

Summary of Deloitte's Report into concerns regarding Wellington Water's financial systems and processes

Purpose

1. This paper sets out a summary of Deloitte's report in relation to concerns surrounding the use of Wellington Water's procurement processes and financial systems (the **Report**).

SUMMARY OF DELOITTE'S REPORT

Background

1. Wellington Water engaged Deloitte to investigate matters relating to Wellington Water's procurement processes and financial system potentially providing opportunities for fraud to occur. Deloitte prepared a report of their investigations (**Report**). This involved, among other things, considering the panel arrangements that Wellington Water has in place.
2. Set out below is a summary of Deloitte's findings and recommendations. We have also included at Appendix 1 to this paper Deloitte's description of the context within which Wellington Water operated.

Findings

3. Deloitte noted that every employee interviewed confirmed that they had not seen evidence of fraud. Additionally, all interviewees confirmed that they had no concerns that fraud was occurring within Wellington Water. They did, however, express concerns that there may be opportunities for waste and/or abuse in Wellington Water's processes. A separate investigation has identified an isolated incident of fraud, and the person responsible no longer works for Wellington Water.
4. Deloitte noted that its key findings indicate systematic and widespread issues relating to the design, operation, control, and assurance, over processes that are fundamental to the operation of Wellington Water, and that this exposes Wellington Water to significant risk. The absence of reliable controls significantly reduced the ability to detect and prevent fraud. Specific findings are summarised below.
5. ***Management and oversight of panels without sufficient competitive tension*** - Deloitte

observed a lack of oversight and/or involvement by Wellington Water in the management of the panels to support and promote competitive tension, quality, and to ensure value for money is being delivered by panel members and the Alliance. In particular, there was insufficient oversight or independent assurance over the panel members performance and financial processes. Deloitte noted that management reporting is based on self-assessment by panel members.

6. Deloitte also observed a historical focus by Wellington Water on prioritising partnership, transparency, and delivery, over competitive tension and achieving value for money. Further, Deloitte noted that interviewees disclosed that the arrangements appeared to prioritise Wellington Water's consultants and contractors over ratepayers, which has contributed to a culture that may indicate that the use of panels was the only option for procurement of services, irrespective of cost, quality or timeliness.
7. Deloitte recommended the panel arrangements are regularly and independently monitored and assessed including that risk and assurance be undertaken on panel members' performance and financial processes to ensure they continue to meet the needs of the organisation in terms of value, quality, and service.
8. ***Lack of clarity in roles and responsibilities, including inherent conflicts of interests relating to key roles*** – Deloitte concluded that project managers for Wellington Water being contracted through the consultant panel creates an inherent conflict of interest in relation to issues such as performance and value for money where the project manager was required to hold their employer (the consultant) accountable to Wellington Water. Deloitte noted that interviewees indicated there was a lack of clarity between the role of outsourced project managers and internal Wellington Water staff. Deloitte noted their expectation that roles should be clearly defined, agreed, and embedded roles and responsibilities, including with appropriate mechanisms for holding consultants accountable for delivery, performance, reporting, and financial transparency.
9. ***Limitations and risks with respect to the structure and design of the panel agreements*** - Deloitte found that the panel and Alliance model has been designed to prioritise trust, partnership, and delivery, without appropriate controls to assess, on an ongoing basis, that the benefits of the panel are commensurate with the cost. As an example, the sharing of Councils' budgets for projects with panel members to support transparency provides panel members with significant insight to funds available for work they are costing which increased the risk that Wellington Water would not be provided with the best price.

10. Deloitte found the allocation of work was done by panel members themselves, rather than by Wellington Water, and tended to be based primarily on equal distribution regardless of whether a particular contractor or consultant was the right fit for the job. While Wellington Water had a contractual right to make the ultimate allocation decision, as Deloitte understood, this right was not used in practice. Furthermore, as Wellington Water retained the risk, cost, and liability of work, panel members were not incentivised to deliver competitive responses or deliver to a consistently high quality, for example, self-allocating work by panel participants without adequate performance-based assessment by Wellington Water risked not achieving those outcomes.
11. Deloitte noted that it was suggested the maintenance of the relationship (and the benefits of security and certainty of supply during a period of increased critical capex investment) took precedence over enforcement of contractual obligations. Deloitte recognised that, at that time, there were limited market testing mechanisms available to validate whether costing was competitive. However, Deloitte noted that the use of the panel had created a closed loop of assumptions which were not regularly market tested, noting that panel costs had escalated significantly since establishment.
12. Deloitte also noted that it was difficult to quantify the legitimacy of cost increases given there were other external factors likely to be relevant, such as the increased cost of construction, materials, and a high inflationary environment.
13. ***Weak financial management processes and controls relating to panel and Alliance agreements*** - Deloitte found the supporting financial controls were insufficient, informal, and unreliable to provide confidence in the legitimacy and accuracy of claims and payments being made under broad annual purchase orders. Invoices were automatically paid prior to any approval or consideration by Wellington Water staff and there were occasions of invoices being rejected by approvers and still being paid by the accounts payable team. The manual processes further increased the risk of error and/or inaccuracy.
14. Deloitte observed that there was no contract management system to manage and/or oversee large projects and programmes, increasing the difficulty for Wellington Water to have oversight to consider the accuracy and reliability of claims. Separately, Deloitte noted interviewees expressed concerns that the appointment of sub-contractors by panel appointed contractors was resulting in both sets of overhead costs being charged to Wellington Water, however, Deloitte did not review any evidence which substantiated these claims.

Recommendations

15. Deloitte recommended a number of actions are taken to improve Wellington Water's processes, including to:
 - a) assess the management arrangements and revise them where appropriate to reflect Wellington Water and its current priorities;
 - b) implement initiative around promoting and increasing the understanding, awareness, and development of a healthy "speak up" culture;
 - c) review the current model for contracting of project managers through the consultant panel and consider whether conflicts can be appropriately managed or whether an alternative model is required;
 - d) review and formalise the roles and responsibilities between project managers and internal Wellington Water delivery roles;
 - e) review current processes, practices, and reporting to determine whether the required structure to maintain competitive tension exists;
 - f) review the performance management procedures and the work allocation processes of the contractor and consultant panels; and
 - g) review and update the key financial controls through the claims process to address weakness and risks in current practices.

16. Deloitte noted that the Report was prepared on a time bound basis and subsequently Deloitte's investigation focused on conducting interviews and understanding supporting evidence. Deloitte did not perform in-depth analysis, reconciliation, or assessment to quantify costs that may be indicative of waste. Deloitte did not engage with any third parties (e.g. members of either panel) during their work.

APPENDIX 1 – Operational Context

Summarised below is Deloitte's description of the context within which Wellington Water operated:

1. Following a sustained period where Wellington Water was underdelivering on its capital programme, several procurement decisions were made to supplement the company's capability and provide reliable access to qualified resources. This included the establishment of the Three Waters Network Operations and Maintenance Alliance Agreement (**Alliance**), and the contractor and consultant panels.
2. The consultant panel was established in 2016 to provide access to experienced, qualified, and reliable consultants to support the design and management of projects with providers who were pre-qualified.
3. The Alliance was established in 2018 to perform operations and maintenance of the network assets which Wellington Water is responsible for.
4. The capex contractor panel was established in 2019 to deliver a regional approach to the capex contractor market which had the capacity and capability to service Wellington Water's business-as-usual capex physical works programme.
5. To minimise disruption, with the expectation that a new entity would be established through water reform that would take over responsibility for water services, the terms of the panels were extended in July 2022 with an anticipated expiry of 30 June 2026.
6. The Report identified that the establishment of the panels and Alliance agreements reflected a point of time when Wellington Water's scale was not sufficient to meet the delivery needs of the network.