



**Notice of the Ordinary meeting of**

## **Audit and Risk Subcommittee**

***Kōmiti Iti mō te Tātari Kaute me te Tūraru***

Date:	Thursday 21 May 2020
Time:	Commencing at the conclusion of the Governance and Finance Committee meeting
Location:	via Zoom

## **Supplementary Agenda**

### ***Rārangi take***

**Chairperson**

Mr John Peters

**Members**

Her Worship the Mayor Rachel Reese

Cr Judene Edgar

Mr John Murray

Cr Rachel Sanson

**Quorum 3**

**Pat Dougherty  
Chief Executive**

Nelson City Council Disclaimer

Please note that the contents of these Council and Committee agendas have yet to be considered by Council and officer recommendations may be altered or changed by the Council in the process of making the formal Council decision. For enquiries call (03) 5460436.

**1. Reserves Contributions for Unit Titles –  
Final Report****4 - 13**

Document number R16954

Note: This report is identified as item 12 on the main agenda.

Recommendation

***That the Audit and Risk Subcommittee***

- 1. Receives the report Reserves Contributions for Unit Titles - Final Report (R16954) and its attachment (A2369193).***

**CONFIDENTIAL BUSINESS****2. Exclusion of the Public**

Recommendation

***That the Audit and Risk Subcommittee***

- 1. Excludes the public from the following parts of the proceedings of this meeting.***
- 2. The general subject of each matter to be considered while the public is excluded, the reason for passing this resolution in relation to each matter and the specific grounds under section 48(1) of the Local Government Official Information and Meetings Act 1987 for the passing of this resolution are as follows:***

Item	General subject of each matter to be considered	Reason for passing this resolution in relation to each matter	Particular interests protected (where applicable)
1	<b>Reserves Contributions for Unit Titles - Breakdown of Discrepancies</b>	<p>Section 48(1)(a)</p> <p>The public conduct of this matter would be likely to result in disclosure of information for which good reason exists under section 7</p>	<p>The withholding of the information is necessary:</p> <ul style="list-style-type: none"> <li>• Section 7(2)(g) To maintain legal professional privilege</li> <li>• Section 7(2)(h) To enable the local authority to carry out, without prejudice or disadvantage, commercial activities</li> </ul>

---

## **Reserves Contributions for Unit Titles - Final Report**

---

### **1. Purpose of Report**

- 1.1 To inform the subcommittee of the underlying causes for inconsistent calculation of reserves contributions during the period from September 2004 to July 2018.

### **2. Recommendation**

***That the Audit and Risk Subcommittee***

- 1. Receives the report Reserves Contributions for Unit Titles - Final Report (R16954) and its attachment (A2369193).***

### **3. Background**

- 3.1 The Audit and Risk Subcommittee requested a copy of the final report at the meeting on 18 February 2020 to better understand the causes of discrepancies which arose during the period from September 2004 to July 2018 in the calculation of reserves contributions for unit title subdivisions.

### **4. Discussion**

- 4.1 The attachment Reserves Contributions for Unit Titles – Final Report on Investigation (A2369193) refers.
- 4.2 As previously reported to the Subcommittee, no fraudulent activity was found.
- 4.3 The main finding of the report is that in the 14 year period from 2004 to 2018 reserve contribution requirements in the Nelson Resource Management Plan (NRMP) have been applied inconsistently accounting for under-recovery of \$527,000 and a potential future shortfall of \$947,000. Of the 28 unit title subdivisions processed, 19 were correct and 9 used incorrect valuations.

## Item 12: Reserves Contributions for Unit Titles - Final Report

- 4.4 During this period, reserves contributions were imposed on resource consents as a condition of consent. The calculation of the amount of the contribution was reliant on a professional valuation.
- 4.5 Council imposed financial contributions for reserves and community services on unit title subdivisions using two different valuation methodologies, depending on which consent condition was imposed on the relevant resource consent. One method closely aligned with the financial contribution provisions of the Nelson Resource Management Plan (NRMP) while the second did not. The first methodology was based on the market value of each additional unit created by the subdivision while the second provided for the value to be based on a notional figure, which was effectively the value after accounting for the cost of developing the unit of land together with its improvements.
- 4.6 The second methodology was first used in 2003 and this approach was only valid during the transitional phase of the Resource Management Act 1991 when financial contributions changed over from the Local Government Act 2002. Chapter 6 of the NRMP was in place from 1 September 2004 and the conditions should have been imposed in accordance with the provisions of Chapter 6 from then on.
- 4.7 The methodologies give two different financial outcomes. One is consistent with the NRMP while the second one results in a lesser valuation and therefore a lower reserves contribution.
- 4.8 The primary cause for this failure was a variable level of knowledge, experience and resource available within the processing team. This meant that in many instances the complexities and changes to subdivision rules during this period were not fully understood. This resulted in differing interpretation of rules, and explains why the processes for unit title subdivisions, which had already been established prior to the change in 2004, were not questioned or updated by any of the many different officers involved over the 14 year period.
- 4.9 From 1 July 2018, Chapter 6 of the NRMP no longer applied and so the inconsistent application of those provisions did not continue. Council's Development Contributions Policy 2018 provides the clarity necessary for consistent interpretation.
- 4.10 The following has occurred since this issue was first identified:
- 4.10.1 An independent review by an external consultant was performed in May 2019. Their report highlighted that the team was relatively small compared with the volume of applications and broad range of consent types processed; and there was a lack of depth of experience across all consent types but notably in the specialist areas of land subdivision and other complex consent applications. Actions taken as a result of the independent review include –

## Item 12: Reserves Contributions for Unit Titles - Final Report

- Instigation of a peer review process of the application of development contributions, both at resource consent and building consent stages.
- The appointment of a principal planner to lift the level of expertise particularly for more complex consents.
- A dedicated senior subdivision planner is currently being recruited to further bolster the Resource Consents Team to ensure appropriate oversight of development contributions.

4.10.2 This internal audit has been undertaken. Recommendations from the audit have already begun to be implemented. In addition to the changes mentioned above, these include –

- Continuing with the plan for additional staffing resources.
- Assigning responsibility for continuous process and document improvements relating to all consenting and closing any quality assurance gaps from the use of contractors.
- Allowing for more emphasis on professional development in resource planning.
- Considering whether the financial processes related to contributions fit better with Finance.
- Considering a standard mechanism to provide evidence that all comparable developments are treated equally and in accordance with the rules.

4.11 This was an unfortunate situation brought on by complex, changing rules and the lack of experience of staff members. Officers have confidence that the checks and balances that are now in place ensure that the process is more robust and the risk of this situation reoccurring is low.

**Author:** Lynn Anderson, Internal Audit Analyst

### **Attachments**

Attachment 1: A2369193 - Reserves Contributions for Unit Titles - Final Report  
[↓](#)



**Review of  
Reserves Contributions for Unit Titles  
FINAL Report**

**For Audit & Risk Subcommittee**

**April 2020**



**Contents**

AUDIT OBJECTIVES: ..... 3

AUDIT SCOPE:..... 3

NOT IN SCOPE:..... 3

BACKGROUND/METHODOLOGY: ..... 3

LIMITATIONS: ..... 4

EXECUTIVE SUMMARY: ..... 5

KEY FINDINGS: ..... 6



<b>AUDIT:</b>	<b>Reserves Contributions for Unit Titles</b>	<b>AUDIT DATE/s:</b>	Dec - Feb 2020
<b>AUDITOR/s:</b>	Lynn Anderson		
<b>AUDIT OBJECTIVES:</b>			
To understand and report on the underlying reasons for discrepancies in the calculations of reserves contributions for unit title subdivisions during the period between 2004 and 2018;			
To evaluate current process and controls to help ensure accurate calculation of reserves contributions, and make recommendations for improvements in order to minimise the chance that incorrect calculations will occur in the future.			
<b>AUDIT SCOPE:</b>			
This audit is carried out on the principles of a 'sampled audit process'; care is taken to extract relevant information from as broad an area as possible during the allocated time. Objective evidence and reference material is gathered and or reviewed during the audit.			
The audit has taken into account the following primary elements relevant to the area being audited:			
<div><div>-</div>Discrepancies relating to reserves contributions decisions and calculations which occurred during the years between 2004 – 2018</div> <div><div>-</div>Ongoing risks related to current reserves contributions procedures</div>			
<b>NOT IN SCOPE:</b>			
Comment on whether the fees and charges relating to reserves contributions established by Council are fair or reasonable; reserves contributions that <u>do not</u> relate to unit title subdivisions; reserves contributions relating to building work. There is no reference to the recent audit which identified there was no evidence of fraudulent activity relating to these discrepancies - as this has been reported separately to the Audit and Risk Subcommittee.			
<b>BACKGROUND/METHODOLOGY:</b>			
<b>Background</b>			
This audit was triggered when a developer questioned the inconsistency between assessments for reserve contributions on two separate unit title developments. An initial investigation found they were calculated using different consent conditions - 1) the registered valuation of the footprint of each unit (less base unit) at the time of consent; 2) the capital value of each unit (at time of sale) less value of improvements including profit & sales costs. The initial investigation also found that this condition matched the Environment Court ruling in the 2000 case <i>Esplanade Investments Limited v Christchurch City Council</i> .			
The Environment Court ruling related to section 407 of the Resource Management Act (RMA), which effectively kept old Local Government Act (LGA) provisions alive where Councils had not yet put financial contribution provisions in its District Plan and provided the discretion to Councils to impose a contribution under that regime which must not exceed 7.5% of the value of the allotments that are			

intended to be used principally for residential purposes. Chapter 6 of the Nelson Resource Management Plan (NRMP), operative from 1 September 2004, gave Council the mechanism to impose contributions conditions (including for reserves) on every subdivision consent. From 1 September 2004 the Environment Court ruling should no longer have been applied by Council for land valuations.

Further investigation revealed other instances during the period from 2004 – 2018 where non-compliance with Council's reserve contribution policy may have occurred for unit title subdivisions which are estimated to total \$1.47m.

### **Methodology**

This audit is sectioned into two to provide -

1. A better understanding of the circumstances present at the time when the discrepancies occurred between 2004 – 2018:
  - 1.1. Methodology to achieve this:
    - Reviews of -
      - 1.1.1. The consents which have already been identified during this period as not complying with legislation or Council rules;
      - 1.1.2. Applicable legislation and other rules relevant to the above;
      - 1.1.3. Managers' job descriptions;
      - 1.1.4. Standard processes, controls, guidance, tools, and documentation related to the decision-making process for these reserves contributions;
      - and
      - 1.1.5. Interviews with current Officers who had some involvement with the files.
2. An evaluation of current practice to identify future improvement opportunities, including where these could help Council meet its responsibilities under the Local Government Act (Section 197AA) which states that the purpose of development contributions (which include reserves contributions) is "to enable territorial authorities to recover from those persons undertaking development a fair, equitable, and proportionate portion of the total cost of capital expenditure necessary to service growth over the long term":
  - 2.1. Methodology to achieve this:
    - Reviews of
      - 2.1.1. The efficacy of current processes, controls, guidance, tools and documentation related to the assessment and calculation of reserves contributions;
      - 2.1.2. The allocation of consent files and the use of contractors;
      - 2.1.3. Knowledge generally in relation to contributions, as well as process and documentation development in response to rule changes that affect contributions;
      - and
      - 2.1.4. Interviews with Officers.

### **LIMITATIONS:**

The quality of documentation, monitoring and management of the various consents will only be commented on at a high level. Further, the Internal Audit Analyst is not a subject matter expert and

there may be justification for choosing not to apply reserves contributions in some instances where it has been indicated otherwise in this report.

#### **AUDIT CRITERIA:**

The criteria for this audit are based upon using good practice auditing protocols and audit processes for assurance and continuous improvement.

#### **EXECUTIVE SUMMARY:**

##### **Incorrect Determinations 2004 - 2018**

Reserves Contributions have provided Council with revenue of between \$2m-\$3m each year. The incorrect determination of these, or failure to be seen as fair or consistent, exposes Council to financial, legal and reputational risk - as has recently been identified. There is no question that the resource consent process for unit title subdivisions is complicated, made more so as these developments more often than not extend over multiple years. During the period a consent is active, policy or legislation can change, and staff may leave. The processing of these requires specialised knowledge and a well-considered, careful and consistent approach, supplemented by strong processes, tools and controls. Counter to this, are the statutory timeframes imposed on the processing of consents.

What happened between 2004 and 2018? We confirmed the processes and rules relating to subdivisions were complex and time-consuming, particularly for those not working with them regularly. The complexity alone led to different interpretations by multiple officers. Further, when the Nelson Resource Management Plan became operative from 1 September 2004, which was the trigger for the notional value to cease as the acceptable method of calculating reserves contributions, there was simply a failure to link this change with practice. We were informed that the writing of policy rested with a separate team created in 1994 although the Manager Consents 1999 job description included the responsibility to "write policies and prepare plans that will implement the requirements of the legislation for Nelson". This apparent overlap in responsibility may in part explain why the failure occurred.

It was clear from our review that throughout, officers believed they were applying the correct reserves contribution condition of consent for unit title subdivisions. Further, knowledge gaps or misinterpretations of legislation and rules were not restricted to the Resource Consents business unit. One effect of this was that when a negative land valuation arose, no action was taken by officers outside the Resource Consents team who were aware of this. In an environment where the lines of responsibility were blurred, resources limited, rules often changing, and specialist knowledge limited or its transfer informal and adhoc, realistically inconsistencies and inaccuracies were inevitable.

Officers identified that during the period from 2004 - 2018, incorrect conditions of consent have put at various levels of risk estimated reserves contributions revenue of around \$1.47m.

### Evaluation of Current Practice

It was reassuring to find there have been a number of improvements since 2018. For example, the wording in the Policy provides greater clarity than has previously existed and is therefore easier to interpret. This should lead to a reduction in inconsistent decisions. Further, since an external review of resource consents processes in February 2019, there has been a positive increase in knowledge through the appointment of a principal planner, and a team leader who has the responsibility for a large percentage of peer reviews.

Specialist subdivision or financial knowledge is still lacking, however we understand that the appointment of a subdivision specialist is planned. In our view this would link policy to practice and go a long way to help ensure a more accurate and consistent approach to reflect Council's development contributions strategy.

Other key areas where we identified potential improvements to current processes, controls and tools are shown below under *Key Risks*. Note that these improvements are not exclusive to the Resource Consents team. Resource Consents are still required to obtain a current land valuation in order to calculate the Neighbourhood Reserves contribution, but the decision whether contributions apply is not their responsibility under the current Policy.

### Closing Comment

Finally, as a general comment, to manage Council's possible future risk, we recommend –

1. The subdivision consents which are still open and include the notional value should be flagged and monitored, and Senior Management and Council should be kept abreast of any changes to risk;
2. At s224 stage, all consents approved before 1 July 2018 are peer reviewed by someone with a high level of expertise and knowledge of the applicable financial contribution regime to at least check the financial and development contribution aspects;
3. Senior Management decide if Finance should take over the financial processes relating to Development Contributions.

### KEY FINDINGS:

#### 2004 – 2018

- 1) There was a failure to translate the changes from the 2004 Nelson Resource Management Plan into practice
- 2) The gap between policy development and its practical application may have been due to duplication of responsibilities relating to policy formation or deficient communication
- 3) The decision as to whether reserves contributions applied was particularly complex over this period due to multiple legislative and rule changes
- 4) There was clear evidence of inadequate reserves contributions knowledge across multiple areas of council
- 5) No one took responsibility for understanding or acting on the unusual outcome of a negative valuation with its implications to Council's revenue

- 6) The determination of conditions for unit titles consents is complex and it was found that throughout the process more emphasis and expertise was directed towards non-financial conditions, including at each peer review stage
- 7) There had been pressure on the Resource Consents team for many years due to shortage of capacity and capability. To compensate for this contractors had been engaged
- 8) Officers believed they were using the correct consent condition which referred to notional value
- 9) Consistency of approach (and therefore equity) was likely restricted to "what we did last time". It is arguable that this approach was more due to the lack of confidence or a lack of officers experienced with these developments. There was only one instance where evidence was found confirming consents officers or peer reviewers considered consistency of approach - although this may have occurred informally
- 10) While it was too late to change the condition of a consent when the valuation forming the basis for reserves contributions due was provided, if the officer responsible for checking this had more expertise, the inconsistencies should have raised a red flag
- 11) There was good separation found between the officers determining whether reserves contributions apply, peer reviewers, and then the officer creating the invoice

#### Evaluation of Current Practice

- 12) While the management of resource consent contractor contracts is in hand, there are gaps in the quality control of their work as on occasions when their consents go direct to a Commissioner they do not always refer to the Senior Engineer Land Development for advice or go to the Team Leader for peer review
- 13) The individual ownership of procedural development and its related documentation for the processing of development contributions through to invoicing is blurred
- 14) There are still some unit title consents which were approved prior to 1 July 2018 which have financial contributions as a condition of consent. The current primary reviewer has not been trained in prior policy (and has limited time to self-learn) and has to date assumed that those presented in Decision Letters are correct. This is not of concern if an alternative expert peer reviews these conditions on all occasions
- 15) With no valuation experience in the Resource Consents team, there is still some risk that Neighbourhood Reserves calculations may not be correctly assessed
- 16) New consent allocation is a daily team meeting occurrence in Resource Consents. We are informed that these are always allocated to the right level of competence. While the Team Leader has weekly one-on-one meetings with Consents Officers, there is no regular overall consent status report referred to for proactive management
- 17) The Promapp procedure *Assess a Development Contribution for a Subdivision* no longer requires the Senior Engineer Land Development to provide or store evidence to confirm how the contributions were calculated. Decision records should be stored
- 18) At present the Senior Engineer Land Development (SELD) calculates all development contributions except Neighbourhood Reserves (which require a valuation) which is the responsibility of Resource Consents. This is not efficient

**SIGN OFF (LEAD AUDITOR): Lynn Anderson**

**AUDITEE: Mandy Bishop 12/3/2020  
(Reviewed by Group  
Manager Environmental  
Management 7/4/2020)**