PROGRESSING THE SLUDGE MINIMISATION FACILITY

PUBLIC EXCLUDED

Grounds: Section s48(1)(a) - That the public conduct of this item would be likely to result in the disclosure of information for which good reason for withholding would exist under Section 7.

Reasons: Section 7(2)(h) - The withholding of the information is necessary to enable the local authority to carry out, without prejudice or disadvantage, commercial activities.

Section 7(2)(i) - The withholding of the information is necessary to enable the local authority to carry on, without prejudice or disadvantage, negotiations (including commercial and industrial negotiations).

Kōrero taunaki | Summary of considerations

Purpose

1. The purpose of this paper to Te Kaunihera o Pōneke | Council is to seek final approval to progress the Sludge Minimisation Facility (SMF) under the Infrastructure Funding and Financing Act (IFFA or the Act) model and for related matters.
2. Officers also seek delegation to the Wellington City Council (WCC) Chief Executive to execute the remaining necessary arrangements for the project including:
    a. Award and execution of the construction contract to deliver the project
    b. Finalisation and submission of the SMF Levy Proposal required under the IFFA
    c. [redacted]
    d. Execution of the Infrastructure Funding and Financing Funding and Administration Agreement (IFFFAAA) between WC and the Crown Infrastructure Partners Special Purpose Vehicle[1] that governs the levy collection and administrative arrangements of the IFFA transaction
    e. Submission of the Infrastructure and Levy Endorsements under the IFFA
    f. Submission of consenting and regulatory approvals to enable construction and operation of the facility

Strategic alignment with community wellbeing outcomes and priority areas

Aligns with the following strategies and priority areas:

☒ Sustainable, natural eco city
☐ People friendly, compact, safe and accessible capital city
☐ Innovative, inclusive and creative city
☐ Dynamic and sustainable economy

[1] Provisionally named Sludge Finance LP

Strategic alignment with priority objective areas from Long-term Plan 2021–2031	☒ Functioning, resilient and reliable three waters infrastructure ☐ Affordable, resilient and safe place to live ☐ Safe, resilient and reliable core transport infrastructure network ☐ Fit-for-purpose community, creative and cultural spaces ☒ Accelerating zero-carbon and waste-free transition ☒ Strong partnerships with mana whenua
Relevant Previous decisions	The sludge minimisation project is included in the Council's 2021- 2031 Long-Term Plan (LTP), under which the funding model of using IFF was adopted as the preferred option. Community engagement was held prior to setting the 2022-2023 Annual Plan Pūroro Waihanga | Infrastructure Committee of 11 November 2021: Agreed to engage further with the community and in particular with: - The residential ratepayer base regarding the indicative change in the proposed levy range compared to what was included in the LTP consultation. - The commercial ratepayer base on the indicative levy. Te Kaunihera o Pōneke | Council of 30 June 2022 agreed Lysis Digestion and Thermal Drying as the preferred option for progressing through detailed design and authorised the Chief Executive to issue a Notice of Requirement to alter Designation 58 to provide for the construction, operation and maintenance of the proposed new SMF at Moa Point. Te Kaunihera o Pōneke | Council of 24 August 2022 agreed to progress the SMF under the IFFA and the commercial principles for setting the IFFA levy
Significance	The decision is **rated high significance** in accordance with schedule 1 of the Council's Significance and Engagement Policy. The Sludge Minimisation Facility is a project of high significance given its importance in achieving the city's waste minimisation goals.

Financial considerations

☐ Nil	☒ Budgetary provision in Annual Plan / Long-term Plan	☒ Change in budget of $40m

3. This paper seeks to confirm overall funding arrangements for the SMF. It seeks approval to fund the project through IFFA funding [redacted]

Risk

☐ Low	☒ Medium	☐ High	☐ Extreme

4. The project involves technical, cost, legal and financial risk due to the complexity of the SMF plant and IFFA financing mechanisms.

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Authoriser	Sara Hay, Chief Financial Officer Siobhan Procter, Chief Infrastructure Officer

Taunakitanga | Officers' Recommendations

Officers recommend the following motion

That Te Kaunihera o Pōneke | Council:
Progressing the SMF

1) **Note** that the 2021/2031 LTP adopted funding through the IFFA as the preferred funding model for the SMF
2) **Agree** to progress the SMF Lysis-Digestion and Thermal Drying wastewater treatment plant at Moa Point at an expected cost of $366.5 million (P50 plus contingency)
3) **Agree** to delegate to the WCC Chief Executive powers to finalise and enter into a construction contract for the SMF project and related works

SMF funding and financing

4) **Agree** to progress the SMF project under the IFFA financing mechanism
5) **Note** that it is critical that funding sources for the SMF project are clearly identified and agreed up front to support the IFFA funding and levy proposal assessment processes
6) **Agree** that funding for the baseline budget to meet expected costs (up to $366.5 million) will comprise (in the following order):
    a. Up to $299 million of core IFFA funding
    b. Already approved and budgeted Council spending on the project for the 2021 and 2022 fiscal years (up to $36 million) and this will be treated as a sunk cost
    c. Additional IFFA funding that can be raised consistent with the buffer provided for in the Levy Proposal (see rec 16a) (up to $31.5 million)
    d. An additional Council contribution (up to $31.5 million), to the extent that interest rate buffer funding provided by recommendation 6c is not sufficient
7) **Agree** that the baseline budget for the SMF project of $366.5 million, including any potential Council contribution provided for by recommendation 6d is incorporated into the Council's LTP by officers once SMF costs are known through the next update due to be completed in 2024.
8) [redacted]
9) [redacted]
10) [redacted]
11) [redacted]

12) [redacted]

13) [redacted]

14) **Note** that execution of IFFFAAA (described in recomendation 25), will require Council to complete the project including securing any necessary additional funding

15) **Note** that the Crown (including Crown Infrastructure Partners (CIP)) are not required to provide any additional funds over and above that provided for by the IFFA transaction as described in this paper.

IFFA Levy Proposal

16) **Agree** to submit an IFFA levy proposal to the Crown for approval consistent with the following parameters

    a. A core project funding amount of $299 million, supported by a buffer equivalent to that required to accommodate base interest rates of up to 6%

    b. A levy area covering the Wellington City rating area

    c. A levy lasting for 30 years, commencing in 2024 and ramping up over four years

    d. Levy allocation methodology of

        i. 70% of the annual levy costs charged to rate payers directly connected to the SMF facility.

        ii. 30% of the annual levy costs charged to all Wellington rate payers (including those not connected to the wastewater network).

        iii. Within each category in a) and b) the costs will be split between residential and commercial rate payers 75% and 25% respectively.

    e. Levies adjusted 75% in proportion to capital values (with the remaining 25% as a fixed charge) for residential properties to support progressivity, affordability and fairness

    f. Levies adjusted 100% in proportion to capital values for commercial properties to support progressivity, affordability and fairness

17) **Agree** that even in circumstances where the buffer allows otherwise, the maximum amount of project funding that can be drawn down under IFFA is capped at $350 million as discussed in paragraph 109

18) **Note** that following the four-year ramp period the annual IFFA levy is expected to range from

    a. $281-$321 per $1 million of capital value for directly connected residential properties

    b. $417 – $476 per $1 million of capital value for directly connected commercial properties

    c. $73 - $83 per $1 million of capital value for un-connected residential properties

d. $108 - $123 per $1 million of capital value for un-connected commercial properties

19) **Note** that IFFA levies will escalate over time at a rate expected to be proportional to increases in property capital values

20) **Delegate** to the WCC Chief Executive the power to finalise and submit the Levy Proposal on behalf of WCC

Consultation and engagement

21) **Note** that consistent with Council direction in August, officers have re-engaged with the community on potential SMF levies, including direct engagement with commercial property stakeholder groups

22) [redacted]

Administrative matters

23) **Note** that the IFFA Levy is for the benefit of the Crown Infrastructure Partners Special Purpose Vehicle (CIPSPV or Sludge Finance LP), but will be collected, administered and enforced by Council

24) **Note** that levies will be administered consistent with existing WCC rates remission and postponement policies

25) **Agree** to waive the Council administration fee of $50,000 per annum to administer the Levy

26) **Agree** to approve the transactions contemplated by the IFFFAAA and enter into the IFFFAAA, which governs the terms on which Sludge Finance LP will fund WCC from the levy proceeds and the collection and administrative arrangements of the IFFA transaction, with Sludge Finance LP

27) **Agree** to enter into, and authorise WCC's Chief Executive to sign, any ancillary documents that are necessary or appropriate for Council to enter into in connection with the funding and financing of the SMF under the Act.

28) **Agree** to submit an Infrastructure Endorsement and Levy Endorsement to the Crown in support of the Levy Proposal

29) **Delegate** to the WCC Chief Executive the power to finalise and submit the Levy Endorsement and Infrastructure Endorsement to the Crown for approval and to finalise and enter into the IFFFAAA with the CIPSPV

30) **Agree** to increase the 2022/23 WCC budget for the SMF project by $40 million to $69.514 million, to support any required project expenditure, prior to financial close, over the initially budgeted $36m.

31) **Note** this increase in WCC's internal budget is fiscally neutral, as any increased expenditure will be offset by additional revenue in the form of IFFA grant funding from CIP.

[redacted]

Regulatory matters

34) **Agree** to delegate to the WCC Chief Executive Officer all necessary powers and functions required to complete all regulatory approvals for the project, and specifically those necessary to make a decision on the Notice of Requirement (NOR) for the SMF following a recommendation made by independent commissioners on behalf of WCC.

Public release

35) **Agree** to publicly release this paper as soon as practicable after the Council meeting [redacted]

Whakarāpopoto | Executive Summary

5. Officers seek a final Council decision to progress the SMF at Moa Point based on an expected cost estimate of $366.5 million, [redacted] A decision to progress now is required to allow project completion before expiry of the existing resource consent for the disposal of sludge at the Southern Landfill.
6. Consistent with Council decisions in August, the SMF is proposed to be funded via the IFFA, supported by some additional Council funding. The IFFA allows the SMF to progress without undue impact on Council debt levels, retaining capacity for other priorities.
7. Officers recommend an IFFA structure that provides a core funding amount of $299 million through a thirty year levy apportioned according to the benefits of the SMF estimated to be received by ratepayers in the Wellington City rating area, in the form of directly connected residential and commercial ratepayers (70% allocation, split 75% and 25% respectively) and unconnected residential and commercial rate payers (30% allocation, split 75% and 25% respectively). Levies are to be adjusted based on capital values. The levy has been sized to provide a buffer for uncertainty in interest rates between now and financial close, which if not necessary for that purpose could provide up to $51 million of additional project funding.
8. To fund the remaining $67.5 million of expected costs of the SMF, officers recommend Council agrees to permanently allocate its already budgeted $36 million of funding permanently to the SMF project. Over and above this officers recommend utilising available IFFA funding from the buffer, and to the extent that is not available making an additional Council contribution.
9. [redacted]
10. [redacted]
11. [redacted]

12. [redacted] It is important to note the IFFA model relies on completion of the project, and the IFFFAAA requires the Council to complete the SMF and if necessary, meet any additional costs of doing so. This means that in this circumstance the ability to cease the project entirely or make large scale changes that could undermine social licence for the IFFA levy will be constrained.

13. [redacted]

14. [redacted]

15. [redacted]

16. Progressing under the IFFA requires a levy proposal to be submitted for assessment by the Ministry of Housing and Urban Development, before recommendation (or otherwise) to the Minister of Housing for approval, Cabinet approval and implementation via Order in Council. In submitting the levy proposal, Council also need to provide Infrastructure and Levy Endorsements which certify Council supports the SMF and levy. These artefacts are primarily for circumstance when a non-Council developer is proposing use of IFFA funding, as in this case support should be self-evident.

17. Once approved the levy is administered by WCC for the benefit of a Special Purpose Vehicle owned by Crown Infrastructure Partners. The IFFFAAA governs the adminstration of the levy, and provision of project funding for the SMF. It requires that Council collect and enforce the levy consistent with its own policies, irrespective of whether a levy payer has met its rates obligations.

18. [redacted]

19. A range of regulatory approvals are required to enable the SMF. These include Notice of Requirement, resource consents and Wildlife Act permits. Approvals are all progressing consistent with project timelines.

Takenga mai | Background

20. The SMF project is an investment in a facility at Moa Point, adjacent to the existing wastewater treatment plant. It aims to decouple the disposal of sewage sludge, a by-product of the Moa Point and Karori wastewater treatment processes, from the Southern Landfill. This needs to be achieved ahead of June 2026, when:

    a. The existing resource consent for disposal of untreated sewage sludge expires. At the time that this consent was granted, strong community feedback and the commissioner's report both indicated that this consent would unlikely be renewed to allow future untreated sewage sludge disposal at Southern Landfill; and

    b. The resource consent for the Southern Landfill expires. Improved treatment and/or diversion of sewage sludge, especially to mitigate odour, environmental and public health risks, is considered to be a key requirement for a new resource consent being granted, which will enable the extension of the Southern Landfill.

21. The project has four key objectives which align strongly with Wellington City Council's strategic community wellbeing and long-term plan objectives, as follows:

    a. By 2026, significantly change the nature, and reduce the volume, of sludge going into Southern Landfill to minimise operational impact on the Southern Landfill, and support WCC to achieve its commitments under the Regional Waste Management and Minimisation Plan

    b. By 2026, provide a sustainable long-term solution for sludge management from Wellington's Wastewater Treatment Plants (WWTPs).

    c. Reduce the environmental impact (in 2026) and associated consenting constraints of sludge management from Wellington's WWTPs.

    d. Align the practice of sludge management in Wellington (Moa Point and Karori) to mana whenua values and principles to the greatest extent practicable.

22. On 30 June 2022 Council approved the SMF business case (refer Sludge Minimisation Facility Business Case – Agenda item 2.2) with a Lysis-Digestion and Thermal Drying plant as the preferred option for progressing through detailed design. The business casing process involved the assessment of 25 potential solutions, including the base case, against the Treasury's Better Business Case model.

23. As there is little prospect of the existing resource consent for disposal at the Southern Landfill being renewed, or for Southern Landfill to obtain its resource consent for extension if untreated sewage disposal continues, 'doing nothing' isn't a viable option. The base case option assessed in the business case involves approximately 30 trucks per week transporting sludge to the nearest suitable landfill at Bonny Glen, near Marton. This option was assessed as having similar costs[2] to the preferred SMF, with clear environmental and local amenity downsides from the heavy transport of sludge through the city all the way to Marton.

24. The preferred option of a Lysis Digestion and Thermal Drying plant will take sewage sludge from the adjacent Moa Point WWTP, as well as the Karori (Western) WWTP, and turn it into a "Grade A" biosolid product that is easy to transport and suitable for a range of potential uses, including as a fertiliser, soil conditioner, fuel in industrial/commercial heating plants,

[2] This was assessed as $220 million versus $247 million on a net present value basis in the business case.

and/or land rehabilitation. Through this process, methane gas is captured to provide energy to run the plant and potentially be provided for wider use. As a low water and weight product, subsequent transport of the biosolid for reuse is very efficient, reducing sludge from 30 a week to two trucks a week.

25. The business case did not seek budget approval at the time as there was a high degree of uncertainty about the project cost estimate. This was acknowledged in the business case which included financial analysis based on a project cost of up to $350 million.

26. The project team committed to progressing design on the preferred option by engaging a main contractor on an “Early Contractor Involvement” (ECI) basis to work with the designers so that officers could bring back a reliable cost estimate in December 2022.

27. On 25 August 2022, Council approved, in principle, funding and financing the SMF project under the IFFA. The IFFA is a new funding and financing mechanism for infrastructure established under legislation enacted in 2020. The purpose of the Act is to provide a funding and financing model for the provision for housing and urban development that supports the functioning of urban land markets, reduces the impact of local authority funding and financing constraints, supports community needs and appropriately allocates the costs of infrastructure.

28. Under the IFFA legislation, a long-term levy, paid annually, is set on properties that are expected to benefit from eligible infrastructure (i.e., properties within the Wellington City rating area that benefit from the SMF). The levy is collected by the WCC, for the benefit of a Special Purpose Vehicle (SPV) 100% owned by Crown Infrastructure Partners (CIP), which is a Crown Entity and 100% Crown owned.

29. The SPV borrows money from the private sector and makes the proceeds available to WCC to meet the costs of constructing eligible infrastructure (i.e., the SMF). The borrowings are then repaid by the SPV using proceeds from the levy collected over time. The Crown provides a Government Support Package which protects against certain risks and helps achieve balance sheet separation for WCC.

30. The overall effect is the IFFA avoids WCC having to borrow to meet the costs of eligible infrastructure from its own balance sheet, providing additional capacity to deliver on other projects set out in the long-term plan, most notably Let’s Get Wellington Moving.

31. Also in August 2022, Council approved, in principle, the ‘commercial principles’ used to design the levy. Council direction was required at that time to allow refinement and preparation of the draft levy proposal for final Council approval in December, and subsequent submission to the Crown for assessment and approval in the new year.

32. Since August the project has continued to build momentum. Significant progress has been made to refine the design, develop cost estimates, and identify “value engineering” opportunities. This has involved working directly with WCC’s appointed designer (Beca) and the appointed construction joint venture (HEB and McConnell Dowell) at the Council offices in the ECI phase. This process has resulted in the cost estimates discussed later in this paper.

33. At the same time, significant progress has been made on the IFFA process including developing the levy proposal alongside CIP, early engagement with the Ministry of Housing and Urban Development (MHUD) and Treasury who will ultimately recommend to the Minister of Housing that the levy proposal be approved (or otherwise) and resolving a range of technical and operational issues necessary for administration of the levy. As discussed at

the August Council meeting, officers have re-engaged interested community stakeholders to provide an update on the potential levy (discussed more fully in Engagement and Consultation section of this paper).

34. [redacted]

Kōrerorero | Discussion

35. In 2019 / 20, a concept design was developed by Wellington Water Ltd, for the preferred option of a Lysis-Digestion and Thermal Drying plant to be located at Moa Point. The concept design provided a level of between 5 – 10% design definition, and was used to develop a project cost estimate at this time, of $158M (expected estimate) to $187M (P80 estimate). The cost estimates were then reviewed by two independent parties, whose own estimates came within 5% of these. This estimate was the basis for the project costs reported in the Business Case in 2022, prior to further design development. Note that because the design had not been developed further the Business Case referenced a potential total project cost of up to $350M.

36. In August 2022, prior to the Early Contractor Involvement (ECI) phase, an initial “pre-ECI” process and plant layout design was prepared. The design was based on a preliminary process design. During this preliminary design process, a discrepancy in sludge flows was identified which had the potential to substantially impact plant size. To keep the project progressing, the pre ECI design was based on the maximum potential size to confirm that it would fit on the available site. Therefore, the design prepared during the pre-ECI phase had not been optimised. Early, high level cost estimates indicated that the scheme would have a significantly higher cost than previously estimated and included In the business case.

37. Since August, a major focus of the project has been refining design and cost estimates to give sufficient certainty of affordability and value to allow a Council decision to proceed with the project.

38. The ECI phase involves collaboration between the WCC project team and WCC’s appointed project designers and constructors to scope, price, design, price and construct a project. The ECI phase allows for the project to benefit from the relevant expertise of the various parties in a collaborative working arrangement.

39. Ultimately, the ECI phase aims to allow for a more certain cost both through developed design and improved understanding of risk. The key outcome of the ECI phase is to arrive at a realistic cost estimate with an appropriate allocation of risk between WCC, the design and the construction parties.

40. The team refined has the design and undertook value engineering to reduce project costs and drive efficiencies. This process identified a range of efficiency opportunities and resulted in a reduction in the building area from 6,200 m2 to 3,600m2, simplification of building cladding systems, simplification of structure foundation systems, reduced scope of works over the Inlet Pump Station, simplified temporary words, reduced scope of changes to the Karori WWTP, a reduced construction period, and potential reductions in risk and profit margins.

41. The current cost estimate also includes more accurate assumptions about the phasing of costs over time, and the impact of inflation and cost escalations. It is a bottom-up estimate compiled by developing a detailed schedule of quantities and utilising available market rates from sub-contractor data and in-house rates. It includes the current best estimate of

contractor direct and indirect costs (e.g., materials, time, labour, civil and earthworks, margins and risk allowance), WCC managed and professional services costs (e.g., design, [redacted] professional services, project team costs) and contingencies (e.g., known risks and uncertainties etc.)

42. The expected cost estimate (P50 plus contingency) resulting from this process is $366.5 million [redacted] Key cost uncertainties include geotechnical conditions in limited parts of the site, final selection of materials, selection of specific plant and equipment manufacturers, and power supply upgrade requirements. These uncertainties have been factored into the P80 estimate in the form of contingencies and risks, consistent with best practice cost estimation practice.

43. The Wellington SMF Project cost is comparable to other plants completed in the USA within the last 5 years. Independent experts have noted that the costs of similar projects overseas, such as in the UK, have risen by approximately 40% over the last two years owing to supply chain pressures and inflation.

44. Although not final, and subject to further refinement, officers are confident that the expected cost estimate is sufficiently robust to base line the project budget. A decision to progress now is required to allow IFFA processes to progress sufficiently to allow financial close before 30 June 2023. This is in turn necessary to allow project completion before expiry of the existing resource consent for the disposal of sludge at the Southern Landfill. Analysis later in this paper sets out the funding options to meet final SMF costs.

IFFA funding and financing

45. Assuming a positive decision to progress the SMF, Council decisions are required to confirm funding the project under the IFFA model and the parameters of the levy proposal submitted by WCC to the Crown. The levy proposal forms the basis of what will ultimately become the Levy Order which provides the legislative basis for the CIP SPV to raise levy revenue from ratepayers to fund and finance the project.

46. The analysis set out in the August paper that informed the Council decision to progress the project under the IFFA model is still relevant (refer Sludge Minimisation Facility Project Funding – Agenda item 4.1 25 August 2022). Progressing under IFFA is the only approach the allows the benefits of the project to be realised without breaching the Council's external debt limits or requiring reprioritisation of the Long-term Plan. For this reason, we continue to recommend progressing under the IFFA model.

47. Since in principle decisions by Council in August 2022 on the commercial principles for the levy, further refinement of levy design has progressed. This has been informed by feedback and input from CIP, alongside further economic analysis of the recipients of benefits of the facility. This work has only resulted in a recommended revision to the beneficiary groups used to set the levy (discussed below), other levy parameters that Council agreed in principle in August remain the same. Key principles, their rationale and any changes since August are set out in the table one below.

Table one: Recommended levy parameters

Parameter	Recommendation	Change	Rationale (original or for any

[3] A P50 estimate represents the cost that is expected to be exceeded with 50% probability, [redacted]

		since August	relevant change)
Levy Area	All current and future rate payers within the existing Wellington City Council rating catchment	No	Benefits of SMF accrue to all ratepayers within catchment
Levy Period	30 years	No	Aligns to expected useful life and depreciation period of the facility. Balances improved levy affordability against higher whole of life costs. NB: The levy period will technically extend for three years after the 30-year period to allow for any delinquent levies to be collected.
Levy start date	Levy to commence in July 2024, at 25% of the full levy and increasing linearly to the full levy over the next three years	No	Aligns levy with visible progress on facility and better aligns levy timing with current projections of general rate changes.
Allocation of levy – beneficiary groups	Group 1: Ratepayers directly connected to the facility – 70% allocation Group 2: All WCC ratepayers– 30% allocation NB: Beneficiary groups are not mutually exclusive	Yes	See paras 48 - 52
Allocation of levy – ratepayer type	75% of levy paid by residential ratepayers, 25% by commercial ratepayers.	No	Residential ratepayers are responsible for a higher relative proportion of wastewater
Allocation of levy – capital value	Residential ratepayer levy 25% fixed per rating unit and 75% variable based on capital value Commercial ratepayer levy 100% variable based on capital value	No	Supports a progressive and affordable levy, whilst generally being consistent with existing Council practice Residential property wastewater generation is relatively uniform due to most households being of similar size, supporting a fixed component. Very large range of commercial property values (<$100,000 to >$100m) could lead to fixed component being unaffordable for

			lower value commercial properties.

Change to recommended beneficiary groups

48. IFFA legislation requires that the application of the levy should consider (amongst other things) the distribution of expected benefits from the SMF and the extent to which each property causes the need for the SMF, while broadly aligning with each property's ability to pay. A summary of the key benefits of the SMF are set out in Table two.

Table two: Key SMF benefits

Key Benefit	**Description**
Reduce solid waste to Southern Landfill	Less sludge to landfill, which lowers amount of solid waste that must also be added. SMF would represent 20% of the target reduction by 2031.
Reduce carbon emissions	Less solid waste means fewer carbon emissions from landfill. Solid waste & wastewater treatment are 90% of Council's gross emissions. Insurance against rising ETS prices.
Enhance resilience of sludge management	Dewatering facility no longer a single point-of-failure, e.g., in an earthquake (previous incidents have impacted all WCC ratepayers through increased transport movements, a reduction in service and increased costs). More options for disposal of sludge, providing insurance against changes in govt policy for sludge disposal.
Discontinuation of sludge pipeline	Sludge no longer piped from Moa Point to Southern Landfill, so lower risk of pipeline failure.
Reduce odour emissions	Lowers the risk of odour emissions.
Enable future economic growth	Expanded capacity for waste production enables greater economic production.
Enable future population growth	Expanded capacity for waste production enables greater population growth.
Beneficial re-use	Potential for improved sludge to provide beneficial re-use, e.g. biosolids application to land for fertiliser. Biogas from the process could be reused for electricity generation.
Improved commitment to Mana Whenua values	Will move sludge treatment more in line with the principles of rahui in disposing of human waste.
Usage	Treatment of wastewater at a long-term fit for purpose and resilient plant.

49. In August 2022, three beneficiary groups were proposed, being properties connected to the SMF (50% allocation), properties connected to the wastewater network (but a different wastewater treatment plant) (25% allocation) and all WCC ratepayers (25% allocation). The three proposed beneficiary groups are not mutually exclusive, a property directly connected to the facility is also connected to the broader network and enjoys the broader benefits of the facility. This meant that under the proposed structure directly connected properties were expected to pay approximately 90% of the total levy, with the rest split across remaining properties.
50. Levy allocations are based on economic benefits analysis carried out by Insight Economics. Since August further refinement of this analysis, including using updated connection and rating information data has occurred, alongside feedback from CIP around the differentiation between the latter two beneficiary groups.
51. Officers agree with the updated benefits analysis and now recommend a simplified structure, retaining connected properties as a beneficiary group (70% allocation), and collapsing the latter two proposed groups into a single group (30% allocation). This approach is simpler and much easier to understand and is supported by stronger analytical backing, as the broader benefits of the SMF accrue equally to everyone in Wellington, irrespective of whether they are connected to the wastewater network or not.
52. Under the revised structure the overall proportion of levy paid by directly connected properties remains broadly the same, increasing by approximately 2% to approximately 94%, with the remainder met by properties not connected to the plant. Consequently, levies for directly connected properties will rise modestly, while properties whose wastewater is treated elsewhere have a reduction in costs. Unconnected property levies also rise modestly. The change in groups and financial impacts on different groups is summarised in table three below.

    Levy estimates

53. Using the parameters described in table three and assuming a $299 million funding amount and an assumed 5% financing base rate, expected annual levies for the first full year (2027) are as shown in Table three for the various ratepayer beneficiary groups. Levies are shown per $1 million capital value.

Table three: Estimated levies and impact of change in beneficiary group structure

Total indicative annual levy per $1 million of capital value (as at July 2027)		
	August three beneficiary group model	Proposed two beneficiary group model
BG1: Directly connected properties		
Residential	$273	$281
Commercial	$417	$417
BG2: Properties connected to wastewater network but not SMF*		
Residential	$124	n/a

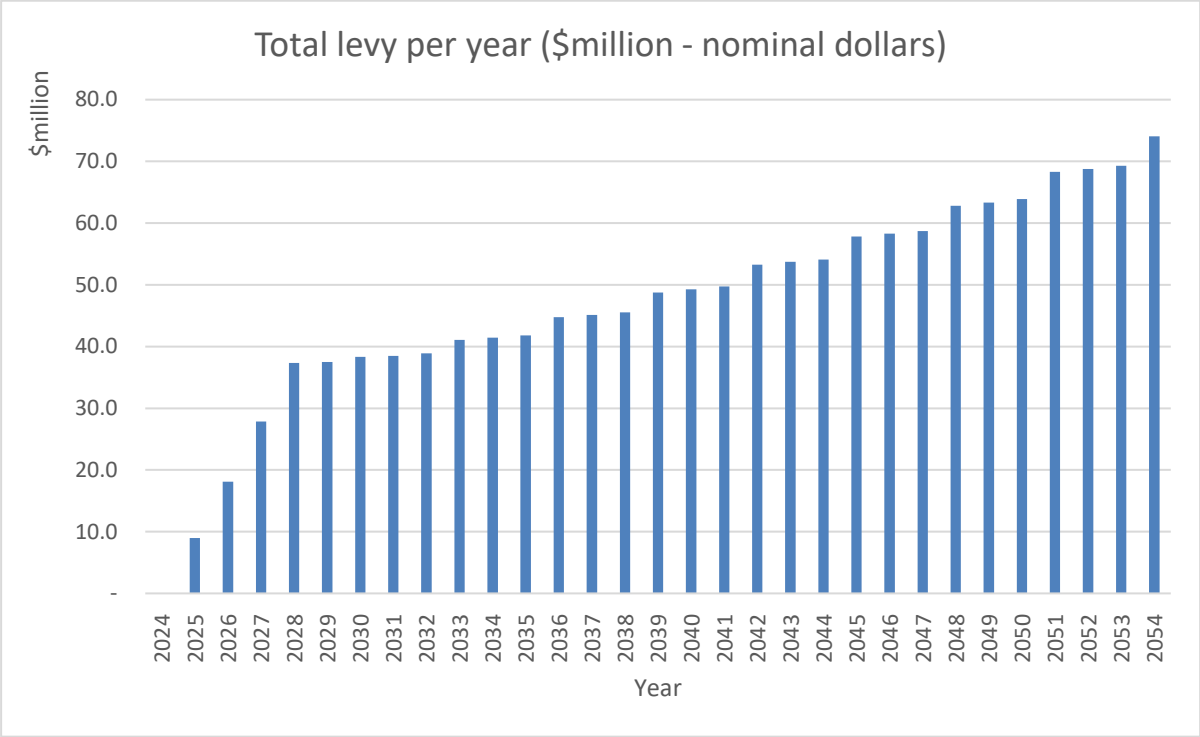
Commercial	$196	n/a
BG3: Other properties		
Residential	$61	$73
Commercial	$90	$108

* - properties in BG2 under the three-group model transition to BG3 in the two-group model.

54. The levy is subject to escalation over its 30-year period. Escalation in the total levy revenue has been based on Council forecasts growth in both the number of rateable properties and capital values. The variable portion of levy charges (applicable to both residential and commercial properties) is forecast such that the nominal levy paid by a given property will remain the same per $million of capital value over the 30-year period.[4] The fixed portion of the levy (applicable only to residential properties) is forecast to grow at a cumulative average growth rate of 1.9% p.a. (from the end of the ramp to the final payment year).
55. Chart one below shows the profile of the annual levy over its 30-year life. At an aggregate level, levies grow on average by 2.7% per annum.[5] The exact impact of escalation on individual properties in each beneficiary group depends on the number of properties in each group in future years and the relative capital values of properties in the group. As a general rule, a property's levy should be expected to grow in line with overall growth in capital value over the 30-year period.

    Chart one: Estimated aggregate levy collected by year

[4] The nominal levy paid by each property is expected to increase on an absolute basis as capital values are expected to appreciate over time.
[5] Excluding the ramp period.



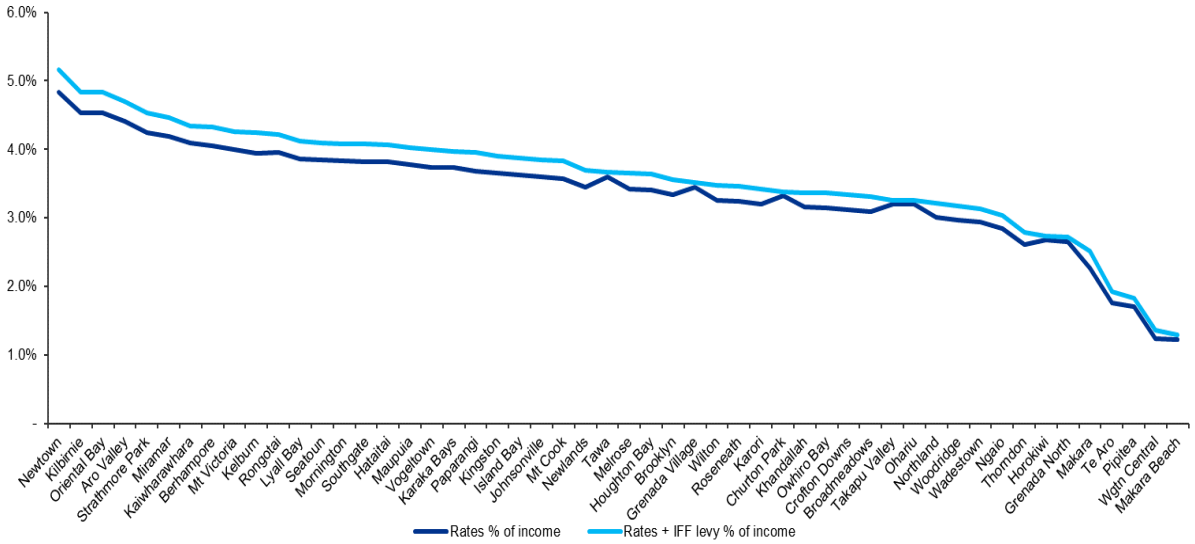
Affordability

56. The impact of the levy on ratepayer affordability (also conducted in August) has been re-examined by assessing the maximum potential levies (see Managing cost risks and contingencies section) to be paid by connected properties, in addition to their forecasted rates, as a proportion of total median household income in rating year 2028. That analysis showed that just one suburb[6] exceeded the 5% of net income, which as set out in the Shand report (2005) is a commonly used indicator, but not a bright line, measure of affordability. It is expected that affordability will improve over time as expected income growth outstrips projected growth in levies and rates.

57. As a proportion of rates, levies for residential properties are expected to represent an increase of approximately 7% to a median household rates bill in rating year 2028.

Chart two: Levy affordability by suburb in 2028 (first full levy year)

[6] Newtown has a levy affordability ratio of 5.2% because it has comparatively high capital values and lower median net income.



58. Affordability has not been assessed for properties not connected to the SMF on the basis that their annual levies will be much lower. We note that properties whose biosolids are not treated by the SMF generally have a lower median CV value, and therefore are expected to have lower income. However, the reduction in levy amount is considered sufficiently large enough to offset any potential income and affordability reduction.

59. Affordability for commercial ratepayers has been assessed by comparing potential levies against commercial rental as a proxy for business costs. Direct comparison of levies against commercial revenue or profit is not possible due to data availability. Rental yields generally range between five and eleven percent meaning a tenant in one million dollar commercial property incurs rental expenses of around $50,000 to $110,000 per annum, meaning the levy represents less than one percent increase in costs.

60. As a proportion of rates, levies for commercial properties are expected to represent an increase of approximately 5.5% to a median commercial rates bill in rating year 2028.

Kōwhiringa | Options

Overall funding arrangements for the SMF

61. In August, Council approved, in principle, a cap on the IFFA funding amount of $299 million (the IFFA cap). The purpose of the IFFA cap was to provide some certainty to allow levy proposal preparation to continue, but also to manage the financial impact of IFFA levies on ratepayers. At the time, it was not a given that the project cost would fall under the cap.

62. The current expected cost estimate for the facility is $366.5 million, which sits above the IFFA cap. This is officers' current best estimate of expected costs of the project.

63. This cost estimate is above the IFFA cap. A necessary feature of the IFFA model is that there is upfront certainty of overall SMF funding. This provides SPV lenders and CIP confidence that the SMF will be built, which in turn is critical to support social licence for the levy, which is used to repay lenders.

64. In addition to project cost uncertainty, there are some factors within the IFFA structure itself that will affect the amount of levy required to raise $299 million of funding. The largest of these is the borrowing rate that can be achieved by the SPV. A higher

borrowing rate will increase the amount of levy income required to support a given level of project financing. Final base rates will not be known and 'locked in' until financial close of the IFFA deal, which is not projected to occur until June 2023.

65. Interest rates have been subject to substantial volatility recently caused by the monetary response to high inflation and by global market volatility. This uncertainty presents a risk to costs under the IFFA structure. For the purposes of the levy estimates set out above assumed base interest rates are 5%. This represents a minor buffer over the current best estimate of borrowing costs which sits around 4.75%.[7]

66. To manage the risk that interest rates rise after the levy proposal is submitted for approval but before financial close, CIP advise and officers support, that the levy proposal should include additional buffer to allow for the risk that interest rise unexpectedly between now and financial close. Officers recommend that the buffer is sufficient to allow for borrowing rates to increase by an additional 1% (i.e., to 6%). The likelihood of interest rates being higher than this level at financial close, and the levy proposal not being sufficient to support the required level of borrowing, is low. If it turns out that borrowing rates are higher than 6%, officers recommend reconsidering options available at the time before advising Council of a recommended approach to proceed.

67. Including the buffer in the levy proposal does not mean that it must be utilised. The levy proposal sets the maximum amount of levy that can be collected in each year over the levy period (i.e., 30 years). However, if it isn't necessary to spend that amount either because project costs are lower than expected or borrowing costs are lower than 6% the IFFA allows for less levy to be collected, or, if it is collected, for it to be returned in the form of lower future levies. This implication is that there is little risk to including the buffer, provided Council support a higher levy amount being charged if it is needed.

68. Levy estimates for the different beneficiary groups with the interest rate buffer are presented in table four. For ease of comparison, we repeat the levy estimates presented earlier in table two.

Table four: Impact of interest rate buffer on levies

Total indicative annual levy per $1 million of capital value (as at July 2027)		
	Assumed base 30-year interest rate	
	5%	6%
Directly connected properties		
Residential	$281	$321
Commercial	$417	$476
Other properties*		
Residential	$73	$83
Commercial	$108	$123

[7] Officers caution against comparing these interest rates against Council borrowing rates which are for much shorter lengths of time. It is not an 'apples and apples' comparison to compare these shorter-term rates against a rate that provides certainty over a 30-year period.

	(Best estimate of levies at publication date)	(Higher levies only if buffer required to be used)

69. The affordability analysis presented earlier in the paper was based upon of these buffer-case levy estimates.

Funding expected SMF costs above $299 million

70. IFFA uses a project financing model, which means that borrowing, levy income and funding towards project costs are effectively ringfenced within the CIP SPV. This approach is necessary to achieve balance sheet separation for the Council. To secure the levy income, the Crown will approve the levy proposal and lock in the maximum levy revenue for its 30-year term.
71. The implication of this model is that it is necessary to have a clearly agreed process for meeting costs ahead of project commencement. Otherwise, the risk that other sources of funding may not be secured could undermine the ability of the SPV to raise finance and/or increase the risk of the levy proposal not being approved.[8]
72. It is therefore necessary to agree now, how SMF costs above $299 million are to be met. [redacted] The options available to manage this risk are:
    a. Increase the IFFA cap to allow for cost risk
    b. Utilise any unused interest rate buffer to raise additional finance
    c. Council meets any costs above the cap from future long-term plan budgets through additional debt
    d. Council funds up to $36 million of project costs from currently approved budgets (treated as a “sunk cost”), which are already budgeted in the 2022/23 Annual Plan
    e. Reduce the scope of the project
    f. Re-assess broader options considered at the business case phase
    g. Not proceed with the project

Option one: Increase the IFFA cap to allow for any cost risk

73. Council could agree to support a levy proposal that provided for additional funding (i.e., up to $366.5 million). To provide funding of $366.5 million, annual levies would increase by approximately 22%. At the worst-case interest rate assumption, annual levies for a connected residential property would rise to approximately $400 per million dollars of property capital value.

[8] Because the ability to charge and collect the levy relies on social license, which may not be present if the SMF is not completed.

74. This approach minimises any risk that IFFA funding will not be sufficient to meet costs, and does not require other funding sources to be used. On the other hand, this approach requires Council to be comfortable with much higher potential levies.

75. Officers do not recommend this approach as such levies could introduce uncertainty of the Crown approval of the levy proposal and therefore of reaching financial close.

Option two: Utilise any unused interest rate buffer to raise additional finance

76. Recognising that it is unlikely that the full interest rate buffer is used, Council may have the opportunity to utilise any unused interest rate buffer to fund project costs.

77. The levy proposal itself sets the maximum levy revenue each year that can be collected. Whilst this maximum was sized by allowing a buffer for increases in interest rates, the levy proposal itself does not require that the buffer is for interest rates or another purpose. On the basis that the likelihood of interest rate buffer being fully utilised is low, Council could decide that the proposed interest rate buffer is sufficient to cover multiple risks.

78. Officers estimate that if base interest rates achieved at financial close are as currently expected, the buffer could provide around $50 million of additional funding for the SMF. Technically, if interest rates fall sufficient the amount of funding supported by the levy could rise even higher. Officers expect that for the purposes of assessing the levy proposal, officials will need clarity around the maximum funding amount for the SMF. Consequently we propose capping the overall funding amount provided at $350 million.

79. If all the buffer was used to fund project costs (rather than higher base interest rates) the impact on levies is the same as if base interest costs were 6%, as shown in table four (right hand column). In this case, expected annual levies for connected residential ratepayers would be $321 per annum per $1 million of capital value.

80. The downside of relying on the buffer is the risk of it providing insufficient funds to cover costs, necessitating the use of other sources of funds. On the other hand, it supports levies remaining at acceptable levels as it does not require any further increase to the levies already presented in this paper.

81. Officers recommend pursuing this option,

Option three: Council meets the costs above the IFFA cap from future long-term plan budgets

82. Council could agree that the $67.5 million of expected costs over $299 million be met from future Council budgets. All else equal this would require either an increase in debt, and future rates, or reprioritisation of the Long-Term Plan.

83. Officers do not recommend relying solely on this option but do recommend partially progressing on this basis.

Option four: Council funds up to $36 million of project costs from currently approved budgets, which are already funded in the Long-Term Plan

84. Council has approved a budget for the SMF project up to the end of this financial year of $36 million. Under the IFFA, these costs are eligible costs and so can be included in the levy proposal to be recouped in the future in the form of grant funding provided to WCC from the CIP SPV.

85. However, in the current long-term plan and fiscal projections, no future IFFA revenue to recoup these costs has been forecast. This means that Council could agree to meet project costs up to the $36 million budget, treating it as sunk cost, and this would have no impact on debt or the need to reprioritise expenditure.

86. Officers recommend pursuing this option.

Option five: Reduce project scope

87. Officers have assessed the option of delivering the SMF under a reduced scope, for example that excludes the thermal dryer component of the plant. Proceeding under this option for a reduced scope would reduce the expected cost of the SMF by approximately $16 million. This reduces the amount of additional funding required for the project.

88. Removing the thermal dryer would have material negative impacts on the outcomes achieved by the SMF. While the SMF would still produce a grade A biosolid without a thermal dryer, the sludge produced is less flexible for re-use (diversion from landfill) and would still require mixing with general waste if sent to landfill, which means that it does not de-couple sludge disposal form landfill operation, a critical project objective. [redacted]

89. The lack of alternative uses increases the risk of needing to dispose the product at landfill, which would have volume fourfold relative to that produced with a thermal dryer. In the absence of a new resource consent for disposal of this product, which is highly uncertain, transport costs and emissions would increase significantly through the double impact of having to transport significantly more waste further to an appropriate site.

90. Officers do not recommend pursuing this option.

Options six and seven: Not proceed with the project or reassess business case options

91. Not progressing the project would require future sludge to be trucked to Bonny Glen once the existing resource consent for disposal lapses. This is not a realistic long-term option because:

    a. The sludge from Wellington's WWTPs is highly unstable and decays readily because it comes from high-rate sewage treatment plants (which is an outcome of the limited space available for the WWTPs). Therefore, the sludge in its untreated form is prone to producing significant amounts of odour as it decays, which occurs very quickly after production. The location of the WWTPs means that the untreated sludge would need to be transported through dense, urban environments, which is unlikely to be acceptable to the community.

    b. Untreated, dewatered sludge tends to leach during transportation, which creates a risk of spillage of effluent from vehicles.

    c. The carbon emissions associated with transporting untreated sludge such long distances will be significant.

    d. Mana whenua are unlikely to support this option. This is because the transportation of human effluent / by-products past wāhi tapu, marae and other significant sites is considered to be culturally abhorrent.

92. Officers have also considered whether reassessing options ruled out at the business case phase is worthwhile given the increase in expected costs of the SMF. Officers assess that the major driver of cost increases are broad based, including cost escalation

of equipment, suppliers and professional services. The alternative solutions would be subject to similar cost increases.

93. A reassessment of options would likely result in the SMF being assessed as the best option, whilst also resulting in delays to project progress that could result in further cost increases and delay ability to cease dumping sludge at the Southern Landfill until potentially after the existing resource consent lapses.

94. Officers do not recommend pursuing these options.

A waterfall approach to meeting expected costs is likely to be best

95. Officers do not recommend further consideration of increasing the IFFA cap, reducing project scope or not progressing the project (options one, five, six and seven) as these options either result in unacceptable levy costs, or materially undermine the outcomes sought from the project.

96. Officers recommend a mix of the remaining options (options two, three and four) to manage cost risk. At the current expected cost estimate, $67.5 million of additional project funding is required.

97. Officers recommend Council agrees to permanently contribute the already approved and forecast $36 million project budget to the SMF. This option treats the current approved budget as a sunk cost and has no impact on existing Council forecasts or debt levels, and mitigates the increase in levies that occur as IFF funding increases.

98. Officers then recommend utilising any unused interest rate buffer to meet remaining project costs. $31.5 million of funding is required from the interest rate buffer to meet the expected cost estimate.

99. There is a risk that interest rates increase by more than expected such the interest rate buffer may not allow for sufficient funding (or any funding) to meet these costs. In this circumstance we recommend that Council agree to meet remaining costs from the LTP should it be necessary. In the worst case, $31.5 million of Council funding could be required.

[redacted]

[redacted]

[9] On the basis that base rates remain as forecast providing a total maximum funding amount of $51 million, and $31.5 million is allocated to meet expected costs.

[redacted]

[redacted]	[redacted]	[redacted]	[redacted]			
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

107. On the basis that no additional Council funding is expected at this point, [redacted], officers propose that any additional funding is only budgeted and included in the LTP at the time it becomes necessary. Any contribution would be debt funded and recovered through future depreciation funded rates (subject to discussion below on the impact of the three waters reform). In this circumstance, officers confirm that based on current forecasts any debt is expected to be accommodated within debt limits given the relatively low potential amounts (refer chart three).

Managing timing risk

108. Project costs could vary between now and financial close and also thereafter. In the first circumstance, additional IFFA funding provided by the buffer can be accessed subject to interest rates being sufficiently low.

109. However, at financial close, a final IFFA funding amount needs to be agreed, and thereafter no further increase to IFFA will be possible. Drawing the maximum available under IFFA provides maximum flexibility to ensure any subsequent cost risk can be managed as outlined in this section. If costs are lower that total funding drawn, the IFFA provides that excess will be returned to levy payers in the form of lower that otherwise future levies[10].

[redacted]

112. For the avoidance of doubt, the IFFFAAA also provides that the Crown (including CIP) will not meet any of the necessary costs to complete the SMF.

Financial implications of additional Council funding in the context of the Three-Waters Reform Programme

113. Officers' current best expectation is that an additional Council funding contribution will not be necessary to meet the expected costs. However, to the extent a contribution was necessary Council debt would increase, and future rates would need to increase as the Council funded portion of the asset was depreciated over time.[11]

114. However, once the SMF is constructed by Council it will vest with the new three waters entity (on the basis that the reforms progress). Under the reforms it is proposed that Council water assets will transfer along with any water related Council liabilities.

[10] The IFFA provides for a Forecast Excess Levy mechanism whereby funding that is not required to meet eligible costs can be effectively returned to levy payers in the form of lower future levies.

[11] For example, if a $30 million contribution was required to fund a proportion of the SMF, rates would increase by the annual depreciation amount associated with that proportion of the plant, which would be $1 million per annum on a 30-year straight line depreciation basis.

Therefore, any additional Council contribution to SMF costs is only likely to increase Council debt levels, and rates associated with depreciation, for the period between those costs being incurred and transition to the new entity. From that point onwards, depreciation funding would be collected as water charges by the new entity.

[redacted]

[redacted]

[redacted]

Chart three: Debt to revenue impact of potential Council contribution

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted] [redacted]

[redacted] [redacted].

[redacted]

Kōrerorero | Discussion – Other matters

Administration of the IFFA structure – project funding and levy collection

141. The IFFA model creates separation of SMF project debt from the Council balance sheet. Project debt sits on the balance sheet of the CIP SPV (Sludge Finance Limited Partnership), with project funding provided to WCC as a 'capital grant'.

142. It is important to note that once approved by the Minister and enacted through Order in Council, IFFA levy revenue is for the benefit of the CIP SPV. For efficiency reasons the IFFA provides for the levy to be collected by the relevant local authority as a separate line item of levy payers' rates bills. It is proposed WCC acts as agent for CIP in collecting the levy.

143. The IFFFAAA is an administrative agreement that governs the arrangements between WCC and Sludge Finance LP for the provision of funding to meet SMF costs and for ongoing collection of the levy on behalf of the SPV. Officers seek Council approval to enter into the IFFFAAA and to delegate power to the WCC Chief Executive to finalise the terms of the agreement. Its key components are discussed below.

Project funding

144. Under the Act and IFFFAAA the CIP SPV is required to provide project funding to WCC upon provision of documentary evidence of WCC incurring eligible SMF costs. Under the Act, eligible costs incurred by WCC include costs of construction of eligible infrastructure and levy administration costs, including collection and enforcement.

145. Construction of eligible infrastructure includes the costs of planning, design, [redacted] enabling works and construction costs incurred directly or via third parties. WCC is, and will continue to, record SMF eligible costs through a dedicated cost centre within the council's internal financial management system to ensure robust financial management practices.

Levy administration and collection

146. WCC will act as Sludge Finance LP's agent in administering the levy. As noted above, the levy will be assessed and collected as part of residents' rates bills, split out as separate line item. Operational work to implement this will be completed between now and levy commencement in 2024.

147. Levies will be collected consistent with current WCC rates remission and postponement policies, such that if a ratepayer is subject to remissions or postponement, any levies applicable to the property will be treated the same.

148. The IFFA allows WCC to recover the costs of administration through the levy itself. Current levy estimates include an allowance for these costs of $50,000 per annum, escalating over the 30-year period.

149. Officers recommend that Council agree to waive this assumed administrative fee on the basis that the marginal ongoing cost to WCC of administration is likely to be low, that waiving the fee helps keep levies lower and for consistency with other IFFA transactions contemplated to date. Costs of administration are likely to be low as it is expected there will be material synergies between the levy raising and collection process and existing rates processes.

Levy enforcement

150. Under the IFFA, levy revenue is subordinated to rates revenue. This means that ratepayer payments are for the benefit of Council until the rates obligation is extinguished and for the benefit of the CIP SPV and meeting the levy thereafter. Therefore, the levy should have no impact direct impact on Council revenue, bad debts or overall fiscal position.

151. As Sludge Finance LP's agent, the IFFFAAA requires WCC to take action to recover any and all levy amounts that have not been paid by levy payers by the due date and that remain unpaid, in a manner consistent with its procedure for collecting unpaid rates, under the Local Government Rating Act. For the avoidance of doubt, this obligation applies whether or not a ratepayer has paid its rates.

152. The only exception to the above is that under the act the Council can elect to inform Sludge Finance LP of its intention not to take action to recover any unpaid levy. In this circumstance, the relevant powers to collect, enforce and apply penalties to the unpaid levy under the act, are available to the SPV and the SPV may, at its discretion, take relevant enforcement action.

153. It is important for Council to therefore understand that in approving the levy proposal it is agreeing to administer and enforce the levy as if it were for the benefit of Council and that its options to make decisions around levy collection are limited to those consistent with its existing policies. Similarly, future changes to remissions or enforcement polices will need CIP approval before they apply to the levy.

[redacted]

Infrastructure endorsement and levy endorsement

156. The IFFA provides for the relevant local authority to provide what is known as a Levy Endorsement and an Infrastructure Endorsement in support of any levy proposal that gets submitted to the Crown for approval.

157. The IFFA is designed to provide flexibility to allow a range of parties to develop and submit levy proposals, including private sector developers. The endorsements foresee

this circumstance and ensure that the Council supports development and associated levies proceeding under the Act in their area of jurisdiction.

158. In the case of the SMF, the Council is both the levy proposer and the infrastructure developer, and the relevant local authority for the endorsement. In this circumstance it should be self-evident that Council supports the project proceeding under the IFFA.

159. Even so, CIP have advised that for completeness the Council should provide the Levy and Infrastructure Endorsements. The Endorsements themselves are simple one-page documents representing Council support of the relevant issue. The Infrastructure Endorsement sets out that the Council is satisfied that the specifications of the SMF are compatible with the wider infrastructure network, that operational and maintenance costs will be able to be met and that WCC is supportive of the infrastructure and the benefits it provides.

160. The Levy Endorsement sets out that WCC endorses the proposes levy, the manner in which it has been structured and that it has no grounds to believe that the levy will compromise its ability to collect rates. Representative versions of the endorsements are appended to this paper for reference.

161. Officers seek Council approval and delegation to the WCC Chief Executive to finalise and submit the endorsements alongside the levy proposal.

[redacted]

[redacted].

[redacted]

[redacted]

Budgetary matters

[redacted] *2022/23 Council budget*

[redacted]

176. [redacted] The current WCC budget for the SMF project for 2022/23 is $29.513 million. Technically, to allow the increased expenditure [redacted] Council need to approve an increase to this year's budget by $40 million.

177. The budget increase is a technical matter, providing Council authorisation to incur the expenditure. Any increased expenditure is fiscally neutral for the Council as it will be supported by additional Council revenue in the form of capital grant funding provided by CIP under the IFFA structure once financial close is achieved.

IFFA funding and SMF project costs

178. Pending approval to progress the SMF, Council LTP and future year budgets need to include costs of the SMF. Similar to outlined above in respect of the prefunding agreement the increase in budget will be offset by additional grant revenue received from the CIP SPV. Consequently, IFFA funded project costs will be fiscally neutral from a Council perspective.

179. Specific phasing of project costs are subject to finalisation. Officers seek Council approval for a baseline budget for the SMF project of $366.5 million and delegation to include these costs, and IFFA revenue, into the Council's LTP through the next update due to be complete in 2024.

Consenting

180. Resource consents and permits have or will be sought for the following matters:

    a. A Notice of Requirement (NoR) to alter Designation 58 (Moa Point Drainage and Sewage Treatment) as is set out below.

    b. Resource consents have been applied for to Greater Wellington Regional Council for the discharge of contaminants to air (odour, biogas flaring and emissions from an emergency diesel generator); discharge of stormwater; and earthworks exceeding 3,000m2 and associated discharge of sediment laden

runoff. Draft conditions have been received and final conditions for these resource consents are due in December 2022.

- [redacted]

d. A permit pursuant to the Wildlife Act has been applied for to relocate lizards from the SMF site, as is expected to be granted by January 2023. A similar permit has been applied for to relocate lizards from the Grassy Knoll.

181. On 30 June 2022 Council authorised the Chief Executive to issue the Notice of Requirement (NOR) to facilitate the SMF at Moa Point under the Resource Management Act 1991. Eleven submissions were received with one in opposition. This NOR has since been publicly considered by an independent hearing commissioner on behalf of WCC, and their recommendation on the NOR is expected approximately 20 January 2023.

182. The next step is for the recommendation to either be accepted or rejected; whereupon following an appeal period and the administrative inclusion of the NOR in the District Plan, construction may begin. The first available time the recommendation can come back to Council is 9 March.

183. Officers recommend delegating the acceptance or rejection of the NOR recommendation to the WCC Chief Executive given the technical nature of the assessment, the lack of public opposition to the NOR (only one individual opposed), and the potential for up to six weeks of time savings.

Whai whakaaro ki ngā whakataunga | Considerations for decision-making

Alignment with Council's strategies and policies

184. The 2021-31 LTP outlined six priority objectives including creating a functioning, resilient and reliable three waters infrastructure. The SMF project fulfils this objective by building a resilient plant which enables the city to reduce its waste volumes at the landfill.

185. During 2021-31 LTP deliberations Council resolved to set the debt to revenue ratio limit at 225%. The Local Government Funding Agency (LGFA) limits the amount of debt Council can hold at 300% of their revenues. This is decreasing down to 280% in 2026. Progressing the SMF under the IFFA maintains agreed debt headroom.

186. The Wellington Region Waste Management and Minimisation Plan (2017 – 2023) committed WCC to a significant reduction in waste to landfill. The key target in this plan is to reduce solid waste sent to Class 1 landfills from 600kg per person per annum to 400kg per person by 2026. Developing a solution that removes the reliance on the Southern Landfill for the disposal of sewage sludge is the largest single initiative WCC can pursue to achieve this target.

187. In the Te Atakura – First to Zero Strategy, WCC committed to reducing carbon emissions by 57% by 2030 and 100% by 2050. The Southern Landfill is the biggest single contributor of carbon emissions from WCC operations, therefore achieving the carbon reduction goals will not be possible without finding a more environmentally

sustainable solution to processing Wellington's sludge, thereby enabling waste minimisation to occur, and reducing carbon emissions from solid waste management activities.

188. The Wellington Resilience Strategy was published by WCC in March 2017 to provide a blueprint for dealing with future shocks and stresses that impact WCC and its communities. In this strategy, WCC has committed to undertake an options assessment for sewage sludge disposal to identify preferred options on the basis that the status quo is not consistent with how Wellington perceives itself environmentally.

189. A Strategic Case for Sewage Sludge Management was prepared ibn 2019. The Strategic Case was completed by Wellington Water to understand the future management of sewage sludge within the Wellington Region, and had three key focus areas:

a. Reduce sewage sludge sent to landfills from 64kg to 4kg per person per annum;

b. Contribute to the zero-carbon act; and

c. Assist WCC with the resource consent processes for the Southern Landfill.

Engagement and Consultation

190. Through the Long-Term Plan 2021, we consulted Wellingtonians on a capital investment for the SMF and the option of IFFA funding. At a high level the feedback was closely split between the funding options. Council adopted IFFA as the preferred options on the basis that it enabled the delivery of other much needed infrastructure, managed financial risks and retained headroom for future projects.

191. In April 2022 WCC carried out further community engagement, primarily targeted at the commercial sector, seeking feedback on the proposed IFFA funding approach. Forty-two submissions were received. Some concern was raised about the impact of levies, particularly on commercial levy payers. The summary of those submissions can be found on Council's website.

192. In November, at the request of Council, officers provided an update on SMF levies to key commercial stakeholder groups (the Wellington Chamber of Commerce and the Property Council) and posted an update on the WCC website. This update included revisions to commercial levies made subsequent to previous engagement, including reducing the share met by commercial ratepayers to 25% from 40%. Both commercial stakeholder groups appreciated officers providing the update, recognised the strategic case for the investment and were supporting of the updates to the levy methodology, whilst highlighting the importance of ensuring the impact of levies on ratepayers was affordable and sustainable.

193. Further information on engagement and consultation considerations have been included in this paper.

Implications for Māori

194. Mana whenua have been directly involved in the multi-criteria assessment process selecting the preferred technology for treating future wastewater in Wellington. As part of this engagement the key principles and values embraced include:

a. The principles of rahui in disposing of human waste

b. Harnessing the resources in sewage sludge to give them another life

c. Kaitiakitanga – having a positive impact on the environment and our communities through the action we take.

195. Engagement is underway with mana whenua in relation to:

a. The resource consents. The key feedback received to date has been the need to implement appropriate accidental discovery protocols and work with mana whenua to ackionledge the signficane of the Moa Point area to Māori.

b. Broader outcomes. WCC and the ECI contractor activerly seeking to idetify opportunities to involve Māori businesses in the construciton and oepration of the SMF.

c. Commence the co-development of a biosolids re-use strategy so that culturally appropriate ways can be established to reuse the biosolids product from the SMF, allowing it to be diverted from landfill.

Financial implications

196. The IFFA model creates separation between the Council balance sheet and project debt. From a Council perspective, financial impacts will involve:

a. Recognition of new revenue equal to the IFFA financing amount (e.g., $299 million) in the form of capital revenue[14] funding from the CIP SPV over the construction period (2024-2026)

b. Capitalisation of the SMF facility as a capital asset on the Council balance sheet as it is constructed

c. Levies collected on behalf of the CIP SPV to have no impact on Council.[15]

197. Once constructed the asset will be operated by the applicable Wellington region water entity (assumed to be Entity B under the Three Waters Reform16). At this point it is expected the asset will vest to that entity without compensation, resulting in one-off loss on sale. Any debt on the Council balance sheet due to the SMF (from a Council contribution for example) will transfer at that point also, mitigating any loss associated with any Council funded element of the plant.

198. Ongoing maintenance and depreciation expense will be met by the relevant operating entity.

Budget and short-term financial implications

199. Paras 174-177 noted the need to increase this year's Council budget for the SMF to allow for early and enabling works. As financial close for the SMF is expected before the end of the fiscal year, this expenditure will be supported by additional revenue in the form of IFFA grant funding for the project. Consequently the budget increase is fiscally neutral.

Funding risks

[14] Similar to Council recognition of revenue from Waka Kotahi funding assistance for transport projects.

[15] Levies to be passed through to CIP similar to rates collected for the benefit of GWRC.

[16] If Three Waters does not progress it is likely the asset will remain on the Council balance sheet with an ongoing depreciation expense recognized over the remaining life of the asset.

200. Officers recommend utilising the existing $36 million Council budget to meet a portion of SMF costs. Doing so has no direct fiscal implications as current fiscal projections do not assume spending is replenished from IFFA grant funding. There is however an opportunity cost of this approach as it foregoes revenue that could otherwise have been received from IFFA grants.

[redacted]

Legal considerations

202. There are significant legal, liability and contractual risks associated with this project.

203. This will be one of the first projects to be considered under the IFFA and there are inherent legal and other risks associated with being the first to test a new legislative regime.

204. Together with external legal advisors, the legal team is engaged on key aspects of the project and the General Counsel is a member of the project governance group.

Risks and mitigations

205. Project funding risks and contingencies were discussed earlier in this paper.

206. The SMF project is utilising industry risk management processes consistent with significant infrastructure project best practice.

207. Use of the IFFA legislation for delivery of infrastructure across New Zealand is emergent. This means the practices to achieve financial close are not well established, including the approval processes managed by MHUD and Treasury, nor are finance offerings to support projects. This adds some risk to achieving project timelines, approval steps and receiving favourable finance terms.

208. Officers are managing these risks though close collaboration with the CIP team and their advisors, who are experts in their respective fields.

209. Transparent pre-engagement with MHUD and the Treasury, and with financiers, aims to ensure there are no surprises as the project progresses and that issues can be identified and resolved early and proactively.

210. As the IFF process progresses reputational risks of a decision not to progress under IFF increase. This will be particularly the case after market sounding for finance, and pre-engagement with the Crown on the levy proposal, occur. Ceasing the process could negatively affect relationships with CIP and the Crown, who are investing resource to support the project. Additionally, overall confidence in the IFF model could be undermined for future projects.

211. The IFFA involves an additional levy on ratepayers to meet the costs of the project. Once enacted this could lead to some concern from ratepayers or community groups. This risk has been managed through the levy engagement process and ongoing communications plan. Alternative options to the SMF would likely lead to higher costs to ratepayers.

Disability and accessibility impact

212. There are no disability or accessibility impacts required in this paper.

Climate Change impact and considerations

213. The SMF project aligns with a number of our Te Atakura goals, through:

    a. Reducing solid waste sent to landfill

    b. Reduction in carbon emissions, pollution prevention and control and sustainable management of living natural resources and land use

    c. Improvement in resilience and reliability of Wellingtons wastewater network

214. This provides an attractive investment opportunity to entities where there are increasing mandates to deploy capital in line with sustainable development goals.

Communications Plan

215. A draft project communications and engagement plan has been developed. Proactive project communications will be managed by WCC's communications team with input and content supplemented by project partners.

Health and Safety Impact considered

216. Compliance with all Health and Safety regulations is a minimum requirement of all project planning and current physical works. All contractors are required to adhere to Health and Safety procedures.

Ngā mahinga e whai ake nei | Next actions

217. Pending Council approval of the recommendations in this paper the project will progress towards construction in the new year. Key milestones are set out in the table below.

Table six: Project milestones

Milestone	Expected Completion
Council Approval	December 2022
Finalisation and submission of levy proposal	February 2022
[redacted]	[redacted]
Main Contractor award	April 2023
Cabinet approval of levy proposal	April/May 2023
Order in Council to enable levy	April/May 2023
Site construction works commence	May 2023
Financial close of IFFA transaction	June 2023
[redacted]	[redacted]
Construction completes	November 2025
Plant commissioned for handover	June 2026

Attachments

Attachment 1. Summary of Previous Consultation and Engagement
Attachment 2. Summary of Feedback Addressing Cost
Attachment 3. Representative Levy and Infrastructure Endorsements
Attachment 4. [redacted]