B.29[00b]

Chief Executive Officer Contract Renewal

2.001 Towards the end of last year a legal adviser to a local authority suggested a need for local authorities to advertise a vacancy before reappointing their chief executive. The implication was that it was illegal for an authority simply to reappoint the incumbent at the end of the contract period.

2.002 The issue largely centres around three sections in the Local Government Act 1974:

- section 119E provides for a maximum term of appointment of five years for local authority chief executives;
- section 119H requires a local authority, in making an appointment, to give preference to the person who is best suited to the position; and
- section 119I imposes a duty on local authorities to notify a vacancy or prospective vacancy in a manner which is sufficient to enable suitably qualified persons to apply for the position.

2.003 We sought the opinion of the Solicitor-General, who concluded that:

> *A vacancy occurs and notification is required whenever a term contract expires. A contract may be extended provided that it is done during its currency and provided that the five year statutory maximum term of appointment is not exceeded. It is not permissible to extend a local authority chief executive's contract beyond five years without notification.*

2.004 Existing practice throughout the local government sector did not comply with this approach, which came as a surprise to both the sector and us.

Implications

2.005 The immediate consequence was that a number of existing contracts were illegal. Approximately 32 chief executives have been in their current position since 1989 or 1990. It is likely that all of those will have had their contracts

rolled over at least once. A similar number of local authorities have had only two chief executives since 1989. It is likely that at least one of those two would have had their contract rolled over at least once. For the other local authorities, there is still a possibility that one of their three or four chief executives has had a contract rolled over.

2.006 The costs of advertising and undertaking interviews using consultants are likely to be between $25,000 and $30,000. For larger local authorities it may be more expensive because they may wish to advertise overseas. If every local authority had to go through this process every five years the cost would be significant.

2.007 A local authority cannot advertise the vacancy until reasonably close to the date of termination of the contract. The incumbent chief executive therefore has to take a 'best guess' as to what the prospects are for reappointment. If reappointment is perceived as being unlikely, then the chief executive may start to look elsewhere well before the date of termination.

2.008 Until receipt of the Solicitor-General's opinion, the assumption had been that, to replace an incumbent chief executive, the person has to be dismissed. This is not an easy option as a local authority needs to be open and honest with its reasons why that is happening.

2.009 One of the implications is that it may be easier for the local authority to replace the chief executive. The explanation will be that, while the incumbent is very good at the job, the authority has found someone who would be better. Conversely, some prospective candidates may see the advertising as a sham if the incumbent is reappointed.

Our Response to the Solicitor-General's Opinion

2.010 On 7 September 1999 we wrote to all local authority chief executives conveying the Solicitor-General's opinion. We told each local authority that we expected that, for any future contracts, it would act in accordance with the Solicitor-General's advice. We also said that, while existing contracts entered into without public notification were illegal, we would not be taking any action over them.

2.011 We were asked to review two instances where a new contract was signed with the current chief executive – without any form of public notification – after receipt of the Solicitor-General's opinion. We were satisfied that in both instances the contract negotiations had been concluded before receipt of the opinion and, therefore, action by us was not necessary.

The Latest Position

2.012 On 21 March 2000 the Local Government (Validation of Reappointments) Act 2000 was enacted.

2.013 The Act validates the reappointment of chief executives where no notification of a vacancy in the position of chief executive took place. The Act covers the period beginning on 1 November 1989 (the date the provisions came into force) and ending on 8 September 1999, (the date of receipt of the Solicitor-General's opinion by local authorities).

2.014 The Act does not amend the provisions in the Local Government Act 1974 dealing with appointments. Local authorities must therefore continue to comply with those provisions for all existing contracts expiring after 8 September 1999.

Separate Rating Apportionments

2.015 Our *Second Report for 1999*[1] included an article about an enquiry from a ratepayer disputing the basis on which they had to pay particular rates. In order to clarify the situation, we sought an opinion from the Crown Law Office.

2.016 The opinion given:

- was that the particular way in which the local authority had levied the uniform annual charges was illegal;
- confirmed that levying separate charges such as uniform annual general charges on rating apportionments of a single property was unlawful; and
- potentially has implications for all other local authorities that had taken the same approach to rating.

1 Parliamentary paper B.29[99b], pages 71-72.

2.017 The two main issues for local authorities arising from the opinion were whether:

- instead of carrying out rating apportionments, the Valuer-General should in fact treat parts of certain properties as "separate properties" in their own right; and
- the separate rates collected unlawfully on rating apportionments are required to be refunded.

2.018 In an attempt to clarify the situation, a group of local authorities and Local Government New Zealand applied for a declaratory judgment in the High Court. Their aim was to establish whether multiple portions of land which go to make up one certificate of title can be rated separately. They sought a specific ruling on whether sample portions of land amounted to "separate property" for the purpose of separate entry on the valuation roll.

2.019 The Court issued its declaration in August 1999.[2] It did not support the established approach of the Valuer-General, but instead ruled that:

- a "separate property" should not be limited to a property with separate legal title; and
- "separate occupation" is a major factor in determining "separate property".

2.020 However, as the judgment was based on the "sample cases" provided, it did not fully resolve the issues. Local Government New Zealand says that local authorities use a wide range of apportionment practices, and the extent to which the ruling covers all existing practices is unclear.

2.021 The group of local authorities and Local Government New Zealand have appealed the High Court judgment. The Valuer-General has also appealed.

- The authorities and Local Government New Zealand are appealing on the basis that the judgment has not gone far enough in allowing other units of property to be separate properties in law.

2 *Rodney District Council v Attorney-General* [2000] 1 NZLR 101.

- The Valuer-General is appealing on the basis that the High Court has gone too far in moving away from the "separate title" approach to defining "separate property".

2.022 The Court of Appeal has yet to hear these appeals.

Accounting Treatment

2.023 As auditor, we have a particular interest in the matter of rates that might have been collected illegally and any associated liability to refund them. We are required to consider the disclosure of such an uncertain event in the annual report of all local authorities that determined rates in this manner.

2.024 In 1998 – following discussions with the Crown Law Office and Local Government New Zealand – we told all our auditors that local authorities should disclose the rates collected as a contingent liability in the financial statements for the year ended 30 June 1998. As the issues had not been resolved in the ensuing year, we adopted the same approach for the year ended 30 June 1999.

2.025 Our view is that this continues to be the best way for local authorities to inform the public about a situation that has a high level of uncertainty. At this stage, we do not anticipate that the issues will be resolved for the 1999-2000 financial statements, and we have told our auditors that we are taking the same approach to those financial statements.

Legislative Implications

2.026 While Local Government New Zealand and the Valuer-General are endeavouring to clarify the lawfulness of the Valuer-General's approach to treatment of "separate property" through the Courts, we believe that legislative solutions may be required to resolve the issues associated with:

- ***Local authorities' liability to refund unlawfully collected rates if all or some apportionment practices are found by the Court of Appeal to be unlawful.*** Because several years are involved and a proportion of properties would have changed ownership or occupation, some local authorities have said that they would have difficulty in locating all people who have made payments under apportionment rating systems should they be required to refund them.

- ***An outcome that does not resolve matters to either party's satisfaction.*** Local authorities may yet need to seek amendments to the Rating Powers Act 1988 should they consider that they cannot distribute rates equitably following the Court's decision. Similarly, the Valuer-General may wish to seek amendment to the Rating Valuations Act 1998 if he considers an occupation-based approach unworkable.

2.027 Our view is that these issues require consideration by the Minister of Local Government, the Department of Internal Affairs, and Land Information New Zealand, notwithstanding the appeals and regardless of their outcome.

Advertising Expenditure Associated with Reorganisation Schemes

2.028 In 1999 the Local Government Commission issued two reorganisation schemes – for the union of Napier City and Hastings District and for the union of Banks Peninsula District and Christchurch City.

2.029 When a local authority is affected by a reorganisation scheme, section 37ZZZIC of the Local Government Act 1974 places a restriction on the amount of money that it can spend on advertising that promotes or opposes the scheme. The local authority is required to determine how much money (if any) it will spend on advertising, up to the limit specified.

2.030 If the reorganisation proposal was initiated by the local authority's electors, the authority is also required to make available to the designated representative of those electors an equal sum of money for advertising that promotes or opposes the scheme.

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2.031 The Audit Office's role in relation to the amount of money spent on advertising by the local authority is set out in section 37ZZZIE. Within one month after the date of the public poll to decide whether the reorganisation scheme is implemented, the local authority is required to send us a return specifying the amount that was spent on advertising. While the legislation is silent on what we are required to do with this return, the presumption is that we will audit its contents.

2.032 Section 37ZZZIE also says that the amount that is spent on advertising in excess of the amount determined under section 37ZZZIC is considered to be a loss within the meaning of section 31(1) of the Public Finance Act 1977. Section 31(1) gives the Audit Office the power to surcharge individual councillors to recover the loss.[3]

2.033 We have completed our responsibilities in relation to auditing the returns of advertising provided by the Napier City Council and the Hastings District Council. We were satisfied that the amount of expenditure included in the returns provided by both local authorities did not exceed the statutory limit. We also made inquiries at each council to identify any expenditure that should have been included in the return that in fact had not been included. Nothing came to our attention that would put in question the accuracy of the returns of expenditure that were made.

2.034 The public poll on the unification of Banks Peninsula District and Christchurch City was held on 18 March 2000. At the time of writing we had just received the returns of advertising for these two local authorities and, consequently, we had not completed our audit responsibilities in relation to these returns.

2.035 Local authorities, in the normal course of their business, communicate with ratepayers on a regular basis. During the time a reorganisation scheme is open for consideration it is vital that such communications are neutral on matters relating to the reorganisation – otherwise the local authority is exposing itself to criticism for bias.

3 The Public Audit Bill at present before the House would abolish the power of surcharge. However, in respect of local authorities, it is proposed to be replaced with a special reporting procedure to enable the Auditor-General to report a loss to a local authority and encourage the local authority to take action to recover the loss as a debt due from those responsible. These provisions would form part of the Local Government Act 1974.

2.036 The issuing of a reorganisation scheme can create very emotive views and polarise the attitudes of individuals and groups. As a result of that circumstance we were drawn into reviewing various issues relating to reorganisation scheme advertising. Because the legislation is complex and procedural in nature, local authorities need to take extra care when they are the subject of a reorganisation scheme to ensure that they are familiar (and comply) with the legislative requirements.

Making the Annual Report Available to the Public

2.037 A further issue that was brought to our attention earlier this year was that some local authorities have been very slow in making their annual report available to the public after its adoption by the council. In some instances the annual report was not made available to the public until several weeks after adoption – in one case nearly three months. In our view, this delay was unacceptable.

2.038 The annual report should be available to the public as soon as practicable after adoption. We will be monitoring this next year.