

**QLDC Council
20 August 2020**

Report for Agenda Item | Rīpoata moto e Rāraki take 1

Department: Property & Infrastructure

Title | Taitara Memorandum of Understanding with the Crown on Three Waters Delivery Reform Programme

PURPOSE OF THE REPORT | TE TAKE MŌ TE PŪRONGO

- 1 The purpose of this report is to sign a Memorandum of Understanding (MoU) with the Crown, agreeing to participate in the initial stage of a central/local government three waters service delivery reform programme (**Appendix A**); and
- 2 Authorise the Chief Executive to enter into the Funding Agreement, to accept a grant from the Crown to spend on operating and/or capital expenditure relating to three waters infrastructure and service delivery (**Appendix B**).

EXECUTIVE SUMMARY | WHAKARĀPOPOTOTANGA MATUA

- 3 In July 2020, the Government announced a \$761 million funding package to provide post COVID-19 stimulus to maintain and improve three waters infrastructure, support a three-year programme of reform of local government water service delivery arrangements (reform programme), and support the establishment of Taumata Arowai, the new Water Services Regulator.
- 4 A Joint Central/Local Government Three Waters Steering Committee has been established to provide oversight and guidance to support progress towards reform, and to assist in engaging with local government, iwi/Māori, and other water sector stakeholders on options and proposals.
- 5 The reform programme is designed to support economic recovery, and address persistent systemic issues facing the three waters sector, through a combination of:
 - stimulating investment, to assist economic recovery through job creation, and maintain investment in water infrastructure renewals and maintenance; and
 - reforming current water service delivery, into larger scale providers, to realise significant economic, public health, environmental, and other benefits over the medium to long term.
- 6 Initial funding from the stimulus package will be made available to those councils that agree to participate in the first stage of the reform programme, through a Memorandum of Understanding (MoU), Funding Agreement, and approved Delivery Plan. The MoU must be signed by the end of August 2020, with the Funding Agreement and Delivery Plan submitted and approved by the end of September 2020.

RECOMMENDATION | NGĀ TŪTOHUNGA

7 That Council:

1. **Note** that:
 - a. in July 2020, the Government announced an initial funding package of \$761 million to provide a post COVID-19 stimulus to maintain and improve water networks infrastructure, and to support a three-year programme of reform of local government water services delivery arrangements; and
 - b. initial funding will be made available to those councils that agree to participate in the initial stage of the reform programme, through a Memorandum of Understanding (MoU), Funding Agreement, and approved Delivery Plan.
 - c. this initial funding will be provided in two parts: a direct allocation to individual territorial authorities, and a regional allocation. The participating individual authorities in each region will need to agree an approach to distributing the regional allocation.
 - d. the Steering Committee has recommended a preferred approach to the allocation of regional funding, being the same formula as was used to determine the direct allocations to territorial authorities.
2. **Agree** to sign the MoU at **Appendix A** and Funding Agreement at **Appendix B**.
3. **Agree** to nominate the Chief Executive of the Council as the primary point of communication for the purposes of the MoU and reform programme – as referred to on page 6 of the MoU.
4. **Agree** to delegate decisions about the allocation of regional funding to the Chief Executive of the Council, with the understanding that the minimum level of funding to the Council be based upon the formula used to calculate the direct council allocations, and noting that participation by two-thirds of territorial authorities within the Otago region is required to access the regional allocation.
5. **Note** that the MoU and Funding Agreement cannot be amended or modified by either party, and doing so would void these documents.
6. **Note** that participation in this initial stage is to be undertaken in good faith, but this is a non-binding approach, and the Council can opt out of the reform process at the end of the term of the agreement (as provided for on page 5 of the MoU).
7. **Note** that the Delivery Plan must show that the funding is to be applied to operating and/or capital expenditure relating to three waters infrastructure and service delivery, and which:
 - a. supports economic recovery through job creation; and
 - b. maintains, increases, and/or accelerates investment in core water infrastructure renewal and maintenance.

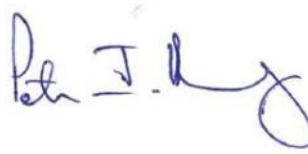
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13/08/2020

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17/08/2020

CONTEXT | HOROPAKI

Issues facing the three waters system, and rationale for reform

- 8 Over the past three years, central and local government have been considering the issues and opportunities facing the system for regulating and managing the three waters (drinking water, wastewater, and stormwater).
- 9 The Government Inquiry into Havelock North Drinking Water – set up following the serious campylobacter outbreak in 2016 – identified widespread, systemic failure of suppliers to meet the standards required for the safe supply of drinking water to the public. It made a number of urgent and longer-term recommendations to address these significant systemic and regulatory failures.
- 10 The Government’s Three Waters Review highlighted that, in many parts of the country, communities cannot be confident that drinking water is safe, or that good environmental outcomes are being achieved. This work also raised concerns about the regulation, sustainability, capacity and capability of a system with a large number of localised providers, many of which are funded by relatively small populations.
- 11 The local government sector’s own work has highlighted similar issues. For example, in 2014, LGNZ identified an information gap relating to three waters infrastructure. A 2015 position paper, argued for a refresh of the regulatory framework to ensure delivery of quality drinking water and wastewater services, and outlined what stronger performance in the three waters sector would look like.
- 12 Both central and local government acknowledge that there are many challenges facing the delivery of water services and infrastructure, and the communities that fund and rely on these services. These challenges include:
 - Underinvestment in three waters infrastructure in parts of the country, and substantial infrastructure deficits. For example, it is estimated that between \$300 to \$570 million is required nationally to upgrade networked drinking water treatment plants to meet drinking water standards; and up to \$4 billion is required to upgrade wastewater plants to meet new consent requirements. These deficits are likely to be underestimates, given the variable quality of asset management data.
 - Persistent funding and affordability challenges, particularly for communities with small rating bases, or high-growth areas that have reached their prudential borrowing limits.
 - Additional investment required to increase public confidence in the safety of drinking water, improve freshwater outcomes, and as a critical component of a collective response to climate change and increasing resilience of local communities.
- 13 COVID-19 has made the situation even more challenging. Prior to COVID-19, territorial authorities were planning on spending \$8.3 billion in capital over the next five years on water infrastructure. However, COVID-19 is likely to cause significant decreases in revenue in the short term. As a result, borrowing will be constrained due to lower debt limits that flow from lower revenues, and opportunities to raise revenue through rates, fees and charges will be limited.

Progress with three waters regulatory reforms

14 Good progress is already being made to address the regulatory issues that were raised by the Havelock North Inquiry and Three Waters Review. The Government is implementing a package of reforms to the three waters regulatory system, which are designed to:

- improve national-level leadership, oversight, and support relating to the three waters – through the creation of Taumata Arowai, a new, dedicated Water Services Regulator;
- significantly strengthen compliance, monitoring, and enforcement relating to drinking water regulation;
- manage risks to drinking water safety and ensure sources of drinking water are protected;
- improve the environmental performance and transparency of wastewater and stormwater networks.

15 Taumata Arowai is currently being built, and will become responsible for drinking water regulation once a separate Water Services Bill is passed (anticipated mid 2021).

16 However, both central and local government acknowledge that regulatory reforms alone will not be sufficient to address many of the persistent issues facing the three waters system. Reforms to service delivery and funding arrangements also need to be explored.

Proposal – central/local government three waters reform programme

Overview of proposed approach to three waters investment and service delivery reform

17 At the recent Central/Local Government Forum, central and local government leadership discussed the challenges facing New Zealand’s water service delivery and infrastructure, and committed to working jointly on reform. A Joint Central/Local Government Three Waters Steering Committee has been established to provide oversight and guidance to support this work. [Further details are provided in Appendix D.]

18 Central and local government consider it is timely to apply targeted infrastructure stimulus investment to enable improvements to water service delivery, progress service delivery reform in partnership, and ensure the period of economic recovery following COVID-19 supports a transition to a productive, sustainable economy.

19 In July 2020, the Government announced an initial funding package of \$761 million to provide post COVID-19 stimulus, support a three-year programme of reform of local government water service delivery arrangements, and support the establishment and operation of Taumata Arowai.

20 The reform programme is designed to support economic recovery, and address persistent systemic issues facing the three waters sector, through a combination of:

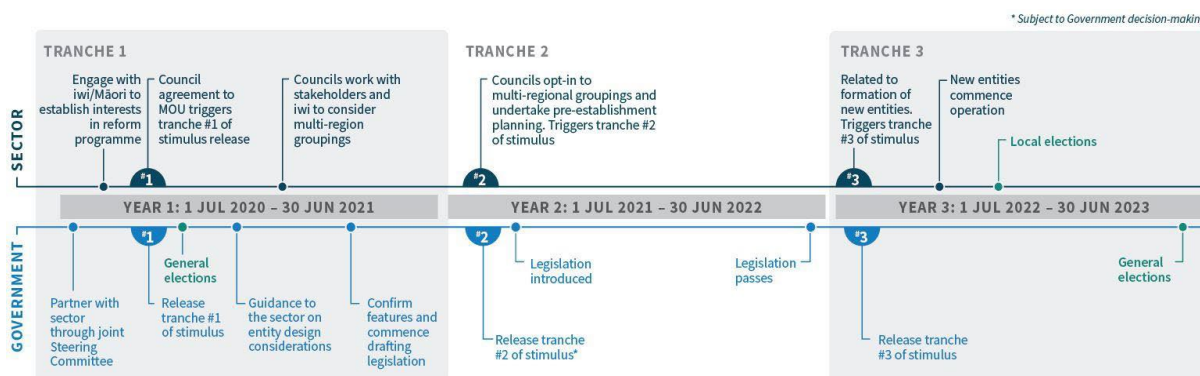
- stimulating investment, to assist economic recovery through job creation, and maintain investment in water infrastructure renewals and maintenance; and

- reforming current water service delivery, into larger scale providers, to realise significant economic, public health, environmental, and other benefits over the medium to long term.

- While the Government’s starting intention is for publicly-owned multi-regional models for water service delivery (with a preference for local authority ownership), final decisions on a service delivery model will be informed by discussion with the local government sector and the work of the Joint Steering Committee.
- Further information on the reform objectives, and the core design features of any new service delivery model, are provided in pages 3 to 4 of the MoU at Appendix A.

Reform process and indicative timetable

- As noted above, this is a three-year programme to reform three waters service delivery arrangements, which is being delivered in conjunction with an economic stimulus package of Crown investment in water infrastructure. The reform programme will be undertaken in stages.
- The initial stage is an opt in, non-binding approach, which involves councils taking the actions and signing the documents described below (MoU, Funding Agreement, and Delivery Plan).
- Councils that agree to opt in by the end of August 2020 will receive a share of the initial funding package, and this is the purpose of this report.
- Any further tranches of funding will be at the discretion of the Government and may depend on progress against reform objectives.
- An indicative timetable for the full reform programme is provided below. While this is subject to change as the reforms progress, and subject to future Government budget decisions, it provides an overview of the longer-term reform pathway.



Allocation of the investment package

- The Government has determined a notional allocation framework based on a nationally-consistent formula.

- 29 The general approach to determining each authority's notional allocation is based on a formula that gives weight to two main factors:
1. The population in the relevant council area, as a proxy for the number of water connections serviced by a territorial authority (75 per cent weighting)
 2. The land area covered by a local authority excluding national parks, as a proxy for the higher costs per connection of providing water services in areas with low population density (25 per cent weighting).
- 30 The investment package is structured into two components:
1. A direct allocation to each territorial authority, comprising 50% of that territorial authority's notional allocation; and
 2. A regional allocation, comprising the sum of the remaining 50% of the notional allocations for each territorial authority in the relevant region
- 31 The allocations relevant to Queenstown Lakes District are:
- \$4.74m (excluding GST) direct allocation for Queenstown Lakes District Council; and
 - \$20.60m (excluding GST) regional allocation for Otago
- 32 The purpose of the Government's regional allocation is to establish collective participation by councils in the reform programme. Each regional group of councils has until 30 September to agree on how best to apportion the regional funds to the individual territorial authorities that make up the region.
- 33 The Steering Committee has recommended a preferred approach to the allocation of regional funding, being the same formula that is used to determine the direct allocations to territorial authorities.
- 34 Officers recommend delegating decisions about the allocation of regional funding to the Chief Executive of the Council, with the understanding that the minimum level of funding to the Council be based upon the formula used to calculate the direct council allocations, and noting that participation by two-thirds of territorial authorities within the Otago region is required to access the regional allocation. In the Otago context this has already been the subject of an initial discussion between the Mayors and Chief Executives last week.

What actions are the Council being asked to take at this point?

- 35 The initial stage of the reform programme involves three core elements:
1. Memorandum of Understanding (Appendix A);
 2. Funding Agreement (Appendix B);
 3. Delivery Plan (Appendix C).
- 36 Initial funding will be made available to those councils that sign the MoU, and associated Funding Agreement, and provide a Delivery Plan.

- 37 This initial funding will be provided in two components: a direct allocation to individual councils, and a regional allocation. The participating councils in each region are required to agree an approach to distributing the regional allocation.
- 38 The MoU is the 'opt in' to the first stage of the reform and stimulus programme. The MoU needs to be signed and submitted by the end of August 2020. The Funding Agreement and Delivery Plan need to be submitted by the end of September 2020, to access the stimulus funding,
- 39 Councils that do not opt in by the end August 2020 deadline will not receive a share of the stimulus funding. Councils will still be able to opt in to the reform programme at a later date, but will not have access to the initial funding package, retrospectively.

Memorandum of Understanding

- 40 A MoU has been developed by the Steering Group, for each council to enter into with the Crown. This is a standardised document, which cannot be amended or modified by either party.
- 41 Signing the MoU commits councils to:
- engage in the first stage of the reform programme – including a willingness to accept the reform objectives and the core design features set out in the MoU;
 - the principles of working together with central government and the Steering Committee;
 - work with neighbouring councils to consider the creation of multi-regional entities; and
 - share information and analysis on their three waters assets and service delivery arrangements.
- 42 At this point, this is a voluntary, non-binding commitment. It **does not** require councils to commit to future phases of the reform programme, to transfer their assets and/or liabilities, or establish new water entities.
- 43 The MoU is effective from the date of agreement until 30 June 2021, unless terminated by agreement or by replacement with another document relating to the reform programme.
- 44 A legal opinion by Simpson Grierson, commissioned by SOLGM on behalf of the Steering Committee, advises that the MoU **does not** contain any explicit triggers for consultation under the Local Government Act 2002.
- 45 At this point Clutha District have agreed to sign the MOU, and Dunedin and Central Otago District will be considering the issue on 25 and 26 August respectively. (For the purpose of the funding Waitaki District is considered to be part of Canterbury).

Funding Agreement

- 46 QLDC has been allocated \$4.74m by the Crown, if it opts into the reform programme. A further \$20.6m has been allocated to the Otago region to agree an appropriate distribution between participating Councils. This funding will be provided as a grant, which does not need to be repaid if the Council does not ultimately commit to reform at later stages of the process.
- 47 There are several options for how the regional funding could be allocated between councils. The joint central-local government Three Waters Steering Committee preferred approach is to apply the same formula¹ used to calculate the direct allocations. Under this approach, the Council would receive an additional \$4.74m contributing to a total funding allocation of \$9.48 [INDIVIDUAL AMOUNT of \$4.74m + SHARE OF REGIONAL AMOUNT of \$4.74m].
- 48 The Joint Mayors and Chief Executives have recently met to consider Otago's regional share and will further consider some jointly held regional funding to investigate future collaboration models under this programme both in Otago and in conjunction with our Southland partner Councils. The proposed position is to enable the Chief Executive to agree the regional allocation with the other participating Councils, on the basis that 10% of the regional value is used to specifically investigate regional collaboration, and the balance to be available to each Council on the present share allocation. Access to the regional share requires (in Otago's case) three of the four Councils to agree to the MoU. It should be noted that access to the funding package, like the MoU, is fixed, apart from how the local Councils choose to share the regional allocation. It should also be noted that prior to this funding, the Councils of Otago and Southland received some limited funding to investigate collaboration options, and this funding also remains.
- 49 The Funding Agreement guides the release and use of funding. It sets out:
- the funding amount allocated to the Council;
 - funding conditions;
 - public accountability requirements, including the Public Finance Act;
 - reporting milestones.
- 50 While there is some local flexibility around how the funding can be applied, the Government has indicated that this investment is intended to support economic recovery, enable improvements in water service delivery, and progress the service delivery reform programme.
- 51 The Funding Agreement will be supplemented by a Delivery Plan, which is the document that sets out how the grant funding is to be applied by the Council. It cannot be used to substitute existing commitment. If approved, staff will do further work to recommend to Council a preferred programme to expend this.

¹ Applying a 75% weighting for population and a 25% weighting for land area, excluding national parks.

Delivery Plan

- 52 The Delivery Plan is the other mechanism for accessing the funding package.
- 53 This Delivery Plan must show that the funding allocation is to be applied to operating and/or capital expenditure relating to three waters infrastructure and service delivery, and which:
- supports economic recovery through job creation; and
 - maintains, increases, and/or accelerates investment in core water infrastructure renewal and maintenance.
- 54 The Delivery Plan is a short-form template, which sets out:
- a summary of the works to be funded, including location, estimated associated costs, and expected benefits/outcomes;
 - the number of people to be employed in these works;
 - an assessment of how the works support the reform objectives in the MoU;
 - reporting obligations.
- 55 The Delivery Plan will be supplied to Crown Infrastructure Partners (and other organisations as agreed between the Council and Crown), for review and approval. Crown Infrastructure Partners will monitor progress against the Delivery Plan, to ensure spending has been undertaken with public sector financial management requirements.

CONSULTATION PROCESS | HĀTEPE MATAPAKI:

> SIGNIFICANCE AND ENGAGEMENT | TE WHAKAMAHI I KĀ WHAKAARO HIRAKA

- 56 A legal opinion by Simpson Grierson, commissioned by SOLGM on behalf of the Steering Committee, advises that the MoU **does not** contain any explicit triggers for consultation under the Local Government Act 2002.

RISK AND MITIGATIONS | NGĀ RARU TŪPONO ME NGĀ WHAKAMAURUTANGA

- 57 The approval of the recommended option will support the Council by allowing access to additional funding.
- 58 Note that participation in this initial stage is to be undertaken in good faith, but this is a non-binding approach, and the Council can opt out of the reform process at the end of the term of the agreement.

FINANCIAL IMPLICATIONS | NGĀ RITENGA Ā-PŪTEA

- 59 Agreeing to participate in this initial stage will provide council with additional funding of up to \$9.48m for delivering three waters service infrastructure.

COUNCIL EFFECTS AND VIEWS | NGĀ WHAKAAWEAWE ME NGĀ TIROHANGA A TE KAUNIHERA

60 The following Council policies, strategies and bylaws were considered: Not applicable.

LOCAL GOVERNMENT ACT 2002 PURPOSE PROVISIONS | TE WHAKATURETURE 2002 O TE KĀWANATAKA Ā-KĀIKA

61 The recommended option:

- Will help meet the current and future needs of communities for good-quality local infrastructure.
- Would not alter significantly the intended level of service provision for any significant activity undertaken by or on behalf of the Council, or transfer the ownership or control of a strategic asset to or from the Council.

ATTACHMENTS | NGĀ TĀPIRIHANGA

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| A | Memorandum of Understanding |
| B | Funding Agreement |
| C | Delivery Plan |
| D | Information on Joint Three Waters Steering Committee |