

TO Siobhan Procter, Chief Infrastructure Officer, Wellington City Council (WCC)

COPIED TO Peter Wells, Manager Service Planning
Mark Ford, GM Business Services

FROM Julie Alexander, GM Network Strategy & Planning

DATE 4 November 2022

PRELIMINARY THREE WATERS 2023/24 ANNUAL PLAN OPEX ADVICE FOR WELLINGTON CITY COUNCIL

Action Sought

	Action sought	Deadline
Siobhan Procter Chief Infrastructure Officer, WCC	Note the recommendations in this paper. Meet with Wellington Water to discuss content of this paper.	30 November 2022

Purpose

1. This paper informs Wellington City Council (Council):
 - a) of the approved operational expenditure (OPEX) budget, and the risks of keeping the budget at this level, and
 - b) that Wellington Water advises additional OPEX funding should be provided above the current approved level to maintain existing levels of service and that subsequent advice on a proposed FY2023/24 OPEX budget will be provided to Council in February 2023.

Recommendations

2. Wellington Water recommends Council:
 - b) **notes** the risks associated with keeping the FY023/24 OPEX budget at the LTP approved level
 - c) **notes** that Wellington Water will provide subsequent advice on the recommended OPEX budget for the FY2023/24 financial year, and that this will exceed the approved FY2023/24 LTP budget
 - d) **notes** advice on the FY2024/25 OPEX budgets will be provided as part of Wellington Water's FY2024-2034 LTP advice
 - e) **notes** the FY2021-31 LTP OPEX budget does not include funding for significant emergency events, which Council funds separately
 - f) **notes** that Wellington Water will need a response from Council on whether it accepts the risks outlined in this document related to continuing with the FY2023/24 OPEX LTP approved budget or is willing to provide Wellington Water with additional OPEX funding to reduce the risks and maintain existing levels of service.

- g) **agrees** to increase the FY2023/24 OPEX budget above the approved FY2023/24 Long Term Plan level for the following priority areas, at a minimum:
- i Asset condition assessments
 - ii Sustainable water supply and leakage management
 - iii Backflow prevention
 - iv Wellington Water management fee

Context

3. Wellington Water provides Council with three waters advice, management and repair services against budgets provided through the Long-Term Planning process. Advising Council of issues and impacts that arise which may impact on our ability to work within those budgets and provide agreed service levels is a vital part of our role as your service provider.
4. Our advice is in the context of strategic investment priorities set out in the Statement of Intent. These priorities are¹looking after existing infrastructure, supporting growth, ensuring a sustainable supply of drinking water, improving environmental water quality, reducing carbon emissions, and increasing the resilience of the services to the impacts of climate change. Funding decisions made for the FY2021/31 LTP mean that only limited performance improvements will be achieved. The expected impact of the investment decisions and the residual risks are set out in the Regional Service Plan².
5. Council-owned three waters assets are ageing. This means they are not being renewed or replaced as quickly as they are wearing out, and that means increasing issues and outages. Over time, this results in higher reactive costs including maintenance, repairs, and renewals.
6. Over the past year Wellington Water has experienced significant increases in the costs of material and labour due to a variety of inflationary factors (inflation in the past financial year has reached over 7%). This has put pressure on the CAPEX and OPEX programmes Wellington Water is delivering on behalf of its client councils. Additionally, new information has been discovered through investigations and additional data analysis. For example, our leakage management programme has given us a much better understanding of the extent of water loss across the network, and the impacts of that loss. These pressures mean OPEX investment at the FY2023/24 LTP approved level will be insufficient to meet Council's level of service targets.
7. Wellington Water remains committed to assisting Council achieve its service level targets, but we are concerned that current agreed funding provided for provision of our services will not allow those targets to be achieved.
8. In April 2022, we advised Council we were concerned that the FY2023/24 agreed budget of \$39.7 million would not be sufficient to meet Council's required service level targets. At this time, Council approved an uplift in OPEX funding of \$5m to increase the total FY2023/24 OPEX budget to \$44.7m (inflated)³. Table 1 illustrates the difference in approved LTP FY2023/24 budget, and the uplifted budget.

² Available at <https://www.wellingtonwater.co.nz/publication-library/advice-and-work/regional-service-plan/>.

³ Email from Nikki Symons, 'WCC - 2022/23 Annual Plan Confirmation', dated 21/07/2022

Table 1: Wellington City Council 2023/24 OPEX budget

Activity (\$ x 1,000)	Original 2023/24 LTP	Approved Uplift (July 2022)	Total FY2023/24 budget incl. uplift
Drinking Water	\$10,483	\$1,350	\$11,833
Stormwater	\$4,345	\$550	\$4,895
Wastewater	\$24,887	\$3,100	\$27,988
Totals	\$39,715	\$5,001	\$44,716

9. Also, please note that Porirua City Council have signalled an increase in Wellington City Council's overall Joint Venture share cost for Porirua WWTP for FY23/24. This is an increase from \$3.3m to \$3.72m for overall cost (opex & capex). We will confirm this increase again in subsequent advice in February 2023.

Risks of keeping the FY2023/24 OPEX budget at the current approved level

10. In our April 2022 advice, we identified several factors which were driving OPEX costs up, for example increasing reactive maintenance requests and increases to labour and material costs. Many of these cost drivers still stand, and some may have increased in likelihood and/or severity. In addition, new risks have been identified. This highlights that an OPEX budget above the approved level of \$44.7m is needed if Council intends to meet its level of service targets.
11. The following risks have been identified and are detailed below. The costs for some of these are yet to be determined and will be provided in the advice we give Council in February 2023.
- a Planned maintenance – Completing critical planned maintenance is good asset management practice and allows for planned work on critical assets. The current level of investment in planned maintenance will mean the frequency of stormwater network flushing and drinking water network maintenance activities such as hydrant flushing and valve maintenance will reduce. This will increase the risk that blockages and overflows will continue to occur, with poor environmental outcomes. A lower level of planned drinking water maintenance carries a risk that hydrants and valves will not operate reliably when needed. As mentioned, these maintenance reductions place additional pressure on reactive maintenance budgets. There also remains a risk that under-investment in pump station maintenance will result in significant issues at pump stations as there is no allowance for increasing maintenance costs, rising number of failures or the ability to address deferred maintenance issues.
 - b Reactive maintenance is considerably below the level of expenditure required and will result in a reduction in levels of service in response times and low priority faults not being addressed and an increasing backlog of faults.
 - c Sustainable water supply and leakage management – Gross water consumption over the first quarter of FY23 for the Wellington metropolitan area averaged 2.9% higher than the corresponding time last year and 7.0% above our 5-year target. All networks are performing poorly based on standardised water loss metrics, with Wellington City Council sitting in the “poor” infrastructure leakage index (ILI) category. Minimum night flows and water balance analyses, climate and population correction modelling, and analysis of dry weather wastewater flows all indicate that leakage is the primary driver of rising demand.

A full programme of mitigation measures has been developed and prioritised; however, Wellington Water requires additional OPEX funding from Wellington City Council of \$1.7m to support these measures. The leak repair programme that was funded through stimulus funding in FY2020/21 and FY2021/22 is no longer funded. This means there is insufficient funding to make a significant impact on water loss and demand. Water use in metropolitan Wellington is now at an all-time high, and it is important to continue to prioritise leak detections and repair as an important tool for managing water loss. Without additional funding, the leak issue and overall consumption will continue to increase, negating recent gains and putting even greater stress on the water supply for the region. As a result, there is an increased likelihood of level 3 or higher water restrictions being needed to control demand this summer. If Level 3 or 4 restrictions are required, then mayors will need to lead communications.

Wellington Water has advised the Water Committee that it is prioritising leak detection and remediation in response to significantly increased regional water usage over the 2022 winter. We expect that councils should also be prioritising this activity, but the underfunding we have identified will significantly impact Council's ability to contribute to this region-wide activity. Reduced leak detection will also see water consumption continue to rise and community engagement in conservation decrease.

- d Investigations – increasing investigations budget will allow Wellington Water to identify and resolve service issues, potentially resulting in better customer and environmental outcomes and will enable preparation of forward capital works plans.
- e Very High Criticality Assets (VHCA) - Between June 2020 and July 2022 Wellington Water completed a condition assessment project to identify VHCA assets and assess their condition. While there is always risk of assets failing unexpectedly, the VHCA programme has significantly improved our understanding of the condition of the assets assessed. Assets identified as requiring remedial actions will need to be funded to prevent unplanned failures. Additional investment in ongoing condition assessment work is strongly recommended to ensure reliable operation of the networks.
 - i Historically, planned maintenance on reservoirs has been limited by very constrained budgets. The VHCA and Water Safety Planning programmes highlighted the need to review the planned maintenance budgets to adequately mitigate contamination risk for reservoirs. The VHCA programme confirmed that contamination risks have surfaced through lack of regular inspection of these reservoirs. To mitigate these contamination risks, an additional \$460k is required to clean and carry out inspections and maintenance activities of a third of Council's reservoirs.
- f Asset register – All activities that Wellington Water performs for Councils rely on a complete and accurate asset register. Stimulus funding enabled good progress on fixing long standing issues with the asset register; the VHCA Programme identified VHCA assets and assessed their condition, and in-roads were made on asset data and information processing backlogs. Councils allocated some funding for ongoing condition assessment work in the approved FY2023/24 LTP and have recently provided additional funding for asset data completeness and quality work. In both areas ongoing funding is required and further increases in funding will enable Wellington Water to accelerate the pace of work and therefore the associated positive impact on service provision. This work also contributes to the National Transition Unit understanding the full complement of assets Council currently owns (providing a complete asset valuation) and supporting smooth transition of services to the new Entity, thus benefitting Wellington City residents.

- g Growth studies –Undertaking growth planning studies in FY2023/24 will help inform the capital delivery programme that will be developed for the 2024-34 LTP. We will continue to work with Council to ascertain whether Council wishes for this work to be undertaken. We estimate \$600k will be required to complete the Southern Growth Study, should Council decide to pick this up in FY2023/24. Additional funding of approximately \$100k is also required to support technical reviews and input into the Let’s Get Wellington Moving programme. Currently, Wellington Water is not funded for this work.
- h Labour costs – Since the 2021 LTP budgets were agreed, labour costs have increased. This is largely due to a current skill shortage in New Zealand resulting in an increased need to use subcontractors/contractors in place of permanent staff. We are expecting significant increases in the amount and hourly rate of subcontractor work. This will have an overall impact on the cost of completing work, particularly for reactive maintenance.
- i Wellington Water management fee – Wellington Water is currently absorbing additional management costs in FY2022/23 and will continue to bear the cost in FY2023/24 if additional funding is not made available. The key reasons for the increasing management fee are:
 - i inflation running at a higher rate than forecast when developing the LTP
 - ii an increase in wages to match market rates and an increase in the proportion of contractors and consultants being used across the industry, and
 - iii increases in staff numbers due to the larger CAPEX and OPEX programmes Wellington Water is delivering, and an increased regulation and compliance activity.

The Wellington Water management fee is charged proportionally across all councils. For WCC, this means that in FY2023/24 we require an increase of \$634k from the 2023/24 LTP budget, to cover the management costs absorbed by Wellington Water to date and to sustain our core business functions. If additional funding cannot be secured from Council to accommodate this year-on-year uplift, Wellington Water will need to reallocate funds from other OPEX budgets to make up for the deficit in management fee. Consequently, this will further impact Council’s ability to achieve its service level targets. It is also worth noting that the management fee is covering some internal staff time costs for work required to be undertaken by Wellington Water to prepare and support the transition of services to the new Water Services Entity, but most of these costs are being met from the additional funding the council is providing out of DIA’s Transition Support Funding.

In addition, under the Government-funded stimulus programme we made progress on understanding and mitigating the immediate cyber security risks across the water network. The Department of Internal Affairs approved stimulus funding for this work to be carried through to FY2022/23. Wellington Water requires ongoing investment from Council in cyber security in FY2023/24 to continue mitigation of this risk. Note, at the time the 2021-31 LTP was developed, we did not know the extent of work required for cyber security, and associated ongoing costs, hence the reason this programme has not been budgeted for beyond FY2022/23. At a minimum, ongoing funding of current cyber security activity needs to continue. Split proportionately across councils, this equates to \$127k being requested from Wellington City council to continue with current cyber security measures. The actual budget needed will be higher than this as cyber security threats change, and we gain greater understanding of the detail of our current security risk.

In total, the updated management fee is \$7.1m including the increase of \$634k in management costs, and the additional funds requested for cyber security activity.

Next steps

12. We will continue to work on your OPEX needs over the coming months and provide detailed OPEX budget advice to Council in February 2023. In the February advice, Wellington Water will recommend Council increase its FY2023/24 OPEX budget above the current approved level.
13. In parallel to providing Council's OPEX Annual Plan advice, we are also determining a 10-year unconstrained OPEX forecast for Council, for submission to the National Transition Unit. This information is due in early December 2022.
14. We are committed to working with you and are keen to meet to discuss the content of this memo when suits.

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