THE TREASURY
Kaitohutohu Kaupapa Rawa

MINISTRY of TRANSPORT
TE MANATŪ WAKA

Auckland Transport Strategy and Funding

Date:	14 November 2003	**Treasury Priority:**	**High**
Security Level:	IN-CONFIDENCE	**Report No:**	T2003/1927

Action Sought

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Minister of Finance	Discuss the Auckland transport funding proposal with Infrastructure Ministers and notify your Cabinet colleagues of the proposal to be discussed with Auckland mayors.	Tuesday 18 November
Minister of Transport	Discuss the Auckland transport funding proposal with Infrastructure Ministers and notify your Cabinet colleagues of the proposal to be discussed with Auckland mayors.	Tuesday 18 November
Associate Minister of Finance (Hon Trevor Mallard)	None	None
Associate Minister of Finance (Hon David Cunliffe)	None	None

Contact for Telephone Discussion (if required)

Name	**Position**	**Telephone**		**1st Contact**
Rosemary Cook	Principal Advisor			✓
Roger Toleman	Deputy Secretary, Ministry of Transport			✓
Elizabeth Anderson	Assistant Manager, Ministry of Transport			

Enclosure: Yes

14 November 2003

SH-8-8

Auckland Transport Strategy and Funding

Executive Summary

1. In July 2003 Cabinet agreed that a joint central/local government process be established to consider Auckland transport strategy and funding (CAB Min (03) 25/3 refers). Following the final report of that group, this paper seeks agreement to a way forward in progressing Auckland transport issues.

2. The JOG key conclusions are based on achieving transport outcomes that are consistent with the NZTS – and accordingly emphasise expenditure on demand management (pricing and non-pricing), public transport, and some accelerated roading.

3. Your proposal to Auckland mayors was that
   - fuel taxes[1] be increased by no more than 5 cents per litre excluding GST (fuel excise duty and equivalent road user charges for diesel vehicles), with a proportionate share (up to 35%) being allocated to Auckland;
   - the Crown matches this by making a contribution of potentially up to $500m over 10 years;
   - tolling be introduced on new roads where practicable, with project specific debt used in relation to those roads;
   - the Land Transport Management Act 2003 provides the basis for assessing projects for funding; and
   - an in principle decision be made to move towards road pricing of existing roads, but with further work to be done, including around the social and economic impacts.

4. You may wish to notify your Cabinet colleagues that discussions with Auckland mayors will continue on the basis of that proposal.

Recommendations

We recommend that you:

a) **note** that the additional expenditure on Auckland transport should be targeted to transport demand management initiatives, increased investment in public transport and an acceleration in the roading programme.

   Noted   Noted

[1] In this report the term "fuel taxes" is used to refer to fuel excise and road user charges.

b) **note** that, for a number of reasons, increased funding for Auckland transport will not be needed immediately, but that an agreed way forward will need to be announced to Auckland elected representatives on December 12;

Noted | Noted

c) **agree** to notify your Cabinet colleagues that discussions with Auckland mayors will continue on the basis of the following proposal:

- fuel taxes be increased by no more than 5 cents per litre excluding GST (petrol excise duty and equivalent road user charges for diesel vehicles), with a proportionate share (up to 35%) being allocated to Auckland;
- the Crown matches this by making a contribution of potentially up to $500m over 10 years;
- tolling be introduced on new roads where practicable, with project specific debt used in relation to those roads;
- the Land Transport Management Act 2003 provides the basis for assessing projects for funding; and
- an in principle decision be made to move towards road pricing of existing roads, but with further work to be done, including around the social and economic impacts.

Agree/Disagree | Agree/Disagree

d) **refer** a copy of the report to the Minister for Economic Development, the Minister of Energy and the Minister for the Environment, the Minister with responsibility for Auckland Issues and the Minister of Local Government.

Referred

Rosemary Cook
Principal Advisor
for Secretary to the Treasury

Roger Toleman
Deputy Secretary
Ministry of Transport

Hon Dr Michael Cullen
Minister of Finance

Hon Paul Swain
Minister of Transport

Background and Context

5. The Joint Officials Group on Auckland Transport Strategy and Funding (JOG) was established in July 2003 with the following objective:

   To develop a funding package that enables the timely implementation of an agreed network strategy, having assessed the fit of the Auckland regional Land Transport strategy (RLTS) with the New Zealand Transport Strategy (NZTS) and other public policy outcomes.

6. The New Zealand Transport Strategy provides the strategic level decision making framework for transport. An opportunity exists to advance a broader range of government policies and initiatives within this context of addressing transport issues in Auckland. These policies and initiatives include the Growth and Innovation Framework, the Sustainable Development Plan of Action, and the National Energy Efficiency and Conservation Strategy. For these reasons, we consider that maintaining an impetus on resolving Auckland transport issues is important.

7. While much of this work has implications for governance, that was outside the brief of JOG. Those issues have been dealt with as part of another process.

The JOG report

8. The key findings to emerge from the JOG report are, broadly:

   - The rate at which infrastructure can be constructed is subject to three main constraints: consents, buildability and funding.
   - It should be possible to double the amount of annual investment in civil construction in Auckland transport to $400m p.a.[2], provided skills shortages can be addressed. However this will not necessarily generate twice the level of activity because of the likelihood of a price premium (up to 30%), particularly in early years. This also assumes the current level of activity in other regions of New Zealand would be maintained but not increased.
   - Road pricing can deliver significant gains against the NZTS objectives and provides a further source of funding for investment in transport.
   - Transport demand management (non-pricing initiatives to optimise the network and change behaviour, e.g. walking and cycling investment, school and business travel plans) can provide early and effective gains against the NZTS.
   - Increased investment in public transport is essential. Additional public transport investment will be required if significant road pricing is introduced in Auckland and best practice indicates that this needs to be in place before road pricing is operational.
   - Accelerated roading does not appear to deliver significant benefits when evaluated at a high level under NZTS objectives. New roads are however

[2] This figure does not include other types of expenditure such as rail electrification, and operating and maintenance expenditure.

likely to be important for community acceptance of road pricing. JOG noted also that increased investment in PT and roading are not mutually exclusive, as buses are an important component of the public transport network.

9. There are some caveats around the JOG conclusions. This is because these conclusions are in some cases based on assumptions that have not been tested due to both time and data constraints. As identified by JOG, further work may be required over time to test these assumptions:

- In particular, the work on buildability was done in conjunction with the local construction industry only. That work took account of projected levels of activity, and capacity, in the Australian and New Zealand construction industries. However, it may be possible that industry participants from further afield (Asia or Europe) might enter the market for sufficiently large contracts, although they may be constrained by availability of local labour.
- Further, the road pricing modelled by JOG was indicative only and there are a wide range of possible alternatives. JOG modelled a cordon toll around the Auckland isthmus, which appeared to deliver both demand management and revenue generation. However a cordon toll of this nature would have large impacts on low income communities living in south and west Auckland and these may not be easy to mitigate.
- While the assessment process JOG used was based on determining which policies are likely to make the greatest contribution to NZTS outcomes, the focus was at the package level. JOG did not assess the contribution individual initiatives (e.g. key roading projects) would make to NZTS outcomes (e.g. reduced emissions, improved public transport and walk/cycle mode share).
- There are also issues related to road safety performance of Auckland roads that JOG did not consider. There is a case to consider a programme of safety retrofitting as part of any increased expenditure on Auckland transport. There may also be significant gains from better integration of the local roading network with state highways.

Discussions with Auckland Mayors

10. Along with the Minister for Auckland Issues, you met with Auckland Mayors in Auckland on 30 October 2003. JOG presented its emerging conclusions to the meeting (a copy of the power point presentation is attached). At that meeting the following points were agreed:

- All agreed with the JOG recommendation to commit funds to TDM non-pricing; public transport and some accelerated roading.
- All agreed on an in principle decision to move towards more road pricing than that envisaged in the Land Transport Management Act 2003, with early delivery of tolling on selected new roads, noting that:
  - to start tolling early would set direction and grow community acceptance.
  - road users, over time, will have to pay more directly for their road use.

    - further work is needed on pricing, including around the social and economic impacts.

- All accepted that there are buildability constraints. There was acceptance that these may lift over time. There was agreement to provide enough programme certainty to allow the industry to gear up to the buildability constraint.
- Funding a gap of $200m p.a. seems achievable.
- Mayors and Ministers are jointly committed to PT.
- All agreed that decisions about timing and funding of particular projects be left to the processes set out in the Land Transport Management Act 2003, through the Auckland Regional Land Transport Committee and Transfund.
- All agreed that some debt would be appropriate.
- All agreed that some level of increase in fuel taxes would be appropriate (petrol excise duty and RUC) but there was no agreement as to appropriate levels of increase.

11. On the basis of these agreed points, you proposed that the Government take the following steps to assist Auckland address its transport issues:
    - fuel taxes be increased by no more than 5 cents per litre excluding GST (fuel excise duty and equivalent road user charges for diesel vehicles), with a proportionate share (up to 35%) being allocated to Auckland;
    - the Crown matches this by making a contribution of potentially up to $500m over 10 years;
    - tolling be introduced on new roads where practicable, with project specific debt used in relation to those roads;
    - the Land Transport Management Act 2003 provides the basis for assessing projects for funding; and
    - an in principle decision be made to move towards road pricing of existing roads, but with further work to be done, including around the social and economic impacts.

Timing of funding increases and certainty of programme

12. It is important to provide some level of comfort to both the Auckland region and to the construction industry that the appropriate increase in funding will be available when required. However, for the following reasons, increased funding will not be required immediately:
    - the construction industry has identified that it will take approximately three years to gear up to the buildability levels;
    - potentially higher than expected revenues from existing levels of fuel taxes may be available (the October baseline update for the National Land Transport Fund indicates that an additional $500m will be generated over the next 5 years if current levels of economic activity are maintained);

- there is unspent money in Transfund (although note that much of this has already been allocated); and
- consultation processes required by the Land Transport Management Act 2003 may slow down the approval process for some projects.

13. Any increase in fuel taxes should ideally occur around the time that the additional revenue is required. If an increase were to occur before there were suitable projects ready for funding, Transfund would have to carry the surplus. While there could be reasons for Transfund to carry some level of surplus (for example where funds are allocated to long term, high cost, projects such as those found in Auckland) we generally consider that fuel taxes should not be increased in advance of need. We therefore propose that officials be asked to monitor forecast revenues in light of Auckland funding needs, and advise the government when additional revenue is required. The work needed to increase RUC and/or petrol would occur at that time.

14. On the basis that additional funding is not provided immediately there are steps that could be taken to provide increased certainty and send the appropriate message to Auckland that central government is intending to address these issues:
    - Government could signal in the Budget Policy Statement (to be issued in December) that it intends to make a contribution to Auckland transport.
    - There are a number of mechanisms within the transport policy context including: provisions in agencies' performance agreements, statutory policy directions, policy statements around priorities, or establishing certain output classes for Transfund in Vote: Transport.
    - Government could signal a readiness to progress some other issues that might alleviate the constraints identified by JOG including skills shortages in the construction industry and consenting issues.

Funding Mechanisms

Fuel Excise and Road User Charges Increases

15. A 5 cents per litre increase gives increased revenue of approximately $165m p.a. (including GST) nationally. On the basis of a one-third allocation to Auckland, this would contribute around $50m p.a. to Auckland transport.

16. While roughly half of fuel excise currently goes to the National Land Transport Fund, it is possible to have the full increase go into land transport, as with the fuel excise increase in February 2002. The total amount of any RUC increase automatically goes into the National Land Transport Fund. Under the Land Transport Management Act 2003, Transfund will apply the allocation process set out in the Act in order to allocate funds to projects.

17. Initial analysis undertaken by the Ministry of Transport indicates that light diesel vehicles pay comparatively less for their road use than do other classes of diesel vehicles, and petrol powered vehicles. This relative cost advantage may

have contributed to the relative increase in the number of light diesel vehicles on the road. This could suggest the need to increase RUC for light diesels at a greater rate than for petrol. Closer alignment between fuel excise duty and RUC for light vehicles would be consistent with the current government policy on vehicle emissions, and longer term, for introducing more equitable and sustainable charging for road use. This issue should be taken into account when the increase is made, and the Ministry of Transport will advise on this at the relevant time.

18. We note also that while other excise duties are inflation indexed, this is not the case for petrol excise. This might be worth considering at a later stage.

19. There are social and economic impacts of increases in fuel taxes:

- JOG has modelled the effect of fuel excise increases on the spending patterns of different households. The results indicate that for most households, the effect is broadly neutral. The impact on households is likely to be between $1.50 and $2.20 per week.
- JOG has also modelled the CPI impacts of a 5 cent per litre increase. Based on 2002 levels this modelling indicates that a 5 cent fuel tax increase would result in CPI change of 0.16 percentage points. As an order of magnitude, a 0.16 percentage point increase in the CPI would give rise to additional net expenditure to beneficiaries of around $20 million.

Crown contribution

20. You have also indicated to Auckland Mayors that there may be some opportunity for a Crown contribution – either a one off grant or annual payments for a period. At this stage you have indicated that it would be very difficult to offer anything above a dollar for dollar matching of Auckland's proposed share of the fuel tax increase.

21. This Crown contribution should be over and above the existing land transport funding, as although Transfund currently has unspent money, most of this has already been allocated. The contribution could be made to the proposed new Auckland governance body, or to Transfund for allocation to Auckland.

Debt

22. You have indicated to Auckland mayors that you are comfortable with specific debt being used to finance some of the proposed increase in spending on Auckland transport. The use of debt in this context is separate from any impact that a Crown contribution to Auckland transport would have on the Government's debt position. Broadly, there are three scenarios where debt is useful:

- where there is a sizeable one off expenditure requirement;
- where there is a new revenue source to service the debt; or
- where a policy decision has been made to shift from PAY-GO funding to spreading the cost of an item of infrastructure over the life of the asset.

23. In the present context, although there is a significant expenditure requirement identified in the Auckland RLTS, it is not clear that the level of expenditure requirement will fall away following the completion of those RLTS projects. Further projects requiring significant expenditure, such as a third harbour crossing, have already been identified. In other words, the expenditure requirement in Auckland is not “one-off”, and the cost of servicing any debt will impact on future spending capacity. Therefore, in the absence of a policy decision to shift from PAY-GO funding, debt should be limited to where there are new revenue sources to service it.

24. If tolling of new roads proceeds, then there will be a source of new revenue available to service debt. Revenues from tolling are likely to be some years off. However, if some of the currently planned new roads such as ALPURT can be part-funded from tolls, then there will be an off-setting cost saving to Transfund from doing so in the next 10 years. If non-project specific debt were to be used in advance of implementation of comprehensive road pricing, then other revenues will be required to service debt.

25. There is a range of options as to who would issue the debt, and Treasury will report to you separately on that, and other related issues.

Next steps

26. You are due to discuss these issues with Infrastructure Ministers on Tuesday 18 November, and then with Auckland mayors by telephone conference on 24 November. While any agreement reached with Auckland mayors will be put to Cabinet Policy Committee on 3 December, you may wish to advise your Cabinet colleagues of the basis on which your discussions with Auckland will proceed.

Consultation

27. DPMC, MED, Transit New Zealand and Transfund New Zealand have been consulted in the preparation of this report