

Hon Michael Wood

Minister of Transport
Minister for Workplace Relations and Safety



24 September 2021

Sue McCormack
Acting Chair
KiwiRail
PO Box 593
WELLINGTON 6140

Dear Sue

Thank you for your cooperative work with Waka Kotahi the NZ Transport Agency the Ministry of Transport and the Treasury to provide me advice on the ongoing delivery on the NZ Upgrade Programme (the Programme). You have made a great deal of progress in bringing the Programme to life. There is much work to do and the efforts made now to establish a clear set of expectations will facilitate delivery of the Programme.

This letter sets out that the Minister of Finance and I (as Joint Ministers) agree to delegate individual project level decisions to the KiwiRail Board for their projects listed in Table 1 below. These delegations aim to provide Waka Kotahi and KiwiRail (referred to collectively as 'Delivery Agencies') Boards with the flexibility to utilise existing capabilities to deliver projects while recognising the Crown's role as funder and over-arching owner of the Programme, and the reporting requirements that apply.

While I have set the expectations that we have of the KiwiRail Board, Joint Ministers retain the right to review, amend or revoke the delegations and conditions at any time. For the absence of doubt, the Crown remains the funder and owner of the Programme and any change to delegations will not change the Crown's responsibility to reimburse KiwiRail for project spend and commitments reasonably incurred. This letter updates my previous delegations and expectations on the Programme.

My expectations set out in this letter are drawn from and align with the information agreed by Cabinet (reference CAB-21-MIN-0374.01).

I place a high level of reliance on KiwiRail's internal monitoring and assurance processes to escalate risks and issues to me. I therefore hold the KiwiRail Board directly accountable to provide Programme Assurance to Joint Ministers. You are to provide comprehensive assurance and a high level of accountability and transparency to me on the Programme. I request that you reply to me in a letter to confirm that you can meet these expectations.

To maintain a balance of delivery momentum and assurance for the Crown on key risk factors, I have agreed on a risk-based management approach to the Programme. Depending on the risk level, Joint Ministers are to be provided with a project baseline containing deliverables for each project. This has been achieved previously through provision of the Establishment

Reports and Baseline reports. Table 1 lists the project baseline that I request for each project and when it is due.

In your reply to this letter, please confirm that you are able to provide me with the project baseline by the date shown in the table or otherwise advise of the appropriate date. Project baselines should include your assessment of escalation thresholds for possible changes to scope. I have asked the Ministry of Transport to provide me with advice on project baselines, as outlined in this letter.

Delegations

Joint Ministers will retain decision-making rights at key points in higher risk and rescope project lifecycles – specifically at Detailed Business Case (DBC) stage (for projects still in this phase) and/or the Implementation Business Case (ImBC) stage (i.e. where the project has progressed beyond the DBC phase, with the next major decision point being construction contract award).

This both enables Delivery Agencies to complete business cases that are fit for purpose for a particular project stage (i.e. not revisiting decisions already made), and ensure proposed projects are consistent with Joint Ministers' expectations on outcomes, scope, benefits, cost, and schedule or that any substantive variations are clearly acknowledged.

For lower risk projects, as shown in Table 1 all amounts under the column heading "Delivery Agency allocation" will be appropriated, for delegated management of underspends and be available for forecast overspends for lower risk projects in a prudent and transparent manner, consistent with the escalation thresholds discussed below. Contracts of any value may be awarded, noting that I seek a briefing prior to awarding contracts over \$100 million for Melling and Drury. If a contract award would result in the project budget exceeding its Estimate at Completion (EAC), Joint Ministers' agreement is to be sought prior to contract award in line with the cost escalation threshold.

For higher risk and rescope projects, Joint Ministers' Tagged Contingency (refer Table 1) is held centrally under Crown control. Appropriation of tagged contingency will be managed by Joint Ministers with advice from KiwiRail, the Ministry of Transport and the Treasury. Business cases require joint Ministers' approval to access this contingency. Business cases should follow the Treasury's Better Business Case guidance and be supported by an Assurance Plan, Project Management Plan, and Quantitative Risk Analysis. In the case of South Auckland projects and Active mode and public transport investments projects that support transit-oriented development, I expect Waka Kotahi to engage with the Ministry of Housing and Urban Development to enable the Minister of Housing and Urban Development to engage in effective and reasonable consultation regarding housing priorities.

Cabinet set Joint Ministers' tagged contingency aside to progress route protection for Takitimu North Link Stage 2. This should be considered separately from the above arrangements. Construction of this project has been removed from the Programme and the level of investment for route protection means it now better fits the lower risk category, and therefore operates under those conditions.

Table 1 – Revised Project Funding Allocations by Sub-Programme and Risk Category

Risk category	Project	Project Baseline	Project baseline due date to Joint Ministers	Total approved funding (\$m)	Delivery Agency allocation (\$m)	Joint Ministers' Tagged Contingency (\$m)
Lower	SH58	Baseline Report	Already supplied	105		
Lower	SH1/29	Baseline Report	Already supplied	40		
Lower	Takitimu North Link Stage 1	Baseline Report	Nov 2021	655		
Lower	Papakura to Drury South Stage 1	Baseline Report	Nov 2021	655		
Lower	Canterbury Package	Baseline Report	Already supplied	300		
Lower	Queenstown Package	Baseline Report	Already supplied	115		
Lower	Melling	Baseline Report	Already supplied	420		
Higher	Penlink	ImBC	Mid 2022	830		
Higher	Active mode and public transport investments	Briefing	ASAP and no later than March 2022	785		
Higher	Ōtaki to North of Levin	DBC	Early 2022	1,500		
Lower	Takitimu North Link Stage 2	Baseline Report	Nov 2021	57		
Rescope	South Auckland	DBC	Early 2022	874		
Rescope	Whangārei to Port Marsden*	DBC	Early 2022			
Sub total - Waka Kotahi Projects (listed above)						
Lower	Wiri to Quay Park	Baseline Report	Sept 2021	318		
Lower	Papakura to Pukekohe electrification	Baseline Report	Sept 2021	375		
Lower	Wellington Railway Station safety	Baseline Report	Sept 2021	88		
Lower	Wairarapa Rail Upgrades	Baseline Report	Sept 2021	156		
Lower	Capital Connection rolling stock	Baseline Report	Oct 2021	26		
Lower	Drury Rail Stations	ImBC	Nov 2021	495		
Lower	Otiria To Whangārei	Baseline Report	Dec 2021			
Rescope	Marsden Point Link*	DBC	Early 2022			
Sub total - KiwiRail Projects (listed above)						
Portfolio Contingency						
Total				8,726		

Note – DBC refers to Detailed Business Case and ImBC refers to Implementation Business Case.

*Allocations to be confirmed once Business Cases for rail and road projects have been completed

Active mode and public transport investments

In line with Cabinet decisions, work on the Northern Pathway project will be stopped. Funding allocated toward that project is to be used for winding up the project, with the remaining funding reallocated towards an alternative mix of investments. Waka Kotahi will identify the appropriate alternative solution for cyclists to cross the Waitematā Harbour and redesign the Seapath project to work without the Northern Pathway and to tie into the alternative solution.

Pending further work by officials and Waka Kotahi to inform Joint Ministers decisions on the above investigations, remaining funding from the Northern Pathway allocation will be used to:

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- Support Auckland Transport Alignment Project (ATAP) funding pressures alongside the National Land Transport Fund (NLTF) with Waka Kotahi to report-back once this has been worked through the ATAP process and endorsed by the ATAP Governance Group. I expect particular support for the Eastern Busway project, [REDACTED]
- Support additional strategic priority investments in the Auckland cycle network, with Waka Kotahi to report-back once this has been worked through the ATAP process and endorsed by the ATAP Governance Group.
- Provide support for regional projects outside of Auckland that support climate change and housing objectives.

Across the re-allocations outlined above, proactive consideration should be given to projects that support transit-oriented developments in priority growth areas. For regional projects, they should complement other investments made through the NLTP and Infrastructure Acceleration Fund.

It is noted the amount of funding available for these additional projects will not be known until the costs for the wrap up of the Northern Pathway project, the redesign of the Seapath project and the alternate crossing for cyclists are determined. However, I expect Waka Kotahi will start identifying the list of potential projects in order to be able to provide Joint Ministers with options as soon as possible and no later than the end of March 2022.

Oversight and monitoring

The Treasury and Ministry of Transport have a shared responsibility for monitoring the Programme. The Treasury is responsible for developing and maintaining the integrity of the investment management and asset performance system under CO (19) 6 and advises the Minister of Finance (as a Joint Minister) on implementation of the Programme. The Treasury is the recipient of Programme drawdown requests from KiwiRail as the funds are provided by way of shareholder equity injection, and advises shareholding Ministers, in consultation with the Ministry of Transport, on the payment of those funding requests. The Treasury is the monitor of KiwiRail's performance as a State Owned Enterprise (SOE).

The Ministry of Transport is the Government's system lead on transport and advises me as a Joint Minister for the Programme. The Ministry of Transport is accountable for the funds appropriated to the Programme and is the primary contact for drawdown requests from Waka Kotahi, which it authorises in consultation with Treasury. The Ministry of Transport is the monitor of Waka Kotahi.

The Ministry of Transport will monitor the Programme with the Treasury. However, it is not accountable for Programme assurance, or the identification of project risks. Instead, the Ministry of Transport will undertake its standard role to Vote Transport accountability, with an additional ability to review reporting and escalate as appropriate.

I expect you to provide the Ministry of Transport with timely information on the phasing of forecast Programme expenditure in future financial years, to support good Vote Management practises including Vote baselines updates.

Joint Ministers have decided on an oversight arrangement that provides increased implementation flexibility. I have reduced KiwiRail's reporting requirements, noting that reporting will still be required to the monitoring agencies for the Programme, the Ministry of Transport and the Treasury, and reporting will no longer be reviewed by an Independent Oversight Group. This reflects my trust in KiwiRail and your direct accountability for KiwiRail's delivery of its share of the Programme.

In placing comprehensive assurance and a high level of accountability on you, I expect a fully engaged and effective Board. I expect the Board to consider KiwiRail's own internal assurance, systems, policies, processes, particularly around those that ensure that each project has a completed and up-to-date Assurance Plan, Project Management Plan, Quantitative Risk Assessment, and Gateway Review for projects and the Programme where appropriate.

The Department of Prime Minister and Cabinet Implementation Unit (the Implementation Unit) has been directed to assess the working arrangements between agencies and officials that support the delivery of the transport component of the Programme, to help ensure that the new governance structures are embedded rapidly and to advise on any improvements required to existing monitoring and performance reporting arrangements.

Reporting

I expect to receive reports on all projects in the Programme as listed in Table 1 directly from KiwiRail on a monthly basis. I expect good practice reports that will advise on expected outcomes, benefits, scope, cost, schedule and risk for each project.

So as not to create duplicative effort, I expect to receive copies of your regular monthly programme portfolio report (as provided to the joint Waka Kotahi and KiwiRail NZUP Governance Group or your Boards). I expect to be appraised outside of the regular reporting cycle as soon as practicable of any matters that reach threshold levels or of any relevant material risks and issues in relation to projects on a no-surprises basis.

You are expected to provide further copies of reports to the Ministry of Transport, the Treasury Vote team (and for KiwiRail the Commercial Performance team) and the Implementation Unit.

Rescoped projects will also be subject to monthly reporting on progress. Until business cases are completed, the Ministry of Transport and the Treasury will continue to work closely with KiwiRail, and provide advice and guidance to Joint Ministers on the emerging / final business case particularly if a significant change in risk, scope or cost warrants intervention outside of the escalation threshold process.

I have recategorised Melling and Drury projects as Lower Risk. However, due to their complexity I require additional reporting in relation to project risks, and a briefing from KiwiRail ahead of award of significant contracts and other key project milestones where there may be risks that KiwiRail consider Joint Ministers should be made aware of, including interdependencies and material risks to the outcomes, benefits, cost, and schedule.

In respect of higher risk and rescope projects, where a contract with a value of over \$100 million is to be approved by the KiwiRail Board, I expect KiwiRail will brief Joint Ministers, confirming awarding the contract is within the expected cost for the project. Delivery Agencies should allow enough time for reasonable consideration of this advice prior to the award of the contract.

Project baselines and business cases

Joint Ministers are to be provided with a project baseline containing deliverables for each project. This has been achieved previously through provision of the Establishment Reports and Baseline reports. For some projects, these reports may remain as the project baseline report previously provided. However, where there have been changes to projects as a result of previous Cabinet decisions or the requirements of this letter, including for rescope projects, a new project baseline will need to be produced. This may be in the form of a DBC, an ImBC, or a new or revised Baseline report. This request is set out in Table 1 above.

Delivery Agencies have been directed to not revisit decisions made by Cabinet within these business cases, meaning that the DBC for Marsden Point Link rail project and ImBCs for Penlink, and Drury Rail Stations will not revisit the Strategic Case, Economic Case or option selection.

For the Northern Pathway project funding, a briefing will be provided to Ministers no later than March 2022 with options for re-purposing the allocated funding. As this funding will be used to support several projects, this briefing will outline the different specification documents that will provide the Joint Ministers with the appropriate project baselines and deliverables, including the timeline for when these will be provided.

Table 1 also sets out the date by which the project baseline is due to Joint Ministers. In your reply to me I request that you confirm the project baseline against which you will measure progress of each project, including the scope escalation thresholds.

Progressing business cases for higher risk and rescope projects

As projects in the higher-risk or rescope categories advance through the project lifecycle they may move into the lower risk category, with appropriate levels of contingency funding drawn down and then managed by KiwiRail. Higher risk and rescope project business cases will set the project's baseline and are to be provided to Joint Ministers for approval after being considered by the KiwiRail Board. Once the project business case for a rescope project has been considered, Joint Ministers will determine, with advice from the KiwiRail, the Ministry of Transport and the Treasury, whether it should advance as a higher risk or lower risk project. Consideration of project business cases for higher-risk and rescope projects will be the decision point for re-visiting risk categorisation and contingency management.

For any projects that do not have a completed Climate Implications of Policy Assessment (CIPA), KiwiRail will provide the Ministry of Transport a completed CIPA for those projects at the point when DBC/ImBC is provided to Joint Ministers, or when the scope has been confirmed.

Where a project is in the procurement stage, an ImBC will be provided to Joint Ministers prior to contract award, consistent with Treasury business case guidance. ImBCs will not revisit the Strategic Case or Economic Case or option selection. This applies to Penlink, and Drury Stations.

Project business case review process for higher risk and rescope projects

All higher risk and rescope projects require Joint Ministers to approve an ImBC or DBC before progression.

Where appropriate and where already developed, KiwiRail should provide to the Ministry of Transport and Treasury, previous business cases or baseline reports to enable provision of guidance on issues that may need to be addressed in proposed or updated project business cases.

Collaborative engagement between KiwiRail the Ministry of Transport and the Treasury during project business case development should be undertaken to enable provision of early feedback and allow development of any necessary advice or briefings prior to completion and/or Delivery Agency Board approval.

At minimum, a check-in with the Ministry of Transport and the Treasury is required during development of the project business case. This includes advice on the Active mode and public transport investments project, on which I expect you to check-in with the Ministry of Transport and the Treasury prior to 30 November 2021. Other project check-in dates will depend on the project and should be when key project options are being considered. Early engagement will reduce timeframes required for formal consideration and reduce delays and cost risks.

KiwiRail is expected to provide a reasonable timeframe for obtaining Joint Ministers' approval of project business cases, including Ministry of Transport and Treasury consideration. In general, a three-week timeframe provides the minimum opportunity to approve business cases. This is made up of 10 working days for the Ministry of Transport and Treasury to review documentation and provide their advice for inclusion in the KiwiRail advice to Joint Ministers, with another 5 working days for Joint Ministers to provide approval. Timeframes assume collaboration and previous exposure to the business case information including a previous check-in as described above, prompt responses to follow-up questions, and adherence to an agreed plan of engagement for the business cases across the Programme. Without these conditions additional time is likely to be necessary to complete the reviews.

The time for approval should consider the project business case and any impacts this timeframe would have on schedule and costs. Delivery Agencies are to advise of any risks to schedule and cost created by these timeframes in advance. Best endeavours will be made to shorten this period where possible but given the importance and significance of these investment decisions, quality advice and assurance is required.

Climate Impact of the Programme

Further to the work done to date on the CIPAs for the Programme, I note that there is a significant amount of embodied emissions associated with the construction of projects within the Programme. As the business cases and implementation phases for each project progress, I request that you investigate options for reducing the impact of emissions incurred during construction of the Programme. This could include for example:

- The potential for use of lower embodied emissions substitute materials (such as lower embodied carbon concrete, sourcing more recycled material where possible, limiting the amount of high embodied emissions materials used).
- Whether there is a possibility and significant emissions benefit of reducing direct fuel usage during the construction period of large projects.
- Whether more materials can be sourced locally to reduce the emissions associated with transport to and from the construction site.

I would appreciate information and updates on initiatives, innovations or construction methods that you are considering or developing, so that I can understand progress we are making on this important topic and the contribution this Programme is making to minimise the negative impacts of emissions on the environment.

Escalation thresholds

I have agreed to manage contingency funding in accordance with a risk-based approach. Risk categories define how additional contingency funding is managed, as well as business case and assurance requirements.

I have agreed that the escalation thresholds in Table 2 (below) apply across the Programme. When thresholds are triggered, I expect you to notify Joint Ministers through a written briefing of risks to cost, schedule and scope. Where a scope change occurs and is close to, but does not trigger the threshold, I remind delivery agencies that this should be reported through to Joint Ministers as part of the general monthly reporting.

Table 2 – Escalation Thresholds

Escalation threshold component	Escalation threshold trigger
Scope	Any change to outputs, as defined in the project baseline, that significantly impacts project benefits and outcomes.
Cost	Delivery Agency Programme Estimate at Completion (EAC) exceeds available funding for each Delivery Agency, excluding the rescope projects (\$ ██████ for Waka Kotahi; \$ ██████ for KiwiRail)*
	Project EAC exceeds Delivery Agency allocation for the project
Schedule	For projects that <u>have not</u> yet awarded the main construction contract: <ul style="list-style-type: none"> - Construction <u>start</u> is delayed by 6 months - Construction <u>end</u> is delayed by 6 months
	For projects that have awarded the main construction contract: <ul style="list-style-type: none"> - Construction start is delayed by 3 months - Construction end is delayed by 3 months

**The South Auckland package, Whangārei to Port Marsden, and Marsden Point Link are excluded from this total until their DBCs are further progressed.*

Escalation will involve a process whereby:

1. Delivery Agencies are expected to give an early warning to the Ministry of Transport and the Treasury that an escalation threshold has been or is at risk of being triggered. If requested by the Ministry of Transport and/or the Treasury you are expected to provide further information to them including:
 - Upcoming milestones and decision points.
 - Drivers of the escalation trigger.
 - Analysis of project and programme implications.
 - For escalations in relation to exceedance of EACs of lower risk projects, any intended re-allocation of funds from other lower risk projects.
 - Advice and options that Joint Ministers may consider (for instance options to descope projects to reduce cost, or access tagged contingency to enable project delivery) with a recommended approach.

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2. Delivery Agencies are expected to notify Joint Ministers (copying the Ministry of Transport and the Treasury) as soon as practicable that a threshold has been triggered. Notification is not necessarily expected to wait for the next reporting period.
3. Following notification of a threshold being triggered and with advice from the Ministry of Transport and the Treasury, Joint Ministers may request KiwiRail to provide comprehensive information and options to Joint Ministers for possible decisions.

Significant work is required to reset the rescope projects in South Auckland, Whangārei to Port Marsden and Marsden Point Link baselines, as well as how the funding for Northern Pathway will be used. These projects are excluded from the threshold escalation process until such time that a DBC has been completed and approved.

KiwiRail is in the process of defining scope parameters that would trigger escalation thresholds for each project. I expect these scope parameters to be shared with Joint Ministers once project baselines are completed.

Schedules for rescope projects will be provided through the project baseline for each project once complete. Baseline reports approved by Joint Ministers will continue as project baselines unless KiwiRail notifies otherwise.

Access to contingency

Tagged capital contingency of [REDACTED] will be retained by the Crown to provide additional funding, if required, and subject to the processes outlined in this letter.

Contingency will be managed in three groups as part of a graduated system of drawdowns, whereby the portfolio tagged contingency will not be utilised until the relevant Delivery Agency or project tagged contingency is exhausted. Access to contingency funding should proceed in the following sequence:

1. KiwiRail contingency – is within the Delivery Agency allocation, with drawdown and management delegated to KiwiRail.
2. Project tagged contingency – should be used only to fund the specific higher risk projects it is tagged to and is at the discretion of Joint Ministers. This amount currently totals \$[REDACTED] but may change as business cases for higher-risk and rescope projects are considered and the risk categorisation and contingency management arrangements are re-visited. For the Whangārei to Port Marsden (road), and the South Auckland (road) projects, drawdown of tagged capital contingency funding is subject to CIPAs being completed and being considered by Joint Ministers and the Minister for Climate Change.
3. Portfolio tagged contingency – should KiwiRail contingency (for lower risk projects) or project tagged contingency (for higher risk projects) be exhausted, portfolio contingency of [REDACTED] may be accessed, at Joint Ministers discretion. This is available across both Waka Kotahi and KiwiRail projects. CIPA and Business Case requirements apply.

Re-scoped projects may not access tagged contingency until DBCs are finalised, baselines are developed, and Joint Ministers provide approval.

For lower risk projects KiwiRail is expected to consider how underspends across their respective projects may fund forecast overspends before requesting access to portfolio contingency.

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Where access to tagged contingency is requested, KiwiRail will advise the Ministry of Transport and Treasury of the request and develop options with associated implications. KiwiRail will provide a briefing with advice and options through its Board to Joint Ministers for consideration. Requests for Portfolio Tagged Contingency will also be considered by the joint Waka Kotahi and KiwiRail NZUP Governance Group.

Requests for tagged contingency are to include confirmation that the project is likely to fall within the total approved funding, and that there are appropriate processes, capacity and capability in place to successfully manage the project.

Drawdown arrangements

The arrangements for drawdown of Crown funding for KiwiRail projects is dependent on the provision of forecast cashflows and agreed supporting information from the KiwiRail Board. The drawdown of Crown funding for this Programme will follow existing arrangements for share subscription and release of equity funding between KiwiRail and the Treasury.

The arrangements for drawdown of Crown funding for Waka Kotahi projects is dependent on the provision of actual expenditure incurred, forecast financial information, and an appropriately completed funding request, including agreed supporting information.

Drawdown requests should follow the following guidelines:

- Funds requested are to be for costs already incurred or that are required to be paid prior to the next scheduled drawdown request.
- Information to accompany requests should include:
 - A breakdown of the request by:
 - Project.
 - Property (within each project).
 - Other (within each project).
 - A schedule of actual costs against forecast costs up to and beyond the period for which the drawdown is sought.
 - Narrative in relation to any large or unusual items that is not otherwise available in the material supplied.
 - A signed approval by an authorised signatory of KiwiRail
 - If reasonably requested by the Ministry of Transport, copies of original invoices and details of internal management costs.

In closing, please convey our thanks to the Board and all staff members for their dedication and hard work on the Programme since early 2020. We look forward to continuing to work together with you as the Programme progresses in 2021. We are confident that KiwiRail will deliver its projects, consistent with the expectations set out above. I look forward to your favourable response.

Yours sincerely

A handwritten signature in black ink, appearing to read 'M. Wood', written in a cursive style.

Hon Michael Wood
Minister of Transport

Copy: Hon Grant Robertson
Minister of Finance

Greg Miller
Chief Executive, KiwiRail

Peter Mersi
Chief Executive, Ministry of Transport