UTILITIES IN THE ROAD – COMPLETING THE JIGSAW

NEW ZEALAND UTILITIES CONFERENCE
22-23 APRIL 2002

Effect of the Local Government Bill and Local Government (Rating) Act on Utility Networks

Peter Winder, Chief Executive
Local Government New Zealand

Slide 1

INTRODUCTION

My job today is to talk to you about the hot issues emerging from the review of the Local Government (Rating) Powers Act (2002) and the review of the Local Government Act. I have my hard hat, flak jacket and entrenching tool.

As you are probably aware, Local Government New Zealand represents the interests of our 86 district, city, unitary, and regional councils. Our mandate is to secure national policies and legislation that support effective local governance, and to help local government get better at doing its job.

The Local Government (Rating) Act and the Local Government Bill (2001) will fundamentally change the basis of local government. My task today is to try and explain how that change may impact on utility networks.

Local Government Bill

Slide 2

First, I want to talk about the Local Government Bill.

We are enjoying a particularly good and strong relationship with the current government. The most visible manifestation of that relationship is the convening of biannual, "central – local government" fora, at which the mutual interests of both parties may be addressed. This relationship recognises that many of the key issues facing our community today cannot, and will not, be resolved without the engagement of local government.

The Local Government Bill empowers local government "to get engaged".

This Bill, and its ensuing implementation, is the next logical step in modernising local government. The process of modernisation began in 1989 with structural reforms, was refined in 1996 with the addition of financial and accountability provisions, and was further refined just last month, with the adoption of the Local Government (Rating) Act. The Local Government Bill (hopefully – to be adopted before the House rises) completes the "form, function, funding" reform package.

Modern local government needs to be responsive to its communities, inclusive in its style, and accountable in its delivery. The Bill provides the foundation for achieving that.

Power of General Competence

The new Bill proposes that local government be granted a "Power of General Competence". This is usually defined as something along the lines of "the

freedom to undertake any action or make any decision which is not specifically excluded by law or central government".

This Power of General Competence is a stark contrast from the current Act under which all councils are only allowed to do those things which are prescribed and provided for. The current Act is therefore long, cumbersome and bureaucratic. It has constrained the ability of councils to respond quickly to the rapid changes taking place in our communities.

As you can imagine the granting of a Power of General Competence to local government is not an idea that has been embraced by everybody. As one member of parliament noted at the Local Government Conference held in 2001, "to give local bodies more powers is foolish in the extreme."

I would suggest that the Power of General Competence outlined in the Bill is less a case of the Government giving local government extra powers, than it is of legislation catching up with practice.

Slide 3

The empowerment of local government will be limited by the general law, the provisions of other Acts, and the specific wording of the proposed Local Government Act itself. In this sense the powers that local government are about to be granted are not "general" at all.

A long established principle of law holds that specific legislation overrides general legislation. This will continue to apply. Where local government has been prescribed a particular role, for example under the Telecommunications Act or the Resource Management Act, local government will be limited to the functions specified therein.

In addition the principle of *ultra vires* will continue to apply. A council will not be able to do anything that is contrary to the purpose of local government, as defined in the Bill.

Slide 4 – Major Elements

Moreover, local government will be subject to rigorous community accountability provisions – some would say, far too rigorous. These include requirements to:

- make substantially greater use of the special consultative procedure;
- prepare a long-term council community plan;
- review all by-laws after five years, and to consider alternatives to by-laws before they are adopted;
- apply new policies before engaging in private/public partnerships;
- apply new and more rigorous reporting and accountability provisions to council-controlled organisations;
- register strategic assets and follow defined procedures before non-council options for delivery are adopted; and
- many other provisions.

Accountability is unquestionably important, but we do have some questions about the compliance costs likely to be faced in meeting them. We need to ensure that any trade-offs between the cost of local government and the need for enhanced accountability, are appropriate for the communities that must pay for them.

Slide 5 – Direct Impact

<u>Provisions of Local Government with direct effect on Utility Companies</u>

And while I'm on the subject of the Local Government Bill, it is appropriate that I should also comment on the aspects of the Bill that may affect utilities directly.

First up, you should note that the accountability requirements that have been suggested for local government will also be applied to council-controlled trusts and other organisations - including local authority controlled energy companies.

Second, council-controlled organisations will not be able to operate outside the boundary of their parent councils, district or region.

Third, changes will be made to the role of the directors appointed to those organisations with the effect that those directors will not know to whom they are accountable – the local authority or the council-controlled organisation.

The Bill also includes a requirement that councils shall make an assessment of water, wastewater, and sanitary services. A literal reading of the new provisions suggests that extensive analysis will need to be carried out. The cost of making assessments and reporting will markedly increase the cost of installations.

More importantly the Bill suggests that local government shall be restricted from "exiting" from the delivery of water and wastewater services. This provision limits the ability of councils to make strategic decisions about the way in which water and wastewater services might be delivered in the future.

While agreeing with the desirability of public ownership of strategic assets like potable water reticulation services, we are concerned that councils may be restricted in their ability to use private sector expertise and experience in the management of these services.

We have suggested amendments to the Bill to overcome these concerns.

Opportunity for Collaboration

Perhaps the most significant instrument provided for within the Local Government Bill is the long term council community plan (LTCCP). This plan will define:

- measurable community outcomes and priorities;
- the council's role in furthering these outcomes;
- how the council will work with other organisations (including suppliers, of utility network services) to achieve these outcomes;
- the funding policy that will be adopted to prudently manage the achievement of these outcomes.

The LTCCP thus provides a very good basis for achieving collaboration and partnership between a local authority and utility network suppliers to meet community outcomes.

Slide 6

VALUATION AND RATING OF UTILITIES

I now want to turn to the Local Government (Rating) Powers Act.

The Editorial in last Tuesday's Dominion indicated that not everybody is enthralled about the idea of councils rating utility networks.

Rates are a tax. Tax systems, as noted by the Court of Appeal, must be applied equitably. Local government intends to be very fair in the way it collects rates.

But there are legitimate questions that utility network companies may ask, and I want to address each of these in turn:

- are utility networks rateable property?
- will the new Rating Powers Act change things?
- how should utility networks be valued?
- are rates a charge for services?
- do utility networks benefit from council services?
- do local authorities have a choice – to rate or not rate?

Slide 7

Are Utility Networks Rateable Property?

With the exception of Auckland City, as a general practice, utilities, until this year, did not appear on valuation rolls. However, the Court of Appeal decision in *Telecom vs Auckland City Council (1998)* made it clear that utilities are rateable property. The Valuer-General therefore really had no alternative other than to instruct councils to have them valued. Councils that fail to value utilities will not have their rolls certified.

Before a property can be rated there are three specific tests that must be satisfied. In order, these are:

- the property has to be “land” (as defined in the Rating Powers Act)
- the property must be a “separate property”
- the property must be rateable.

Land is defined in the Rating Powers Act as “*all land, tenements, and hereditaments, whether corporeal or incorporeal and all chattels, and other interests therein…*”

The key part of this definition is the phrase “*and other interests therein.*” The Court of Appeal has held that the owners of gas, phone and telecommunications networks do have an “interest in land”.

A “separate property” is a more ethereal concept. There is no definition of separate property in any of: the Rating Powers Act, the (now repealed) Valuation of Land Act, or the Rating Valuations Act 1998. There is some guidance in sections 7 and 8 of the Valuation of Land Act but there is a large amount of discretion for the Valuer-General in deciding what is and isn’t a separate property.

Not surprisingly there has been litigation on this point, including one case that is currently under appeal to the Privy Council – a case involving ourselves and the Valuer-General.

The Valuer-General has said, in effect, that the primary determinant of what a separate property is, should be the existence of separate title. He has also said that property, without separate title, could be a separate property if there is some other instrument or interest that confers the right to sell on the holder of that instrument or interest – and this is how a distribution network qualifies.

Our view is that in many cases separate occupation is sufficient to create a separate property. We have a hearing scheduled for July and do not expect a decision much before September.

As for rateability, a property is rateable unless the first schedule of the Rating Powers Act says otherwise. The only exemption noted in that schedule that has even a remote bearing is the so-called “machinery” exemption.

The Court of Appeal has ruled in each of the Telecom, Auckland Gas and Hutt Valley Power cases that the machinery exemption does not apply to utilities. In each case, the Court has held that the word machinery was used in its popular or ordinary sense and did not cover transmission lines, mains or pipes. And in the case of telecommunications, the Telecommunications Act itself draws a clear distinction between lines and machinery.

Slide 8

Will the new Local Government (Rating) Act Change things?

How will the new Local Government (Rating) Act change things when it comes into force on 1 July next year? The short answer is, utility operators will still be rateable and (if anything) the law has been amended to provide even more clarity as to how utilities should be treated.

The Act contains amendments to the Rating Valuations Act which create something called a "rating unit". This is the equivalent of a "separate property".

The definition of rating unit has two parts – one for land where there is a certificate of title, and one for land without a certificate of title.

Land without a certificate of title can qualify as a rating unit if it has one or more of the following characteristics:

- it can be separately defined

- it can be sold

- there is no larger or prior interest in the land.

To us, it seems reasonably clear cut that utilities meet the first two of these criteria. They probably also meet the third. If I can be slightly cheeky here for a moment, many of you here today, who are representatives of utility network companies, must also share this view, or you wouldn't have put the effort into lobbying for an exemption.

How should utility networks be valued?

And now to turn to the actual valuation of networks. I know that the Valuer-General and representatives from utility operators and local authorities have put effort into developing a set of principles and a methodology for valuing utility networks.

But, as Stephen Parker from the Gas Association has clearly pointed out to me, the task is not yet complete. The New Zealand Utilities Advisory Group have proposed an initiative that will complete the task. John Hutchings will tell you more about that tomorrow.

Slide 9

Are Rates a Charge for Services?

Some commentators argue that rates are a charge for services. That may be true of things such as water by meter, and to a certain extent - for separate service rates, but it is not true for general rates. General rate are most definitely a tax. Even the previous Treasurer acknowledged that simple fact!

Legally speaking, the primary recent authority on rates as a tax is the Court of Appeal decision in *Woolworth and Others* vs *Wellington City Council (1996).* In the unanimous decision of the Court, Richardson P said

> *"There is force in Mr Barton's submission for the Local Government Association that it is implicit in the scheme of the legislation that a rating*

> *system, in its diversity, remains primarily a taxation system and not a system inherently based on a principle of user pays."*

Sir Ivor Richardson went on to say that the Courts should only be willing to intervene and invalidate local authority rating decisions in cases where the Council has taken irrelevant matters into account or failed to take relevant matters into account, or where the final decision is so unreasonable that no reasonable local authority could have contemplated it. In Sir Ivor's words

> *"There comes a point where public policies are so significant and appropriate for weighing, by those elected for communities for that purpose, that the courts should defer to their decision except in clear and extreme cases."*

This is not to say that the law allows for open slather on rating. Far from it. The benchmark for "unreasonable" (in the legal sense) is the Court of Appeal decision in *ECNZ* vs *Mackenzie District Council.* Here the council was rating on undifferentiated capital value. Various dams in the district had just become rateable. The Court held that the council's decision to treat the dams as if they were just another ratepayer was unreasonable.

The Court, in this case, appears to have been swayed by two factors. First, the value of the dams was such that the amount of rates collected from ECNZ would have amounted to 75 percent of the total rating revenue for that district. Second, the Council had made no plans for spending the money.

These are pretty unique circumstances and, by and large, it is unlikely that the average local utility network will not come anywhere near those circumstances. For the most part the average network is going to struggle to demonstrate that it is a standout ratepayer in "legal" terms. Unless it can do so, no obligation for special treatment will exist.

Having said that, a local authority is obligated to approach any request that a utility company may make for differential treatment, with an open mind and to consider it with due process.

Slide 10

Do Utility Networks benefit from any Council Services?

Utilities do receive benefits from services provided by local authorities. The provision of the road system provides a corridor that you have access to. Services like planning and traffic control benefit you. Flood control works help provide you with protection systems. Utility networks may therefore also be subjected to separate rates:

- the road itself
- stormwater
- any activity that provides for the integrity of the corridor

Slide 11

Do Local Authorities have a Choice?

Another myth doing the rounds is that local authorities somehow have a choice in what they rate. Once a property appears on a valuation roll as a separately rateable property local authorities **have** to rate the property.

Local authority discretion, as far as remitting rates goes, either in whole or in part, is limited to a narrowly defined set of circumstances. Utilities currently will generally not qualify for these.

This situation will change, come 1 July next year, when local authorities will be given powers to remit rates, more or less, as they and their communities see fit. The process will go like this: first, Councils will have to prepare a remissions policy. Second, this policy will need to explain what categories of property will qualify for remission and why. Third, this will have to be adopted through the special consultative procedure.

In other words, those utility companies who want to argue for a remission will not only have to convince the local authority, but also the local community.

While local authorities don't currently have a choice whether or not to rate a phone line or a gas pipe, they do have a choice in terms of "how" utilities get rated. A local authority that wants to give a utility company rates relief can adopt a differential "in favour" of that utility company.

The process established in law requires local authorities to consult on decisions to adopt, amend or disestablish a differential rating system. Currently this may be undertaken through the special order process. Come 1 July 2003 this may be achieved through the annual planning process. Again it's not just the members of the Council that have to be convinced.

We recently conducted an email survey of our members on how they plan to rate utilities. About half of New Zealand's councils use a capital value system for rating. Within this group of councils, we found two dominant approaches:

- those councils that do <u>not</u> have differentials are, for the most part, likely to treat utilities as an any other property;

- those councils that do have differentials are generally considering treating utilities as a commercial property.

A handful of other councils are considering giving utilities a differential in their favour.

It seems to me that the approaches of all the local authorities who responded to our survey will be defensible before a Court, given the nature of the legal test that a Court will apply.

You also need to be aware that regional councils do not currently have the powers to make a differential on their general rate. This means that once you're on the

regional roll you get rated in the same way as everyone else . This will change on 1 July next year when regional councils will get the same powers as territorials.

Another misconception that seems to be floating around is that 42 councils with land value rating systems cannot rate utilities. Strictly speaking this is not true. Utilities are liable for rates made on any of the land value, capital value, or annual value system. However there is a legal precedent that holds that a utility does not have an unimproved value – so any rates made on unimproved values will always be zero.

However, utilities will be liable for any uniform annual general charge that a territorial local authority may levy. This is a flat charge on all separate properties regardless of value.

The point I want to leave you with is that local authorities have no choice other than to put utilities on their roll, and once on the roll - to rate them.

CONCLUSION

The legislative environment governing the form, function and funding of local government has been significantly amended.

Local government will soon have a statutory framework that will allow each council to reflect the diversity of New Zealand's communities. This means that councils will be in a better position to respond to their community's needs and to

work collaboratively with central government agencies, utility network companies and others, to achieve positive outcomes for those communities.

As noted by Basil Morrison this morning, we have a shared responsibility to provide our communities with the best possible access to utility services – at least cost. The Local Government Act will certainly contribute to that objective. The Local Government (Rating) Act will also play its part – by providing a more equitable framework, for local revenue collection. But I am sure there are some in this audience who remain to be convinced of that.

THANK YOU