CASH TO ASHES:

The inefficiency of fire service reforms

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TAXPAYERS' UNION

FOREWORD

Cash to Ashes raises fundamental questions about the accountability of one of our most valued services, Fire and Emergency New Zealand (FENZ). Although the Insurance Council has had no hand in this report, the questions it raises are ones that every person who insures their home, contents or vehicle should ask. That's because it is they who pay the tax or levy that funds FENZ.

An even more fundamental question is why should those who insure be the ones that fund FENZ? Everyone benefits from FENZ services, not just those who take responsibility to insure themselves. Ironically, much of FENZ's work is to save lives, not the insured property. Ambulances don't attend vehicle accidents to save the car. For these reasons, most other countries don't tax people who insure their property to fund these services. Other options include general taxation, a levy on car registration or through rates. If central government had a bigger role in funding FENZ instead of the 1% it currently provides, then more accountability would be demanded of how FENZ spends its money.

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SUMMARY

In 2017, the Government reformed the decentralised rural fire service and the centralised NZ Fire Service into a new national body – Fire and Emergency New Zealand ('FENZ'). The new centralised organisation was expected to deliver efficiency savings while ensuring service provision was more equal around the country.

In March 2017, PWC concluded that the 2015/16 budgeted expenditure of $389 million was appropriate for the function and output responsibilities FENZ has. The report stated that "Overall, we conclude that the existing level of funding is appropriate for the scope of NZFS's business as usual activities as existed in 2015/16."

Cabinet expected improved efficiency when it approved the centralisation programme pushed by then-Minister of Internal Affairs Hon. Peter Dunne, but these expectations have been ignored. FENZ is projected to spend nearly $338 million more in its first three years than was forecast when Cabinet approved the merger in 2016.

FENZ claims that growth in expenditure is driven by increases in employee costs and depreciation, which reflects nation-wide investment and service standardisation. In reality, documents obtained under the Official Information Act indicate the vast bulk of spending increases have been devoted to administrative and support services. Investment spending is heavily focused on gold-plating regional infrastructure.

On 2 November 2018, FENZ proudly announced that the Tinui Fire Station had received a significant upgrade. Previously, the Tinui Station had been a "corrugated iron shed with a dirt floor". Now, Tinui Fire Station "includes a double bay shed with reinforced flooring, a kitchenette, training room, office, shower, toilet, laundry area, mezzanine storage level, two 20,000L water tanks that will make it easier to refill trucks after training or incidents."

For larger cities or towns experiencing resource shortages, an upgrade of this nature would make sense. But Tinui has a population of approximately 20 people. The opening of the new Station was attended by FENZ's CEO Rhys Jones, Chairman Paul Swain, a Government Minister (Ron Mark) and the local MP (Alastair Scott). The sheer quantity of human and financial resources devoted to building and opening a fire service shed in a town of 20 people is strongly suggests a growing culture of gold plating waste.

One reason FENZ has been able to increase its budget so substantially is that it is not required to justify its wasteful spending, since it is able to collect revenue through the fire insurance levy without having to go through Treasury like other departments. Any increases in revenue from the levy are therefore able to be spent with little accountability or impetus to lower the levy – since FENZ is not subject to any competitive or commercial pressure.

As part of the Fire Services Reform agenda, the Government was expected to introduce a new levy system to provide income for Fire and Emergency New Zealand. However in March 2019, Minister of Internal Affairs Tracey Martin announced the implementation of the new levy system is on hold as she is now reviewing the funding model for FENZ. This is politically unsurprising, given NZ First's strong opposition to the FENZ reforms when they were being shepherded through Parliament by Minister Dunne.

THE PURPOSE OF REFORM: GOALS AND EXPECTATIONS

Prior to the urban and rural fire centralisation in July 2017, urban fire services operated under the New Zealand Fire Service and were funded by a fire levy on building insurance, while rural areas were funded from rates and operated with a local level of governance model. Naturally this caused some degree of variation in cost profiles, equipment and performance across the country – reflecting the different needs of communities. This decentralised rural fire structure did however generally keep costs to a respectable level for forest and rural stakeholders.

From an urban fire service perspective cost profiles today remains extremely high for some urban communities. Similarly sized towns in similar locations experienced significant variation in cost. Figure 1 demonstrates this variation:

Timaru is located between Ashburton and Oamaru, but Timaru's fire services costs are more than three times the costs of either Ashburton and Oamaru. This is representative of the network of fire services across New Zealand prior to reform: different communities with different cost profiles and service offerings. In the mind of former Minister of Internal Affairs Peter Dunne, this needed to change. In a 25 April 2017 newspaper column, Dunne argued:

"The reforms will enhance, but not essentially change, the approach to firefighting and fire management in our communities. We recognise the success of existing structures in managing risk and reducing unwanted fire. However, we also know that some rural communities have not seen the investment in local services they need. Some are struggling to attract, retain, and support volunteers. Ageing vehicles and stations without electricity or running water are common."

The intention Dunne had to significantly increase investment in rural fire services is clear from his comments. The purpose of reform was clearly to ensure an ironing out of operational differences across the country – even though some rural areas might require reduced or different services to dense urban areas.

However, putting the varied needs of communities aside, fire services were performing strongly prior to centralisation. Figure 2 – taken from the FENZ 2017/18 Annual Report – demonstrates the steady decline in fire incidents over five years despite a growing population.

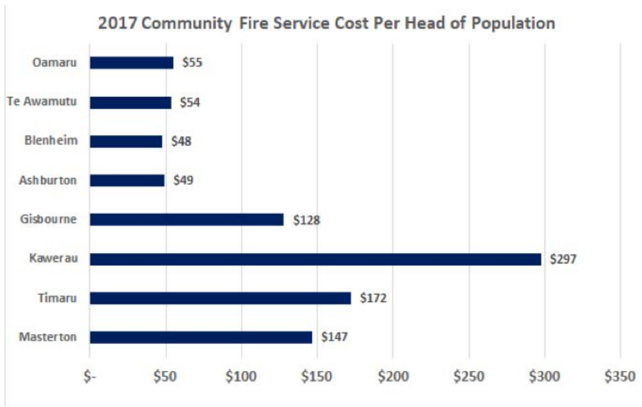


Figure 1

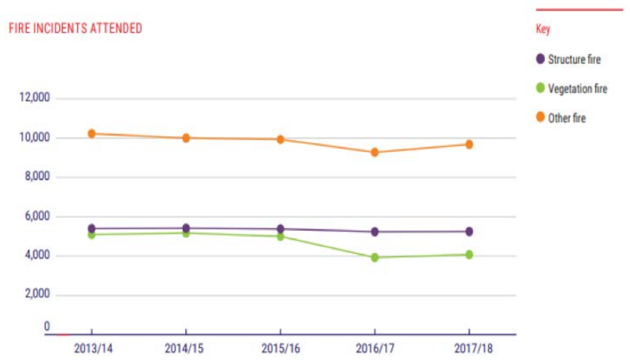


Figure 2

Additionally, volunteer and career stations were largely meeting (or close to meeting) the performance standards of the New Zealand Fire Service, as outlined in Table 1 below (taken from the 2016 New Zealand Fire Service Annual Report).

Measure		2015/16 Actual	2014/15 Actual	2015/16 SPE target
2.2.1	Number of structure fires attended (including number where Fire Service equipment required to extinguish fire e.g. one hose reel or more)	5,384	5,413	Information measure only
2.2.2	Number of non-fire emergencies attended (total):[8]	29,263	28,199	Information measure only
	▸ Number of medical emergencies attended (including number where CPR/defibrillation carried out)	11,339	10,304	Information measure only
	▸ Number of motor vehicle accidents attended (including number where extrications performed)	5,518	4,815	Information measure only
	▸ Number of hazardous materials incidents attended (including number where Fire Service active management required)	3,195	3,245	Information measure only
2.2.3	Response times for structure fire incidents inside fire districts will be monitored for performance against the national service delivery guidelines of:			
	▸ 8 minutes for career stations	84%	84%	90%
	▸ 11 minutes for volunteer stations	88%	89%	90%
2.2.4	Response times for non-fire emergencies will be monitored for performance against the national service delivery guidelines of:			
	▸ 30 minutes for motor vehicle accidents	97%	97%	90%
	▸ 20 minutes for incidents requiring the specialist Hazmat within major urban areas	84%	84%	90%
	For response to medical emergencies inside urban fire districts:			
	▸ 8 minutes for career stations	89%	88%	90%
	▸ 11 minutes for volunteer stations	87%	86%	90%

Table 1: Performance Standards for 2015/16 – NZ Fire Service Annual Report 2016

While some standards were not met, performance was generally very high. It would be difficult to extrapolate from these results that the New Zealand Fire Service required hundreds of millions of dollars in additional spending.

Cabinet clearly agreed with that appraisal when approving the centralisation programme for FENZ. One of the major justifications for fire service centralisation was the delivery of efficiencies, to ensure taxpayers received better value for money while still enjoying the benefits of a well-functioning national fire service.

More specifically, Cabinet supported the reforms on the basis that FENZ would deliver $47.7 million in efficiencies by 2021/22, achieved by:

- matching investment in people, resources, and services with community risks and needs;
- a new flexible service model – not a rigid 'one-size fits all' approach;
- fire reduction activities leading to reduced fires;
- better management of health and safety risks across the sector;
- improved use of capital;
- improved strategic thinking that informs planning and service delivery; and
- improved systems and processes.

These efficiency expectations were clearly signaled by the Minister responsible for the reforms, Peter Dunne, who commented in April 2017 that while "[there] will be additional costs … these will not be in perpetuity" and that "[the] Government's expectation is that after this transitional period operating costs will reduce." In short, improved efficiency was an essential justification for advancing with the reform of fire services.

EFFICIENCY ABANDONED: THE FINANCIAL COST OF REFORM

Despite the Government's expectations, FENZ's expenditure is expected to explode in coming years. While Cabinet forecast expenditure to eventually fall to $439 million in the 2021/22 financial year, from $486 million in 2020/21, the latest forecasts show expenditure at $617 million in 2020/21. In total, taxpayers are worse off by $338 million (just over the period 2018/19 through 2020/21) compared to forecasts when Cabinet approved the centralisation reforms: approximately $143 more per household in fire services spending. It's also disturbing to see, even when fire levy income has exceeded what was approved by Government in 2016, that the FENZ Board has unrelentingly continued to draw down on a $112 million capital injection Government loan to assist in funding the transition costs of the urban/rural merger over the first four years.

How taxpayers are impacted is damaging, but complicated. Instead of receiving funding from the general consolidated fund, like most departments and ministries, FENZ collects its own revenue through a levy which applies to insurance premiums on products which insure against fire. This means FENZ does not have to go through a formal budget bid process through Treasury, allowing them to collect revenue and spend taxpayers' money with very little accountability.

Strangely, this means individuals and organisations which choose to self-insure receive a tax advantage and are able to free-ride on others: the levy disincentivises taking out formal insurance coverage. Additionally, the financial penalty disproportionately affects commercial organisations, since while residential property is subject to a levy cap of $106, commercial property faces a potentially unlimited levy rate.

FENZ argues in its 2019 Statement of Performance Expectations that the significant spending growth is the result of growth in depreciation and staff costs due to service standardisation across the country, reflecting the goal of equal capability and performance across the country central to the process of reform. On the surface, that makes sense: higher depreciation costs simply reflect large amounts of capital expenditure, so the $48 million increase in depreciation over the forecast period reflects massive upgrades to the FENZ property portfolio.

However, the nature of capital expenditure raises serious questions over need, quality of spending, and value-for-money. In 2018, FENZ announced upgrades to two career fire stations: Wigram, and Woolston. The station upgrades at Wigram and Woolston (both Christchurch locations) cost $7.4m and $6.9m respectively.

Given their urban location, the Christchurch upgrades could be justified, but the Tinui two bay upgrade does not represent value for money for ratepayers. Tinui is an extremely small town – it has a population of approximately 20 people – in the Wairarapa. Yet, it has received "a double bay shed with reinforced flooring, a kitchenette, training room, office, shower, toilet, laundry area, mezzanine storage level, [and] two 20,000L water tanks that will make it easier to refill trucks after training or incidents."

Lake Okareka and Wanaka volunteer firefighters have also recently received new fire stations and equipment. Lake Okareka – a township of 600 people – is receiving a new fire station estimated to cost $1.9 million, while Wanaka – a small resort town – has a new fire station estimated to cost $4 million. In contrast, a new two-bay shed (with a training area) is estimated by the Country Fire Authority in the Victoria, Australia to cost approximately $600,000 NZD. It's unclear why expanding the fire service capability in rural New Zealand e.g., Lake Okareka, should be significantly more costly than similar forms of spending in Australia.

It appears that FENZ is gold-plating its property portfolio, rather than investing in desperately needed infrastructure.

There is plenty of generally wasteful spending taking place at FENZ as well. $69.3 million of the $261.3 million increase ('other expenditure') in spending is neither additional staff costs or depreciation.

The most important component of the increase in 'other expenditure' is the increase in spending on 'communications and computers' – approximately $43 million over three years.

There is no explanation in either of FENZ's recent Statements of Performance Expectations as to why FENZ requires a $43 million investment in ICT equipment, or why that spend delivers significantly improved services. For example, if the roadmap of reform was to standardise service delivery across regional and volunteer stations (in line with urban stations), how does ICT specifically improve capability? More explanation is needed.

External consultants are also putting upward pressure on expenditure at FENZ. In 2017/18, FENZ spent $9.9 million on external consultants. FENZ has budgeted $11 million and $6.5 million for external consultants in 2018/19 and 2019/20 respectively. Again, FENZ has not explained the value of spending millions of dollars on external consultants specific to the justifications for reform.

Perhaps most importantly, the vast majority of expenditure increases ($163.3 million of $205.3 million) between the 17/18 and 18/19 Statements of Performance Expectations is not allocated to any urban area or region, but to 'Support Services'. In other words, back-office bureaucracy is being heavily supported by the change – with only a small share of the increase in expenditure being allocated to front-line operations.

Alongside these significant increases in expenditure is the expectation of Cabinet when approving centralisation that FENZ achieve $47.7 million in efficiency savings by 2021/2022. That's a significant saving, likely requiring work across the organisation in the lead up to 2021/2022. In an Official Information Act Request, we asked FENZ for any reports, documents or advice they had received on the value of efficiencies found since centralisation. FENZ's response was brief:

"Cabinet has asked Fire and Emergency to ensure efficiencies from 2021/2022."

In other words, FENZ has no reports, documents or advice on the value of any efficiencies within the organisation. This can only be interpreted to mean that FENZ has not only found zero efficiency savings, but has also identified no possible future efficiency savings. This is clear in the latest FENZ Statement of Performance Expectations which forecasts revenue and expenditure for 2021/22: none of the $47.7 million of efficiencies have been earmarked for the 2021/22 Financial Year.

CASE STUDY: COSTS OF THE PIGEON VALLEY FIRE SUGGESTS DRAMATIC REDUCTION IN EFFICIENCY

In addition to general increases in wasteful spending and gold-plating of the FENZ property portfolio, the response of FENZ to the Pigeon Valley forest fire last summer suggests a dramatic reduction in efficiency.

On 5 February 1981, a remarkably similar fire to Pigeon Valley started next to the urban area of Nelson in the Hira forest, requiring significant investment in manpower and resources to limit its spread. In total, the NZ Forest Service spent $174,317 (1981 NZD) broken down into:

(a) NZ Forest Service Salaries - $33,577

(b) NZ Forest Service Wages - $31,020

(c) NZ Forest Service Vehicle & Plant - $11,814

(d) Aircraft - $67,587

(e) Other external costs - $30,317

Additionally, Murray Dudfield – a former National Rural Fire Officer – estimates the cost to Nelson City Council for the Hira forest fire was approximately $31,831 – giving a total cost of approximately $206,000 – or $912,000 in 2019 NZD.

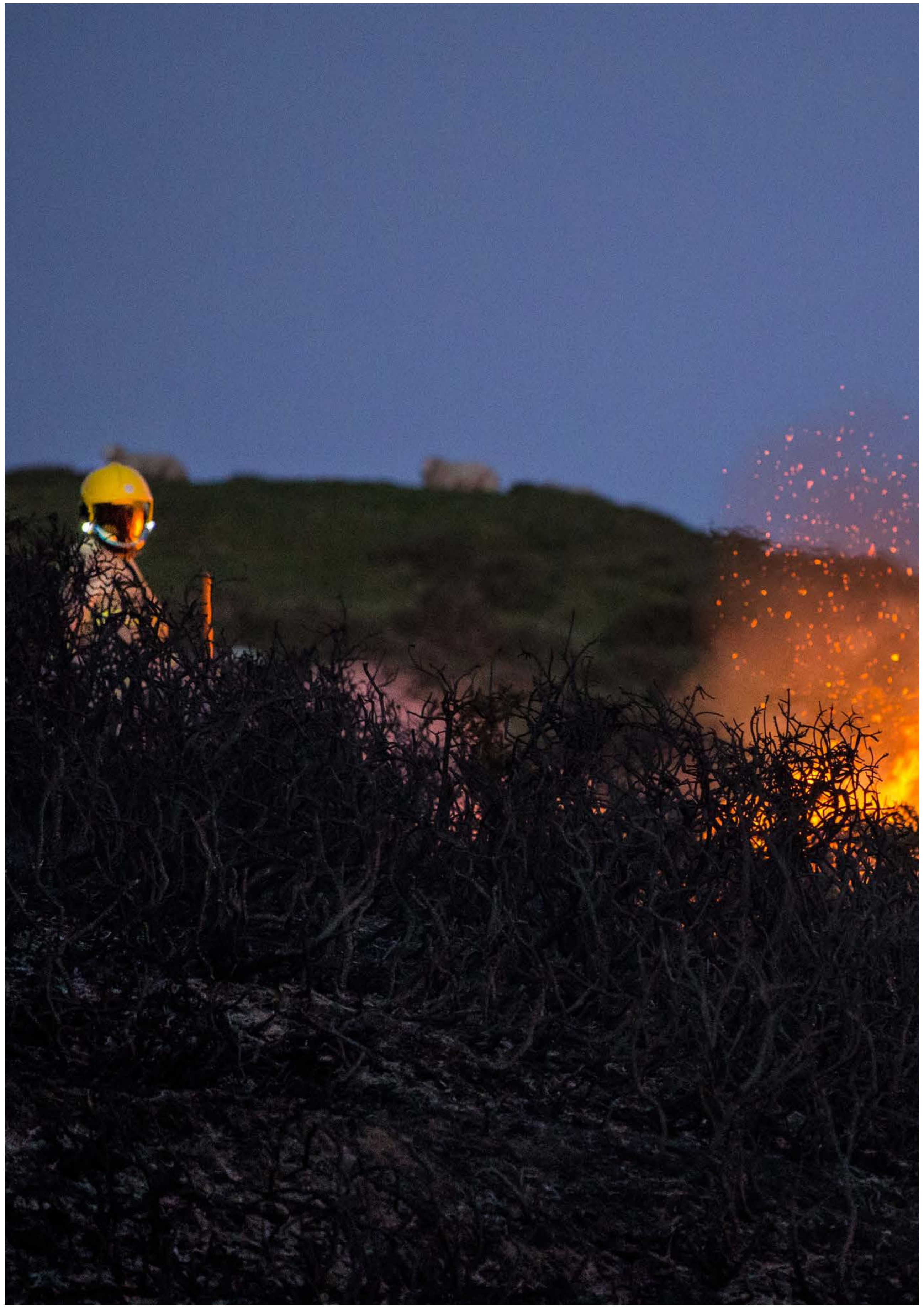
On 5 February 2019, 38 years to the day of the Hira forest fire, the Pigeon Valley fire broke out near Nelson. According to Drought Code and Build Up Index, which measures moisture content and fuel conditions in the area, the natural environment on the 5th of February was approximately the same in 1981 and 2019.

However, the response of Fire and Emergency New Zealand was markedly different in 2019 compared to 1981. For example, while the use of aircraft can be effective in combatting the early stages of a fire, they become much less effective following the initial attack phase. Instead, 25 helicopters and two fixed wing aircraft were used at Pigeon Valley in the first ten days to combat the forest fire. In addition a large cost was incurred in establishing large tracts of fire breaking external to the forest boundary.

The result: fighting the Pigeon Valley fire cost $17 million – more than 17 times the cost of fighting the very similar Hira fires in 1981, even after accounting for inflation.

There have been no dramatic improvements in the majority of the technology used to fight fires that would explain the increase in costs – trained forest firefighters, bulldozers, shovels, fire hoses, pumps, and helicopters were all used in both 1981 and 2019. One important advance, however in 2019, has been the availability to fire controllers of real-time weather data from automated weather stations along with much improved fire behaviour models for various vegetation types. This adds no cost to managing a fire but properly used it enables rural fire managers to better predict fire behaviour and better match tactics to the situation.

We suggest the decrease in efficiency is a result of the lack of financial accountability on FENZ: spending is not assessed by Treasury and FENZ is not required to justify future spending bids to Treasury officials. Instead, FENZ is able to spend its levy income as it desires.

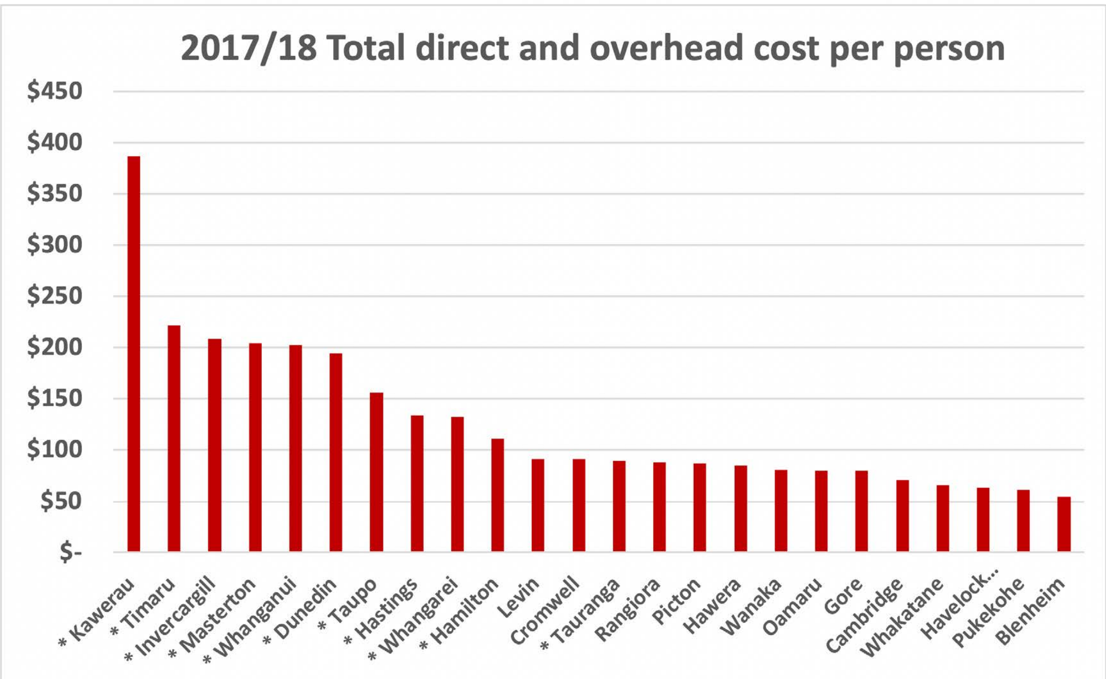


CONCLUSION

Fire services are often raised by taxpayers as a classic example of a service where government should be involved to manage externalities and public goods problems. However, that does not mean that FENZ should enjoy a blank cheque or be immune from criticism and reform. The sheer scale of FENZ as an organisation and its immunity from Treasury revenue guidance means it has become a largely financially unaccountable organisation – with taxpayers forced to pick up the bill via insurance costs.

With the FENZ levy regime now under review, there is an opportunity to reform some parts of the organisation in order to deliver better value for money for taxpayers. A good initial first step would be to require that FENZ cannot collect its own revenue through the levy regime and instead require that levy revenue pass through the general consolidated fund. Requiring FENZ to make Budget bids and go through the usual scrutiny and rigour of public sector spending decisions may improve the quality of spending and put downward pressure on the levy, if the revenue is implicitly ring-fenced and large potential surpluses are identified. It may be beneficial to abolish the levy altogether and simply collect the revenue through general taxation, given the disincentives that apply to insurance coverage stemming from the levy regime. While waste needs to be generally combatted within the organisation, reforming the culture of waste within the organisation would be difficult without outside rigour.

More immediately, it may be valuable for the Minister responsible for FENZ, Hon. Tracey Martin, to put pressure on FENZ to meet the efficiency expectations outlined by Cabinet when centralisation was approved. Given New Zealand First's historic opposition to the reforms, it could be politically useful for the Minister to pressure the Opposition on their recent support of the reforms and demonstrate to the public that centre-left governments can reform and be efficient when required.



LAKE OKARAKA RURAL FIRE FORCE TO IL4. FLOOR AREA 348 SQM. COST **$1.9 MILLION** 2019

WANAKA URBAN VOLUNTEER FIRE STATION BUILD. FLOOR AREA 585 SQM. COST **$3.96 MILLION** – 2017

LYTTELTON URBAN VOLUNTEER FIRE STATION BUILD. FLOOR AREA 497 SQM. COST **$3.85 MILLION** – 2017

KEY SOURCE DOCUMENTS

Cabinet paper with original expenditure forecast: *Fire Services Review: NEW FUNDING ARRANGMENTS* (p 20)
Actual expenditure in 2018/19: *Annual Report 2018/19* (p 61)
Latest expenditure forecast: *Statement of Performance Expectations 2019/20* (p 32)

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