

12 April 2013

Lyn Provost
Controller and Auditor-General
Office of the Auditor-General
PO Box 3928
Wellington 6140

By email: enquiry@oag.govt.nz

Dear Ms Provost,

REQUEST TO CONDUCT A PERFORMANCE AUDIT UNDER THE PUBLIC AUDIT ACT 2001

- 1 I am writing on behalf of Transparent Hawke's Bay to request that you conduct a review of the Hawke's Bay Regional Council's ("**HBRC**") compliance with its statutory consultation obligations in relation to HBRC's proposed Ruataniwha Water Storage Project ("**RWSP**").

Summary

- 2 Transparent Hawke's Bay is concerned that the RWSP was initiated and is being advanced without adequate disclosure to, or consultation with, Hawke's Bay ratepayers regarding the full costs, financial implications and financial risks to the public associated with the scheme.
- 3 In particular, we have identified significant flaws with the way in which the RWSP was described during consultation on the HBRC Long Term Plan 2012-2022. For example, ratepayers were invited to submit on a proposal under which the HBRC would invest enough funds to secure 51 per cent HBRC ownership, but late and un-notified changes to the estimated costs of the RWSP have significantly changed the likely ownership structure and the attendant risks.
- 4 You are empowered to examine a public entity's compliance with its statutory obligations under section 16(1)(b) of the Public Audit Act 2001, and (in the alternative) to inquire into any matter concerning a public entity's use of its resources under section 18(1) of that Act.
- 5 Your review of the consultation process is crucial now as HBRC, through its wholly-owned company, Hawke's Bay Regional Investment Company Ltd ("**HBRIC**"), will soon request that various resource consents and plan changes required for the RWSP to proceed be referred to a Board of Inquiry for determination.
- 6 This will inevitably lead to the expenditure of more public funds on a project about which the people of Hawke's Bay have not had fair opportunity to have their say. The projected costs to HBRC (including through HBRIC) for advancing the project are

\$6,313,705 to February 2014 (**HBRC financial report attached as Appendix 1**). These costs do not appear in the HBRC's annual report for 2013/2014.

- 7 Transparent Hawke's Bay is also concerned that four of the directors of HBRIC are members of HBRC. The four HBRC appointees are the Council chairman, two councillors and the HBRC Chief Executive (as managing director). This gives rise to at least the perception of a conflict of interest.

Background

- 8 The RWSP involves the construction of a dam in the Hawke's Bay region to provide for irrigation. The project was first described to the Hawke's Bay public in the HBRC Draft Long Term Plan 2012–2022, which was released to the public in April 2012. The description of the RWSP indicated an estimated cost of \$170 million and a planned HBRC investment of \$80 million.

- 9 It was strongly signalled that such investment would secure 51 per cent HBRC ownership of the scheme. For example:

- (a) Page 28 of the Draft Long Term Plan 2012-2022 states under "Investment Company Risks" that "[t]he estimate of the potential effects of the uncertainty is best illustrated by stating that for every \$10M increase in project costs, HBRC will need to invest a further \$5M if they are to retain their 51% investment"; and
- (b) The summary document released by the HBRC on the Draft Long Term Plan 2012-2022 states (at page 8):¹

"Regional Investment Company will invest in:

- Ruataniwha Plains Water Harvesting, \$80 Million

Dam building and related infrastructure programmed 2014-2018. Funding required for 51% of equity in proposed subsidiary company."

- 10 Only 81 people (out of the many hundreds of submissions received by the HBRC) commented on the RWSP in their submissions on the draft plan. Most people who did either opposed it (43 in total) or complained that they were in no position to make a judgement about the project or the HBRC investment due to a lack of information (26 in total).
- 11 For some people the lack of information prevented them from forming a view on the project, and for others it was the basis of opposition.
- 12 Public submissions on the draft plan closed on 16 May 2012.
- 13 On 11 June 2012 the HBRC staff made their own submission on the draft plan (**extract attached as Appendix 2**). The submission noted that the cost of the RWSP should be re-stated in the final long-term plan at \$230 million. Significantly, the staff recommended that HBRC investment remain at \$80 million to avoid the need for further consultation, with the consequence that the HBRC may have a less than 51 per cent share in the equity of the scheme.
- 14 Since the draft long-term plan submission process closed in May 2012, Hawke's Bay ratepayers have had one further opportunity to comment on the RWSP. In mid-

¹ [http://www.hbrc.govt.nz/HBRC-Documents/HBRC%20Document%20Library/ourplaceApril12\(v15p5-8\).pdf](http://www.hbrc.govt.nz/HBRC-Documents/HBRC%20Document%20Library/ourplaceApril12(v15p5-8).pdf)

September 2012 HBRC released *Tukituki Choices*, a document that presented four different scenarios for water management in the Tukituki catchment, two of which assumed that the RWSP had gone ahead. The public had an opportunity to make comments on the *Tukituki Choices* document in late 2012, but no hearings were held.

Transparent Hawke's Bay

- 15 Transparent Hawke's Bay is a soon to be incorporated society, chaired by Pauline Elliott and comprised of concerned Hawke's Bay ratepayers, that has been established to strive for open process, reliable information and public involvement in HBRC decision-making.

Summary of legislation

- 16 The RWSP, as already mentioned, is provided for as part of the HBRC Long Term Plan 2012–2022.
- 17 As you know, section 93 of the Local Government Act 2002 (“**the LGA**”) requires all local authorities such as the HBRC to have a long-term plan. The long-term plan not only describes the activities of the local authority but also aims to provide integrated decision-making and co-ordination of the resources of the local authority; provide a basis for accountability of the local authority to the community; and provide an opportunity for the public to participate in decision-making processes on activities to be undertaken by the local authority (see section 93(6) of the LGA).
- 18 A local authority must, when preparing and adopting a long-term plan, act in such a way, and include in the plan such detail, as the authority considers on reasonable grounds to be appropriate (section 93(8) of the LGA). When deciding what is “appropriate” for these circumstances, the local authority must, among other matters, take account of the significance of any matter (section 93(9) of the LGA).
- 19 The special consultative procedure the local authority must use when adopting or amending a long-term plan is set out at section 83 of the LGA. The process involves preparing a statement of proposal, which is made available for the public to view.
- 20 Where a statement of proposal relates to a decision to which section 97 of the LGA applies, certain information must be included in that statement of proposal, including details of the proposal, reasons for it and an analysis of the reasonably practicable options for achieving the objective of the decision: see section 84(3) of the LGA.
- 21 The authority must give public notification of the statement of proposal and allow the public to make submissions. Those who make submissions are to be given a reasonable opportunity to be heard by the local authority. Every meeting at which submissions are heard or at which the local authority deliberates on the proposal are to be made open to the public.

Complaint

- 22 Transparent Hawke's Bay argues that the HBRC has failed to comply with the above statutory criteria in two ways, both of which are interlinked.

Insufficient detail

- 23 First, HBRC failed to describe the RWSP with sufficient detail in the long-term plan, in particular the financial implications of the project, as required by section 93 of the LGA.

- 24 The draft plan did not discuss the wider costs associated with the project, such as the expenses local farmers would face if the scheme went ahead. Other key dependencies – such as the level of local farmer investment in the scheme (affecting both scheme revenue, as farmer payments are the only source of income for the scheme, and scheme ownership, as more external investors or lenders would be required) – have also not been discussed, either in the draft long-term plan or in subsequent documentation such as HBRC draft Annual Plan 2013–2014.
- 25 This lack of detail is compounded by the fact that the HBRC increased the estimated cost of the RWSP in the final long-term plan without informing the public.
- 26 There are a number of implications that arise from the HBRC's decision to incorporate the figure of \$230 million in the final long-term plan. First, there was the obvious lack of consultation. At the time the public had an opportunity to comment on the RWSP (between 10 April and 16 May 2012) the estimated cost was \$170 million. The restated cost of \$230 million – a further \$60 million – did not occur until after public submissions had closed.
- 27 Moreover, HBRC's investment in the RWSP remained at \$80 million – meaning that public ownership of the project would be less than 51 per cent. The water storage project as described in the final long-term plan was therefore in some respects fundamentally different to the project as described in the draft plan and which the public had an opportunity to comment upon.
- 28 The revised ownership structure gives rise to a range of attendant risks. For example, the safety of the Port of Napier – which is wholly owned by HBRIC and is therefore a major asset of the region – has not been assured. If the RWSP is not profitable and the HBRC goes into deeper debt, the port will be jeopardised as loan collateral; further the port's dividend paid to HBRC, projected at \$6.55 million or 17 per cent of HBRC's operating budget in 2013-14, would be jeopardised, increasing ratepayer exposure considerably.

Failure to comply with section 84(3) of the LGA

- 29 Secondly, the HBRC have breached the obligations to provide information on the RWSP in the statement of proposal as required by s 84(3).
- 30 The RWSP would alter significantly the intended level of service provision in relation to water storage, supply and irrigation in particular, and is therefore an activity to which section 97(1)(a) of the LGA applies. Accordingly, it was incumbent on the HBRC to provide the details required by section 84(3) of the LGA, including an analysis of the reasonably practicable alternative options.
- 31 Once again, the HBRC's failure to do so has curtailed the ability of members of the public to comment meaningfully on the project in their submissions.

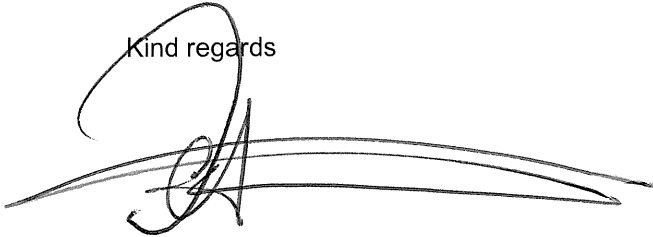
Potential conflict of interest

- 32 Transparent Hawke's Bay is also concerned that four of the directors of HBRIC are members of HBRC and the HBRC's chief executive is HBRIC's managing director.
- 33 What is in the interest of the HBRC and its ratepayers is not necessarily what is in the interests of HBRIC, and the substantial overlap in membership gives rise to at least a perception of a conflict of interest.

Request for investigation

- 34 Transparent Hawke's Bay therefore requests that you review HBRC's compliance with its statutory consultation obligations in relation to HBRC's proposed Ruataniwha Water Storage - particularly sections 84(3) and 93 of the LGA.
- 35 Transparent Hawke's Bay also request that you look into the perceived conflicts of interest arising from the substantial overlap in membership of the HBRC and HBRIC.
- 36 We look forward to hearing from you.

Kind regards

A handwritten signature in black ink, appearing to be 'N. Anderson', with a long horizontal flourish extending to the right.

Nicholai Anderson
Principal (Public Law)

DDI: +64 4 471 5792
E-mail: nicholai.anderson@chenpalmer.com

HAWKE'S BAY REGIONAL COUNCIL
RWS FINANCIAL REPORT TO 31 DECEMBER 2012

| | Actuals to Dec-12 \$ | 2012/13 Budget \$ | Total Budget to Feb 14 \$ |
|---|----------------------------|-------------------------|------------------------------------|
| COSTS | | | |
| <u>RWS Phase 2 Costs</u> | | | |
| HBRC Project Team Seconded to HBRIC Ltd | 189,156 | 399,520 | 695,440 |
| HBRC Internal Staff - Other | 114,588 | 152,000 | 206,050 |
| RMA Legal Advisors | 37,698 | 200,000 | 200,000 |
| Project Team Consultants | 90,685 | 190,000 | 190,000 |
| T&T Optimisation | 133,950 | 220,000 | 220,000 |
| Clients Engineer - SMEC | - | 275,000 | 700,000 |
| Water Contract & Sales Advisory | - | 100,000 | 200,000 |
| Other Consultants | 82,523 | 697,000 | 767,000 |
| BNZ Commercial Advisory | - | 50,000 | 2,100,000 |
| Commercial Legal & Tax Advisors | 2,665 | 300,000 | 600,000 |
| Contingency | - | 100,000 | 200,000 |
| Total RWS Phase 2 Costs | 651,265 | 2,683,520 | 6,078,490 |
| <u>EPA Process</u> | | | |
| HBRC Project Team Seconded to HBRIC Ltd | - | 12,740 | 42,460 |
| RMA Legal Advisors | - | 217,700 | 622,000 |
| Project Team Consultants | - | 123,900 | 354,000 |
| Other Consultants | - | 35,000 | 166,000 |
| Witnesses | - | 100,000 | 500,000 |
| EPA Expenses | - | 625,000 | 1,500,000 |
| Miscellaneous & Contingency | - | 31,500 | 90,000 |
| Total EPA Process | - | 1,145,840 | 3,274,460 |
| TOTAL COSTS | 651,265 | 3,829,360 | 9,352,950 |
| FUNDED BY: | | | |
| MPI (50% of RWS Phase 2 Costs) | - | 1,341,760 | 3,039,245 |
| HBRC (\$400k of EPA Process) | - | 170,000 | 466,000 |
| HBRIC Ltd (Through Advances from HBRC) | 651,265 | 2,317,600 | 5,847,705 |
| TOTAL FUNDING | 651,265 | 3,829,360 | 9,352,950 |

Recommendation

- 14.3. That a sum of \$630,000 be carried forward from 2011/12 to 2012/13 to provide funding for the deferred maintenance of Council's current Operations Group offices and for the extension of that office to accommodate up to 16 staff to be transferred from Dalton Street to Guppy Road. It is noted that Council has yet to receive a formal proposal for this development and the expenditure of this money.
15. **Project 996 – Ruataniwha Water Augmentation Investment**
- 15.1. The budget estimates for this project have been based on the figures available in February 2012 for the Ruataniwha water harvesting project which at that time had a figure of \$170m as the capital cost. This cost has been included in the draft LTP and calculations of the cost for Council to take up a 51% shareholding has been estimated at \$80m, this figure being included in the Plan.
- 15.2. Since February, costs for the construction of the dam and infrastructure to deliver water to the farm gate have been revised at \$230m. This is the capital cost to be used in the financial feasibility currently being undertaken, this feasibility is on track to be submitted to Hawke's Bay Regional Investment Company and Council by the end of August 2012.
- 15.3. It is proposed to correctly reflect the revised capital cost of this project in the final LTP and to amend the \$170m where mentioned in the Plan to \$230m. The potential for cost adjustments is clearly signalled in both the introduction and the right debate segments of the draft LTP. The cost adjustments reflect more accurate information, in particular the refinement of the off-farm infrastructure costs. Costs relate to additional storage capacity and the infrastructure required, hydro-generation capacity and the infrastructure required and additional costs associated with the engineering solutions to various geotechnical aspects relating to the storage site specifically.
- 15.4. The inclusion of information covering the extent of Council's proposed commitment to this project, namely \$80m, was specifically discussed with Audit New Zealand who advised that the inclusion of this information in the draft LTP was essential. It is proposed that Council retains the commitment of \$80m towards a potential equity investment in this project. This may result in Hawke's Bay Regional Investment Company having a less than 51% share of equity in the scheme. However capital structuring and assessment of other investors in the potential scheme will be a subject of major focus going forward and will no doubt influence arrangements.
- 15.5. Staff have discussed with Audit New Zealand, the impact on the LTP process if the commitment to Council either decreased or increased from the \$80m included in the draft LTP. In their opinion LTP process issues will only occur if Council is required to commit significantly more than the \$80m (a figure of over 10% additional funding was mentioned). In their opinion this would trigger an amendment to the LTP and this amendment would need to be consulted on again.

Effect on Plan

- 15.6. There is no financial effect on the Plan as Council's input into the Ruataniwha water harvesting project is proposed to be retained at \$80m, however the narratives in the Plan will be updated to reflect the current costs of \$230m for this project.

Recommendation

- 15.7. That where the draft LTP includes the cost of the Ruataniwha water harvesting project at \$170m that this be revised to \$230m and, further, that Council's financial commitment to the purchase of equity in this project be retained in the final Plan at \$80m.