Report to:	**Council – Public Excluded**	
Date:	26 February 2025	
Subject:	Local Water Done Well – Options for the Future Delivery of Water Services	
Prepared by:	W Doughty – Chief Executive Officer	
Input sought from:		
Authorised by:	W Doughty – Chief Executive Officer	

1. PURPOSE

The purpose of this report is to provide information about options for the future delivery of water services to enable the Council to decide the options it wishes to consult the community on.

2. SUMMARY

The coalition government repealed legislation that had been established under the previous government and replaced it with new legislation enacting their Local Water Done Well policy. Although left to individual Councils to decide overall arrangements for service delivery, the new approach is that water services must operate more like an independent utility business and will be subject to strict economic, environmental and water quality regulation.

Under the new legislation, the Council is required to submit a Water Services Delivery Plan (WSDP) to the Department of Internal Affairs by 3 September 2025. The WSDP will outline the Council's intended approach to the delivery of water services and an implementation plan for how it will deliver those services over at least the next ten years.

Over the past few months, the Council has been engaging with the Hurunui District Council and the Waimakariri District Council investigating options for working together more closely regarding the delivery of water services, potentially including a joint water services council controlled organisation (WSCCO). Following advice from the Waimakariri District Council on their preferred position, the joint WSCCO explored in this paper relates to two councils (Kaikōura and Hurunui).

The three Councils have been working with Malcolm Alexander from YuleAlexander and Castalia to develop options including financial modelling and assessment. Castalia has prepared a report outlining and evaluating three possible legal structures for the delivery of water services. There are options as to how these may be implemented from an operational perspective.

The Council is required to consult the community about at least two possible options for the future delivery of water services. At present it is proposed that the consultation period will be 20 March to 23 April 2025 and that hearings would be held on 7 May (with 8 May as a reserve day).

3. RECOMMENDATION

It is recommended that the Council:

1. That the Council agrees to consult the community regarding the following options for the future delivery of water services:

   (a) **Option 2:** Providing water services through a jointly established water services council controlled organisation owned by the Kaikōura District Council and Hurunui District Council as shareholders (preferred option);

   (b) **Option 1A:** Remaining with the existing approach for delivering water services in house (enhanced and adjusted as required by legislation).

2. Notes that the Water Services Delivery Plan is required to cover water, wastewater and stormwater and it is currently envisaged that the proposed joint water services council controlled organisation would be responsible for all water, wastewater and stormwater services.

3. Notes that it is proposed that the consultation period will be 20 March to 23 April 2025 and that hearings would be held on 7 May (with 8 May as a reserve day) with Council final decision on a preferred option on the 28th May 2025.

4. Delegates the Chief Executive to determine the release of this public excluded report.

4. REASONS FOR RECOMMENDATION

Under section 61 of the Local Government (Water Services Preliminary Arrangements) Act 2024, when deciding whether or not to establish/join a water services council-controlled organisation (WSCCO) or a joint local government arrangement, the Council must consider at least:

- remaining with the existing approach for delivering water services (enhanced and adjusted status quo); and
- establishing or joining a Water Services Council Controlled Organisation (WSCCO) or a joint local government arrangement.

The Council may identify other options for delivering water services.

"Remaining with the existing approach for delivering water services" is assumed to refer to the situation where the Kaikōura District Council continues to own three waters assets, holds three waters debt and carries out most water activities in house.[1]

However, legislative requirements particularly those relating to the economic regulation of water services, mean that there will be significant change in some aspects of water services irrespective of which option is adopted. The current status quo is not an option under the new legislation.

Some reasons for selecting the establishment of a joint WSCCO as the preferred option include:

- Under all models considered the tariffs for consumers in Kaikōura District increase significantly from the current status quo due. However, from the work done to date a joint CCO with Hurunui District Council has the lowest tariffs for consumers, best outcome for future Council borrowing ability and is the most likely to provide KDC with safe, resilient, reliable, customer responsive water services at least cost over the longer term when evaluated against a number of criteria.
- A joint WSCCO would have independent directors appointed based on competence. Collectively they would be required to have a set of skills stipulated in legislation. The directors will be subject to obligations and liabilities under Part 4 of the Commerce Act.
- Establishing a WSCCO is in line with central government expectations regarding the Local Water Done Well programme. Having a WSCCO in place may make it easier to take advantage of future opportunities for working with others, including Hurunui District Council and Waimakariri District Council.
- This approach would also provide flexibility if the WSCCO decided to progress working more closely with other water organisations at a later date. This would be a matter for the board of the WSCCO to determine.
- Whilst being able to leverage off economies and efficiencies from size and scale, it is expected that each District will still only pay for the costs associated with their water services delivery (i.e. it is not expected that there would be cross-subsidisation of water activities between council).

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[1] Some specialist services are outsourced as well as maintenance. Additional services may be outsourced during periods when there is insufficient resource in house. This includes existing shared service arrangements with Waimakariri Council.

5. BACKGROUND

Under section 8 of the Local Government (Water Services Preliminary Arrangements) Act 2024, each territorial authority must prepare a financially sustainable Water Services Delivery Plan (WSDP), which ensures that drinking water quality standards are met. Two or more territorial authorities may prepare a joint WSDP. Any joint WSDP plan must cover water, wastewater and stormwater services. The plan is required to be submitted the Department of Internal Affairs for review and approval by 3 September 2025. (Appendix 2 provides an overview from the Department of Internal Affairs as of November 2024).

Malcolm Alexander from YuleAlexander and Castalia have been contracted to support the development of the WSDP including options development and assessment. In a report dated 10 February 2025, they identified and assessed the following options (refer Appendix 1):

- Option 1A - Remaining with the existing approach for delivering water services (enhanced and adjusted as required by legislation).
- Option 1B - Providing water services through a council controlled organisation for which the Kaikōura District Council is the sole shareholder, but the council controlled organisation owns the water assets, is liable for the water debt, and is responsible for water operations.
- Option 2- Providing water services through a joint local government council controlled organisation owned by the Kaikōura District Council and Hurunui District Council as shareholders. This shared CCO would Act as a unified entity, consolidating resources and operations to deliver services.

Initially, some of the options investigated by Castalia included joint arrangements involving the Waimakariri District Council and the Hurunui District Council. At this stage a joint Hurunui/Kaikōura arrangement which potentially retains some shared services with Waimakariri appears to be the most viable option. Hurunui District Council is open to discussions regarding a joint local government arrangement with the Kaikōura District Council.

It is recognised there are options in addition to those identified above. For example:

- Legislation permits a water organisation to be owned by a community trust.
- It would be possible for a joint WSCCO to contract out water services to the current providers. However, it would need to be able to demonstrate that this was the most cost effective way of providing the service.
- The Council could enter into discussions with other Councils regarding options for working more closely together. However, this would take time and there is limited time prior to the 3 September deadline. Not doing so at this time does not rule out the option of having conversations with others at some time in the future should it be in the interests of the communities concerned.

6. ECONOMIC REGULATION

Under recent legislation water services providers will be required to provide water services in a cost-effective and financially sustainable manner. An overview from the Commerce Commission with regard to economic regulation and water is included in Appendix 3.

Going forwards, it will be mandatory for finances relating to three waters to be fully ring-fenced. At present, Council finances relating to three waters are largely ring fenced. There are separate income and expenditure accounts for water, wastewater and stormwater. There are also separate development contributions accounts and the internal debt is separated out for water, wastewater and stormwater.

Having said that, if the Council were to continue to provide water services in house (whether directly or through a CCO), it may be necessary to review overhead allocation procedures and debt financing calculations to make it easier to demonstrate ring fencing.

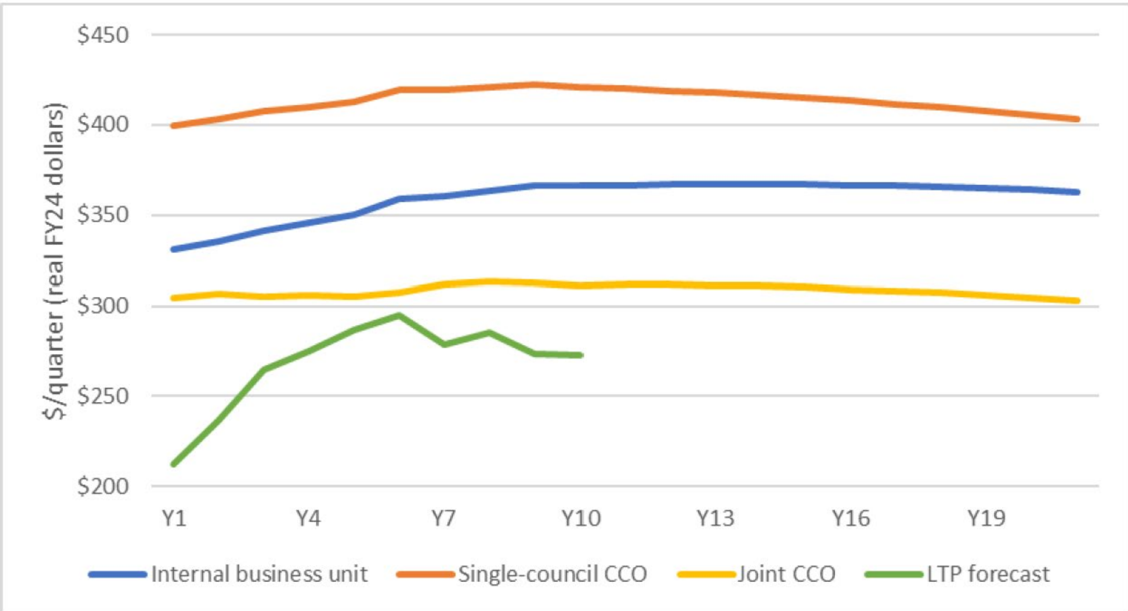
At this time, the Council does not fund depreciation on water related assets. This will not be permitted going forward. Clause 16(1)(b) of the Local Government (Water Services) Bill 2024 provides that a water service provider must ensure water services revenue is **"sufficient to sustain the provider's long-term investment in the provision of water services".**

It is likely that the water services provider (whether the Council directly or a water organisation) will be required to fully fund depreciation. Accordingly, irrespective of which option is implemented, there is likely to be a sharp increase in water services tariffs for consumers.

If the Council were to establish a joint WSCCO, there is a risk that water consumers may interpret the increase in water service tariffs to the establishment of the WSCCO, not realising that the increase would have occurred in the event that water services had remained in house. The Consultation Document will cover this matter. However, this remains a significant risk.

The significance of this matter is demonstrated by the following chart from the Castelia report, which shows projected quarterly tariffs for relativity. The green line shows the water tariffs based on the Long Term Plan. The other lines show the projected tariffs for an internal business unit (Option 1A), KDC WSCCO (Option 1B), and joint CCO (Option 2) – assuming depreciation is fully funded.

Figure 1.0: Kaikoura—modelled tariffs under different scenarios



It is expected that there will be costs associated with ensuring compliance with regulatory obligations. The Castelia report has assumed 1-3 FTE will be required per entity for this purpose, depending on which model is chosen.

7. WATER SERVICES DELIVERY OPTIONS

Option 1A - Remaining with the existing approach for delivering water services (enhanced and adjusted as required by legislation)

Under this option, the Council would continue to own the three waters assets and be responsible for the three waters debt. The Council would continue to provide services using its in house team. Some implications include:

- The Council would retain direct control of three waters services, and would be able to direct activities, providing it complies with all regulatory obligations.
- Having said that, its control over tariff setting would be greatly reduced. It is likely that tariffs would need to increase more rapidly than projected in the Long Term Plan 2024-2034 in order to demonstrate financial sustainability.
- The Council's three waters debt would remain on the Council's balance sheet. This is currently not an issue for Kaikōura District Council as water related debt is negligible. However, this could become a greater concern in the much longer term.
- There would be no direct impact on current employment arrangements. Additional resources or outsourcing would be required to meet all legislative requirements.
- As with all three options, it is likely there would be significant additional costs associated with meeting regulatory obligations.

Some risks/downsides associated with this option include:

- Because councillors would have direct control of water operations, there would be a risk of legal liability in the event of a breach of Part 4 of the Commerce Act 1986.
- There is a requirement to ensure ring fencing of three waters revenue and expenditure. It may be more difficult to demonstrate effective ring fencing arrangements for in house business units (e.g. regarding overhead allocations).
- This option does not provide the potential for cost savings and efficiencies provided by the joint WSCCO model.
- The coalition government has signalled it is seeking sectoral reform. If the recently established regulatory settings do not achieve the government's objects, then it is possible there could be further reforms focussed on increasing sectoral efficiencies.

Option 1B – Kaikōura District Council establishes a sole owned Water Services Council Controlled Organisation (WSCCO)

Under this option, the Kaikōura District Council would transfer the council's water assets and liabilities to the newly established WSCCO. The Council would establish the constitution for the new organisation and would be the sole shareholder. It would establish a Statement of Intent for the operation of the entity.

The operation of the WSCCO (including water services and financial management) would be the under the control of the board of the WSCCO. However, it would need to operate in accordance with the constitution, the Statement of Intent and the statutory framework.

The Local Government (Water Services) Bill 2024 which is currently before Parliament provides that elected members and Council staff are not eligible to be board members of a WSCCO.

- Because the Kaikōura District Council would be the sole shareholder, it would have more influence over the WSCCO than under the joint WSCCO option. However, the board would be directly responsible for the activities of the WSCCO.
- The Council may choose whether or not to collect revenue from water services users on behalf of the WSCCO.
- Under this option, the three waters debt would be transferred to the WSCCO. As identified with Option 1A this is currently not a significant benefit but could be in the much longer term

Risks/downsides under this approach could include:

- A key risk relates to "stranded overheads". Assuming the three waters operations currently carried out by the Kaikōura District Council were transferred to the wholly owned WSCCO, and that the WSCCO operated independently of Council, some existing overhead-type functions within Council would be under-utilised. While there are options, it is possible that there would need to be some reduction in the scale of these functions within the Council in the future.

- The implications for existing external service contracts including ongoing operations and maintenance would need to be considered.
- There would be additional costs associated with the establishment of the WSCCO, e.g. directors fees, which would need to be fully met by Kaikōura consumers (no opportunity to share establishment costs as per Option 2).
- While the attached analysis has assumed that the establishment of the WSCCO with an independent board would result in some efficiencies, because there is only one Council involved, there would be no change in purchasing power, and hence reduced opportunities for cost savings and efficiencies compared with Option 2.
- This option is not in line with the government's objects for sectoral reform. In the event of further sectoral reform, it is possible that further changes could be imposed on the Council.
- As with all government initiatives, there is the possibility that future governments could adopt a different approach. It would be appropriate to take this into consideration in establishing the WSCCO constitution.

Option 2 – Kaikōura District Council and Hurunui District Council form a new joint local government Water Services Council Controlled Organisation (WSCCS) which provides water services to both Kaikōura and the Hurunui district.

This approach would require the establishment of a new CCO and the two Councils would need to agree shareholdings and governance arrangements.

Some benefits of this approach may include:

- Under all models considered the tariffs for consumers in Kaikōura District increase significantly from the current status quo due. However, from the work done to date a joint CCO with Hurunui District Council has the lowest tariffs for consumers, best outcome for future Council borrowing ability and is the most likely to provide KDC with safe, resilient, reliable, customer responsive water services at least cost over the longer term when evaluated against a number of criteria.
- This approach more closely reflects central government's intent regarding the Local Water Done Well programme. This may prove advantageous in the event that central government progresses additional sectoral reforms.
- This approach would provide flexibility in the event that the WSCCO decided to progress working more closely with other water organisations. This would be a matter for the board of the WSCCO to determine.
- There could be benefits from joint purchasing. However, it is likely the benefits would be modest. More significantly, by forming a single WSCCO, rather than having two WSCCOs (one each for Kaikōura and Hurunui), it may be possible to achieve synergies regarding regulatory compliance as well as resilience in resourcing and service provision.

Risks/downsides include:

- As with Option 1B, it is possible there would be stranded overheads, and hence a potential for future changes within the Kaikōura District Council as well as our current service delivery contracts.
- While the Councils would retain some influence over the WSCCO through the establishment of the Constitution and the Statements of Intent, there would be less direct control than under Option 1A.
- It is possible that one or other of the shareholders could decide at a later date that they no longer wished to be part of the WSCCO. Accordingly, it would be prudent to establish a mechanism to cover this scenario should it arise.

- Given a number of Councils are likely to be establishing WSCCOs at the same time, and that Kaikōura and Hurunui are smaller councils situated some distance from urban centres, it may be difficult to attract suitably qualified independent board directors. This could impact the performance of the WSCCO.
- It would be important to ensure clarity regarding obligations and liability should an adverse event arise.
- As with all government initiatives, there is the possibility that future governments could adopt a different approach. It would be appropriate to take this into consideration in establishing the WSCCO constitution.

Other options
The Local Government (Water Services) Bill 2024 which is currently before Parliament provides for alternative options, including contracting out water services to a water organisation or ownership by a Community Trust.

8. CASTALIA EVALUATION
The Castalia report assessed Option 1A – Internal business unit, Option 1B – Single Council WSCCO and Option 2 – Joint WSCCO from the Kaikōura District Council perspective against a framework consisting of six elements or "parameters for success" towards achieving the ultimate objective of water reform:

Safe, resilient, reliable, customer-responsive waster services and least cost.

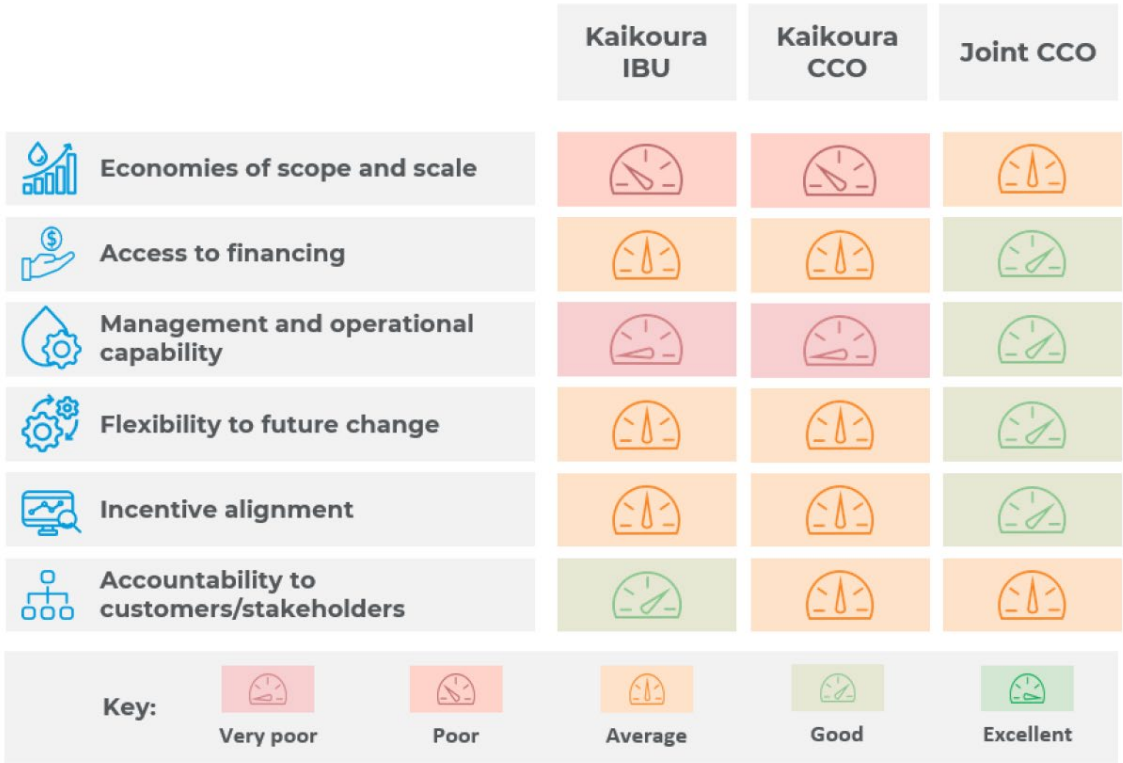
The six elements are shown in Figure 2.0 and explained in the report including how each parameter relates to achieving the overall objective.

Figure 2.0: Decision-making framework for evaluating water reform options

Source: Castalia, based on advice to LGNZ and DIA

The results of Castalia's evaluation for each option for Kaikōura District Council according to the framework are shown in Figure 3.0 below.

Figure 3.0: KDC evaluation results



9. CONSULTATION PROCESS

Under section 62 of the Local Government (Water Services) Act 2024, the Council is required to consult when making decisions in relation to a proposed model/arrangement for delivering water services in its WSDP. This includes a requirement to consult about any proposal to establish a water services council controlled organisation or to enter into joint local government arrangement for water services delivery.

Section 82A of the Local Government Act 2002 specifies that when a Council is consulting about a proposal under the Act, it must make publicly available an analysis of the "reasonably practicable options". By contrast, under section 61(2), the Council is only required to identify two options (including the existing approach to water services delivery), although it may identify additional options if it wishes. If the Council elects to apply section 61(2), then section 82A of the Local Government Act 2002 does not apply.

It is possible that a decision to change the model/arrangement for delivering water services could require a consequential modification to the Council's Long Term Plan (LTP). If this is the case, the Council would not be required to consult on a proposal to change the LTP provided that:

- It has already consulted the community about the water services delivery proposal;
- It is satisfied the community understands the implications of the proposal; and
- It is satisfied it understands the community's views about the proposal.

To enable sufficient time for the preparation of the WSDP prior to the September deadline, it is proposed to commence the consultation as soon as practicable. It is currently proposed that the key dates will be as follows:

Date	Milestone
19 March (Extraordinary Council Meeting)	Draft consultation document provided to Council for consideration
20 March	Commencement of the consultation period
24 March – 10 April	Public meetings
23 April	End of the consultation period
7 May and 8 May (reserve day)	Council hearing oral submissions
28 May	Council decision regarding preferred option

10. LEGAL AND POLICY IMPLICATIONS

Section 8 of the Local Government (Water Services Preliminary Arrangements) Act 2024 provides that:

"Each territorial authority must prepare a water services delivery plan that—

(a) identifies the current state of the authority's water services; and

(b) demonstrates publicly its commitment to deliver water services in a way that—

***(i)** ensures that the territorial authority will meet all relevant regulatory quality standards for its water services; and*

***(ii)** Is financially sustainable for the territorial authority; and*

(i) ensures that the territorial authority will meet all drinking water quality standards; and

(ii) supports the territorial authority's housing growth and urban development, as specified in the territorial authority's long-term plan.

Sections 60-64 of the Local Government (Water Services Preliminary Arrangements) Act 2024 set out some alternatives to the consultation provisions in the Local Government Act 2002 which may be applied regarding Local Water Done Well. Some consultation obligations in the Local Government Act 2002 continue to apply, including section 81 relating to consultation with Māori and section 82 regarding the principles for consultation.

The Local Government (Water Services) Bill 2024, which is currently before Parliament, sets out the framework for commercial regulation of water services providers.

11. DELEGATIONS

This decision is required to be made by Council.

12. FINANCIAL IMPLICATIONS

The Castalia report shows the projected tariffs for three waters services. These indicate that three waters tariffs are likely to increase markedly for all options due to environmental and economic regulation. Based on the assumptions in the report, the highest tariffs would be for the single Council CCO option, while the lowest tariffs would be for the joint WSCCO with Hurunui District Council option. There will be costs associated with the consultation process.

Requirement	Explanation
What is the cost?	Depending on the approach adopted, the consultation could cost around $10,000. There will also be staff costs associated with consultation processes.
Is this budgeted in the Long Term Plan or Annual Plan?	Yes
Where is the funding coming from?	It is expected that the consultation process will be funded from the transitional funding provided from the previous government.
Are there any future budget implications?	At a later stage there will be costs associated with the implementation of whichever option is progressed.

The Council is contributing to the cost of the work carried out by Malcolm Alexander and Castalia. Central government has contributed some of the costs of this work

13. SIGNIFICANCE AND ENGAGEMENT ASSESSMENT

Requirement	Explanation
Level of significance and rationale	The significance of this decision is considered to be high. The Significance and Engagement Policy identifies the water, wastewater and stormwater networks as a whole as being strategic assets.
Summary of engagement already undertaken	Although the Council has undertaken consultation regarding the previous central government's proposed "three waters reforms", this is the first time the Council will have consulted the community regarding the specific options currently under consideration.
What future engagement is required?	The requirements regarding consultation on water services delivery options are detailed in the Local Government (Water Services Preliminary Arrangements) Act 2024. Providing the Council complies with sections 61 to 64 of this Act, then it is not required to comply with the equivalent provisions in the Local Government Act 2002. However, it is still required to comply with other provisions in the Local Government Act.
Consideration of mana whenua?	This decision does not involve a significant decision in relation to ancestral land, a body of water or other elements of intrinsic value. The Council has informally discussed Local Water Done Well with Ngāti Kuri. The Council will seek further input from mana whenua during the consultation process.
Consideration of Local Government Wellbeings	The manner in which water services are delivered may potentially have an impact on all four local government wellbeings (social, economic, environmental and cultural). For example, the various options are likely to have differing set up and operational costs.

14. COMMUNITY OUTCOMES SUPPORTED

Community
We communicate, engage and inform our community

Environment
We value and protect our environment

Development
We promote and support the development of our economy

Services
Our services and infrastructure are cost effective, efficient and fit-for-purpose

Future
We work with our community and our partners to create a better place for future generations

Appendices
Appendix 1 - Report by Castalia
Appendix 2 – DIA Local Waters Done Well Update - November 2024
Appendix 3 – Commerce Commission Economic Regulation and Water – November 2024.

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Memo to Hurunui District Council and Kaikoura District Council on water reform options

10 February 2025

Executive Summary

Castalia is assisting Hurunui District Council (HDC), Kaikoura District Council (KDC) and Waimakariri District Council (WDC), (the North Canterbury councils) with modelling the financial implications of joint arrangements for councils' water services. This is part of the North Canterbury councils plan to prepare a Water Services Delivery Plan, as required by the Local Government (Water Services Preliminary Arrangements) Act 2024. Castalia completed financial modelling of several scenarios, including go-alone options and several joint delivery options.

Since submitting the financial analysis and an evaluation of each model, the three councils have had further discussions. It appears that WDC is unwilling to enter into a joint council-controlled organisation (CCO) or a management, operations and maintenance CCO owned by all three councils.

HDC and KDC are now exploring whether it is possible to work together to prepare a joint WSDP. HDC and KDC have asked Castalia to provide additional analysis of a two-council CCO, referred to as joint CCO, and compare this against their best go-alone option.

The key question for this memo is whether a joint CCO model is financially viable and will it provide HDC and KDC with safe, resilient, reliable, customer-responsive water services at least cost.

We recommend that HDC and KDC consider a joint CCO option

A joint CCO option has the lowest tariffs, best outcome for future council borrowing ability and best score on our evaluation matrix. Of the analysed options, a HDC-KDC water services CCO appears to be financially viable, and the most likely to provide HDC and KDC with safe, resilient, reliable, customer-responsive water services at least cost.

Tariffs are lowest under a joint CCO model, which appears financially sustainable

A joint water services CCO had the best financial modelling outcomes. The joint CCO would see each council contribute all water assets and it would raise financing independently of council. This provides the best outcome for each council's borrowing headroom.

Our financial modelling approach adopts a "no worse off" principle. This means that the customers in HDC and KDC's council areas only pay water tariffs that recover the costs of the services in those council areas. There is no cross subsidisation between councils. Nevertheless, because of greater borrowing capability in a CCO and the ability to save some money from a joint approach, the tariffs are lowest. The tariff results are set out in the two charts below:

Figure 0.1: Hurunui—modelled tariffs under different scenarios

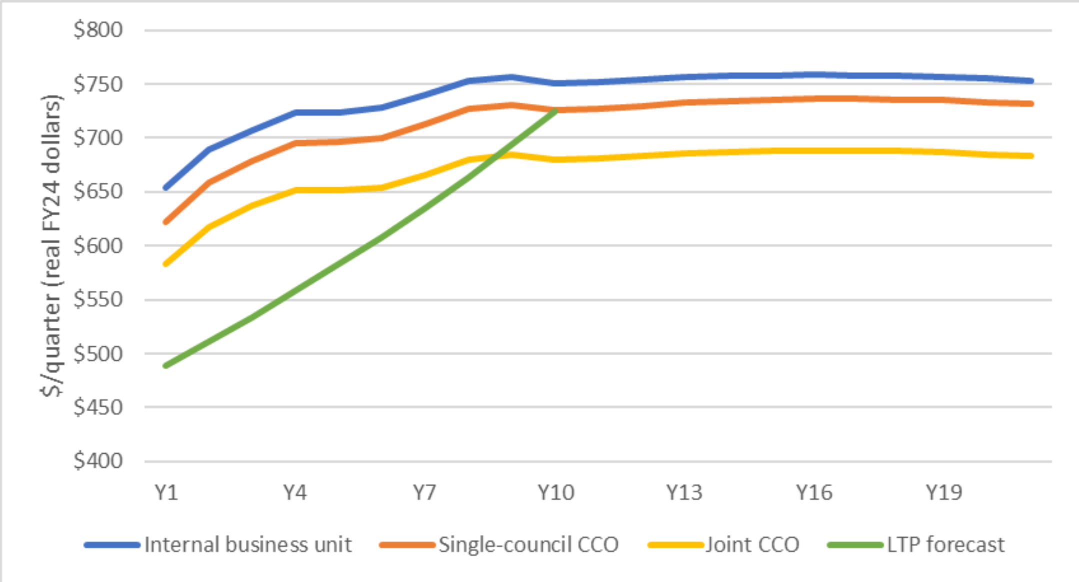
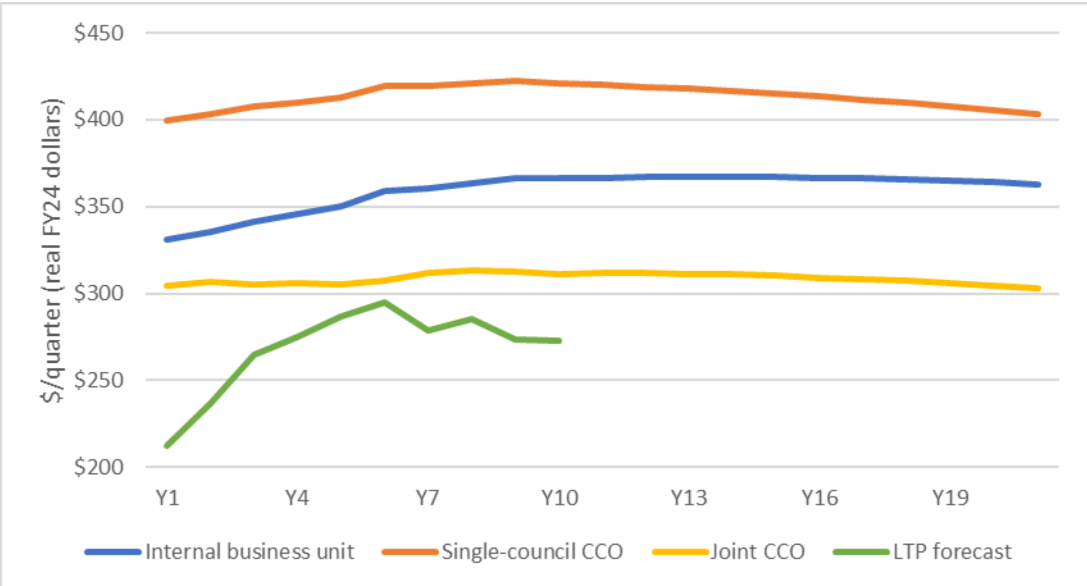


Figure 1.0: Kaikoura—modelled tariffs under different scenarios



Evaluation results suggest joint CCO model is best

Castalia's evaluation of the go-alone vs joint CCO options against six criteria used to assess water reform options suggests that a joint CCO is the best of the currently available options for HDC and KDC. A joint CCO leaves both councils flexible to future change: the CCO could accommodate additional councils (under the "no worse off principle"), or procure a third-party to manage, operate and maintain the water services under contract following a competitive tender process. The CCO is also more likely to ensure management and operational capability is maintained, which is critical for resilience. Overall, the joint CCO option is most likely to ensure that water services are safe, resilient, reliable, and customer responsive at least cost.

1 Introduction

Castalia has been appointed to evaluate short-listed options for water reform for HDC and KDC, since determining that a joint option with WDC may not be possible. This memo evaluates the two basic options of go-alone (either as an internal business unit or CCO) or a joint HDC-KDC CCO. This memo is structured as follows:

- Key assumptions for the two models for water services are set out in section 2
- Evaluation criteria for available options are explained in section 3
- Financial modelling results are in section 4
- Evaluation results are presented in section 5
- Finally, our conclusion and recommendations are set out in section 6.

2 Two options for water services

We set out the two options, and the key assumptions that underpin them in this section. The two high-level options for water service provision are:

- Go-alone option, either:
  - Internal business unit of council
  - Single-council CCO
- A joint CCO option, where both councils transfer their water and wastewater council functions into a water services CCO. The CCO will deliver water and wastewater services to the residents of both councils.

2.1 Go-alone options

The go-alone options for each council are either run water services as an internal business unit or incorporate a wholly-owned CCO.

2.1.1 Internal business unit

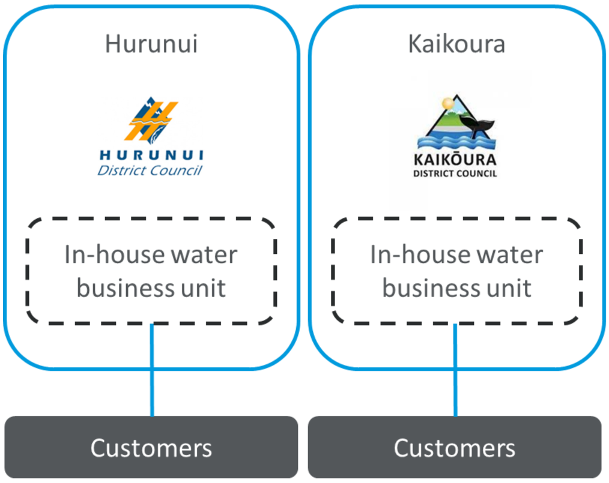
An internal water service business unit would be a department or operational team within the council that directly manages and delivers water services. It would have to be ringfenced, with separate accounts, revenues, and assets. This is the closest option to the status quo, as the councils all have some degree of ringfencing and separation already. In KDC's case, via the management contract with Innovative Waste Kaikoura Limited (IWK), which also provides waste management services.

Governance of the business would sit at the elected member level. This means elected members would be ultimately responsible for compliance with regulatory bottom lines. This includes potential liability for pecuniary penalties under Part 4 of the Commerce Act (subject to clarification in Local Government (Water Services) Bill).

Assets would be held on each council's balance sheet, and finance raised at the council level. This means borrowing for water investments would be constrained by the councils' ability to raise debt, and any relevant net debt-to-revenue covenants.

Figure 2.1 illustrates the structure of internal business units for each council.

Figure 2.1: Diagram of internal business units



Key assumptions about internal business unit

We make some assumptions about the additional costs of an internal business unit, compared to the status quo. This is because there will be additional regulatory compliance required under the Local Water Done Well legislation. Additional regulatory staff to ensure ring-fencing of activities and accurate reporting to Commerce Commission will be required. We assume 2 FTEs per council at a cost of $600,000 (including salary and overhead costs). We also assume there is a minor efficiency gain from regulation, compared to status quo of 0.20 percent.

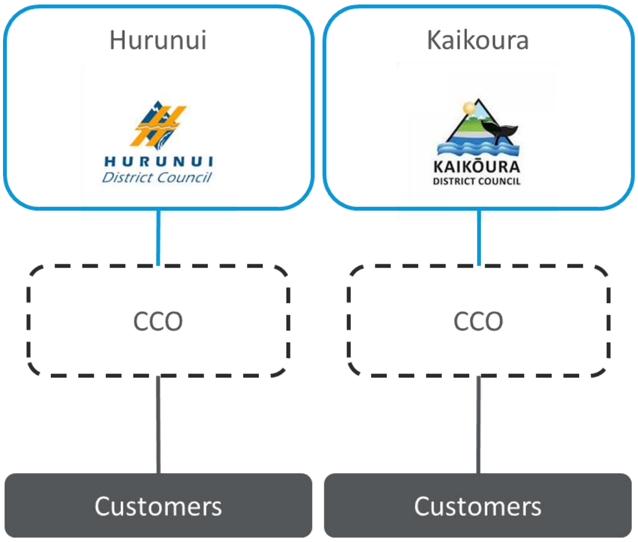
2.1.2 Single-council WSCCO

Under this option, each council would establish a wholly owned water services CCO. The CCO would manage, operate, and maintain the water infrastructure. It would hold the water assets on its balance sheet. Alternatively, a long-term lease of assets could be granted by the council (which retains ultimate ownership of assets) to the council-owned CCO.

The WSCCOs would be separate entities, with a board, and owned and controlled by their individual councils but operating with some degree of commercial independence. The councils would set performance expectations, which could be supplemented by management contracts to improve incentives and better define outcomes. However, the WSCCOs would have autonomy over day-to-day operations.

LGFA confirmed that it would consider a WSCCO with a board of majority independent directors eligible for its expanded lending programme (lending to WSCCOs at a net debt-to-revenue ratio of 500 percent). Figure 2.2 illustrates the structure of single-council WSCCOs for each council.

Figure 2.2: Diagram of single-council WSCCOs



Under the go-alone option each council will continue to deliver water services to residents in their council area. As set out in Castalia's earlier reports, and in advice from YuleAlexander Limited, this does not mean that the status quo operating model can continue. HDC and KDC will have to meet the requirements of current and future expected Local Water Done Well legislation—Local Government (Water Services Preliminary Arrangements) Act 2024 and Local Government (Water Services) Bill and future economic regulation.

Each council will also have to decide on the structure and operating model for their go alone business, either an internal business unit of council, a wholly-owned Water Services CCO (WSCCO), or some other model (for example, contracted out to a third party, or a council-owned CCO like IWK).

Key assumptions for single-council CCO

There are some additional costs with a single council CCO:

- Board members for CCO: We assume three board members, remunerated at $25,000 to $35,000 per annum would be required
- One-off set up costs are assumed to cover legal matters, any initial hiring costs, setting up systems and processes and any space leases. We assume councils' existing water sector staff and assets are transitioned and used to minimise costs:
  - HDC: $500,000
  - KDC: $300,000
- Additional regulatory staff are required: 1-2 FTEs per CCO which equates to $400,000 to $800,000 in additional costs (salary plus overheads)

There are also some expected efficiencies that should emerge from a single-council CCO, compared to internal business unit set out in the table below:

Table 2.1: Cost savings from efficiencies, compared to LTP forecasts

Factors	Efficiency savings type	Time period	Single-council CCO assumption
Capex cost efficiency	Fixed savings	Fully in force after 5 years	1.5%
Staff cost efficiency	Annual compound	Begins after 3 years	0.50%
Water operations cost efficiency	Fixed savings	Fully in force after 5 years	2%
Other overhead cost efficiency	Fixed savings	Fully in force after 5 years	2%

2.2 HDC-KDC joint CCO option

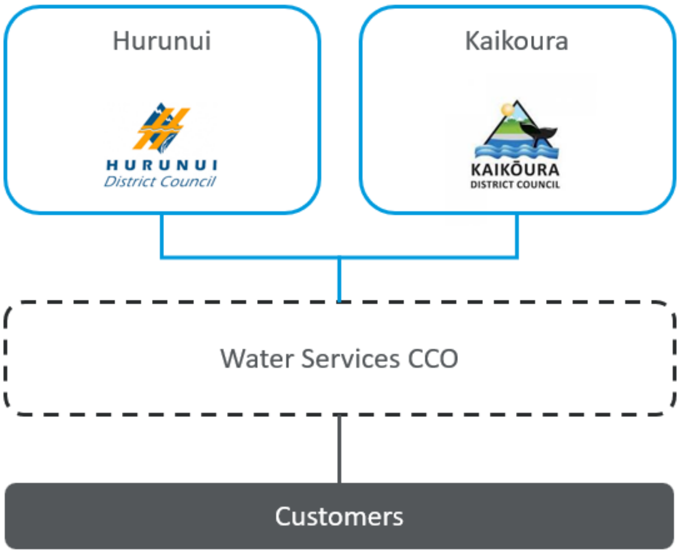
Under a joint model, the Hurunui and Kaikoura councils form a joint CCO and deliver water services to the residents of both councils. We have developed a joint-CCO option that is workable and financeable and ensures equity between HDC and KDC. The joint CCO option has the following design features:

- A newly incorporated company (CCO) with at least a majority of independent directors to qualify for LGFA financing
- Ordinary shareholding is in proportion to the net assets each council contributes
- Special voting shares could be used to determine voting rights on key matters (although this is not essential to the option design at this stage)
- All water-related assets would be transferred to the joint CCO (although a long-term lease is possible)
- All water-related debt would be transferred to the joint CCO
- For the purposes of billing, the joint CCO will record the value of assets in each council in separate accounting codes so that customers will pay only for the assets required for their council area

The CCO would then manage, operate, maintain, and finance water infrastructure across the three councils. This shared CCO would act as a unified entity, consolidating resources and operations to deliver services.

Figure 2.3 illustrates the structure of a Joint CCO between HDC and KDC.

Figure 2.3: Diagram of a Joint CCO



Key assumptions for a joint HDC-KDC water services CCO

We make several key assumptions for the joint CCO option. We adopt a "no worse off" assumption. This means we assume that the Joint CCO would keep three asset and debt accounts for each council. Customers would pay the depreciation and return on assets related to their council's specific asset and debt account. Furthermore, the joint CCO would keep separate accounts to split opex costs where they are incurred. This change ensures that customers are paying closer to the cost of supplying them, discrepancies in debt and future capex are not cross-subsidised, and no council is worse off compared to their go-alone position.

The jointly owned CCO would also have access to financing up to a net debt-to-revenue ratio of 500 percent. The joint CCO would also be able to exploit some economies of scale, share overheads and compliance costs over more customers and improve the competence of management and operations (operating as a larger organisation).

Additional costs of a joint CCO

We assume additional costs from the joint CCO. We generally assume that both councils will seek to minimise transition costs and utilise existing systems, and transfer employees and assets (such as vehicles, any leases and so on) to the CCO. We assume existing council office space and facilities will be leased at cost to the new CCO, minimising set-up costs.

Nevertheless, some additional costs will need to be met:

- Board members: Five board members remunerated at $35,000 each
- One-off CCO set up costs, including legal advice, and so on: $1,000,000
- Additional regulatory staff of 3 FTEs at $600,000 to $900,000 cost (salary plus overheads)

Cost savings and efficiencies from a joint CCO

Key cost savings assumptions for the CCO are set out in the table below:

Table 2.2: Cost savings from efficiencies, compared to LTP forecasts

Factors	Efficiency savings type	Time period	Joint CCO assumptions
Capex cost efficiency	Fixed savings	Fully in force after 5 years	2.5%
Staff cost efficiency	Annual compound	Begins after 3 years	1%
Water operations cost efficiency	Fixed savings	Fully in force after 5 years	5%
Other overhead cost efficiency	Fixed savings	Fully in force after 5 years	10%

3 Relevant evaluation criteria

Castalia has developed a framework for assessing water reform options. We have used this framework in advice for several councils, Local Government New Zealand, Communities 4 Local Democracy, and in advice to DIA. The framework consists of six elements or “parameters for success” towards achieving the ultimate objective of water reform:

> Safe, resilient, reliable, customer-responsive water services at least cost.

We explain the framework in detail below, followed by guidance on how each parameter relates to achieving the overall objective.

3.1 The framework

The framework is outlined in the following diagram. We then describe each element in detail below.

Figure 2.0: Decision-making framework for evaluating water reform options

Source: Castalia, based on advice to LGNZ and DIA

3.1.1 Economies of scope and scale

Economies of scale and scope can provide benefits in the delivery of water services. However, it is important to assess the specific facts of the reform and if the actual economies being generated (if any) are from the reform interventions.

When a firm’s scale of production leads to lower average costs, there are economies of scale. The relevant output for assessing the existence of economies of scale in a structural reform is the number of connections: Does an increase in the number of connections lower the average cost of provision? As the number of connections increases, there may be savings in operating costs (for example, corporate head office services) on a per-customer basis. However, this is likely to be a small proportion of the total cost per customer.

Economies of scope are proportionate cost savings from producing two or more distinct goods. In water services this could be a cost saving from one service provider delivering both the clean drinking water and wastewater services. Economies of scope in water services are more often assumed than empirically verified. Economies of scope also exist between water services and other municipal services. This can be true for both small and large entities.

3.1.2 Access to financing over long-term

Water providers require access to the lowest risk-adjusted cost finance available on terms that align with their capital and operating cost needs. The market sets the cost of finance and reflects the market's assessment of the provider's ability to earn revenues to repay its lenders.

Water services involve high-cost assets with long lives and lumpy investments. Financing instruments like bonds need to reflect a long-term investment horizon. The water services of many councils in New Zealand are constrained in accessing finance due to the overall indebtedness levels of the council's consolidated balance sheet and caps imposed by credit rating agencies that, if breached, would increase the cost of debt. HDC is currently at the limits of its borrowing capacity due to these caps. Castalia's 'access to financing parameter' assesses reform options for the extent to which water service providers can access finance that reflects the riskiness and revenues of the water business and its projects alone. Ways to maximise financing access include:

- Establishing an appropriate ownership structure. Most councils in New Zealand provide water services as part of the council's normal business, thus constraining access to finance for water services due to the overall indebtedness of the council's consolidated balance sheet. Separating water services from the council balance sheet can help to unlock additional debt limits, specific to the water infrastructure. The LGFA announced a financing facility available to qualifying Council-Controlled Organisations (CCOs) that meet certain requirements.
- Maximise financing options through scale. Larger organisations have larger balance sheets and access to more funding and financing. This enables the organisations to better sequence projects in a way that optimises between financing and timing of expenditure. This can allow service providers to achieve better access to financing for long-term investment programs.

3.1.3 Management and operational capability

Capable and sophisticated management and operations happen when management meets organisational objectives, uses available resources efficiently, maintains high levels of employee performance and professionalism, and provides excellent service to customers. This is essential to safe, resilient, reliable water services at least cost.

Small councils, and councils located in remote areas, have challenges attracting and retaining the skilled staff. Water service providers with poor management and poor remuneration can also struggle to lift management and operational capability.

Management and operational competence involve basic safety matters, such as ensuring filters are changed or chlorine drips discharge at the correct rate. Competence can be correlated to scale, competition between water services, outsourcing, regulatory enforcement, and profit incentives. The delivery entity should be evaluated according to the likelihood and extent to which the competence of management and operations is improved. There are several ways to achieve this, not all of which necessarily follow from increased size. For example, contracting out of key functions can improve capability.

3.1.4 Flexibility to future change

Flexibility and adaptability to change following new information are desirable in water service providers. Societies needs and expectations regarding water services are always changing. For example, changes to population will affect investment needs. Public opinion about how water and wastewater is treated can also lead to the need for change. These changes or new information require water services to adapt in response.

Water service providers that are closer to customers can generally adapt more easily due to better local knowledge and understanding. Appropriate institutional settings can also ensure that service providers can readily adapt to customer needs over time. Castalia's criteria suggest that institutional settings should be assessed on the extent to which they are responsive to change and new information.

In the Local Water Done Well context, flexibility to future change means being able to adapt as the regulatory settings change, or as opportunities emerge for councils to work together.

3.1.5 Incentive alignment

This element refers to the institutional settings that incentivise those charged with governance and management of the water service to make decisions that achieve the overarching objective. The incentives can be short or long-term. Ideally, both short and long-term incentives are aligned with the objectives.

Short-term incentives of governance and management can be aligned via performance contracts and financial targets. Institutional incentives generally arise from accountability to shareholders. Long-term incentives can also be aligned with more care.

Long-term incentives are a challenge in any institution, especially where assets have long lives, and investment needs span decades. One key issue is ensuring sufficient long-term capital investment. Institutional settings, such as ownership interests or regulation, need to ensure that management is incentivised to make costly capital expenditures even where the benefits will not produce immediate returns. Adequate regulation can also ensure long-term incentive alignment via statute.

3.1.6 Accountability to customers/stakeholders

There is a cost and quality trade-off in providing water services. Service providers must remain accountable to customers for where the service sits on the cost and quality continuum. Customer accountability allows customers to act on concerns and receive the level of service they want for a given price. Water service quality can be highly variable, even above safe minima.

Consumers also want to ensure that water services are provided at a fair price. It is, therefore, important that the cost/quality trade-off is made by an entity or in a way that provides accountability to customers. Customer accountability can be achieved through local government (current model), independent regulators, regional/council-owned entities, and direct ownership by consumers. Various institutional options exist to give customers and communities accountability for price and quality preferences in water services. The institutional design options need to be evaluated to determine the extent to which they are likely to be effective in the New Zealand environment.

In New Zealand, accountability to hapu and iwi is also important. Hapu and iwi have significant rights and interests in waterways, other water sources and the receiving environment for treated wastewater (both land and water discharge). Many councils have obligations of consultation and have specific agreements that relate to natural resources affected by water service provision.

4 Financial modelling results

Castalia modelled the two Go-Alone options, IBU and single-council CCO, for each council, as well as a joint CCO of both councils. The modelling found that the joint CCO option resulted in both the lowest tariffs for council residents and the lowest debt levels for councils. At a high level, Hurunui benefits from Kaikoura's low debt levels, while Kaikoura benefits from Hurunui's larger population to spread its revenue requirement across in the form of tariffs.

4.1 Tariff implications

We modelled the tariff implications of each option: internal business unit, single-council CCO and joint CCO for each council. We compared tariffs to the forecast water rates assumed in councils' long-term plans (LTPs).

The key takeaway from the modelling is that both councils benefit from the joint CCO's cost efficiencies. KDC benefits from having a larger population to spread its revenue requirement across. For HDC, the joint CCO's efficiencies of scope and scale reduce its revenue requirement below the cost of a single-council CCO. For KDC, the joint CCO's division of operating expenses significantly reduces their revenue requirement and per-household tariffs.

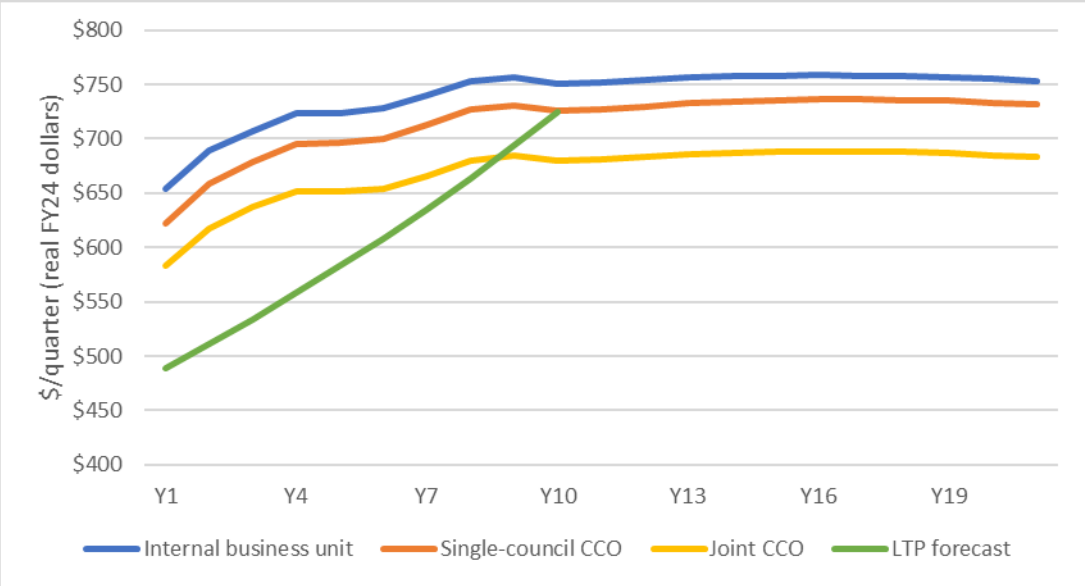
Hurunui tariff implications from potential reform options

HDC's revenue requirement is spread across its population in each scenario, meaning reductions in the revenue requirement translates to reductions in water tariffs paid by Hurunui residents. The joint CCO carries marginally higher staff costs than the two Go-Alone scenarios, but joint CCO savings from operating expense efficiencies drive down HDC's total revenue requirement, creating the tariff reductions reflected in Figure 4.1.

The joint CCO's initial regulatory asset base (RAB) requirement is $50 million to stay in compliance with the LGFA's 500 percent net debt-to-revenue covenant for qualifying CCOs. KDC's low debt levels mean it requires zero initial RAB, allowing for HDC to "contribute" all $50 million of the initial RAB. The return on capital allowance and depreciation allowance are divided between HDC and KDC proportionate to their contributions to the RAB. As a result, HDC is allocated 100 percent of these two initial allowances, decreasing to 91% by the end of the modelling period. While this does mean HDC pays higher tariffs than a population-proportionate split, it is more equitable due to KDC not needing debt relief as much as HDC does.

HDC's water tariffs are forecast to plateau after FY2033. This is due to Hurunui's compounding population growth outpacing the revenue requirement growth, causing the eventual decline in per-household tariffs in the latter years of the modelling.

Figure 4.1: Hurunui tariff comparison

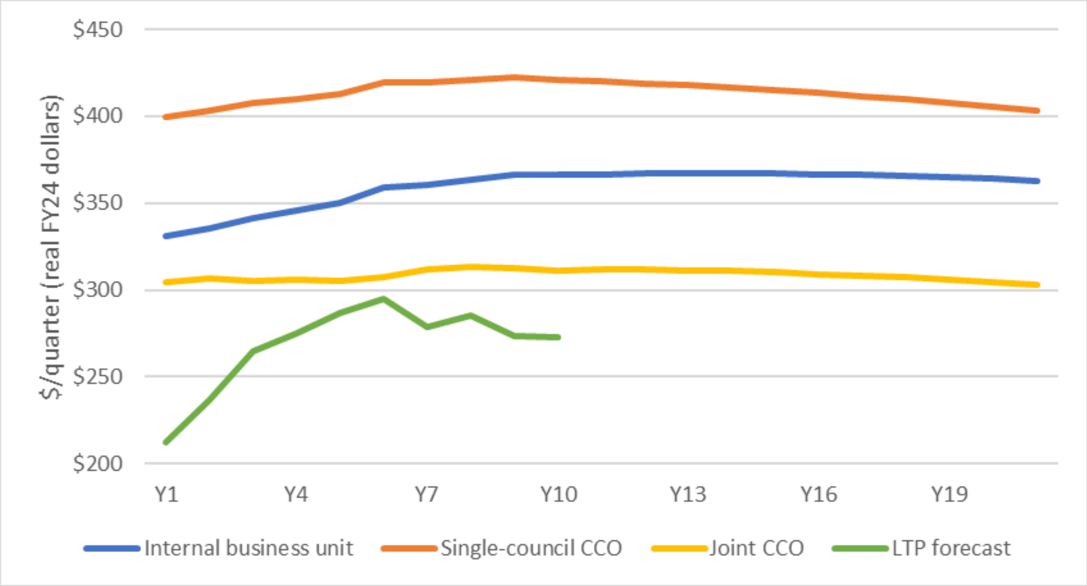


Kaikoura tariff implications of reform options

KDC's low debt levels and small contributions to the RAB mean that most of its revenue requirement is made up of opex (staff costs and overhead costs). The total operating expense allowance of the joint CCO is divided up by population, and Kaikoura makes up between 20 and 23 percent of the total population of the two councils over the modelling period. This allows Kaikoura to spread the increased opex of the joint CCO by population, which benefits Kaikoura; KDC's revenue requirement under a single-council CCO is more than $800,000 greater than their revenue requirement under the joint CCO.

The forecast decline of per-household tariffs after year 10 is due to population growth outpacing revenue requirement growth. Per-household tariffs for KDC under the three reform options are displayed alongside LTP forecasts in Figure 4.2.

Figure 4.2: Kaikoura tariff comparison



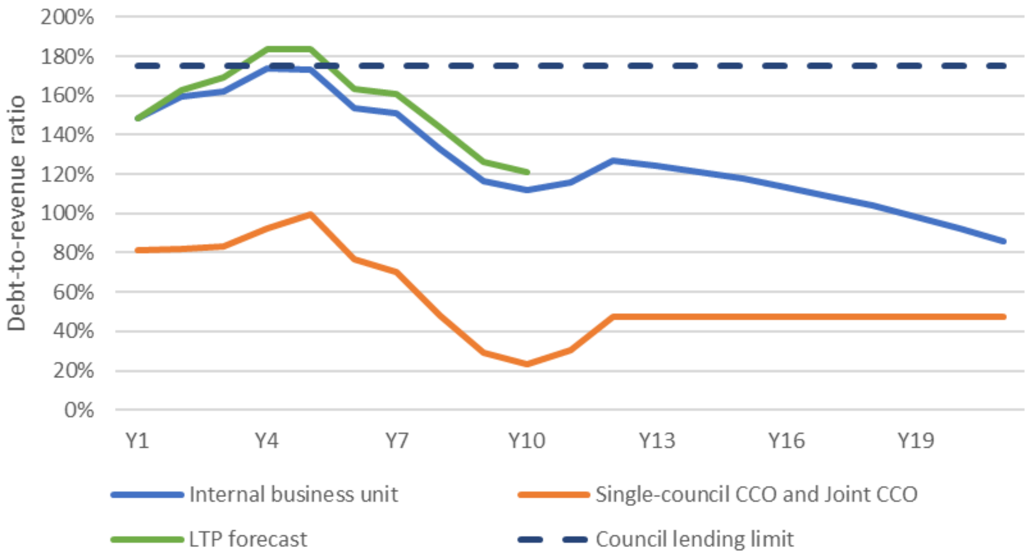
4.2 Remaining council debt implications

The councils' ability to transfer debt to either a single-council CCO or joint CCO benefits both councils, but HDC benefits more from this debt transfer. The LGFA imposes a 175 percent net debt-to-revenue covenant on councils and a 500 percent net debt-to-revenue covenant on qualifying CCOs; the analysis below explains how the CCO options interact with these covenants.

Hurunui council debt impacts from reform options

HDC's LTP data indicates a two-waters debt balance of over $47 million at the end of FY2024. Under a council internal business unit model, HDC would require an initial RAB of $83 million for revenues to remain high enough for HDC stay in compliance with the 175 percent covenant. This would pass through to consumers in the return on capital allowance, increasing household water tariffs. The single-council CCO and joint CCO both allow the council to offload this debt onto the CCO, adding 67 percent of headroom below the covenant and reducing the initial RAB requirement to $56 million and $50 million respectively. As seen below in Figure 4.3, HDC is well below the covenant over the modelling period under the single-council CCO and joint CCO.

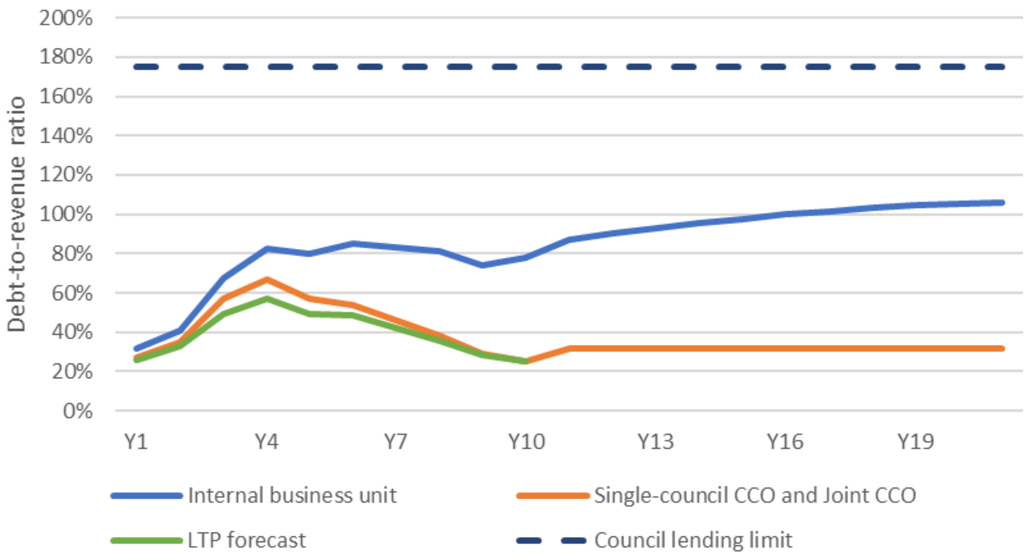
Figure 4.3: HDC net debt-to-revenue ratio comparison



Kaikoura council debt impacts from reform options

KDC's council debt is negligible and would not require a CCO solution to remain in compliance with the 175 percent net debt-to-revenue covenant. However, KDC can still benefit from the debt transfer to either a single-council CCO or joint CCO. As indicated by Figure 4.4, council debt-to-revenue slowly grows after year 11 as new borrowings outpace IBU revenue. However, this debt remains off KDC's books under the CCO options, leaving the council's debt-to-revenue levels unimpacted by the water business. It would also save hundreds of thousands of dollars on interest payments that will be incurred by the CCO instead of KDC.

Figure 4.4: Kaikoura DC debt-to-revenue ratio comparison



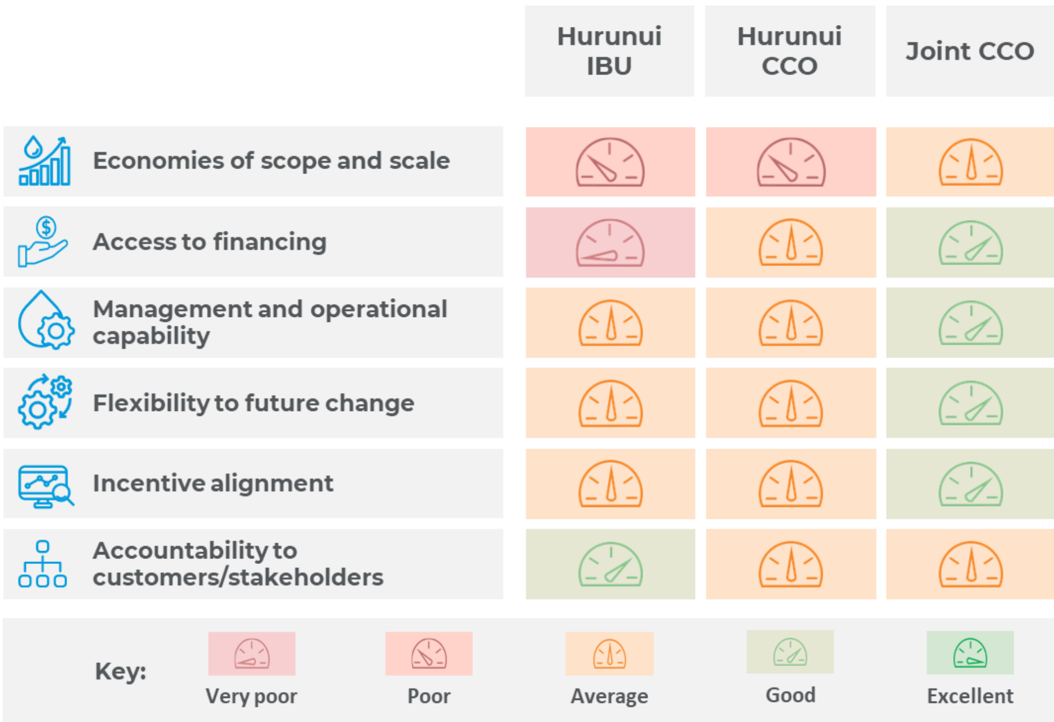
5 Evaluation results

We set out the results of the evaluation below.

5.1 Hurunui District Council evaluation results

We set out the results of our evaluation according to the framework in section 3 for HDC below:

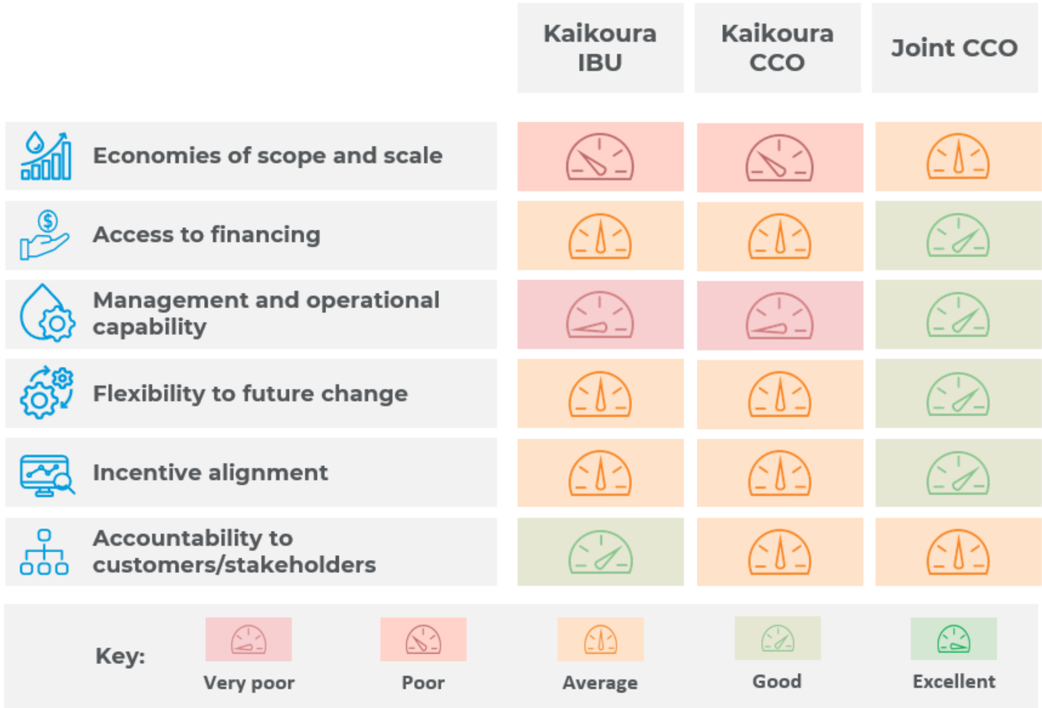
Figure 5.1: HDC evaluation results



5.2 Kaikoura District Council evaluation results

We set out the results of our evaluation for KDC according to the framework in section 3 below.

Figure 5.2: KDC evaluation results



6 Conclusion and recommendations

Of the options evaluated, a joint CCO appears to provide the greatest benefits to both HDC and KDC.

Go-alone options might give HDC and KDC more direct control over water services. However, with economic regulation (Commerce Commission), water quality regulation (Taumata Arowai) and increased focus on environmental outcomes (ECan), this “control” is limited anyway. Also, go alone options have higher operational costs due to fragmentation, limited economies of scale, and duplication of resources. As a larger entity, the joint CCO could also secure better terms for a competitively procured third-party contract for management, operational and maintenance services, compared to go-alone options.

We therefore recommend that HDC and KDC consider a joint CCO option as the best approach The key points are:

- Tariffs are lowest for both councils under a joint CCO. Modest cost-efficiencies, better balance sheet structuring, and sharing of borrowing capability across both councils lowers tariffs
- Economies of scale are improved, compared to go-alone options
- Access to financing is greatly improved for both HDC and KDC. One key benefit of forming a WSCCO is the enhanced ability to access financing, particularly through the LGFA. Qualifying WSCCOs will have access to much higher net debt-to-revenue limits

through the LGFA that councils–likely up to 500 percent of their revenue. Thus, they will have far greater financial flexibility to invest in large-scale infrastructure projects

- Management and operational capability can be improved from a joint, dedicated water services joint CCO.
- Flexibility to future change is preserved under a joint CCO. The CCO is small enough to change as new information emerges, and ensure the water services remain resilient. For example, the joint CCO:
  - Could admit one or more additional councils in future (expanding the CCO)
  - Could competitively procure third-party management, operational and maintenance services under a contract. The joint CCO would have a much stronger negotiating position than if each council went alone
  - Increases resilience for the two councils, allowing for them to share environmental and infrastructure risks and reduce the impacts of adverse events.
- Incentives of board and management can be better aligned with the regulators' requirements and the interests of consumers
- The joint CCO may be slightly less accountable to customers, however, with robust governance and oversight, plus regulatory monitoring, the joint CCO could be just as accountable to customers as go alone options.
- Finally, the joint CCO aligns with the Government's expectations for the sector and may provide strategic benefits in future (for example, in relation to regional deals).

Local Water Done Well update

Michael Lovett, Deputy Chief Executive Local Government branch

LGNZ Rural & Provincial and Metro Sector Meetings
22 November 2024

Te Kāwanatanga o Aotearoa
New Zealand Government

Te Tari Taiwhenua
Internal Affairs

A new approach to water services delivery

PLANNING AND ACCOUNTABILITY FOR WATER SERVICES

WATER SERVICES DELIVERY PLANS

PLANNING AND ACCOUNTABILITY FRAMEWORK

WATER SERVICES DELIVERY ARRANGEMENTS

STREAMLINED PROCESS FOR WATER CCO SET-UP

NEW WATER SERVICES DELIVERY MODELS

FINANCING FOR COUNCILS AND WATER ORGANISATIONS

FUTURE ARRANGEMENTS FOR STORMWATER

ECONOMIC REGULATION AND CONSUMER PROTECTION

INFORMATION PROVIDED VIA WATER SERVICES DELIVERY PLANS

FULL ECONOMIC REGULATION REGIME

WIDER REGULATORY SYSTEM

DRINKING WATER QUALITY REGULATION

STANDARDS TO HELP REDUCE WATER INFRASTRUCTURE COSTS

ENABLING LEGISLATION

LOCAL GOVERNMENT (WATER SERVICES PRELIMINARY ARRANGEMENTS) ACT

LOCAL GOVERNMENT (WATER SERVICES) BILL

Councils can choose from a range of water services delivery models

1	Internal business unit or division	• Status quo for many councils • Minimum requirements for water service providers will apply • New financial sustainability, ringfencing rules, and economic regulation will apply
2	Single council-owned water organisation	• New company established, 100% owned by the council • Financial sustainability rules will apply, but retains a financial link to the council • Councils with existing water council-controlled organisations will be required to meet minimum requirements
3	Multi-council owned water organisation	• New company established with multi-council ownership • Appointment of a Board through shareholder council (or similar body) is advisable but not a statutory requirement • Option to access Local Government Funding Agency finance with the provision of parent support or to create a more financially independent organisation
4	Mixed council/consumer trust owned	• Consumer trust established to part-own a water organisation • One or more councils own the remainder of the shares • Structure enables financially independent organisation to be established while retaining some council ownership
5	Consumer Trust owned	• Council transfers assets to consumer trust owned organisation • Consumers elect trustees to represent their interests in the organisation • Most financially independent of the available models

Minimum requirements for water services providers

Regardless of the model chosen, all local government water service providers will have to meet clear minimum requirements set out in legislation.

All water service providers:

- Will be subject to economic, environmental and water quality regulation
- Will be subject to a bespoke planning and accountability framework for water services
- Must be financially sustainable, including ring-fencing of water services
- Must act consistently with statutory objectives
- Will be subject to restrictions against privatisation.

Financing available via LGFA, to support long-term investment

In August 2024 LGFA confirmed it will provide financing to support water council-controlled organisations (CCOs) that are financially supported by their parent council or councils.

These new arrangements provide councils with access to the level of financing needed to make the necessary investments in water infrastructure, at low cost of financing, while managing the impact of rates rises on ratepayers.

Increased borrowing to fund investment in water infrastructure reduces the need to fund investments directly from rates and other revenue.

This can smooth the impact of investments across longer periods of time, which should be reflected in smaller increases in rates and water charges.

In many cases, the benefits of additional borrowing headroom, created through the set-up of a water CCO, to fund investment are evident for individual councils as well as for groups of councils working together.

Benefits of establishing water CCOs

The establishment of a water CCO under Local Water Done Well will enable:

1. Retained local ownership of and direction setting for water services and infrastructure assets, at minimal financial cost to councils
2. Reform of the water services industry that will create opportunities for new capital and operating efficiencies for water CCOs
3. Additional flexibility and financial resilience to ensure financially sustainable water services provision.

The establishment of a water CCO under Local Water Done Well and more effective utilisation of debt financing provided by LGFA will enable:

1. Improved financial resilience for water services delivery and councils
2. Increased or accelerated investment against what councils can currently fund or deliver in-house
3. Lower prices for communities than achievable under the status quo
4. Increased borrowing headroom and financial resilience for owning councils.

New planning and accountability framework for water services

The Government is proposing a new planning and accountability framework for water services, which is fit for purpose for the new water services delivery system.

The framework will help to improve transparency and accountability, and support an enhanced focus on water services.

The Local Government Water Services Bill will set out the details of the new framework. It will apply to all local government water service providers.

THREE CORE DOCUMENTS
1. Statement of expectations
2. Water services strategy
3. Water services annual report

Economic regulation ensures sufficient, high-quality investment

The Government is establishing a new economic regulation and consumer protection regime under Local Water Done Well, which will be implemented by the Commerce Commission.

- The regime will support water infrastructure to be appropriately invested in, maintained and delivered for the long-term benefit of consumers.
- The Commerce Commission will have a range of regulatory tools, including mandatory information disclosure, to promote efficient practices and protections for consumers.
- The Government intends to introduce legislation to give effect to the new regime in December 2024.
- The Commerce Commission will start implementing the full economic regulation regime after the legislation is passed, which is expected in mid-2025.

In preparation for the full economic regulation regime under Local Water Done Well, councils will disclose information on water services as part of the development of their Water Services Delivery Plans.

- The Plans do not have a regulatory purpose, however information collected through them will be shared with the Commerce Commission, to support the development of the full economic regulation regime.

Key considerations in delivering water services in future

- Under Local Water Done Well, water services providers will have to operate more like independent utility businesses, like telecommunications or electricity utilities.
- Water services providers will be structured and operated like corporatised utilities, rather than public services.
- This will require a fundamental change in how water services providers behave and think.
- Water Services providers will be directly accountable to customers, regulators, and councils.
- Their accountability to councils will differ from current systems – focusing on accountability of strategic vision and leadership rather than daily operations and funding.

Consumers will pay **cost-reflective charges** based on the services they receive

Water services providers must meet **service and performance standards**

Water services providers are incentivised to **finance sustainably and efficiently** and must ringfence revenues

Water Services Delivery Plans provide foundation for Local Water Done Well

The Local Government (Water Services Preliminary Arrangements) Act 2024 requires councils to develop Water Services Delivery Plans by 3 September 2025.

The Plans are a way for councils to reflect on their current approach to water services delivery and whether it will be 'fit for purpose' into the future, to ensure water services are financially sustainable and meet quality standards.

Plans need to address three key areas:

1. Financial sustainability (investment, revenue and financial sufficiency)
2. Anticipated or proposed delivery model
3. Implementation plan.

The information required for Plans is expected to come from councils' existing public documents, such as long-term plans, financial accounts and asset management plans.

The Department is providing technical support to councils – and detailed guidance, templates and other information is available on our website.

- One-off, transitional documents
- Cover drinking water, wastewater and stormwater
- Have no regulatory function
- Can be developed by individual or joint councils
- Streamlined approach to consultation
- 10-year timeframe; may cover up to 30 years, with detailed info on first three

Indicative timeline for Water Services Delivery Plan development

An indicative timeline for Water Services Delivery Plans development is outlined below. This builds on the Plan development process set out in the Guidance material and is intended as a guide only (the only formal requirement for Councils is to submit a Plan by 3 September 2025).

Financial viability assessments Councils assess their standalone financial positions	**Financial sustainability and delivery model** Councils consider their preferred delivery model and explore alternative models	**Community consultation** Councils decide on their preferred delivery models and consult their communities	**Finalise Plans for submission** Councils finalise Plans for submission	**Department review and acceptance of Plans** Councils submit their final Plan. The Department reviews Plans and works with councils who are required to do further work on their Plan.
Sep– Oct 24	Nov 24 – Jan 25	Feb – Apr 25	May – Jul 25	Aug – Sep 25 (& ongoing)
Phase targets: All councils have assessed their own standalone financial positions and discussed with the Department. Councils have completed a stocktake of their current water services delivery arrangements and understand where information gaps are.	**Phase targets:** Councils are considering their preferred delivery model and exploring alternative models. Councils are discussing with the Department how they plan to address any barriers to financial sustainability.	**Phase targets:** Councils have decided on their preferred delivery model and have begun consultation with their communities. Some councils may undertake consultation at a later date alongside their annual Plan.	**Phase targets:** Councils are finalising their Plans for submission to the Department. Councils can request the Department to review their draft Plan. Councils that require an extension have requested an extension (before 3 Aug 2025).	**Phase targets:** Councils submit their final Plans (by 3 Sep 2025). The Department communicates either acceptance or need to resubmit. Clear pathways of support are identified to ensure all Plans are received by 3 Sep 2025.

Next month – Local Government (Water Services) Bill introduced

- Updated information and factsheets available.
- Further guidance to be shared with councils, to help inform your consideration of future arrangements:
  1. Establishing a water CCO or consumer trust
     - Summary information to support decision making
     - Model templates for the key documentation involved
  2. Information and insights about key considerations involved with delivering water services
  3. Worked examples showing impact of using additional debt headroom

Key milestones

Ongoing	Technical support for councils to prepare Water Services Delivery Plans (through to September 2025)
Dec 2024	Local Government Water Services Bill expected to be introduced to Parliament – opportunity for feedback at select committee
Mid-2025	Local Government Water Services Bill expected to be enacted – guidance material to be shared to support implementation (following Bill enactment)

Further information

www.dia.govt.nz/Water-Services-Policy-and-Legislation

Contact us

waterservices@dia.govt.nz

Questions

Te Tari Taiwhenua
Internal Affairs

Economic Regulation and Water

Water NZ webinar, Water Utilities Association meeting

Rural and Provincial sector, and Metro sector presentation

14, 21 & 22 November 2024

The Commerce Commission

- We are an independent competition, fair trading, consumer credit and economic regulator.
- We have regulatory responsibilities in telecommunications, energy networks, transport fuel, the banking retail payment system, groceries, dairy, airports, and now water.
- The three main areas of work that the Commission undertakes are:
  - Promoting competition in markets throughout the economy
  - Influencing monopoly infrastructure performance for better essential services
  - Tackling harm, including from unfair trade practices and irresponsible lending.
- Our four main outcomes as an organisation are:
  - **Stewardship:** New Zealanders, including Māori, have trust and confidence in the regulatory systems we implement and enforce
  - **Competitive Markets:** New Zealanders receive the benefits of competition: greater value, innovation, productivity and choice.
  - **Fair Trade:** Consumers, including businesses, are informed, empowered and their interests are protected.
  - **Essential Services:** Consumers get quality and value from reliable essential services.

The importance of economic regulation

- In many OECD countries, economic regulation of prices (and/or revenue) and quality is often imposed in infrastructure markets where competition is limited (e.g. natural or statutory monopolies) and infrastructure is providing an essential service.
  - For instance: electricity/gas/fibre networks, airports, rail, ports, and water.

- If competition is limited, suppliers of goods and services may:
  - Raise prices to earn higher profits
  - Provide services at a reduced quality
  - Face weaker incentives to invest and operate efficiently, and to innovate.

Our role in the wider water landscape

<table>
<tr><th></th><th>Health outcomes</th><th>Environmental outcomes</th><th>Infrastructure sustainability and resilience outcomes</th><th>Financial Sustainability</th></tr>
<tr><td rowspan="2">Department of Internal Affairs</td><td colspan="4">Policy, Stewardship, legislation – local government system / water services system. Requires and assesses Water Services Delivery Plans</td></tr>
<tr><td colspan="2">Monitors Taumata Arowai</td><td></td><td></td></tr>
<tr><td rowspan="3">Taumata Arowai</td><td>Drinking water regulations</td><td>Wastewater standards</td><td></td><td></td></tr>
<tr><td colspan="2">Oversight of performance of wastewater and stormwater networks</td><td></td><td></td></tr>
<tr><td colspan="2">Reviewing wastewater/source water risk management & drinking water safety plans</td><td></td><td></td></tr>
<tr><td rowspan="3">Commerce Commission</td><td colspan="4">Foundational Information Disclosure</td></tr>
<tr><td colspan="4">Crown Monitor for Watercare</td></tr>
<tr><td colspan="4">Enduring economic regulation regime (awaiting Local Government Water Services Bill)</td></tr>
<tr><td rowspan="4">Ministry for the Environment</td><td colspan="2">NES – sources of human drinking water</td><td>National Adaptation Plans</td><td></td></tr>
<tr><td></td><td>Freshwater management regulations (inc. NPS-FM)</td><td>Emissions reduction plans</td><td></td></tr>
<tr><td></td><td colspan="2">Administers Environmental Reporting Act 2015</td><td></td></tr>
<tr><td></td><td colspan="2">Policy, Stewardship – resource management system</td><td></td></tr>
<tr><td rowspan="2">Regional Councils</td><td colspan="2">Regulator – source and receiving waters, and wastewater/ stormwater networks (in region)</td><td></td><td></td></tr>
<tr><td></td><td>Regional Plans</td><td></td><td></td></tr>
<tr><td>Ministry of Health</td><td>Policy advice – public health matters relating to drinking water</td><td></td><td></td><td></td></tr>
<tr><td>National Emergency Management Agency</td><td></td><td></td><td>Administers Civil Defence Emergency Management Act 2002</td><td></td></tr>
<tr><td>Te Arawhiti</td><td colspan="4">Policy lead on the Crown's Treaty of Waitangi obligations – including Treaty settlements</td></tr>
</table>

The Commerce Commission and water reform

- The Government has indicated the Commerce Commission will be the economic regulator for the Government's Local Water Done Well (LWDW) regime. We are currently awaiting the Local Government Water Services (LGWS) Bill that will implement the full system.
- In the meantime, the Local Government (Water Services Preliminary Arrangements) Act 2024 enables specified entities to be subject to an early form of information disclosure by the Commission ('foundational information disclosure'), prior to the full economic regulation regime. While this is unlikely to apply to all providers, and will not apply to Watercare, we will have the ability to consult broadly under the transitional regime.
- Under the long term regime, we will have a range of tools to promote sufficient revenue recovery, and efficient investment and maintenance so that water services meet regulatory requirements and are delivered at a quality that communities expect.
- We intend to create a regime that is flexible and proportionate, in line with councils' different needs and situations and government policy. This will provide the clarity and stability water service providers need to make the best investment decisions.
- We want to influence behaviour, have much greater transparency, and, over time, provide assurance that the right level of investment is happening at the right time and represents value for money.

Water team


Andy Burgess GM, Infrastructure Regulation


Charlotte Reed Implementation Director, Water


Tim Hewitt Principal Adviser


Emily Botje Principal Water Engineer


Tobias Maugg Principal Adviser


Zoe Moffat Chief Adviser


Mele Betham Chief Adviser


Monica Quinn Senior Analyst


Josh Riley Analyst


Chloe Sheridan Project Coordinator

- There are also other members of the Commission that provide support such as legal, economics, technical expertise and understanding of treaty obligations with mana whenua.

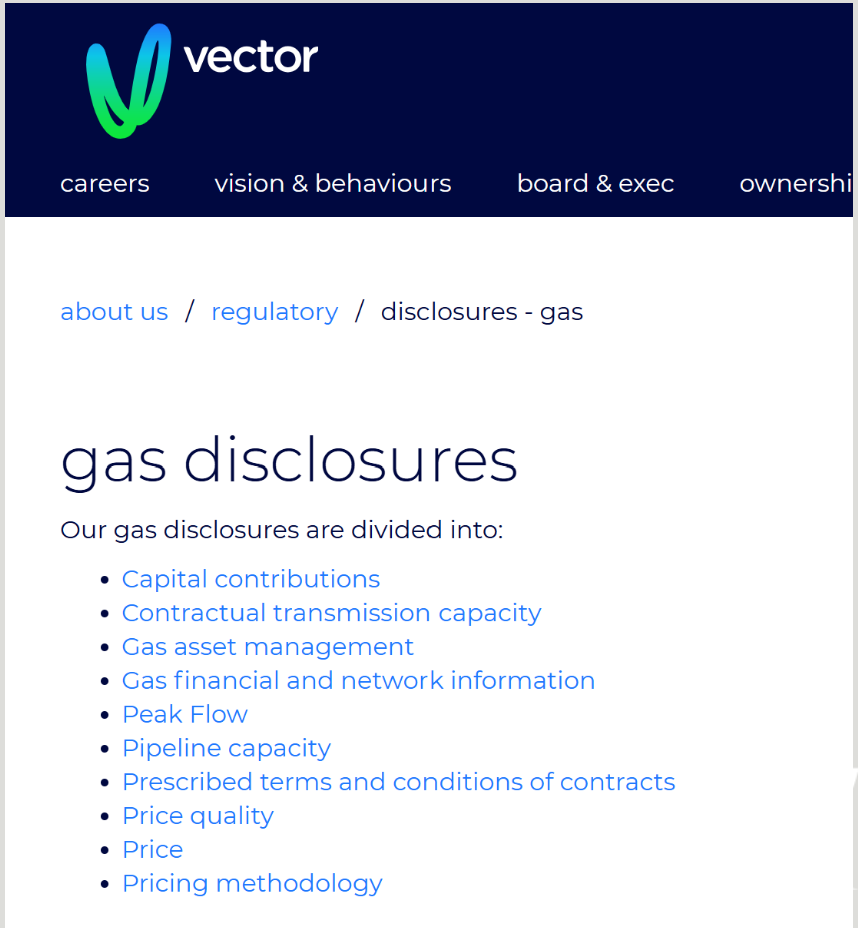
Information disclosure

Local government water services suppliers will be required to publicly disclose information in a prescribed form set by the Commerce Commission.

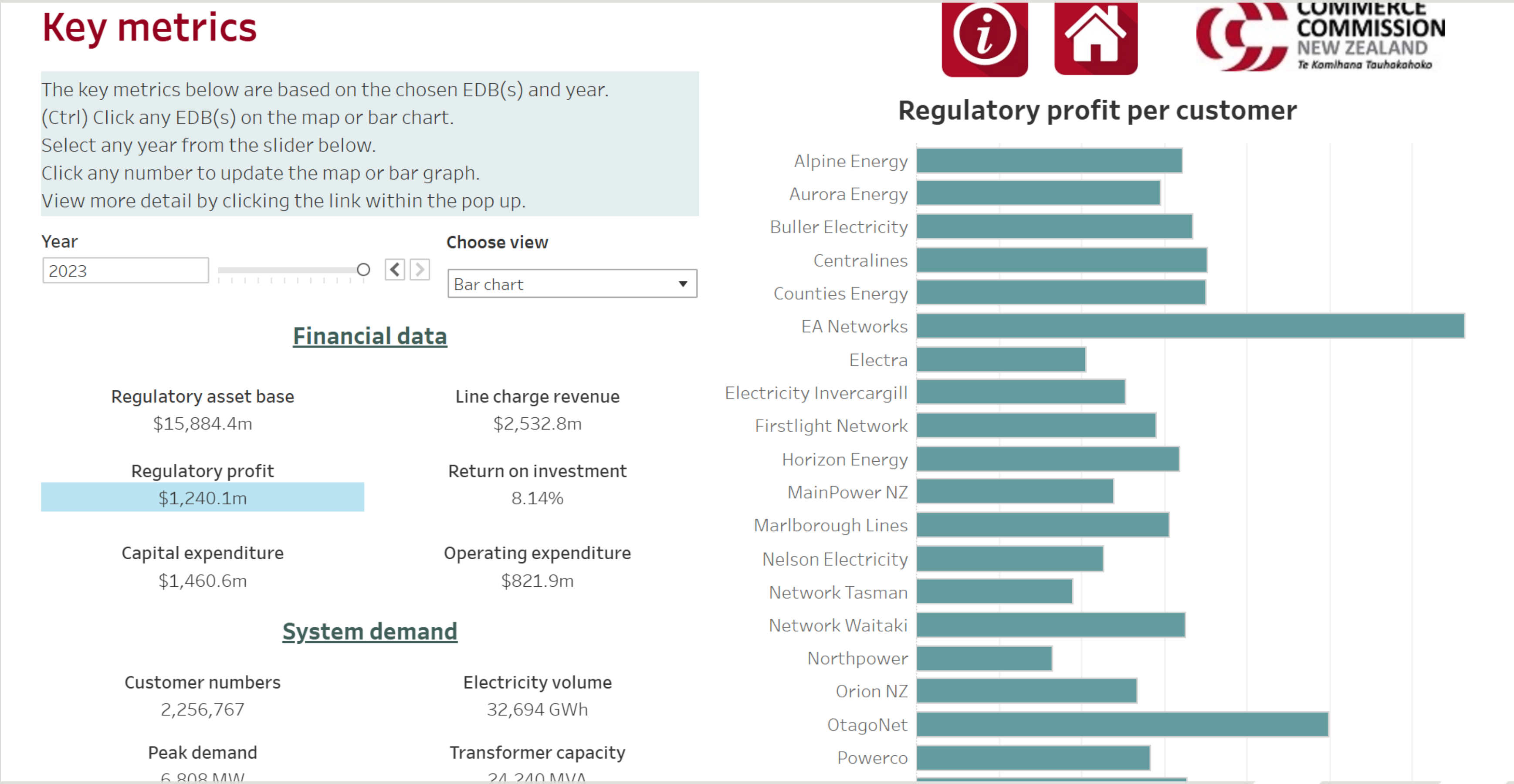
- The Commission will first be focusing on information disclosure to require water services providers to publish robust information on planning, investment, and performance.
- We expect to set initial ID requirements around six months after the commencement of the Local Government Water Services Bill.
- The information required will be set by the us but is expected to initially include details about actual and forecast capital investment plans and expenditure, operating costs, revenue, tariffs/charges, financing plans, service quality, customer engagement and asset management.
- These requirements will build on information provided under Water Service Delivery Plans in 2025.
- We will be talking to stakeholders early next year to start shaping up the foundational information disclosure regime. We'll be asking for stakeholders' views on a range of topics to support us in developing foundational information disclosure requirements, with a view to the longer-term information disclosure regime.

How does Information disclosure work?

- Governance, ownership, transparency.



League tables



Investigations

Spark NZ 5G 11:55 AM

Commerce Commission's post

Commerce Commission

6 Nov 2024 ·

Following complaints about high fuel prices in Thames, we began making enquiries. We are pleased to see that prices there have since fallen substantially and are now closer to those in nearby locations. Prior to those declines, higher prices were costing motorists in the order of $200,000 more a month than if prices had been in line with nearby Ngatea. We sought further information to help us understand the cause of the unusually high prices.

Other proposed tools – economic regulation

- While information disclosure will be our initial focus, we will have other tools available to us, should they be required.

Tool	Description	Timing
Revenue thresholds	Powers to set minimum and maximum revenue thresholds to issue clear expectations to providers regarding what level of revenue needs to be collected for investment in, and operating of, water infrastructure.	From 2026, when necessary.
Monitoring and enforcement of financial ringfence	The ability to monitor and enforce the requirement that water service revenue is spent on water services.	After commencement, when necessary.
Quality regulation and/or performance requirements	The ability to set infrastructure and service quality standards and require water services providers to take certain actions to improve performance, such as to make certain types of investments, to consult or seek approval from the Commerce Commission on investment programmes, or to undertake cost-benefit analysis.	If required, after designation from 2026.
Price-quality regulation	Ability to set minimum and/or maximum prices that may be charged, and/or minimum and/or maximum revenues. Alongside quality and performance requirements.	If required, after designation from mid-2026.

Other proposed tools – consumer protection

- The new information disclosure requirements will allow the us to collect and analyse information relating to consumer protections, such as service quality and customer engagement. If information gathered reveals that issues exist, a range of tools would be available to allow consumer protections to be strengthened.

Tool	Description	Timing
Complaints regulations	Regulations could be made specifying requirements relating to complaint processes, the provision of information on complaints, the recording of complaints, and/or reporting.	After commencement, by recommendation from Minister of Commerce and Consumer Affairs.
Dispute resolution regulations	Regulations could be made specifying requirements relating to external dispute resolution.	
Guidelines on service quality codes	The Commerce Commission will have the power to issue guidelines to water services providers on matters relating to a service quality code.	After commencement, when necessary.
A mandatory service quality code	The Commerce Commission will have the power to develop and implement a service quality code that water service providers must comply with, if: • there is no sector-led service quality code; or • the Commerce Commission is satisfied that the purpose of Part 4 of the Commerce Act 1986 could be better met by a mandatory code.	After commencement, by recommendation from the Commission or from Minister of Commerce and Consumer Affairs.

Crown Monitor

- In September 2024, the Government appointed the Commerce Commission as the Crown monitor for the interim regulation of Watercare, until full economic regulation of water services is established.
- The role of the Crown monitor is to monitor and report on Watercare's performance against the Watercare charter, which will be set by the Department of Internal Affairs.
- We are expected to engage with all parties that have a role in delivering water services to Auckland consumers, including Auckland Council, Watercare, Taumata Arowai and the Department of Internal Affairs (DIA).
- As part of our responsibilities, we are required to produce and annual report on Watercare's performance under the charter during the previous financial year.
- We are also required to report quarterly on our performance of our functions, duties or powers, as the Crown Monitor.
- We attend Board meetings of Watercare, including committee meetings, as required to deliver our function.

Working with other agencies

- There are areas of common interest between the **Water Services Authority – Taumata Arowai** and the Commerce Commission and that there are opportunities to coordinate and align our respective activities. We have a strong working relationship with them, backed by a Memorandum of Understanding and a joint work programme.
- We are also conscious that there are other key parties collecting and reviewing council information including the **Department of Internal Affairs, the Office of the Auditor General and Regional Councils**.
- A key focus for us is to ensure we minimise unnecessary duplication of reporting from suppliers and maximise opportunities to share information across the system insofar as the law allows.

Timelines

Workstream	Next 6 months (Jul-Dec 2024)	Jan -Jun 2025	Jul-Dec 2025	Jan-Jun 2026	Jul-Sep 2026
ECONOMIC REGULATION					
Crown monitor for Watercare (interim economic regulator for Watercare)	Crown monitor appointed Watercare Charter under development	Crown monitor quarterly reporting and annual reporting (first report for year ending 30 Jun 2025, due 30 Nov 2025) Watercare develops business plan and submits to DIA	Watercare Charter in place		
Ringfencing of water services	Councils must consider ringfencing as part of WSDPs		Consideration of ringfencing requirements and impacts on council operations, and implementation of financial controls to enable ringfencing of water services financial information	Water service providers prepare stand-alone financial statements for water supply, wastewater and stormwater, and in aggregate, for the period to 30 June 2026, as part of annual reporting (anticipated)	
Information disclosure	Councils provide information as part of WSDPs	Commerce Commission consultation on potential information disclosure requirements Early information disclosure on assets and investments for some councils (subject to ministerial approval)		Information disclosure requirements in place (within 6 months of Bill 3 enactment)	
Revenue thresholds				Revenue thresholds in place (if required)	
Quality standards and performance requirements				Quality-only regulation and performance requirements can apply	
Price-quality regulation				Price-quality regulation can apply	

Department of Internal Affairs: Local Water Done Well Implementation roadmap (as at August 2024)

COMMERCE COMMISSION
NEW ZEALAND
Te Komihana Tauhokohoko

Please send through any questions to wai@comcom.govt.nz, or let us know if you want to be included in our mailing list.