



## **Petition 2005/106 of Penelope Bright and 40 others**

Report of the Local Government and  
Environment Committee

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Forty-eighth Parliament  
(Steve Chadwick, Chairperson)  
September 2007

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*Presented to the House of Representatives*

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## Petition 2005/106 of Penelope Bright and 40 others

### Recommendation

We have examined petition 2005/106 of Penelope Bright and 40 others and recommend that the House take note of our report.

### Background

The Local Government and Environment Committee has considered petition 2005/106 of Penelope Bright and 40 others requesting that the House conduct an inquiry into the charging and other practices of Metrowater and Watercare Services Ltd, and the actions and practices of Auckland City Council's Finance and Corporate Business Committee.

#### Metrowater

Metrowater is one of six local network operators providing water and waste water services in the Auckland region. Metrowater provides these services to approximately 140,000 homes and businesses in Auckland city. Auckland City Council is the sole shareholder of Metrowater, which was established in 1997 as a charitable local authority trading enterprise. It became a council controlled organisation under the Local Government Act 2002 and has retained its charitable constitution and its ability to make tax-exempt charitable payments to the council.

#### Watercare Services Ltd

Watercare Services Ltd provides water to all six local network operators (including Metrowater) in the Auckland area, who retail it to residential and business customers. Watercare also provides waste water services to four of the six local network operators. Watercare is owned jointly in unequal shares by councils in the Auckland region and is a council organisation under the Local Government Act 2002. Watercare is also regulated by parts of the Local Government Act 1974.

### Charitable payments by Metrowater to Auckland City Council

Metrowater's constitution requires it to pay any profits not reinvested in the company as charitable payments to its shareholder, Auckland City Council. Money that is passed to the council in this way is tax exempt. The council can use payments from Metrowater only for charitable purposes, which its constitution defines in terms of the Income Tax Act 1994.<sup>1</sup> This definition includes any matter beneficial to the community. The constitution includes water and waste water services as examples of charitable purposes.

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<sup>1</sup> This Act has been superseded by the Income Tax Act 2004.

The first charitable payments from Metrowater to the council were made in the financial year 2003/04. During the 2003/04, 2004/05 and 2005/06 financial years the council received charitable payments of between five and twelve million dollars per annum.

In the process of preparing its 2006–16 Long Term Council Community Plan, the council advised Metrowater that it expected significantly larger charitable payments from Metrowater in the future. Between 2007 and 2017, the council expects charitable payments totalling approximately \$324 million.

**Table 1: Charitable payments expected by Auckland City Council from Metrowater in the financial years ending 30 June 2007 to 30 June 2017**

Year	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
\$000	18,018	24,118	26,218	28,518	31,018	33,516	36,218	39,118	42,118	45,316	38,100

Source: Office of the Auditor-General, Briefing, 26 July 2007, p. 2.

The council informed us that these charitable payments were required to pay for upgrading the city’s stormwater system, which fits within the definition of a charitable purpose in Metrowater’s constitution.<sup>2</sup>

### Charitable payments expected by Auckland City Council

Auckland City Council’s expectation that it receive charitable payments appears to conflict with clause 3.2.2 of Metrowater’s constitution, which prevents the council, in its capacity as shareholder, from influencing the amount of any charitable payment by Metrowater. This apparent contradiction highlights the complexities of Metrowater’s relationship with the council.

We were informed by the Office of the Auditor-General that both Metrowater and Auckland City Council have received reliable legal advice declaring that the council is acting within the law in setting the amount of the charitable payment, which it does through Metrowater’s Statement of Intent (SOI). Metrowater is required to issue an SOI each year in accordance with the Local Government Act 2002, and the council, as shareholder, can use this process to influence Metrowater’s operations, by including an expectation of a certain level of return on its investment. The council can exercise this right when Metrowater submits the SOI to the council for consultation, or by using measures intended to allow the shareholder to modify the SOI at other times. The council has exercised this right in recent years. In particular, when consulting with Metrowater over its 2006 SOI the council asked Metrowater to alter its financial planning to ensure that Metrowater would provide the council with a certain amount in charitable payments. Metrowater complied with this request.

The council’s legal advice is that such use of the SOI process to determine the charitable payments received by the council does not contravene Metrowater’s constitution. Clause 3.2.2 of the constitution was intended to ensure that individuals could not direct

<sup>2</sup> Submission from Auckland City Council, 12 June 2007, p. 3.

Metrowater's funds for their own benefit, and to provide the means by which Metrowater was to be tax exempt. Because the council can use the payments only for charitable purposes, it is not breaching the intention of the constitution.<sup>3</sup>

### **Increased water charges and the charitable payment**

We considered the indication in Auckland City Council's consultation documents of the rate at which water charges would rise after 2006. During public consultation to arrive at its Long Term Council Community Plan for 2006—16 the council issued a Statement of Proposal, which included discussion of the council's expectation of increased charitable payments, and how they would be expended. This document discussed various options, one of which involved Metrowater raising its water and waste water charges in order to make a larger charitable payment to help fund an upgrade to the city's stormwater system. The increase was described as "modest" and "small".<sup>4</sup>

The council and Metrowater undertook modelling, which suggested that water charges might increase by 6.5 percent in 2006/07, by 5.5 percent in 2007/08 and by 3 to 4 percent in subsequent years. The description of increased water charges as "modest" relied on these initial figures. However, these figures were raised during negotiations between the council and Metrowater on Metrowater's SOI for 2006/07. Water charges were forecast to increase by 8.05 percent in 2006/07 and by approximately 3 percent in following years. Subsequent revisions of these figures resulted in a forecast increase of 9.1 percent for 2007/08, with increases of between 5 and 11 percent for later years. The final forecast increases were substantially influenced by the council's requirement that Metrowater make charitable payments to the council.

The council should ensure that the information given to the public in consultation documents is accurate and we consider the description of the price rises in the Statement of Proposal not to have met this standard. Nor did the council's assessment of increased water charges as "modest" acknowledge increases that had taken place over the previous three years to meet the council's expectation of receiving charitable payments.

The price increases are significant. Auckland City Council estimated that the 9.1 percent increase Metrowater instituted from 1 July 2007 would result in an increase of \$7.50 per quarter for low users (to total \$82 per quarter), \$25 per quarter for medium users (\$274 per quarter), and \$45.50 per quarter for high users (\$500 per quarter). The average household fits between low and medium use and its bill is likely to be \$177.50 per quarter for approximately 183 cubic metres of water per annum.<sup>5</sup> These figures include a prompt payment discount.

In providing water to Metrowater, Watercare is required by its constitution to keep its prices to a minimum relative to the consumer price index. Watercare has not increased its water charges in 2007.<sup>6</sup> Watercare charges Auckland City Council and four of the other six

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<sup>3</sup> Office of the Auditor-General, Briefing, 26 July 2007, p. 5 and Briefing, 21 August 2007, pp. 1—4.

<sup>4</sup> Office of the Auditor-General, Briefing, 26 July 2007, p. 6.

<sup>5</sup> Figures taken from url:<http://www.ourwater.co.nz/prices/default.asp>.

<sup>6</sup> For example, for the period 1 July 2005 to 30 June 2008 Watercare set the price at which it charges the local network providers like Metrowater at the Consumers' Price Index minus three percent. Submission from Watercare Services Ltd, 11 June 2007, p. 7.

local network providers 45 cents per cubic metre for water, but this will rise to 50 cents from 1 July 2008. In July 2007 Metrowater raised its price from \$1.28 per cubic metre of water (including GST) to \$1.40 per cubic metre. Metrowater's price for water is higher than its counterparts in the Auckland region, whose prices will range from \$1.15 to \$1.32 per cubic metre. (These figures do not take into account prompt payment discounts, and exclude the unusually high Rodney District Council prices, which include a surcharge to pay for the Orewa no. 1 water main.)<sup>7</sup>

### **Public consultation**

We consider that the council should have kept the public better informed about the charitable payments, the rise in water rates, and the decision made to direct the payment from Metrowater into upgrading the Auckland stormwater system. We note that while the council issued its draft Long Term Council Community Plan in its Statement of Proposal for public consultation, and received submissions on it, as the details of the council's negotiations with Metrowater over its SOI are not required to be open, the public of Auckland was not well informed about the process by which charitable payments were to be used to upgrade Auckland's stormwater system. We consider that the Long Term Council Community Plan could have been more transparent on this matter. This situation shows the importance of the council consulting with the community, and the provision of full, accurate information.

In future the council should ensure that the public is better informed and that its decision-making process is transparent. We note the advice that the council and Metrowater acted within the terms of Metrowater's constitution and the letter of the law, but we consider that for a public body to stretch the charitable payments provisions to this degree was unwise and harmful to the public's trust in this local authority.

### **Charitable payment not best practice**

We are, nevertheless, concerned about the council's use of charitable payments. While other councils receive dividends from companies that they own, no other council receives charitable payments on the scale of the forecast payments by Metrowater to Auckland City Council. The availability of such large charitable payments has implications in other areas. For example, it may mean that the council can avoid increasing rates to the extent that might otherwise be necessary. We are concerned that raising large amounts of money in this way avoids the public scrutiny to which the collection of revenue by councils should be subject.

We consider that the charitable payments engineered by the city council from Metrowater were on a scale that undermined the intent of the constitution of Metrowater when it was established by the council. If the council had intended payments on this scale (\$324 million), it should have revised the constitution of Metrowater rather than abusing the provisions providing for charitable payments.

We consider that the use of charitable payments in this way, and to this extent, is not best practice, and emphasise our concern that it should not be adopted by other local

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<sup>7</sup> Submission from Watercare Services Ltd, 11 June 2007, p. 6.

authorities. It is not acceptable. We strongly advise Auckland City Council to reconsider its requirement for charitable payments from Metrowater in the years 2007 to 2017.

### **Revision of Metrowater's constitution**

We consider that Metrowater's constitution does not accurately reflect the way the company's relationship with the council has developed. The council has asked the Commissioner of Inland Revenue to make a binding ruling on Metrowater's tax status and the charitable payments it makes to the council. The council does not wish Metrowater's constitution to be amended until this ruling is made. When that process is complete, Metrowater's constitution should be amended to clarify the status of the council's influence over the company and the nature of payments the company makes to the council.

### **Grievances of Metrowater customers**

Submissions from the petitioner contained details of a number of personal grievances of Metrowater's customers. Select committees are not a court of last resort for the resolution of disputes of this kind, so we will not comment on this issue.

### **Conclusion**

Our detailed examination of the petition has revealed some significant concerns about the use of charitable payments as a source of revenue for Auckland City Council. We consider that our report will serve to bring these concerns to the attention of the council, and the public. Therefore, having examined all the relevant facts, we do not endorse the petitioner's call for a commission of inquiry.

### **Summary of conclusions**

- We consider Auckland City Council's description of the price rises for Metrowater customers as "modest" and "small" in the Statement of Proposal to have been misleading and to have led to the anxiety and concerns behind the petition.
- We consider that the scale of the charitable payments engineered by the city council from Metrowater undermined the intent of the constitution of Metrowater when it was established by the council. The council should have revised the constitution rather than abusing the provisions providing for charitable payments. We consider that Metrowater's constitution should be amended anyway, in order to clarify this relationship.
- We consider that the council could have kept the public better informed about the charitable payments, the rise in water rates, and the decision made to direct the payment from Metrowater into upgrading Auckland's stormwater system. In future the council should ensure that the public is better informed and that its decision-making process is transparent.
- We note, however, the advice that the council and Metrowater acted within the terms of Metrowater's constitution and the letter of the law, but we consider it unwise for a public body to stretch the charitable payments provisions so far, and this undermined the public's trust in this local authority.

- We consider that the use of charitable payments in this way, and to this extent, is not best practice, and emphasise our concern that it should not be adopted by other local authorities.
- We strongly advise Auckland City Council to reconsider its requirement for charitable payments from Metrowater in the years 2007 to 2017.

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## Appendix

### Committee procedure

Petition 2005/106 of Penelope Bright and 40 others was referred to the Local Government and Environment Committee of the forty-eighth Parliament.

### Submissions received

We received submissions from the petitioner, Watercare Services Ltd, Auckland City Council, Metrowater, North Shore City Council's Infrastructure (Water) Services Division, the Department of Internal Affairs and the Office of the Auditor-General. We heard evidence from the petitioner, Auckland City Council, Metrowater Ltd, the Department of Internal Affairs and the Office of the Auditor-General.

### Committee members

Steve Chadwick (Chairperson)  
John Carter (Deputy Chairperson)  
Mark Blumsky  
Jacqui Dean  
Russell Fairbrother  
Martin Gallagher  
Hon Marian Hobbs  
Hon Dr Nick Smith  
Mētiria Turei