



KOMITI NGĀ WAI HANGARUA **WELLINGTON WATER COMMITTEE**

Meeting to be held in the Council Chambers, 2nd Floor, 30 Laings Road, Lower Hutt on
Friday 26 July 2024 commencing at 10.00am

SUPPLEMENTARY ORDER PAPER

PUBLIC BUSINESS

8. **INDEPENDENT REVIEW OF ESTIMATION ERROR BY WELLINGTON WATER LIMITED**

Memorandum dated 25 July 2024 by the Democracy Advisor

2

Jack Kilty
Democracy Advisor
Hutt City Council

TO: Chair and Members
Komiti Ngā Wai Hangarua | Wellington Water Committee

FROM: Jack Kilty, Democracy Advisor, Hutt City Council

DATE: 25 July 2024

SUBJECT: INDEPENDENT REVIEW OF ESTIMATION ERROR BY
WELLINGTON WATER LIMITED

Purpose of Memorandum

1. The purpose of the memorandum is for the Committee to review the key findings of Roy Baker and Kevin Jenkins' final report regarding Wellington Water Limited's error in providing information to its shareholder councils.

Recommendation:

That the Committee receives and notes the memorandum.

Appendices

No.	Title	Page
1	Final Report Review of Wellington Water Limited capital programme estimating and budget systems 22 July 2024	3

External Review

Wellington Water Limited: capital programme estimating and budget systems

Final Report by Roy Baker and

Kevin Jenkins

22 July 2024

This Review has not been independently verified or audited. We have made reasonable efforts to ensure the information contained in this report reflects the range of views expressed by the people we spoke with. The Reviewers do not accept any liability if this report is used for some other purpose for which it was not intended, nor any liability to any third party in respect of this report, nor any liability arising from or otherwise in connection with this report (or any omissions from it), whether in contract, tort (including for negligence, breach of statutory duty, or otherwise), or any other form of legal liability (except for any liability that by law may not be excluded). This note supplements the Terms of Reference for our engagement.

Acknowledgment

Most of the interviews undertaken by the Reviewers were with employees of Wellington Water Limited. We would like to acknowledge and thank each of them for the quality of discussion, and for their generosity in openly sharing their experiences and views to help us identify lessons.

We also spoke to representatives of the shareholding councils and extend our sincere thanks for their participation and feedback to help ensure such a situation does not arise again.

The Reviewers were assisted by Suzanne Carter.

Administrational support was provided by Garry Butler and Sheree Matheson of Wellington Water. Thank you.

Contents

Key findings	4
Introduction	5
Recommendations	6
Wellington Water's operating context	9
Answers to Questions - from the Review's Terms of Reference	10
Section a. How the estimation error occurred	10
Section b. What happened in response	17
Section c. The contribution of culture to the error	17
Appendix 1 : External Review Terms of Reference	28
Appendix 2 : Timeline of key events	32
Appendix 3 : How the estimation error occurred	35
Appendix 4 : Wellington Water's Process to Develop the LTP	36
Appendix 5 : COSO Framework	41
Appendix 6 : Lessons from the 2022 Inquiry into the cessation of water fluoridation by Wellington Water that repeat in this Report	42

Key findings

The reviewers were asked to investigate an error that Wellington Water Limited (Wellington Water) had made in the information it gave to its shareholder councils on or around 1 May 2024 for their longterm planning, which incorrectly excluded Wellington Water's corporate cost.

The error and how Wellington Water responded to it

We established a timeline of what happened, and we drew on several frameworks to put what happened in context. This shed light on the causes of the error and the changes that Wellington Water needs to make to prevent similar problems in the future.

We found that the error had multiple inter-related causes. The error arose because of deficiencies in structures, systems, and processes, including a lack of strategic leadership at the highest levels of the organisation, and in wider problems of organisational culture. The problems went wider, and higher, in the organisation than any single function.

Importantly, the consequences of the error, including for the trust and confidence of the shareholder councils, were magnified by how Wellington Water responded to it. When they became aware of the error, the organisation did not react quickly enough or take it seriously enough and downplayed the problem in their communications with councils. Had the information given to councils been corrected when Wellington Water first became aware of the error, the impact for the councils could have been minimised. Wellington Water had numerous opportunities over the next three to four months to address the problem but did not take them.

An organisation that has not kept pace with increased demand

In our review we discovered an organisation that was not as mature as we would expect it should be. Wellington Water is now 10 years old, but it has not evolved in step with the evolution of its functions and as an organisation has not kept pace with increased demand.

We found unclear structures and accountabilities, with like functions not being grouped with like; a control environment that is loose and not fit for purpose; inadequate systems and processes; some missing competencies (including strategic leadership); under-resourcing in the Finance and the Risk functions; and a mismatch between Wellington Water's values and, as described to us, its culture. Our recommendations address those issues.

We also found a culture of not wanting to hear or present bad news. There is a tendency to want to manage bad news before informing stakeholders, and to try to shape their perceptions and reaction to the problem in order to minimise it. Although staff and middle management had formed good relationships with the shareholders, we were told that Wellington Water comes across as defensive to shareholders.

Our recommendations for how Wellington Water can prevent further errors and recover lost trust and confidence

We were struck by how much our recommendations align with those of the 2022 Inquiry into the Cessation of Water Fluoridation by Wellington Water. We observe that some problems identified in that Inquiry have not yet been fixed. Our review found a tendency to see problems with the organisation's structure, systems, and processes as issues to be put off and addressed by the new entity to which Wellington Water will transition.

However, the problems this review has identified need to be addressed urgently, otherwise errors of the type investigated by the 2022 Inquiry and this review will happen again. The work to be done includes, critically, recovering the lost trust and confidence of Wellington Water's shareholder councils. For the senior leadership, it also includes recovering some lost trust and confidence among their own people.

Introduction

1. On 24 May 2024, Wellington Water apologised to shareholding councils for an error made in their advice to council shareholders for capital programme water assets. They explained the exclusion of a 6% corporate cost for major projects in the first three-year delivery of a 10-year plan, accumulated to a shortfall of \$51 million. Wellington Water proposed to mitigate the impact of the deficit by re-programming activities to reduce the impact on Council's and rate payers. [Wellington Water apologises for error in budget advice](#)
2. At the same time, the Board of Wellington Water announced an independent review to understand the circumstances and cause of the error, and to provide recommendations for improvement.
3. On 13 June 2024, we – Roy Baker and Kevin Jenkins – were appointed as Reviewers. We were asked to present our findings to the Wellington Water Committee on 26 July 2024.
4. The purpose of the review is to inquire into and report on how the estimation error occurred and identify lessons appropriate for an entity with a limited life to learn from, to minimise future occurrences.
5. To reach their findings we undertook a process of inquiry and discovery, interviewing 42 people involved in Wellington Water, including Board Members, leaders, managers, team member employees, contractors, and representatives of the six shareholding Councils.
6. We also reviewed approximately 450 documents including Board, management, corporate and operational papers, internal and external emails and attachments, and public documents relevant to Wellington Water to write our Report.
7. Once we had documented our findings, we returned to the documents and compared our findings with those already on the public record.
8. While in draft, our Report was shared with those Wellington Water employees who had met with us and discussed their views so they could offer any corrections or comment on other material matters. We have incorporated some of that feedback into this Final Report. Some feedback we received was in our view either outside of the Terms of Reference or expanded on points in detail that are already made this Report, this feedback has not been included.
9. Given the tight timeframe for preparing this report, we have not been able to address comprehensively every matter that was raised in this review. The review did not involve a forensic assessment of finance functions, and it has not sought to prove or disprove numbers. People capability has not been factored into observations. We have focussed on what we believe to be the critical factors given the purpose of the review as stated in the Terms of Reference (see Appendix 1).

Recommendations

Our recommended actions are intended to help Wellington Water learn from these events and improve its response to any future occurrences. Given Wellington Water's impending transition into a new entity, we understand the remaining short-term life of the organisation in its current form and the need for pragmatism. However, we believe that if there is not investment in the areas covered in our recommendations, there is a high risk that further problems, similar to the estimation error or the cessation of fluoridation, could occur.

Rebuild the trust and confidence of shareholding councils in Wellington Water

- Review the capital projects across the tri-ennium to ensure that the appropriate corporate cost is accurately recorded, enabling fact-based discussions to occur with councils as their capex programmes are actioned.
- Establish controls to ensure accuracy and transparency of the allocation of corporate costs in a timely manner.
- Wellington Water needs to be front and centre in the budgeting process, overseeing all the financial processes (including capital/investments) for Wellington Water and ensuring strategic focus, providing high-quality advice, and appropriate controls.
- Wellington Water needs to work with Council CFOs to:
 - Improve the quality, reliability, and timeliness of monthly reporting data to Councils, especially forecast capex and opex spend.
 - Ensure that Councils are aware of the cost estimates levels that are applied to projects and programmes and how they are determined, thereby improving the accuracy and confidence in the projected forecast investments.
 - Create comprehensive and streamlined annual planning processes.
 - Determine a more transparent process for how the corporate cost for the capital programme is managed, including showing the corporate cost as a separate line item for councils and eliminating the need for each individual capital project to estimate and account for those costs.
 - Review the 2022 Service Level Agreement with Councils – section 11 of the three-Year Plan – to ensure that it is still current, especially the delivery date for the three-Year plan to councils.
- The Board of Wellington Water works with the shareholders to determine if one standard set of monthly financial reports for all councils (both opex and capex) could be agreed, in order to minimise complexity within Wellington Water reporting.
- Strengthen the sign-off process and include common checklists for projects across Wellington Water, to ensure the corporate cost element is correctly included.

Rebuild the trust and confidence of middle management and staff in Wellington Water's senior management

- Ensure Wellington Water's budget planning cycle to start at the same time as, or before, any Annual Plan/LTP planning for Councils.
- Ensure that the Senior Leadership Team and Tier 3 managers have a better understanding of the process and the importance of all aspects of planning.
- Inculcate the values of the organisation into all work areas and behaviours and acknowledge employees' values-based actions.

- Return to a “no blame” culture by changing behaviour to better align with Wellington Water’s values.
- Consider working with staff (beginning with senior leadership) to fully define expectations around individual behaviours and actions that support Wellington Water’s values and include the outcome of this work in the Code of Conduct.
- Reverse the tendency in the business to manage first rather than share first (with external stakeholders) – that is, make the default to signal issues early.
- Build a mutually supportive culture based on listening and responding.
- Increase the organisation’s focus on outcomes.

Restructure the organisation so that accountabilities are clear, and capabilities can be substantially enhanced in the lead-up to the new entity

- Introduce an orthodox structure that has clear role accountabilities and responsibilities for role holders – for example, group like functions with like.
- Strengthen the strategic finance function.
- Introduce more finance/business partner capacity to help run the whole business.
- Consider establishing a Chief Operating Officer-type role dedicated to achieving rapid business as usual (BAU) business and process improvements both for short-term quality control and in readiness for the transition to a new water entity.
- Consider where IT and HR functions are best located given the organisation’s size.

Treat Wellington Water’s readiness for reform as separate from the BAU work programme

- Consider establishing a separate team that focusses solely on the move to a new entity to keep BAU separate, and to ensure focus remains on delivery with no slippage in delivering the opex and capex programmes for councils.

Review Wellington Water Annual Plan processes to deliver capital programmes for councils

- Streamline and clarify integrated planning and finance processes and ensure they are universally understood across the business; prioritise key risk areas and use best-practice guidance to create clear standards, ensuring guidance or policies around their use are in place.
- Map key processes immediately, particularly around the use of spreadsheets and data transfer.
- Create and update standard procedures for quality control, including Wellington Water-wide templates, checklists, gateways, audit requirements, authorisation, and communication.
- Ensure that ownership and accountability of key processes are understood and reflected in position descriptions.
- Reduce reliance on financial and other stand-alone spreadsheets and explore new cost-effective collaboration and productivity tools (this need not wait for the new entity and the new processes and systems it may adopt).
- Require transparency in external and internal reporting as a default, unless there is a good reason not to.
- Consider how to further optimise the relationship with Watercare and its new model, for future synergy.

- Once the review of major projects confirms corporate cost is accurately recorded, ensure that collectively the overall Wellington Water corporate cost will be recovered (see above).

Strengthen governance oversight

- Increase the focus on oversight of any recommendations implemented from this Report, using an internal audit function to report to the Board on progress and issues.
- Ensure that shareholding councils have high-quality information and that there is improvement in the relationship between each council and Wellington Water.
- Ensure that internal governance groups (more aptly described as “management committees”) are established to oversee the Long Term Plan (LTP) and that annual planning continues to be accountable until the project has been completed and formally signed off.
- Review the risk management system so that it is:
 - Fit for purpose (best practice is unlikely to be achievable in the period leading to the establishment of the new entity but, in order for this function to have any impact, it needs to be refocused on key risks).
 - Integrated into strategic and operational management.
 - Accorded the mana necessary for it to identify and call out risks as they emerge.
- Ensure that the capacity of the assurance functions is the right size for the risk profile of the organisation.
- Review the quality and content of information provided to the Risk and Audit function and determine if there are any gaps to be addressed.

Wellington Water's operating context

Wellington Water Limited was established in 2014 following the merger of Capacity Infrastructure Services and Greater Wellington Regional Councils water supply group. Six councils own and fund Wellington Water: Greater Wellington Regional Council (GWRC), Hutt City Council (HCC), Porirua City Council (PCC), South Wairarapa District Council (SWDC), Wellington City Council (WCC) and Upper Hutt City Council (UHCC).

Wellington Water sets out its role on its website: "We give our councils advice on their assets, and they make decisions on what to fund through their Long-Term Planning (LTP) process. Councils also set the levels of water services and set policy. We work to the budgets they set and prioritise our work to make the best use of the funding and resources provided to us".

Wellington Water has been waiting on planned water reforms for several years. The Three Waters reform, evolving into Local Water Done Well, has delayed investment in assets and infrastructure and, as it continues to await decisions about its future, Wellington Water is operating continuously in a "change is coming" context.

The Government is progressively rolling out its Local Water Done Well policy. The Local Government (Water Services Preliminary Arrangements) Bill, which is expected to be enacted in August, will require councils to prepare Water Services Delivery Plans setting out how they plan to deliver water services on a financially sustainable basis. It is anticipated that many councils in the region will opt to submit a Joint Plan and continue work to establish a new regional Council-controlled organisation (CCO). Future legislation that will provide for new forms of council owned water services organisations is expected to be introduced in late 2024 and enacted in mid-2025. This is the earliest a new form of regional CCO would be able to be established.

Under Local Water Done Well, councils will be responsible for deciding whether and when to establish a new regional CCO. The ten councils comprising the Wellington region and Horowhenua District signed a Memorandum of Understanding on 10 May 2024 to work together on a joint water services delivery plan and to develop a joint delivery model that can address the challenging long-term funding and delivery requirements for water in the region. We understand this process is subject to several "off ramps" for individual councils to decide whether to commit to the joint delivery model, and no decisions have been taken around the timing for establishment of a regional water services organisation.

Planning to prepare for the transition of Wellington Water into a new entity has slowed significantly with the need for councils to drive reform locally rather than relying on central government resourcing. Planning and preparing budget information relating to investments required for the 2024-2027 investment cycle and for the 2024-2034 planning period has been undertaken. However, major investment in new systems has been deferred until transition has occurred; improvements to asset information and management, processes and systems need to be oriented to the short term, in readiness for a transition.

Wellington Water has also been under the public spotlight. It has had to deal with a confidence issue around the non-fluoridation of drinking water at Te Mārua and Gear Island water treatment plants, repair several thousand leaks due to aging water infrastructure, and manage a potentially significant water shortage through the recent summer. It has also had to manage ongoing non-compliance and poor performance at wastewater treatment plants across the region for many years. Issues such as these intensify scrutiny and corrode reputational capital. Failing infrastructure is regarded poorly by the public and Wellington Water are viewed as responsible for failing to respond, as well as their shareholders.

Since 2021, Wellington Water has grown from an organisation of 265 to 395 people to meet demands arising because of these issues, the increased size of its capital programme, and its core role; operating and maintaining existing infrastructure, renewing it when necessary, delivering projects of significant investment and providing recommendations and budget advice about future capital projects for each Council's LTP.

