Revenue and Financing Policy

Background

The Revenue and Financing Policy is a requirement of the Local Government Act 2002. The policy is supported by analysis of the funding of each activity group and recognises that the funding policy is more than just a device for raising revenue but is also one of the instruments that can be used to promote community wellbeing.

Under S102(2) of the Local Government Act 2002, a local authority must, to provide "predictability and certainty about sources and levels of funding" adopt certain policies. The Revenue and Financing Policy is one of these. The policy is supported by analysis of the funding of each activity group and recognises that the funding policy is more than just a device for raising revenue but is also one of the instruments that can be used to promote community wellbeing.

Funding needs analysis

The Revenue and Financing Policy must demonstrate how Council has complied with the funding policy process under section 101(3) of the Local Government Act 2002. To achieve this, Council needs to review each individual activity and its funding in developing its Revenue and Financing Policy.

As part of that process, Council needs to consider the nature of the activity provided and the benefits and beneficiaries of the activity.

Activity group

Council's work has been grouped into nine key activities in which we provide a service to the community. These are:

- District Strategy and Governance – a new activity group compared to the Long Term Plan 2015-25, that provides transparency regarding performance and expenditure of strategy and governance for Council
- Transportation
- Water
- Wastewater and Drainage
- Stormwater
- Flood Control
- Solid Waste Management
- District Planning and Regulatory Services
- Community Facilities and Services.

The activity groups are listed in the attachment.

Activity

Each activity group is made up of operating projects – 'activities' – that the Council delivers as services. Any one activity may have one or more operating projects which, when combined, provides the total level of service provided by the Council. The activities, within the activity groups, are listed in the attachment.

Step one

When assessing the funding for each activity the following need to be considered:

Community Outcomes

Which Community Outcome the activity primarily relates to and the rationale for doing it. The Council's vision is:

A vibrant, attractive and thriving district.

Community Outcomes:

- Efficient and resilient core services:
  - it is easy and safe to travel around the district for everyone
  - there are opportunities to walk and cycle
  - the District is well prepared for growth and can adapt to change
  - services are supplied in ways that benefit the environment.
- Positive about the future:
  - our district has productive land, people and a thriving city centre
  - there is a fair urban/rural balance
  - Council has clear, simple documents and rules
  - our District embraces new technology and opportunity.
- Caring for the environment:
  - communities work to keep the environment clean and healthy
  - access to the coast is protected
  - open spaces in parks and streets, are places where nature thrives
  - our District is positively adapting to climate change.
- Proud to be local:
  - our district is neat, tidy and looks attractive.
  - public areas feel and are safe
  - there is always something to do and see
  - there are opportunities for people of all abilities, ages and life stages to be active.

User/beneficiary pays principle – distribution of benefits between individuals or groups and the community i.e. private or public good principle.

Inter-generational principle – the period over which the benefits are expected to accrue.

Exacerbator pays principle – the extent to which actions or inactions of individuals or groups contribute to the need to undertake the activity and the costs that occur as a result.

Costs and benefits of funding the activity – distinct from other activities. i.e. user pays or targeted rates.

Step two

Consideration then needs to be given to the overall impact of any allocation of liability for revenue needs on the community. This may result in an alteration of the results of the first step, with the funding option or the level of funding from any source altered to ensure that there are no barriers or disincentives and that an inequitable burden is not placed on any particular community sector or group.

Some questions to ponder as part of this consideration are:

- how will the mix of funding impact on affordability, e.g. on the elderly or those on low incomes?
- will the policy impact on accessibility to some services?
- can we charge the amount required, or is it restricted by legislation?
- do we want to encourage or discourage a particular activity or behaviour?
- what is the effect on a particular sector of our community, community groups or rating categories?
- how will this impact based on current economic conditions?

Funding sources

Section 103 of the Local Government Act (2002) requires a local authority to state the sources of funding for its operating expenses and its capital expenditure. The sources of funding for each category are set out below.

Funding Sources for Operating Expenses

Operating expenses are for the day-to-day spending by Council delivering ongoing services and for the maintenance of Council's assets. This includes contributions to the wear and tear on assets used (depreciation), interest charged on borrowing for capital projects and corporate overheads.

Council must consider the funding for each activity in a way that relates exclusively to that activity. Some activities may be best funded using user charges, others with targeted rates and others from general rates. Distinct funding enables ratepayers or payers of user charges to assess more readily whether the cost of the service provided to them either directly or indirectly represents good value. They can also more easily determine how much money is being raised for the service and spent on the service, which promotes transparency and accountability.

The different mechanisms available for funding operating expenses are:

General rates are used to fund those services where there is a benefit to the whole community (public benefit) or where there is no practical method for charging individual users. General rates fund a range of activities which are used by individual ratepayers to varying extents.

Rates are regarded as a tax, as there is no direct link between the activity or service provided and the individual ratepayer.

To maintain as simple rating as possible this Council currently uses general rates to fund a broad range of activities, rather than a number of targeted rates. This makes it easier for ratepayers to understand how they are being rated and it is more cost effective to administer.

General rates are currently assessed based on a property's land value and as a uniform annual general charge.

Value-based general rates are assessed on land value and are differentiated by land use.
The differentials to be applied are:

- residential differential, including remissions for high value properties
- rural differential
- multi-unit differential
- commercial and industrial differential
- miscellaneous properties

Full details of the differentials used may be found in the Funding Impact Statement.

A uniform annual general charge (UAGC) is applied to each separately used or inhabited part of each rating unit (SUIP). The UAGC is to be assessed by Council annually and set at a level considered to be reasonable. The UAGC is used to fund the same activities as the general rate and ensures every ratepayer contributes a base level of rates irrespective of property value or services used.

Targeted rates are used where an activity benefits an easily identifiable group of ratepayers (such as the commercial or residential sectors) and where it is appropriate that only this group be targeted to pay for some or all of a particular service. The funds collected are used for the purpose for which they are rated. Targeted rates are only used where Council considers it is an appropriate mechanism to fund that activity or where Council wishes to make clear the purpose for which the rate is collected. The revenue collected in any one year may result in a surplus, which is used to repay debt or to fund capital expenditure in future.

User fees and charges are used where the beneficiaries can be identified and charged. They include consent fees, licence fees, sales of goods, hire fees or recoveries of costs incurred. When setting fees and charges, Council will consider any indirect benefit to the community, the distribution of those benefits and ability to pay. Some fees may be limited by legislation, meaning full recovery of costs is not possible.

Grants and subsidies apply to some activities when income from external agencies is received to support that activity. Each year the Council receives funding from NZTA as part of the overall roading programme for the city's roading infrastructure. Operational subsidies fund maintenance, of roading infrastructure. Council recognises the funding as income in accordance with GAAP.

Borrowing is not generally used to fund operating expenses, but is used to smooth the inter-generational benefits of the capital expenditure programme. Council may use borrowing to give a capital grant to a community organisation to fund a community facility, or for addressing storm damage (see below).

Interest from investments is used to reduce the requirement from general revenue and is used to fund activities in the same way that rates do.

Distributions and dividends

- Council receives distributions from its joint venture investment in Northland Regional Landfill Limited Liability Partnership. These are directed to reduce the requirement from general revenue and is used to fund activities in the same way that rates do.
- Council currently receives dividends from LGFA which are used to reduce the requirement from general revenue and is used to fund activities in the same way that rates do. Any other dividends would be treated in the same way.

Rental income is generated from Council's various property types:

- from Council's pensioner housing is used to fund the expenses of operating and maintaining Council's pensioner housing stock. It can also be used to fund capital expenditure on pensioner housing. Pensioner housing is a ringfenced activity so if pensioner rental property income is not fully spent in a given year then it will be reserved and carried forward to the next year.
- from Council's investment properties is used to ensure the overall portfolio is maintained in terms of ongoing purchasing power and any excess income is used to initially fund the District Strategy and Governance Group and if there is any residual funds after this then these are used to reduce the requirement from general revenue and is used to fund activities in the same way that rates do.
- from Council's community properties used to fund the expenses of operating and maintaining Council's community properties and any excess income is used to fund Council's other community operating expenses.

Enforcement fees are charged where possible. They are used to promote compliance rather than to raise revenue and may not recover the full cost depending on the level of compliance and the extent to which charges are limited by statute or the court. Any excess income from enforcement fees is used to reduce the requirement from general revenue and is used to fund activities in the same way that rates do.

Other sources of operating expense funding

Council also funds operating expenditure from other sources including:

Reserves:

- *Other reserves and ring-fenced funds*
  Restricted funds or special funds including the property reinvestment reserve, are those reserves within Council's equity that are subject to special conditions of use, whether under statute or accepted as binding by Council, that may not be revised without reference to the courts or a third party.

  Subject to meeting any specified conditions associated with these reserves Council may expend money, of an operating or capital nature, from these reserves.

- *Specific reserving of operational funding*
  Where expenditure has been funded in a year for a specified purpose e.g. a grant to fund an external groups project and because of timing issues the conditions of the grant are not met in that year then the grant can be reserved at the end of the year to provide funding for the project in a future year once the conditions are met.

- *Reserving and use of general surpluses from previous financial periods*
  Where Council has recorded an actual surplus in one financial period it may pass this benefit on to ratepayers in a subsequent financial period.

  A surplus arises from the actual recognition of additional income or through savings in expenditure when compared to the annual plan for a given year. A surplus would only be finalised once the Annual Report for the year was adopted and it is the net surplus that needs to be considered.

  Council considers that passing this benefit on to ratepayers in future financial periods improves the principle of intergenerational equity, in that any financial benefit is passed on to those ratepayers who shared the rates-funding burden in the financial period that the surplus was generated.

  The amount of any surplus carried forward from previous financial periods will be reserved on the balance sheet and used to offset the operating deficit created by the expenditure to be funded by the surplus in the year the benefit is passed on to ratepayers.

  Only those factors that are operating in nature and cash in nature will be available for use in determining the level of surplus to be carried forward. Council will not carry forward surpluses in relation to:

  - The sale of assets. Such surpluses shall be used for either the repayment of borrowings or in the case of investment properties transfer to the property reinvestment reserve.
  - Trust and bequest revenue. Such surpluses shall be applied in accordance with the terms on which they are provided.
  - Revenue received for capital purposes. Such surpluses shall be retained to fund the associated capital expenditure.
  - Revenue received from targeted rates such as water and wastewater.
  - Depreciation.
  - Development and lump sum contributions.
  - Unspent budgeted operating expenditure associated with a capital project that is being carried forward.

- Unrealised gains arising from fair value adjustments to assets and liabilities. These gains are unrealised accounting adjustments in the period in which they are recognised.
- Vested or found assets.

Trusts and bequests

Council is the recipient/holder of several trusts and bequests. These funds can only be used for the express purposes for which they were provided to Council. Each year, Council may expend money, of an operating or capital nature, from its trusts and bequests in accordance with the specified conditions of those funds. For the avoidance of doubt, Council does not fund the expenditure from its trusts and bequests from any of the sources of operating revenue.

If Council receives bequests in the future, then it will treat those in the same manner.

Overheads

There are some activities within council that provide support to specific cost centres or to the entire council but do not provide a direct benefit to the community. The costs of these activities are treated as overheads and are reallocated against activities that do provide a direct benefit to the community.

This concept is particularly important when analysing the costs of delivering services and arriving at the appropriate fees and charges for those services.

Storm damage

If because of storm damage, infrastructure assets need repair, an option for funding this (so as not to impact on the capital works programme for the year), is utilising debt, if there is projected headroom under the net core debt cap for the year. If it is determined that there is no headroom under the net core debt cap, then council will look to defer operational and capital expenditure planned in the year to accommodate funding the repairs and renewals required.

Funding Sources of Capital Expenditure

For the purpose of this Policy capital expenditure represents expenditure on:

- property, plant and equipment,
- intangible assets, and
- property.

Property, plant and equipment are tangible assets that are held by Council for use in the provision of its goods and services (for example: infrastructure assets such as land, roads, bridges, parks, water treatment plants and non-infrastructure assets such as computer hardware and libraries), or for rental to others, or for administrative purposes.

Intangible assets are assets such as software that Council purchases or creates as part of a project with an economic benefit longer than a year.

Property includes Council's pensioner housing, Council's investment properties and Council's community properties. It can also include property purchased for strategic reasons, for instance where a future road is planned to be constructed.

As described in the Financial Strategy 2018-28, Council while managing its existing assets, also has a challenge to manage growth, affordable rates increases and debt and deliver as many of the communities desired projects as possible. To achieve the appropriate balance between these variables Council takes the following approach:

- Council sets the annual rates requirement
- the activity operating cash revenue and expenditure budgets are determined, within this constraint
- the net cash operating costs are determined
- this leaves a cash surplus that is available for capital costs. This largely represents rate funded depreciation but may include operating surpluses from some activities and accounting provisions not held in reserve funds – this is funding not held by activity and available to fund any capital costs
- Council also sets the limit on debt, which determines the debt funding available for capital expenditure.

Consequently, despite the potential availability of the funding sources, this process results in the following funding available for capital costs:

General rates

General rates may be used to fund a portion of capital expenditure when it is considered appropriate to do so. This will be balanced against affordability for current ratepayers and the current and future needs of the community.

Targeted rates

Targeted rates are used to fund operating expenditure but can be used to fund a particular capital project benefiting a discrete and identifiable group of beneficiary ratepayers.

User contributions are typically paid in the form of a targeted rate by an identified group of direct beneficiaries. In many cases this group would have lobbied for the inclusion of the project during a consultation process.

Borrowing

This is an appropriate funding mechanism to enable the effect of peaks and troughs in capital expenditure to be smoothed and to ensure the costs of major developments are borne by those who ultimately benefit from the expenditure. It is not appropriate or sustainable for all capital expenditure to be funded from borrowings. In periods of low capital expenditure, borrowing will be reduced.

Proceeds from property sales

These will be invested in the property reinvestment reserve and the funds may be used to purchase other commercial properties in future. Any funds in the reserve may be used to fund capital expenditure in other activities to smooth Council’s overall cashflow requirements.

Proceeds from other asset sales

These may be used to fund capital works or to repay debt.

Depreciation

Depreciation is an indirect source of funding as depreciation reserves are not created. However, rates are set at a level that offsets the calculated non-cash depreciation cost. Operating surpluses (where available) are then used to fund renewal capital expenditure.

Development and financial contributions are used to fund the growth component of capital expenditure. The growth in our District drives a portion of our capital work requirement to maintain Levels of Service to a larger community. As the costs of growth are driven by development, Council considers it equitable that a development should contribute to the costs that are being imposed.

Council has a development contributions policy which sets out the level of contributions required to fund infrastructure requirements.

Financial contributions will be used to fund capital expenditure in accordance with the Resource Management Act 1991.

Grants and subsidies are used when they are available. NZTA provide capital subsidies (accounted for as operating revenue) to fund agreed roading capital projects. This funding source also includes other contributions for various capital projects.

Reserves including retained earnings from operating surpluses from previous years may be used to fund capital expenditure. Reserves for specific activities such as Water can be created.

The below table shows the primary funding sources for the different types of capital expenditure and each of the activity groups.

By expenditure type:	General rates*	Targeted rates*	Borrowings	Development Contributions	Subsidies and Grants	Reserves	Property sales
Renewals		✓	✓		✓	✓	
Level of service		✓	✓		✓	✓	
Growth			✓	✓	✓	✓	
By activity group:							
Transportation	✓		✓	✓	✓		
Water		✓	✓	✓		✓	
Wastewater		✓	✓	✓	✓	✓	
Solid Waste		✓	✓			✓	
Stormwater	✓						
Community Facilities and services	✓		✓	✓		✓	
Flood Protection		✓					
Corporate/property/other	✓		✓			✓	✓

*General and targeted rates create cash surpluses by funding depreciation, which is non-cash. These surpluses are then used to fund for renewal projects.

Review of funding sources and the funding bands

Having decided on:

- the activity groups
- activities within the activity groups.

Using the steps above, the funding sources and the funding bands from each source have been assessed for each activity to provide guidance for the Long Term Plan 2018-28. Suggested funding bands are set out in the attachment.

Attachment

Activity Funding Analysis

(to be read as part of the Policy) [LTPREP-647166279-348]

		Operational Expenditure Funding Sources					
Activity Group 18-28	**Activity / dept**	**User Fees**	**Subsidies and Grants**	**Other**	**Rental Income**	**Targeted Rates**	**General Rates**
District Strategy & Governance	Iwi Liaison						100%
	Strategy & Governance						100%
	Economic growth - District Development						100%
	Economic growth - Property *			100%	100%		
	Economic growth - Marina Facilities				100%		
	Economic growth - Airport Facilities						100%
Transportation	Roading Network		25-50%	0-10%			50-75%
	Car Parking	80 -100%			0-20%		
	Footpaths						100%
Water	Water	0-5%				95-100%	
Waste and Drainage	Wastewater	5-20%		0-10%		80 -100%	
	Public Toilets						100%
Stormwater	Stormwater						100%
Flood Control	Flood Control (Hikurangi Swamp)				0-10%	90-100%	
Solid waste management	Rubbish/Recycling Collection and Disposal	0-50%		0-10%		50-100%	
	Litter Control	0-5%					95-100%
District Planning and Regulatory Services	Resource Consents	30-50%					50-70%
	RMA Compliance	30-55%					45-70%
	Building Consents	70-90%					10-30%
	Building and Environmental Monitoring						100%
	Food	40-60%					40-60%
	Health	0-15%					85-100%
	Alcohol licensing	90-100%					0-10%
	District Plan Development	0-20%					80-100%
	Noise Management						100%
	Animal Management	55-75%		15-30%			5-30%
	Parking Enforcement			100%			
	Warrant of Fitness Enforcement	100%					

	Swimming Pool inspections	100%					
	Bylaws						100%
Community Facilities and Services	Sport and Recreation Facilities	0-10%					90-100%
	Parks Reserves and Natural Areas						100%
	Play areas, walking Trails, Coastal						100%
	Cemeteries and Crematorium	35-55%					45-65%
	Libraries	5-12%					85-95%
	Pensioner Housing				75-90%		10-25%
	Community Safety						100%
	Community Development, Community buildings & spaces and Residential Strategic property				70-90%		10-30%
	Community Funding		0-5%	5-20%			75-95%
	Venues and Events	5-20%		5-20%			60-90%
	Village Planning						100%
	Civil Defence						100%
	Visitor Information Services	5-20%		25-40%			40-70%
	Customer Services	0-5%					95-100%

* Investment property generates surplus revenue after allowing for investment property operating expenses. This investment property surplus is used to fund the Strategy & Governance Activity, and any residual surplus if any is used to fund overall operating expenses like general rates.

Note Support Services is not shown as a separate activity because the costs of running Support Services which provides support to the organisation are allocated over the activities and departments delivering WDC’s external services.