disclosure requirements, as part of the fulsome economic regulatory regime. The extent to which councils comply with this will influence its ongoing policy development.

Proposal Two: Water Service Delivery Plans (WSDPs)

375. The Department will be responsible for accepting these WSDPs from councils. As part of this process, the Department will be required to assess whether these WSDPs meet statutory requirements. The effectiveness of these plans in achieving the policy objectives can be evaluated against the following metrics:

a) **The proportion of councils that meet the submission deadlines** can be used as an indicator of how well the sector responds to increased regulatory oversight. It will also likely be an indicator of that council's capacity and capability.
b) **The proportion of plans that meet statutory requirements** can be used as an indicator of response to regulatory oversight, capability, and capacity, as well as of governance capability across councils.
c) **The proportion of councils that submit joint water service delivery plans** could be an indicator of how effectively councils have been incentivised to take opportunities for efficiency.

Proposal Three: Legislative amendment to support establishment of CCOs

376. As this would be optional for councils to use, there would not be a formal monitoring, evaluation or review role for the Department. However, through its relationships with

councils, the Department may be able to determine which councils and groups of councils decide to use the new provisions to establish a sole or joint water services CCO. Through that information, we would be able to determine metrics like what proportion and type of councils take up the option. This would in turn provide us with an indication of the effectiveness of these new bespoke arrangements in incentivising councils to take opportunities for efficiency, to change incentive structures, and potentially also increase governance capacity.

Proposal Four: Explore options for the financial separation of Watercare

377. Given that this proposal is being led by Auckland Council and there is considerable work to complete, a monitoring and evaluation framework cannot yet be developed. The Department can consider this as it supports Auckland Council through their process as required.

Wider monitoring and review provisions

378. There are a number of wider monitoring and evaluation provisions in place for water services across New Zealand, many of which have been used to inform the evidence for this RIS. For example,

    a) audit reports, including water performance audits and LTP audits, from the Office of the Auditor-General,

    b) regular reporting on drinking water quality and network environmental performance measures to Taumata Arowai and the Ministry of Health

    c) Water New Zealand's National Performance Review.

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Annex Two: Council-specific case studies

The Department has collected information from three councils as case studies. These councils are all different in terms of the size of their organisation and communities, maturity, and geographic location and size. They highlight that council are not homogenous, but also shows how the large remit of council operations can have a wider impact on water services.

Case study one: Auckland Council and Watercare

Auckland Council is New Zealand's largest local government body, with over 1.7m residents. It is a Unitary Authority, so carries out the functions of both a Regional Council and Territorial Authority. Its water services are run by Watercare, New Zealand's largest utility provider. It operates 9,096km of waterpipes and 27 water sources across the council to supply more than 400m litres of water to Auckland every day.

In its 2021-31 LTP the Council outlined its infrastructure strategy which included $15 billion to be invested into water services. It identified five major challenges facing Auckland's infrastructure: climate change, natural hazards, growth, equity, and funding. Regarding water, these challenges manifest in a range of ways, including increased demand on the existing water assets, less certainty for the security of supply, increased breakages, overflows, and maintenance requirements.

The 2023 Annual Report discussed the impact severe weather events, including Cyclone Gabrielle, had on residents, transport infrastructure, public services and buildings, and stormwater, drinking water and wastewater networks. It also noted that because of this event many council programmes and projects were delayed due to damage sustained and reprioritised funding to support the immediate and short-term recovery.

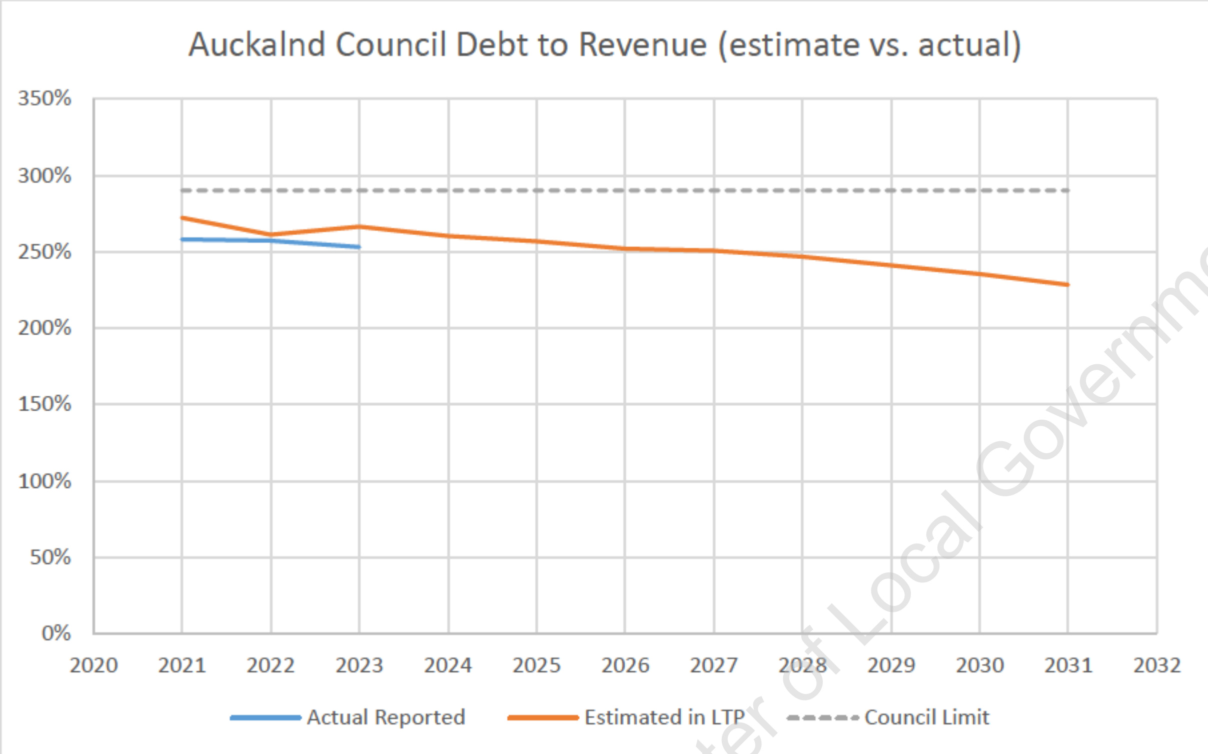
In response to Cyclone Gabrielle and the increased frequency of severe weather events across the country, the council has committed to establishing a recovery plan and a "Making Space for Water" programme. The purpose is to establish a practical and achievable programme of operational flood management works for the next six years.

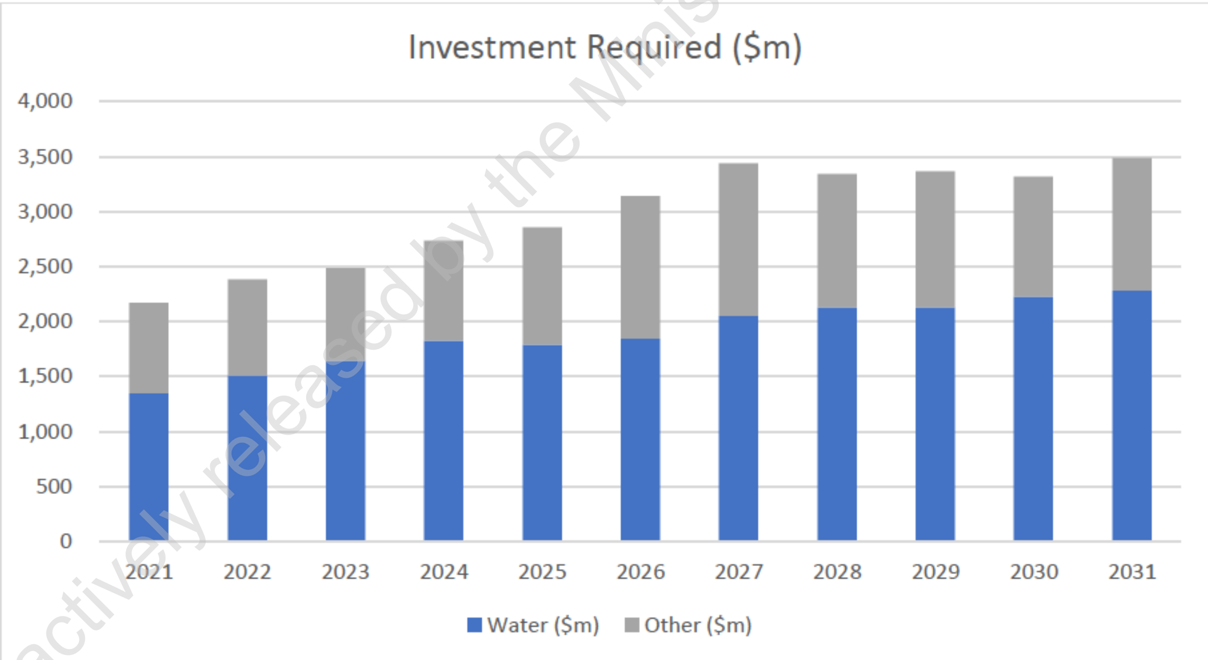
The Annual Report also noted that there was a net increase in staff costs to deliver water services, driven by increases in contract labour and temporary staff to backfill vacancies due to the tight labour market. Supplier costs also increased beyond budget due to inflation, supply chain disruptions and materials shortages. Both of these increases were further exacerbated by the severe weather events requiring significant unplanned repairs and maintenance to the network.

Capital spending on water was also higher than planned due to the work associated with securing an additional 150 million litres per day from the Waikato River catchment project and catch-up works on a prior year backlog of connections and water meter installations.

The debt to revenue ratio (depicted below) shows the Council is in a slightly better position than estimated in their LTP. However, the justification behind this raises some concerns. The 2023 Annual Report explains that there was higher-than-average revenue due to donations, asset transfers and larger than anticipated grants resulting in $421 million in additional revenue. This included the Waka Kotahi grant for $28 million in repairs following severe weather events. Operating costs were also higher at $25 million over budget due to an additional $45 million spent on response and recovery after severe weather events. The result of this expenditure elsewhere is that $50 million of the operational budget for projects was postponed to offset the costs of recovery. As a result, the debt to revenue ratio is in a better position than anticipated, at the cost of deferring delivery of infrastructure.

Supporting Data





Auckland estimates included in 2021-31 LTP

Auckland Council	Ann Plan	LTP	LTP	LTP	LTP	LTP	LTP	LTP	LTP	LTP	LTP
($millions)	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031
Funding Water	828,019	876,424	846,817	910,883	1,067,475	1,299,807	1,386,488	1,210,684	1,237,640	1,091,473	1,209,447
Funding Other	1,343,686	1,504,772	1,639,501	1,822,292	1,786,381	1,842,061	2,048,930	2,128,996	2,124,698	2,222,608	2,276,664
Opex Water	(4,445,388)	(4,672,884)	(4,808,446)	(5,008,293)	(5,269,366)	(5,465,208)	(5,684,977)	(5,899,070)	(6,120,569)	(6,301,061)	(6,511,494)
Opex Other	(448,962)	(486,592)	(505,006)	(535,104)	(565,034)	(594,047)	(622,809)	(655,955)	(671,051)	(692,889)	(713,696)
Capex Water	(828,019)	(876,424)	(846,817)	(910,883)	(1,067,475)	(1,299,807)	(1,386,488)	(1,210,684)	(1,237,640)	(1,091,473)	(1,209,447)
Capex Other	(1,343,686)	(1,504,772)	(1,639,501)	(1,822,292)	(1,786,381)	(1,842,061)	(2,048,930)	(2,128,996)	(2,124,698)	(2,222,608)	(2,276,664)
Debt to Revenue Ratio	272%	261%	266%	260%	257%	252%	251%	247%	241%	235%	228%
Total Debt	11,038,882	11,744,860	12,782,801	13,340,325	13,827,508	14,292,423	14,966,380	15,517,776	15,944,710	16,178,618	16,343,110
Total Interest Cost	451,619	445,758	476,842	510,238	523,976	539,999	567,589	591,106	598,191	597,554	587,662
Total Revenue	4,056,125	4,498,199	4,797,874	5,124,915	5,385,308	5,672,298	5,969,666	6,291,208	6,618,665	6,873,009	7,159,542

Auckland LTP Estimate Costs vs. Actual Reported

Estimates vs. Actual Reported	Annual Plan	Annual Report	LTP	Annual Report	LTP	Annual Report	LTP
($m)	2021	2021	2022	2022	2023	2023	2024
Funding Water	828	**927**	876	**1,070**	846	**1,122**	910
Funding Other	1,343	**4,388**	1,504	**4,606**	1,639	**5,551**	1,822
Opex Water	(4,445)	463	(4,672)	576	(4,808)	553	(5,008)
Opex Other	(448)	3,288	(486)	3,099	(505)	2,003	(535)
Capex Water	(828)	881	(876)	816	(846)	918	(910)
Capex Other	(1,343)	2,398	(1,504)	1,266	(1,639)	1,816	(1,822)
Debt to Revenue	272%	**258%**	261%	**257%**	266%	253%	260%
Total Debt	11,038	**10,687**	11,744	11,363	12,782	12,457	13,340
Total Revenue	451	**5,315**	4,498	5,676	4,797	6,673	5,124

Case study two: Queenstown Lakes District Council

Queenstown-Lakes District Council is an increasingly popular domestic and international tourism destination. In 2021, the council projected that the average daily population of the district will more than double by 2041, and peak daily population will double by around 2051. Most of this growth is driven by visitors and requires significant increases in the capacity of water, transport, and housing infrastructure.

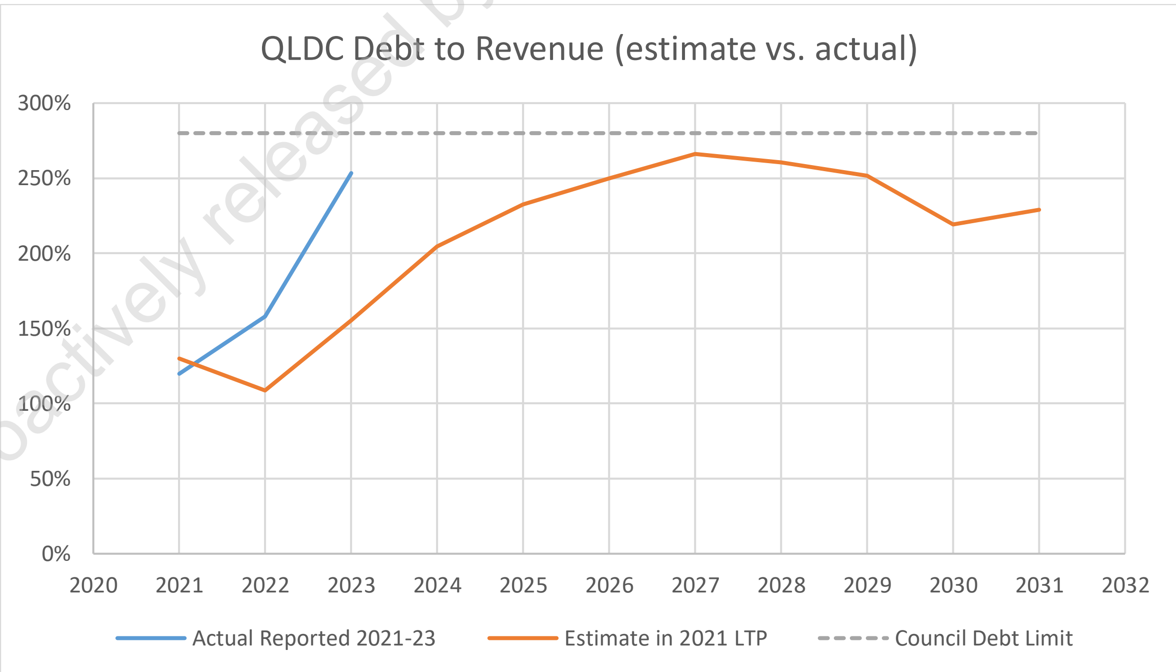
The council's 2021 LTP acknowledged the challenge of balancing growth with maintaining service levels and renewals. 46% of the council's projected capital expenditure from 2021-31 was allocated to drinking water, wastewater, or stormwater projects, including plant upgrades and construction of new facilities in areas of projected high growth, such as Kingston (a satellite town of Queenstown located 47km away at the southern tip of Lake Wakatipu).

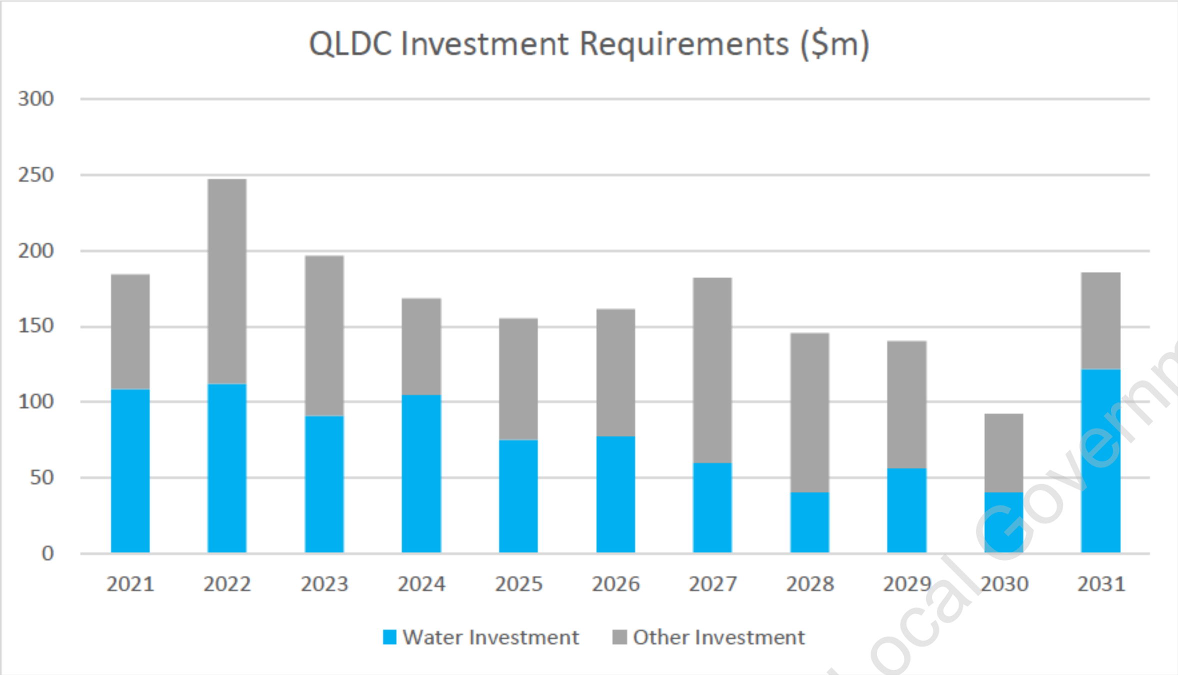
Since 2021, the council has faced several unexpected cost pressures, including a leaky building claim settlement that was not fully budgeted. In the 2022/23 financial year, the net debt to revenue ratio was 253.4% - significantly higher than the forecast level (189.5%). This is despite having increased rates by 6.5% (higher than the forecast increase of 5.87%) in response to inflationary pressures and increasing interest rates.

Debt increases for water supply and wastewater were much lower than forecast for 2022 and 2023. This appears to have come mostly at the expense of capital expenditure to meet additional demand and improve the level of service (spending on replacing existing assets was slightly higher than forecast for both years).

In response to these financial pressures, the Annual Report for 2023 indicates that the council has deferred (or is looking to defer) the completion of several significant water infrastructure projects through the upcoming LTP process including the $52.4m Wanaka Water Treatment Plant.

Supporting Data




QLDC Investment Requirements ($m)
300
250
200
150
100
50
0
2021
2022
2023
2024
2025
2026
2027
2028
2029
2030
2031
Water Investment
Other Investment

Queenstown Lakes estimates included in 2021-31 LTP

Forward Estimates based on LTPs	Ann Plan	LTP	LTP	LTP	LTP	LTP	LTP	LTP	LTP	LTP	LTP
($000)	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031
Funding Water	36,555	45,437	51,623	51,053	55,167	60,664	65,209	72,414	76,417	81,065	86,741
Funding Other	135,363	185,052	189,048	171,445	175,890	183,268	198,502	214,459	228,599	226,082	242,334
Opex Water	(22,160)	(23,852)	(27,366)	(30,499)	(33,885)	(37,693)	(40,871)	(42,714)	(44,306)	(46,501)	(49,380)
Opex Other	(136,729)	(155,675)	(162,647)	(177,665)	(188,477)	(198,558)	(208,200)	(218,274)	(231,135)	(241,215)	(441,056)
Capex Water	(108,590)	(111,810)	(90,973)	(104,580)	(74,862)	(77,106)	(59,710)	(40,066)	(56,273)	(40,254)	(121,854)
Capex Other	(75,608)	(135,439)	(105,424)	(63,631)	(80,211)	(84,223)	(122,424)	(105,379)	(83,726)	(51,703)	(63,543)
Debt to Revenue Ratio	130%	109%	155%	205%	233%	250%	266%	261%	252%	219%	229%
Total Debt	138,684	138,684	138,684	138,684	138,684	138,684	138,684	138,684	138,684	138,684	138,684
Total Revenue	171,918	230,489	240,671	222,498	231,057	243,932	263,711	286,873	305,016	307,147	329,075

Queenstown Lakes LTP Estimate Costs vs. Actual Reported

Estimates vs Actual Reported	Ann Plan	Ann Report	LTP	Ann Report	LTP	Ann Report	LTP
($000)	2021	2021	2022	2022	2023	2023	2024
Funding Water	36,555	26,814	45,437	28,692	51,623	31,039	51,053
Funding Other	135,363	193,978	185,052	209,842	189,048	235,160	171,445
Opex Water	(22,160)	(18,320)	(23,852)	(21654)	(27,366)	(30922)	(30,499)
Opex Other	(136,729)	(122,347)	(155,675)	(160,006)	(162,647)	(234,878)	(177,665)
Capex Water	(108,590)	(35987)	(111,810)	(45272)	(90,973)	(35938)	(104,580)
Capex Other	(75,608)	(49,590)	(135,439)	(134,080)	(105,424)	(137,807)	(63,631)
Debt to Revenue Ratio	130%	120%	109%	158%	155%	253%	205%
Total Debt	138,684	265,533	138,684	376,549	138,684	574,473	138,684
Total Revenue	171,918	220,792	230,489	238,534	240,671	266,199	222,498

Case study three: Clutha District Council

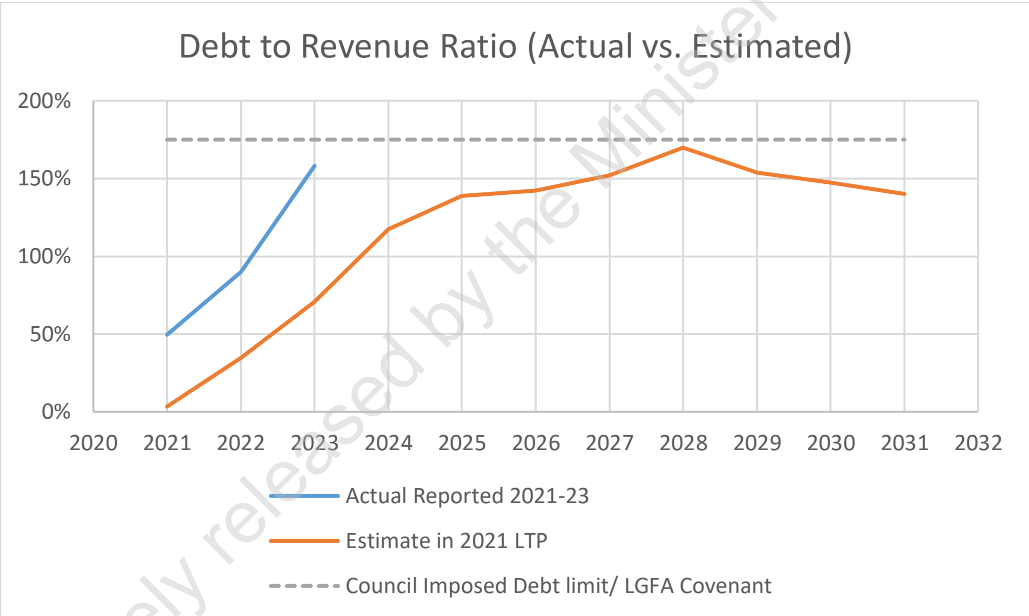
Clutha District Council is a small rural council serving a community of approximately 18,500 people spread over 6,334km^2. The population is sparsely distributed across 9 main population centres and surrounding small communities. As a result, Clutha has one of the longest networks of pipelines in New Zealand by council area, comprising of 22 supplies (10 urban and 12 rural) and 11 wastewater schemes.

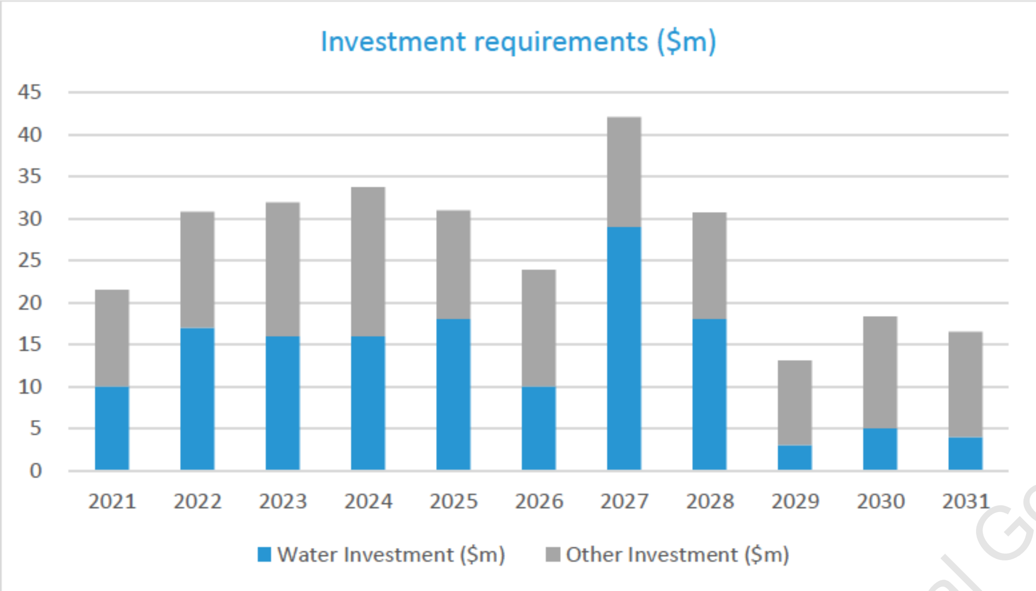
In the 2021 LTP the Clutha District Council outlined its need for infrastructure investment. 5 of the 10 infrastructure projects outlined were water infrastructure projects covering upgrade, replacement, and growth of water infrastructure.

In the 2023 Annual Report the council reported a 229% increase in water rates fees, and charges over the LTP estimate. The council has faced workforce shortages causing an overreliance on contractors. This is in addition to increased costs due to inflation, increased interest rates and increased cost of construction. The establishment of Taumata Arowai and the release of the Drinking Water Standards also poses a cost to the non-compliant councils.

In addition to significant rates rises, Clutha has had to increase its debt significantly beyond forecast levels over the last two years in order to fund water services.

Supporting Data





Clutha District LTP Estimate Costs vs. Actual Reported

Estimates vs Actual Reported	Ann Plan	Ann Report	LTP	Ann Report	LTP	Ann Report	LTP
($000)	2021	2021	2022	2022	2023	2023	2024
Funding Water	11,756	13,948	12,887	13,028	14,545	12,604	15,187
Funding Other	31,688	41,436	32,809	35,001	32,690	38,381	33,332
Opex Water	(8,035)	(14,266)	(8,295)	(9327)	(8,703)	(12,806)	(9,096)
Opex Other	(33,264)	(36,861)	(44,570)	(38,702)	(39,080)	(38,179)	(39,605)
Capex Water	(10,341)	(7,072)	(17,114)	(10,356)	(15,790)	(20,589)	(19,789)
Capex Other	(11,524)	(15,548)	(13,792)	(10,292)	(15,902)	(12,581)	(17,758)
Debt to Revenue Ratio	3%	50%	35%	90%	71%	158%	118%
Total Debt	28,017	31,027	45,180	47,251	60,480	87,693	81,080
Total Revenue	43,444	55,382	45696	48,029	47235	50,985	48519

Clutha District estimates included in 2021-31 LTP

Forward Estimates based on LTPs	Ann Plan	LTP	LTP	LTP	LTP	LTP	LTP	LTP	LTP	LTP	LTP
($000)	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031
Funding Water	11,756	12,887	14,545	15,187	15,486	17,924	34,223	19,279	17,951	18,448	19,006
Funding Other	31,688	32,809	32,690	33,332	36,193	37,924	37,806	38,169	38,058	39,219	39,562
Opex Water	(8,035)	(8,295)	(8,703)	(9,096)	(9,521)	(9,956)	(10,262)	(10,394)	(10,770)	(11,054)	(11,274)
Opex Other	(33,264)	(44,570)	(39,080)	(39,605)	(41,261)	(42,189)	(44,169)	(44,966)	(45,575)	(47,239)	(76,018)
Capex Water	(10,341)	(17,114)	(15,790)	(19,789)	(17,992)	(10,608)	(29,191)	(17,999)	(3,329)	(4,501)	(4,733)
Capex Other	(11,524)	(13,792)	(15,902)	(17,758)	(12,935)	(13,877)	(13,095)	(12,742)	(10,133)	(13,381)	(12,529)
Debt to Revenue Ratio	3%	35%	71%	118%	139%	142%	152%	170%	154%	148%	140%
Total Debt	28,017	45,180	60,480	81,080	93,580	97,580	103,880	113,880	108,880	107,880	105,880
Total Interest Cost	697	689	1,057	1,416	1,747	1,912	2,015	2,178	2,228	2,168	2,138
Total Revenue	43,444	45,696	47,235	48,519	51,679	55,848	72,029	57,448	56,009	57,667	58,568

Annex Three: Comparison of water demand management tools

Council	Types of water management tools						
	Water meters	**Charging (volume & excess)**	**Active Leak reduction/ detection**	**Information for the public / Engagement**	**Pressure Management**	**Water Restrictions**	**Rebates on a rainwater tank, financial incentives**
Auckland Council (Watercare) [56]	Yes	Yes - Volume		Yes		Yes	
Kāpiti Coast District Council	Yes	Yes - Volume	Yes	Yes	Yes		Yes
Palmerston North City Council [57]	Yes		Yes* (limited)	Yes	Yes		
Carterton District Council [58]	Yes	Yes – Excess	Yes			Yes	
Tauranga City Council [59]	Yes			Yes		Yes	Yes
Greater Wellington Regional Council	Yes	Yes – Volume	Yes	Yes	Yes		
Christchurch City Council [60]	Yes	Yes – Excess (more than 900L a day)		Yes		Yes	
New Plymouth District Council [61]	Not yet – district-wide rollout initiated.	Fixed charge (paid via rates)	yes			Yes - to be reviewed post meter rollout	

This table is indicative of how councils across New Zealand are utilizing different water management tools. This does not mean that councils are not using other methods in some way; it's just that those other methods are not as prominent.

[56] Watercare (2024), *Water meters*, https://www.watercare.co.nz/Water-and-wastewater/Water-meters

[57] Palmerston North City Council (2016), *Water Conservation Management Plan*, https://www.pncc.govt.nz/files/assets/public/v/2/documents/council/plans/water-conservation-management-plan-2016.pdf

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[59] Tauranga City Council (no date), *Te hinonga tiaki wai Tauranga: The Tauranga Water Conservation Project*, https://www.tauranga.govt.nz/council/water-services/the-tauranga-water-conservation-project

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