

Implementation of Part VIIA of the Local Government Act 1974

6.001 As indicated in the introduction to this report, much of our audit focus this year will be on how local authorities are implementing Part VIIA of the Local Government Act 1974. Two projects are being undertaken which will look at:

- the underlying processes and considerations, and the transparency of information provided to communities, in the exercise of judgements when preparing the long-term financial strategy and the funding, investment and borrowing management policies¹ adopted under Part VIIA; and
- reporting of the achievement of and changes and variations in the strategy and policies.

Working with “the Early Nine”²

6.002 During the rest of this year, we will work with the nine early compliers with the Part VIIA requirements, and with other councils that have decided to review their strategy and policies early. The results of our work will assist with providing suggestions and advice to the majority of local authorities that will be reviewing and adopting their strategy and policies later this year.

6.003 We will look at the processes and considerations applied in the exercise of judgements and the transparency of information provided to communities. We will particularly explore with the early nine how they have:

- Integrated the range of key policy and planning documents – including those required by Part VIIA, the annual plan, the strategic plan, and the district plan.

1 From here on referred to collectively as “the strategy and policies”.

2 Those local authorities that elected to comply with Part VIIA one year early – see our *First Report for 1998*, parliamentary paper B.29[98a], pages 63-64; and *Second Report for 1999*, parliamentary paper B.29[99b], pages 15-18.

As the purpose of Part VIIA is to provide an integrated financial management regime, the extent to which the key policies and plans of the council are consistent with each other is an indicator of the council's implementation of the framework.

- Complied with the requirement to determine who should pay for services and how the services should be paid for, and how the authorities have made the results of these decisions transparent for communities.

This relates to sections 122F, 122G, 122H, and 122O and the interaction of these sections with the process for striking and levying rates under the Rating Powers Act 1988.

- Assessed the costs and benefits of different options.

Undertaking this analysis for decisions with significant financial consequences is one of the principles for prudent effective and efficient financial management as set out in section 122c(1).

- Determined the activities the council will undertake and why.

This information links the council's overall strategic directions with the financial estimates in the long-term financial strategy that underlie those directions. It explains the rationale for the activities and services that the council has chosen to deliver and forms part of the content of the long-term financial strategy (section 122L(b)).

- Identified and assessed the potential impact of the forecasting assumptions used to prepare the long term financial strategy.

This tells communities the assumptions on which financial planning information is based, and gives assurance about the veracity of the data used and the thoroughness of the preparation of the strategy. Addressing forecasting assumptions forms part of the long-term financial strategy (section 122M).

6.004 We will consolidate our views on these requirements from our work with the early nine and report again later this year.

Sections 122T, 122U and 122V of the Local Government Act

- 6.005 Sections 122T, 122U and 122V require disclosure of changes, errors and variations in annual plans and reports and provide the operative means by which changes are made in the strategy and policies required by Part VIIA. These provisions, though apparently small, are important to the overall effectiveness of Part VIIA because they provide for monitoring and reporting on the achievement of plans and policies. They are therefore a key means of accountability to communities for the strategic choices that the elected members of their local authority have made.
- 6.006 We set out the specific requirements of sections 122T, 122U and 122V in paragraphs 6.007-6.010. In paragraphs 6.011-6.029 we discuss what we believe to be the relevant considerations in making disclosures under those sections, and the approach we are taking in developing guidance on the subject.
- 6.007 **Section 122T(1) provides for reconciling the previous year's strategy and policies to the coming year.** An explanation is to be given in the annual plan of significant changes in the strategy and policies in relation to the annual plan being considered for adoption compared with the strategy and policies in place for the previous financial year.
- 6.008 **Section 122T(2) provides for replacing plans and strategies as a result of material errors.** Where material error is identified in the strategy and policies the local authority must:
- as soon as practicable, publicly notify and adopt a council resolution to amend the strategy or policy; and
 - adopt a replacement strategy or policy as early as is lawfully practicable, unless no-one will be significantly disadvantaged by not replacing the strategy or policy.
- 6.009 **Section 122U provides for consistency between the strategy and policies.** Disclosure is to be made in the annual plan of material inconsistencies between the long-term financial strategy, funding policies, and investment and borrowing

management policies; and an explanation given of how the inconsistencies are proposed to be addressed for future years.

6.010 Section 122v provides for comparing the plans and strategies against actual achievements. Information is to be provided in the annual report on the extent to which the objectives and provisions of the strategy and policies have been met during the year.

6.011 Disclosures under sections 122T, 122U and 122v will be most meaningful when confidence has been established in the reliability of the information and processes underlying the development of the strategy and policies.

6.012 Currently, local authorities are finding that their strategy and policies are requiring adjustment as a result of:

- improved information becoming available, particularly in relation to assets;
- the requirement to fund the loss of service potential coming into force in the 1999-2000 year; and
- changes in policy direction (for example, as a result of the local body elections in 1998).

6.013 Local authorities are asking what they should be doing about the changes and how the Audit Office would treat changes in the strategy and policies in terms of sections 122T, 122U and 122v. Some authorities are also suggesting that the middle year of the three-year electoral cycle would be the best year to prepare the strategy and policies.

6.014 We are at this stage indicating to local authorities what we believe the legislation requires in order to assist them in preparing for reporting under sections 122T, 122U, and 122v as they review their strategy and policies. We will be collecting information about experience in complying with those requirements during the 1999-2000 audits.

6.015 We have also indicated to local authorities that, because of the importance of sections 122T, 122U and 122v, disclosures need to be complete, accurate and meaningful in order to provide information that will allow communities to assess the impact of changes and participate in decision-making.

6.016 We have also told local authorities and our auditors that, in our view, best practice requires that:

- disclosures reflect the period of plans and policies;
- public information and summaries relating to any year are consistent and accurate;
- the public should be able to reconcile actual performance with that projected in the long-term financial strategy, funding policies and investment and borrowing management policies; and
- disclosures should provide the public with full and meaningful information on the impact of changes.

Disclosures should reflect the period of plans and policies

6.017 Disclosures should provide cumulative information on changes over the three-year life of the strategy and policies and the annual plan, rather than provide only year-on-year changes. The impacts of changes in annual plan summary information should be shown over the ten-year span of the long term financial strategy in order that the public can understand the impact of changes and make choices about future directions of the local authority.

Public information and summaries relating to any year should be consistent and accurate

6.018 Where significant changes have not affected the strategy and policies, some local authorities are continuing to produce summaries of their long term financial strategy in their annual plans that reflect the originally adopted financial estimates – rather than revised estimates that reflect all changes. This can lead to estimates for the three years of annual plan information differing significantly overall from the long-term financial strategy information.

6.019 In our view, this is likely to be confusing for the public and hinder their ability to comment on estimates and proposals. Therefore, we recommend as best practice that the strategy and policy summaries be updated to be consistent with the annual plan.

The public should be able to compare actual performance with that projected in the strategy and policies

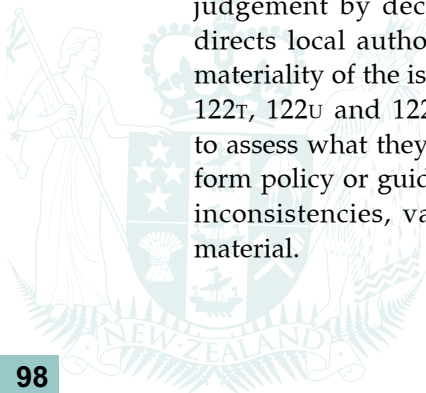
- 6.020 Some local authorities are suggesting that, if the financial information in their long-term financial strategy is updated each year with their annual plan, longer-term records of achievements against the strategy and policies adopted need not be provided. In our view, the process of revising financial estimates does not address all the requirements of revising the LTFS. Observance of the principles of Part VIIA should lead to longer-term records of performance achievements being provided as best practice.
- 6.021 The contents of the LTFS specified by section 122L do not help to make clear what the provisions and objectives of the strategy being reported on would be and, therefore, what the section 122V disclosures should be. However, in our view disclosure under section 122V should be complementary to, and enhance, the information provided in the statement of service performance required by section 223E(3)(e) of the Act.

Disclosures should provide the public with full and meaningful information on the impact of changes

- 6.022 To provide the public with full and meaningful information about the extent to which the strategy and policies and the annual plan were achieved and have changed, disclosure will be required at levels appropriate to the change rather than only on an entity-wide basis.

Significance and materiality

- 6.023 Because Part VIIA places reliance on the exercise of judgement by decision-makers, in several provisions it directs local authorities to consider the significance and materiality of the issues before them. In relation to sections 122T, 122U and 122V, this suggests that authorities need to assess what they regard as significant and material, and form policy or guidance for determining whether changes, inconsistencies, variations and errors are significant or material.



- 6.024 In our view, such guidance would need to:
- identify the users of the various documents and their differing interests in the services and activities of the local authority;
 - consider what constitutes a change, inconsistency, variation or error; and
 - provide direction on how to evaluate the significance of changes, inconsistencies, variations or errors, taking into account the two previous considerations.
- 6.025 We have asked our auditors to collect information during the 1999-2000 audits about:
- how local authorities have determined significance and materiality;
 - whether the section 122T, 122U and 122V disclosure requirements have been complied with; and
 - how full and meaningful these disclosures are.

Annual Report disclosure

- 6.026 As already noted, we regard sections 122T, 122U and 122V as the key to the effective operation of the Part VIIA framework. Section 223E of the Local Government Act requires that the disclosures required by section 122V be included in the Annual Report.
- 6.027 We are encouraging local authorities to include section 122V disclosures in the statements and information that are subject to audit and covered by the audit report – because, in our view, these disclosures form part of the information required to fairly reflect the authority’s year-end position.
- 6.028 During the coming year we will be giving consideration to:
- the disclosures required by section 122V (see paragraph 6.019); and
 - the question of whether our audit report should specifically refer to section 122V disclosures.

6.029 We have also asked the Department of Internal Affairs to consider incorporating the section 122v disclosures in the contents of the financial statements that section 223E(3) requires to be audited.

Special Studies

6.030 As well as the issues outlined in paragraphs 6.001-6.029, projects on the following subjects are currently being planned or are in progress:

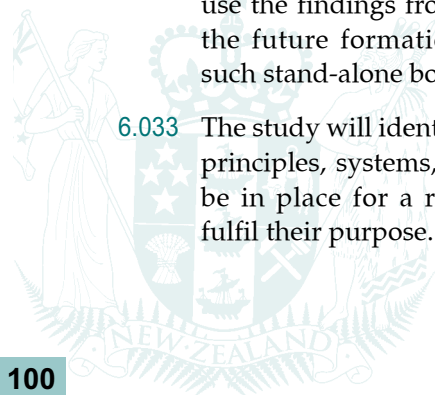
- governance arrangements by local government;
- Papakura District Council water and wastewater franchise update;
- consultation and community participation;
- audits of long-term financial strategies; and
- sale and lease of land.

Governance Arrangements by Local Government

6.031 Local authorities are free to use a variety of structures or arrangements as vehicles to perform their functions or carry out their activities – for example, local authority trading enterprises and trusts. In addition, local authorities have a range of interests in such bodies - such as funder, parent, minority shareholder and joint venture partner.

6.032 The major objective of looking at governance arrangements is to comment and report on the appropriateness of arrangements for the conduct of selected activities by stand-alone bodies throughout local government. We will use the findings from case studies to provide guidance for the future formation, governance and accountability of such stand-alone bodies.

6.033 The study will identify those governance and accountability principles, systems, processes and practices which need to be in place for a range of institutional arrangements to fulfil their purpose.



Papakura District Council Water and Wastewater Franchise

6.034 In April 1998 we issued our report on the Papakura District Council's water and wastewater franchise.³ At the time we said that we planned to conduct a follow-up audit in three years' time. The follow-up audit, the report of which is scheduled for later in the year, will:

- assess the extent of franchise monitoring by the Council;
- determine the extent to which the Council's original objectives have been met; and
- review the appropriateness of the franchise approach.

Consultation and Community Participation

6.035 We are continuing to receive a number of ratepayer complaints about the lack of consultation by local authorities with their stakeholders. Consultation is the platform on which local government credibility is based and it is apparent that not all local authorities are treating the issue as seriously as they might.

6.036 We have been pleasantly surprised by the number of requests we have had for copies of our report *Public Consultation and Decision-making in Local Government* (see Part 4). It is clear that community groups and individual ratepayers are using the report to judge the performance of their local authority.

6.037 Because of the importance of consultation and participation in local government we have initiated a project to explore how local authorities engage their communities and facilitate community participation. We intend to evaluate a range of community participation practices used by local authorities against models and characteristics of good participation.

³ *Papakura District Council: Water and Wastewater Franchise*, April 1998, ISBN 0 477 02852 7.

- 6.038 The Local Government Act 1974 emphasises that one purpose of local authorities is to engage local communities through participation, and it places significant obligations on local authorities to facilitate public participation in decision-making. The primary formal mechanisms under which this currently occurs are consultation and liaison with community boards.
- 6.039 Our study involves undertaking an audit into how local authorities are meeting their statutory obligations to facilitate community participation from the perspective of efficiency and effectiveness. It will focus on:
- the goals and strategies in place to engage communities in structured, ongoing relationships with local authorities;
 - the range of models operating;
 - the rationale behind the particular choices made by local authorities; and
 - how the success of strategies is evaluated.

Audits of Long-term Financial Strategies

- 6.040 We have already undertaken a pilot project to audit the long-term financial strategy (LTFS) of the Opotiki District Council (see page 69).
- 6.041 During 2000 the audit methodology developed for the pilot project will be tried with the Western Bay of Plenty District Council to test its application in a local authority strategic planning environment that is experiencing high growth.

Sale and Lease of Land

- 6.042 We receive a number of complaints from ratepayers who are concerned about the way in which local authorities have sold or leased council land. The legal requirements on this subject are reasonably complex, and the procedures to be followed by a local authority depend on the type of land being disposed of and its history.

- 6.043 The complainants usually allege that the local authority has failed to meet these requirements, especially by failing to ascertain the precise status of the land before disposing of it. Sale of endowment land and use of the proceeds is a matter of particular concern. Several instances have been alleged of misuse of local authority powers to sell or lease land for commercial or industrial purposes.
- 6.044 We have asked our auditors to review two or three property transactions to assess the local authority's compliance with the legal requirements.
- 6.045 We will report our findings in next year's report to Parliament on local government .

Employment of Chief Executives

- 6.046 During 1998-99 and so far this year, we have dealt with a number of issues related to problems in the relationship between a council and its chief executive. Notable examples include:
- the Rodney District Council, which has resulted in the unprecedented use of the Minister's review powers to disband the Council and appoint a commissioner; and
 - the Gisborne District Council, in response to its concerns about the actions of the Mayor and Chief Executive in connection with the millennium celebrations.
- 6.047 The chief executive is:
- the sole employee of the council of a local authority under section 119c of the Local Government Act 1974; and
 - responsible for employing, on behalf of the local authority, staff of the local authority.
- 6.048 Section 119c(3) requires that the local authority, in appointing a chief executive officer, should appoint a person who:
- (a) *Can discharge the specific responsibilities placed on the appointee; and*
 - (b) *Will imbue the employees of the local authority with a spirit of service to the community; and*

- (c) *Will promote efficiency in the local authority; and*
- (d) *Will be a responsible manager; and*
- (e) *Will maintain appropriate standards of integrity and conduct among the employees of the local authority; and*
- (f) *Will ensure that the local authority is a good employer; and*
- (g) *Will promote equal employment opportunities.*

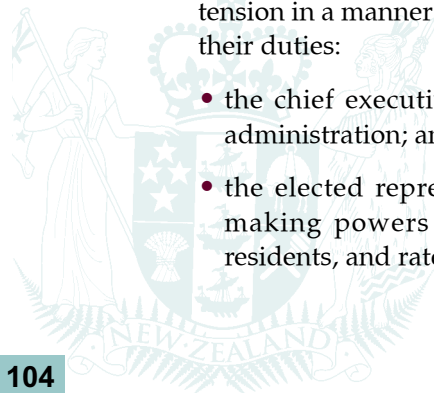
6.049 Section 119D sets out the responsibilities of the chief executive for:

- (a) *Implementing the decisions of the local authority;*
- (b) *Providing advice to members of the local authority and any community boards;*
- (c) *Ensuring that all functions, duties, and powers delegated to him or her or to any person employed by the local authority, or imposed or conferred by any Act, regulation, or bylaw are properly performed or exercised;*
- (d) *Ensuring the effective, efficient, and economic management of the activities and planning of the local authority.*

6.050 Because the chief executive is the link between decision-making by the elected members and service delivery by the staff, effective relationships with councils are of paramount importance in the ability of local authorities to achieve their objectives.

6.051 Being a local authority elected representative or a chief executive is a high-profile position, and for that reason tension is a natural part of the dynamic process of decision-making and accountability to communities. Both elected representatives and chief executives need to manage this tension in a manner that allows both to effectively discharge their duties:

- the chief executive to advise the council and lead the administration; and
- the elected representatives to exercise their decision-making powers in the best interests of the district, residents, and ratepayers.



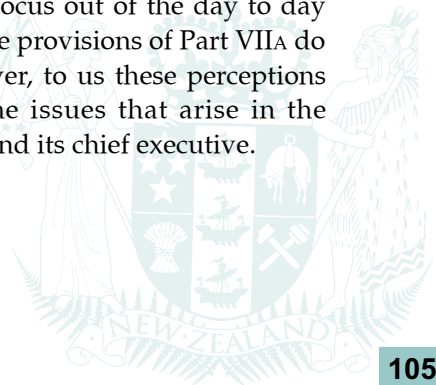
- 6.052 However, we believe that the range of issues we have seen raised in the last 18 months stemming from the relationship between council members and chief executives has increased. We are concerned by this increase and, while we are uncertain of the reasons, three contributing factors (among others) have been identified to us and are discussed in paragraphs 6.053 to 6.057.

Turnover in Elected Representatives

- 6.053 Each local body election since 1989 has seen a turnover of approximately one-third of all mayors. In 1998, over 41% of people elected had not previously held the position they were elected to.
- 6.054 Such rate of change requires both staff and elected representatives to negotiate their expectations and ways of working together. It is possible that this period of negotiation has not occurred as successfully for some local authorities as for others.

New Financial Management Regime

- 6.055 The 1996 amendments to the Local Government Act 1974 brought in a planning regime under which a framework is provided for councils to make their strategic long-term decisions. We have heard some councillors – accustomed to operating on an annual plan basis – say that the requirement to commit to a long-term direction has limited their decision-making discretion.
- 6.056 Some of the benefits reported to us by local authority staff are that these requirements help clarify the role of elected representatives by lifting their focus out of the day to day management. Of themselves, the provisions of Part VIIA do neither of these things. However, to us these perceptions shed light on the nature of the issues that arise in the relationship between a council and its chief executive.



Chief Executive Contract Renewal

6.057 The impact of the clarification during 1999 was that the Local Government Act requires chief executive contracts to be advertised no less frequently than every five years (see pages 33-35). This requirement was not the basis on which most councils and chief executives had been operating and, therefore, introduced a new element of uncertainty.

Future Work

6.058 In 1994, we published a guide entitled *The Employment of Local Authority Chief Executives*.⁴ We are conscious that, in the light of recent cases of friction between chief executives and their councils, this advice could be enhanced to better address issues associated with:

- managing the relationship with the chief executive by the diverse range of individuals who form a council and together comprise the “employer”; and
- the effective discharge of the chief executive’s duty to advise the council.

6.059 To do this we propose to seek information from local authority elected representatives and chief executives on:

- day-to-day issues and problems that emerge in relationships between elected representatives and their chief executives;
- perceptions of whether there are underlying factors that contribute to these issues and problems; and
- practical experiences of how issues have been successfully dealt with in a manner that maintains the confidence of elected representatives in their chief executive and allows them to effectively discharge their duties to their electing communities.

6.060 We anticipate republishing our guide and reporting later this year on any findings that result from our discussions with elected representatives and chief executives.

⁴ ISBN 0 477 02846 2.