



# **Peer Review of the draft report to the Ministry for the Environment on Administrative Costs of Proposed Freshwater Package on Regional Councils.**

**For the Ministry for the Environment.**

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## Purpose

1. The purpose of this peer review of the report on the impact of the Essential Freshwater package on councils is to check that the assumptions used, and the conclusions reached are credible and reasonable. It is intended that this review provides a comprehensive assessment of the report, highlighting any critical gaps in the analysis and areas where the report or underlying assumptions need further explanation.
2. Any review of this nature must reflect the context and intended purpose of the report that is being reviewed. The Castalia report is intended to be used to inform a Regulatory Impact Statement (RIS) that supports Cabinet consideration of the Essential Freshwater Package. This means that “credible and reasonable” must be considered in the context of a national assessment of impacts where there is considerable uncertainty, and this is only one of many matters that Cabinet will need to consider.

## The Reviewer

3. The review has been undertaken by Peter Winder. I have a Master of Arts degree with first class honours in geography from the University of Auckland. For the last ten years I have managed a consulting practice supporting a wide range of local authority and government clients across the country. My work has included:
  - advice to all regional councils on the interpretation and implementation of the first and second iterations of the NPS for Freshwater Management
  - compilation of best practice information on freshwater management across the regional councils
  - significant performance reviews and management advice for Environment Canterbury, Environment Southland, Horizons Regional Council, and the Otago Regional Council, Christchurch City Council, Southland District Council, Alexandra District Council and Far North District Council
  - advice on the potential for shared services across the Waikato, Bay of Plenty, Hawkes Bay, Canterbury and Southland regions
  - a review of the government financial assistance package for the Chatham Islands Council (for the Department of Internal Affairs)
  - developing for the Local Government Commission the local government re-organisation proposal for the Wellington region.
4. My most recent and relevant experience in relation to this review is the 9 month period over 2018 and 2019 in which I worked in depth with the Otago Regional Council to support the Chief Executive to develop new organisational strategy, restructure the organisation, and rebuild and re-shape its regulatory, consenting and compliance functions. Through this work I developed an in depth understanding of the costs and drivers of Otago’s approach to regulation and compliance, as well as the key differences between Otago and other regional councils.
5. I was one of the commissioners appointed to govern the Kaipara District Council in 2012 in order to turn around a dysfunctional council in financial difficulty. On the return of Kaipara District Council to a democratically elected council in 2016 I and was appointed as a Crown



Manager to resolve a number of outstanding litigation matters. That appointment ended in October 2019.

6. Before commencing my consulting practice in 2010 I was for 6 years the Chief Executive of the Auckland Regional Council. Immediately prior to that I was the Chief Executive of Local Government New Zealand.

## Approach

7. The peer review uses my experience and knowledge of the way in which regional councils operate, their business models, and their business systems and processes, to assess the credibility and reasonableness of the approach and assumptions used by Castalia and the conclusions that they have reached. The judgements set out in this report reflect my personal knowledge of regional councils and unitary authorities and my experience.
8. This review sets out a comprehensive assessment of the report and highlights some critical gaps in the analysis and areas where the report or underlying assumptions need further explanation.

## Assumptions, Critical Gaps and Further Explanation

### Cost drivers

9. The report correctly identifies that the key driver of additional costs for most elements of the package will be the additional staff that are required by each regional council to meet the new requirements. A methodology that uses increased staffing costs as the foundation of total cost estimates is therefore appropriate and relevant in the context.
10. Using the current number of consents as a way of estimating some costs is reasonable given the purpose of the report. It should be noted however, that the package is likely to result in some councils requiring quite a large number of consents where they currently have a permitted activity framework. Where this occurs, using the current number of resource consents to estimate future costs will result in an under-estimate of the costs.

### Different business models and site visits to support desk-top auditing

11. The methodology that has been adopted is driven by the labour costs required to implement each aspect of the programme. A key cost driver is the number of hours that would be required to audit farm plans. This is difficult because the scope and nature of a farm plan is still uncertain. The eight hours (on average) assumed for each audit could only be achieved if councils adopt a desktop audit model and no site visits take place.
12. There are risks associated with a desktop only audit process. It is likely that in the first round of farm plan auditing there will be considerable uncertainty on the part of landowners that may require intervention, or at least ground-truthing of enough farm plans to be confident that they are robust. In the second cycle of auditing and reporting there are likely to be landowners who have not undertaken the actions that they committed to in the first cycle and a degree of ground-truthing will be necessary to ensure that requiring farm plans actually



results in changes in on-farm practice. On-farm visits would significantly change the cost structure that Castalia has developed.

13. Regional councils have different business and engagement models that reflect a different reliance on desktop assessments and site visits, and different underlying levels of landowner regulatory compliance. Those councils that already have a high touch engagement model and regular site farm visits would find it considerably easier to integrate site visits for farm plan auditing into their other operations. For those council that currently have very low touch engagement models any move to include on-site assessments as part of an audit would involve significant cost.
14. Allowing for site visits would likely increase the cost per audit well above the 8 hour average assumed. I consider that the report would benefit from a discussion around this point and recognition that there will be both cost differences, but also qualitative differences in the regulatory outcomes and different regulatory compliance risks associated with different approaches.

### **The methodology relies on Waikato being representative enough to model cost increases – is it representative?**

15. For a large number of the cost elements the underlying assumption is that the estimated impact on staffing at the Waikato Regional Council can be used as the basis for estimating the impact on other councils. In the context of the report and its intended use, it is reasonable to use a method of this nature. It would be unnecessarily expensive to attempt to directly estimate the direct impact on each council. The issue is not so much the approach, as how the report deals with uncertainty and the variability of impact across the country and how material that may be for the overall cost estimate.
16. All regional councils have different business models that reflect, amongst other things, key differences in the extent to which they engage with land owners, the balance of effort that they devote to providing advice as opposed to compliance monitoring, and the extent to which they have already embraced the use of farm plans and/or land use consents for farming activities. Waikato has a well-developed business model with high levels of engagement. This may tend to mean that for others, with a considerably less intense business model, the impact would be proportionately larger. Given the reliance on Waikato for estimating impacts I think the report would benefit from a discussion on the how “representative” Waikato is and link that to the discussion on uncertainty in the overall cost estimates.

### **The approach probably understates some costs and excludes the early cashflow impact of some important costs**

17. In the context of making a national estimate of additional costs it makes sense to use the standard charge out rate for staff as the best current way of reflecting the total cost of the organisation – where the core cost driver is the number of staff.
18. In this instance the average fully loaded staff cost of \$145 per hour for staff is a reasonable approach but has limitations. Not all councils seek to recover all of their costs from consent applicants. This is intended to reflect the public good dimension of effective regulation. For some this ‘under-recovery’ is built into the charge out rate, for others it is reflected in policies which may mean the first hour of time is not charged, or the expectations of billable hours



are lower than would otherwise be the case. This means that the average fully loaded charge out rate may not reflect the current actual total cost.

19. Using the fully loaded charge out rate for staff will work well at the margin for costing additional staff. However, I consider that the total number of additional staff goes beyond a change at the margin. This raises an issue about the timing of some costs, as opposed to the overall quantum of costs.
20. From my direct experience, it if either Environment Southland or the Otago Regional Council needed to add even a relatively small number of additional staff they would need significant new office accommodation – even if the staff were distributed to locations across their regions. There would be related costs to increase the size of their vehicle fleet (especially if sites visits are part of the audit process). Over time these costs would be reflected in the fully loaded staff cost. However, the incidence of the costs will be at the beginning of the implementation period not spread out evenly over it.
21. In a related sense, the likely scale of changes in staffing will drive early recruitment and training costs that will be lumpy at the outset. Many of the disciplines that will require additional staff are already in short supply nationally, and there will be demand for people with those skills from consultants and others who are supporting landowners to develop and lodge plans and consent applications. A national shortage of skilled people will push up labour costs. Significant in-work training is likely to be required to develop the competencies required and that will all add to costs and mean that it will take time to reach optimal processing times. I think this at least warrants discussion in the report because it goes to both the profile of costs, but also to implementation risks. If the regional councils are unable to recruit and train the necessary staff, they will not be able to implement the package.
22. Perhaps the most significant other cost will be a systems development cost associated with the management of this new type of farm plan and the number of farm plans that will need to be maintained. Some councils already manage farm plans. Others have regulatory or consent systems that are not equipped to manage the nature or volume of farm plans required by the package. The scope of possible changes to regulatory or consent systems which are likely to be required is unknown and would be difficult to estimate. They may add considerable front-end costs to implementing the package. The need for IT systems change would also add to the implementation risk of the package. I think these issues at least warrant discussion in the report.
23. The nature and timing of the costs discussed above means that the estimated cost of new requirements set out in Figure 4.1 (showing annual expenditure between 2021 and 2026) is likely to underestimate both total costs and the costs in the early years.

## **Non-staff Plan Change Costs**

24. A number of the package requirements include changes to plans and rules under the RMA. While the NPS requires changes that have a particular effect, there remains considerable scope for costly processes and potential appeals associated with, for instance, the specific thresholds for in-stream sediment and where they specifically apply, or the specifics of the rules that are developed to ensure that in-stream sediment levels reduce.
25. Plan changes are costly, and generally involve considerable external costs associated with legal advice, advice and evidence from recognised experts, and significant public engagement and consultation. These costs can extend into the millions of dollars for complex



and highly contested plan changes where high levels of expert evidence are required and there are complex and conflicting submissions reflecting irreconcilable views. Castalia's approach does not adequately addresses these costs. I think they ought to be included because the NPS will require a number of changes to each RPS and a number of regional plans. For some regional councils this will need to involve the whole architecture of their plans and possibly combining separate, standalone regional plans into more comprehensive documents. This will in part be addressed through the national planning standards – but I feel the report should at least consider these costs and whether or not they should be counted.

## **Cost of Sediment Management**

26. From the level of detail provided it is not possible to comment on the nature of the assumptions or the robustness of the estimates of the additional cost associated with the sediment management part of the package.

## **Cost of addressing Māori involvement in freshwater management and Te Mana o Te Wai**

27. Across the regional councils there is considerable variation in the current level of involvement by Māori in freshwater management and in the extent to which a long-term vision for Te Mana o Te Wai has been developed. This reflects the different mix of pre and post-settlement iwi and the underlying robustness of relationship and partnership between regional councils and the iwi and hapū within whose roponen不分 they operate. The cost of delivering meaningful involvement in freshwater management will vary across the country depending on the nature and depth of that engagement with relevant iwi and hapū. For some, I suspect this will require a wholesale shift in the nature and basis of relationship and is likely to include a requirement to resource hapū to effectively engage. In those instances, the costs are likely to significantly exceed 1.5 additional FTEs per council.

## **Understanding the significance of the increase**

28. The report estimates the total cost of the package for regional councils nationally and the average cost per council. This is the key number required, however, it would have far more meaning, and make a more meaningful contribution to the policy debate and consideration if it was put into the context of current regional council expenditure. It is difficult to express the increase as a proportion of existing expenditure on freshwater because of the different ways that regional councils report their activities. But it would be helpful to express the increase as a percentage of total current regional council operating expenditure. Given that this increase would need to be funded by increases to rates or user charges (or both), expressing it as a percentage of total operating costs would put it in perspective.

## **Allocating Costs to Regions**

29. The discussion on pages 17 and 18 and Table 3.19 explores the costs to each regional council. Table 3.19 appears to set out the cost drivers and the assumed proportion of the variable cost that have together been used to allocate variable costs to each region. The report provides no explanation of the methodology that has been used here. Neither does it provide any justification for the assumed proportion of variable costs related to each cost driver. In the absence of any explanation or justification of these assumptions I have no way



of knowing whether these are reasonable assumptions or not. This goes directly to the reliability and usefulness of the reported costs by region.

30. One of the overall conclusions discussed below is that the report does not adequately deal with uncertainty in the cost estimates. The greatest level of uncertainty in the estimates is likely to be at the most detailed level of the estimates. The estimates of costs, by activity, by region on pages 23 and 24 will have the highest level of uncertainty. It is important that decision-makers understand that, and the likely range of uncertainty that surrounds the estimates.
31. If one of the intended or possible uses of the report is to consider the level of assistance that may be provided to regional councils to implement the package, I consider that the reported cost to each council would require attention. This would usefully include ground-truthing the assumptions by working a bottom-up cost assessment (similar to the Waikato estimates that have been used to drive the analysis) for one or two other regions to test whether that approach gives a similar cost estimate to the approach used in the report.

## Specific Comments

32. Introduction (page 1) – the text does not consistently deal with “**additional**” costs, it refers to “total administrative costs”, “the costs of new requirements”, “administrative costs”, and “the costs estimated here”. It would be useful to have a consistent and clear definition of the focus of the report – which is presumably on “additional costs”.
33. Section 2 page 2 – the first paragraph states “We have assessed these new requirements to identify the exact requirements for new resources ...” – given the uncertainty that is involved in the estimates in the report these should not be referred to as “exact requirements”.
34. Page 4 second box – “ply” should be apply.
35. Page 4 – Improving contact recreation. This is not a material matter, but the approach adopted depends on the current contact recreation monitoring being comprehensive enough to meet the new requirements. This qualification may be worth noting.
36. Page 8 second paragraph – councils will only be able to debt fund capital expenditure that is relevant to this activity. Councils must operate a balanced budget and, other than in exceptional circumstances, do not borrow to fund operating costs.
37. Table 3.15 Costs of Measuring and Reporting Water Takes – without reviewing the Manawatu-Whanganui work it seems at face value that this estimate may not consider the costs of monitoring, compliance and enforcement activity associated with takes of this nature. Small takes like this are likely to have high levels of technical non-compliance with water measurement standards and require considerable and quite labour intensive follow up. These costs will not be material in the overall estimate of package costs, but should at least be noted, or confirmed to be part of the Manawatu-Whanganui estimates.
38. Page 16 - The estimated cost for a new consenting regime for stock holding areas and feedlots appears to only be the cost for processing consent applications and does not seem to include likely additional compliance and enforcement costs. These costs will not be material but will be real.



39. Page 10 Table 3.3 – “non-notified content” should be “non-notified consent”.
40. Page 17 – first paragraph – “les than a third” should be “less than a third”.

## Overall conclusions

41. My overall conclusions are that:

### **The methodology is generally defendable**

42. The approach is generally appropriate for the intended use and purpose of the analysis. That is, to provide a national estimate of the costs that regional councils will incur to implement the freshwater package.
43. The methodology for estimating the costs for each individual region is less transparent and the more detailed the breakdown of costs (by region, by element of the package), the greater the level of uncertainty there will be over the estimates.

### **There is considerable uncertainty over cost impacts**

44. Overall I consider that the report does not express the level of uncertainty around the cost estimates clearly enough. The commentary on pages 25 and 26 suggests a considerable range between the lower and higher estimates based on the three largest cost items. At the high end of the range of uncertainty that is explored, the total cost would be around \$50m (27%) higher than the stated estimate. That is a significant variation. Decision-makers should be aware of the level of uncertainty and the potential for actual costs to be significantly higher than the core estimated level.

### **The estimated costs are probably at the lower end of potential impacts**

45. There are number of factors that are not explicitly included in the cost estimates. The most significant of these is likely to be the external costs associated with multiple, significant and complex plan change processes. The potential significance of the cost factors that are not included mean that the estimated costs are probably at the lower end of potential impacts.
46. In addition, there are likely to be significant set up costs that mean that the incidence of costs will be earlier than has been estimated. For some councils that required increase in staff will trigger costly and difficult decisions about office accommodation and some fundamental changes to their business model and systems.

### **None of the identified issues make this work unsuitable for the purpose for which it is intended**

47. As with any national level assessment of costs of this nature, Castalia relies on a number of simplifying assumptions in order to cost-effectively produce an estimate of potential impacts. None of the issues identified in this peer review make the work unsuitable for the purpose for which it is intended. However, greater clarity of the limitations of the work would provide the users with more confidence and with more clarity over how it can be interpreted.