



Cabinet Committee on State Sector Reform and Expenditure Control

SEC (12) 99

Copy No: 35

Summary of Paper



9 November 2012

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Wellington Office Accommodation Strategy: Single Stage Business Case

Portfolio State Services

Purpose This paper seeks approval for the *Single Stage Business Case: Wellington Office Accommodation Strategy* for five large agencies, and approval for the Chief Executive, Ministry of Social Development (MSD), to negotiate the development agreements and deeds of lease.

Previous Consideration



In April 2012, Cabinet agreed that MSD should explore other possible accommodation solutions in the context of the broader government property strategy for lease negotiations in Wellington being developed by the Property Management Centre of Expertise (PMCoE) in conjunction with a number of government agencies whose lease terms also end over the next three to four years [CAB Min (12) 12/3A].

Summary

Head office accommodation leases within the Wellington Central Business District are due to expire for [redacted] the Ministry of Education (MoE) and [redacted]



In June 2012, the various stages of business case and procurement processes undertaken by the above five agencies were merged into the PMCoE-led process. Approval of the attached *Single Stage Business Case: Wellington Office Accommodation Strategy* is sought, that sets out the preferred accommodation solution for the above five agencies.

The preferred accommodation solution has a collective reduction in footprint of 30 per cent. This translates into a 20 per cent cost avoidance for the Crown over the 20 year appraisal period than if the agencies continue to occupy their existing footprints.

A summary of the preferred solution for each agency is set out on page 2 of the paper, and in Appendix 1 on page 14.

Authorisation is sought for the Minister of Finance and the relevant responsible agency Minister to agree to the final investment decision for each agency's accommodation, [REDACTED]

Agreement is also sought for the Chief Executive of MSD, in consultation with the relevant agency, to negotiate development agreements for the preferred buildings, or negotiate a development agreement with alternate short-listed suppliers, if required.

**Regulatory
Impact Analysis**

There are no regulatory implications.

**Baseline
Implications**

The preferred solution results in a significant reduction in potential cost escalation compared to the status quo. No additional funding is sought.

The 20-year whole-of-life funding arrangements by agency as compared to the status quo are set out in the table on page 10.

**Legislative
Implications**

None.

Timing Issues

[REDACTED]

Announcement

The Minister of State Services may release communications, in consultation with the State Sector Reform Ministers, as required.

Interest from the property industry in the co-ordinated approach is expected. This will be managed by the media team of MSD on behalf of the PMCoE.

Consultation

Paper prepared by [REDACTED] MoE, [REDACTED]
[REDACTED]

[REDACTED]

The Minister of State Services recommends that the Committee:

- 1 note that the Property Management Centre of Expertise (PMCoE) and the participating agencies have identified a preferred head office accommodation solution, following a joint procurement and business case process;
- 2 approve:
 - 2.1 the *Single Stage Business Case Wellington Office Accommodation Strategy* attached to the submission under SEC (12) 99;
 - 2.2 the preferred accommodation solutions for the [REDACTED]
[REDACTED] the Ministry of Education (MoE); [REDACTED]
[REDACTED]

- 3 authorise Joint Ministers (the Minister of Finance and responsible agency Minister) to agree to the final investment decision for each agency's accommodation, except [REDACTED] within a 5 per cent variance of the collective anticipated net present value whole of life costs of \$592.480 million;
- 4 note that Cabinet authority is required for investment decisions with a whole-of-life cost over \$25 million, as per Cabinet Office Circular CO (10) 2;
- 5 direct the Chief Executive of MSD:
- 5.1 in consultation with MoE [REDACTED] to negotiate development agreements for the preferred buildings and report to those Ministers delegated in paragraph 3 above for approval;
- 5.2 to negotiate a development agreement with alternate short-listed suppliers from the PMCoE-led request for proposal process, in the event that an agreement cannot be reached with a preferred supplier;
- 6 invite the Minister of State Services to release media statements in relation to this co-ordinated procurement and business case process within the context of functional leadership;
- 7 note that despite projected increases for property-related costs across the 20 year appraisal period, the preferred solution:
- 7.1 does not require additional Crown funding;
- 7.2 delivers a collective shortfall (in nominal terms) of only \$35.28 million which agencies have committed to funding within current baselines over the next 20 years;
- 7.3 achieves cost avoidance of \$339.860 million compared to the projected status quo;
- 7.4 realises baseline savings:
- 7.4.1 [REDACTED]
- 7.4.2 [REDACTED]
- 7.4.3 [REDACTED]
- 8 note that:
- 8.1 in addition to the benefits in paragraph 7 above, it is also estimated that agencies have collectively saved the equivalent of approximately \$1.000 million in reduced procurement and business case processes;
- 8.2 building owners have also benefited from the streamlined process to respond to multiple government agencies;

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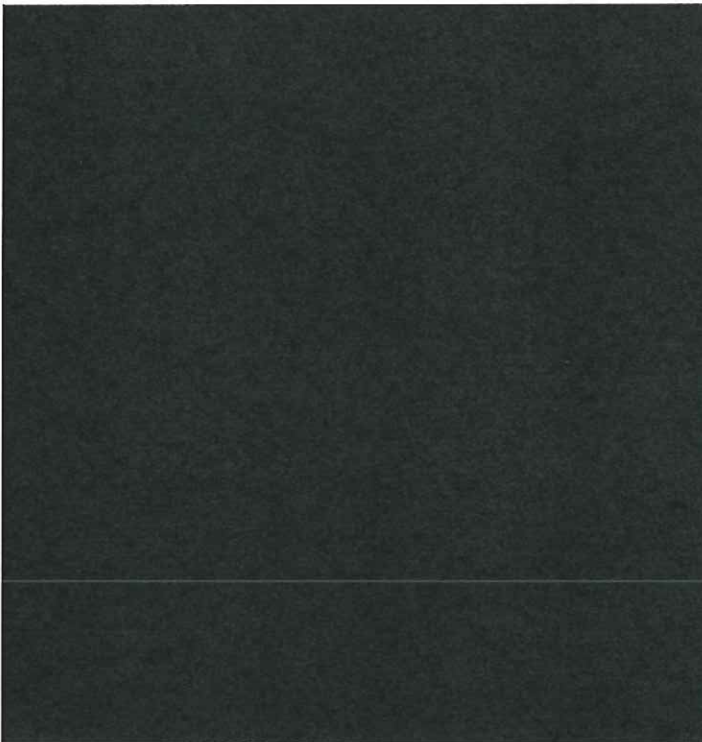
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12 note that the preferred accommodation solution offers buildings with greater levels of safety and standards than those already occupied by the participating agencies, improving staff safety and reducing the risk to business continuity;

13 note that collectively the participating agencies have had a reduction of 30 per cent in their property footprint (124,447m² to 87,522m²), and will occupy the following space as part of the preferred solution:



13.5 MoE:

13.5.1 current footprint: 21,179m²;

13.5.2 preferred option footprint: 13,179m²;

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Sam Gleisner
Committee Secretary

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Office of the Minister of State Services

Chair
Cabinet Committee on State Sector Reform and Expenditure Control

WELLINGTON OFFICE ACCOMMODATION STRATEGY

Proposal

1. This paper seeks approval of the attached business case for Wellington head office accommodation for [REDACTED] Education; [REDACTED], and to direct the Chief Executive of the Ministry of Social development (as Functional Leader for property), to negotiate the development agreements and deeds of lease.
2. It is proposed that the Minister of Finance and the responsible Ministers for these agencies (less Crown Law) be delegated the authority to agree to the final commercial terms following the negotiation phase. [REDACTED]

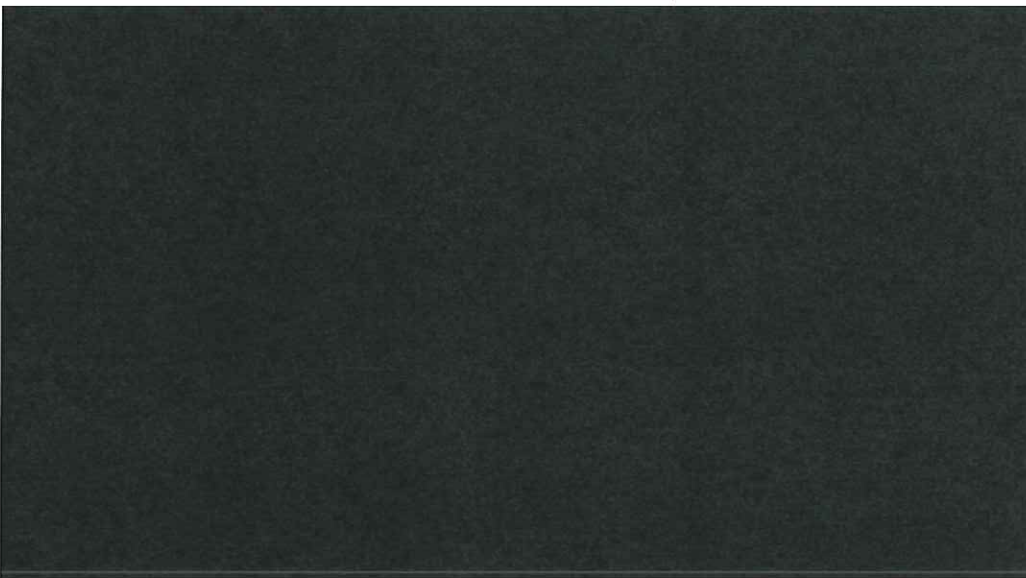



Executive Summary

3. Head office accommodation leases within the Wellington Central Business District (WCBD) are due to expire for the [REDACTED] Education (MoE), and [REDACTED]. In addition, the [REDACTED] is also seeking head office accommodation, but has secured a co-located tenancy within the existing Ministry of Justice head office building.
4. A business case has been prepared by the Property Management Centre of Expertise (PMCoE), hosted at MSD, pursuant to the functional leadership mandate delegated from the Head of State Services to the Chief Executive of MSD.
5. These agencies were at various stages of business case and procurement processes, all of which were merged into the PMCoE-led process in June 2012. This centrally-led procurement and business case process for Wellington head office accommodation has resulted in a preferred solution which has been agreed by the participating agencies and supported by The Treasury.
6. The preferred accommodation solution has a collective reduction in footprint of 30% (124,447m² to 87,522m²). This translates into a 20% cost avoidance for the Crown over the 20 year appraisal period (\$152.25m reduction at 6.5% NPV) than if the agencies continue to occupy their existing footprints.
7. The key outcomes from the business case and procurement process are as follows:
 - No additional funding required for property costs over the forecast period
 - Enhanced agency effectiveness via co-location and single site solutions
 - Projected property cost savings for some agencies
 - Establishment of locational clusters of agencies, based on operational linkage

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- Improved building safety and business continuity capability
- Support for subsequent relocation from CBD for non-centre facing functions
- Minimal staff disruption from multiple moves and minimal legacy lease tails
- A reduction in short-medium term fiscal pressures, and significant cost avoidance for the longer term
- Improved flexibility for change
- Leveraging of the Government's scale for negotiation advantage.

8. A summary of the preferred solution for each agency is as follows:

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- 
- 
- MoE: Will relocate to 33 Bowen St when MBIE agencies vacate in 2014. Some refurbishment will be required before MoE takes occupation, likely to bring it up to 82% NBS.
- 

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10. The significant reduction in projected expenditure is primarily achieved through agencies adopting 13m² per workpoint and from improved procurement processes. For agencies, this will mean adopting higher density workplaces through more efficient use of office furniture solutions; supported by greater utilisation of ICT. The status quo is based upon agencies retaining their current footprints and not undertaking any internal reductions of that space. The significant cost avoidance projected can therefore not be based solely upon the role PMCoE has had in this process as agencies would have undertaken some degree of their own reductions to meet cost pressures on baselines.

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11. Following approval of this business case and preferred solution, it is proposed that PMCoE lead (in conjunction with the participating agencies) negotiations for these preferred sites, for approval by joint Ministers of final commercial terms in March / April 2013.
12. This project represents only around 18% of the Crown's Wellington-based office accommodation and is the first tranche for this strategy. Subsequent tranches will be developed to allow the remaining State Services agencies to rationalise their head office requirements. The planning for the second tranche will occur in 2013.

Background

13. Office accommodation leases in the Wellington Central Business District (CBD) are due to expire for the [REDACTED] Education, [REDACTED] A [REDACTED] A single consolidated business case has been prepared by the Functional Leader for property.
14. Government agencies have in the past undertaken office accommodation procurement and business case processes largely independently of each other. This has resulted in solutions that are less efficient and effective from the viewpoint of the Crown's property portfolio, for reason such as:
 - duplication of cost and effort (for both Crown agencies and property owners);
 - competition within government for a limited pool of suitable office accommodation available at the time, which potentially increases cost;
 - difficulty in identifying and utilising surplus space available within the Crown portfolio in order to reduce costs;
 - little or no coordination of agencies' locations within the Wellington CBD to enhance linkages and cross-agency interactions;
 - difficulty in leveraging the Crown's economies of scale in the procurement of property-related goods and services;
 - agencies adopting property footprints that are over best practice benchmarks¹; and
 - a property portfolio that is less flexible and responsive to the changing needs of the Government.
15. In order to address this, the PMCoE was established in April 2011² and was tasked with driving efficiency and effectiveness gains in property management across Departments and Crown Agents by providing leadership, guidance and support, monitoring and brokerage, but without changing the accountability for decision making from individual agencies.
16. In July 2012, the Better Public Services Functional Leadership initiative strengthened the mandate of the PMCoE by appointing the Chief Executive of the Ministry of Social Development as the Functional Leader for property. This strengthened mandate has enabled the PMCoE to integrate the business case and procurement processes of the

¹ Report on the Crown Office Estate (as at 30 June 2011) – On average, State Services FTEs occupy the equivalent of 20.5 m² of office accommodation in Wellington, as compared with the expectations of Cabinet of between 12-16 m²

² Cab Min (11) 14/14 Establishment of Property Management Centre of Expertise, dated 4 April 2011

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five agencies into a single process in order to drive efficiency and effectiveness gains for the Crown.

17. In order to mitigate rising property-related costs, greater value for money needs to be achieved from the Crown's property portfolio. A strategy was developed to reduce the amount and cost of accommodation occupied by the Crown in Wellington. The primary value drivers were:

- to optimise existing space already occupied by the State Services;
- minimising whole-of-life costs per workpoint; and
- reducing future requirements by adopting best practice benchmarks and incorporating office design solutions that allow greater density within buildings. Greater use of technology and better utilising the Crown's scale in negotiations will support this approach.

18. In addition to fiscal drivers, there is an increased demand in Wellington for buildings that offer an appropriate level of seismic resilience. Government agencies and private sector alike are moving towards buildings offering a higher level of seismic resilience. This shift in preference is seeing an increase in demand (and therefore rental) for resilient buildings, and an increase in insurance costs particularly for less resilient buildings. Compounding this issue is the fact that the Crown and the private market are competing for the limited supply of these buildings.

Analysis

Process and approach

19. Each of the participating agencies was at a different stage of the business case and procurement processes when the decision was made to combine these under a single process led by the PMCoE. These agencies were at the following stages:

- [REDACTED]
- MoE had Cabinet approval⁴ to negotiate with its preferred supplier and it was agreed to continue this negotiation on the basis that this building would be included within the short-list from which collective solutions would be developed.

- [REDACTED]
- [REDACTED]

³ [REDACTED]

⁴ Cabinet Social Policy Committee SOC Min (12) 4/2 dated 29 March 2012

⁵ [REDACTED]

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20. Due to the significant work that had previously been undertaken by participating agencies, and also the concurrent development of the Functional Leadership Cabinet paper, Treasury approved a single stage business case in lieu of the two-staged business case normally required for investments over \$25m.⁶
21. The procurement and business case processes were led by PMCoE, supported by a Working Group of senior property staff from participating agencies, with governance provided via a Steering Group of Deputy Chief Executive-level representatives from each agency. Treasury provided a single point of liaison for the process.
22. In July 2012 the PMCoE issued an RfP for office accommodation for the participating agencies. This RfP sought proposals for accommodation both within the CBD and also the wider Wellington region. This was to enable analysis of the cost-benefit of locating (or co-locating) some agency functions that are not centre-facing to non-CBD locations. Non-centre facing staff are defined as those staff that do not need to be located in the CBD or near parliament to carry out their roles effectively.
23. A small number of responses were received for non-CBD locations; however, none of these met the short-list criteria and are not part of the proposed solution. For this reason, only Wellington CBD-based options were developed during the business case. However, as discussed below, a further process will be undertaken by the PMCoE in 2013 that will investigate non-CBD options for non-centre facing functions. This analysis does not impact on the preferred option, as any subsequent re-location of functions can be offset by re-use of the buildings which are suitable for multiple agencies, and which will contain standardised layouts.
24. Overall, 25 proposals were received for the RfP, and nine were short-listed (evaluation criteria are detailed in the business case). The information from these short-listed proposals was used to develop options that underwent cost-benefit analysis and a preferred solution was agreed by the Steering Group.
25. The key dates for the approval requirements and implementation are as follows:
 - Cabinet approval of business case and preferred solution: November 2012
 - Detailed negotiations with property owners: November 2012 – March 2013
 - Final approval of commercial terms by Joint Ministers: March/April 2013
 - Design / undertake fit-out / occupy: April 2013 onwards (to 2017).
26. PMCoE will lead the negotiations with the preferred suppliers, with the participating agencies supporting this process. Once the development agreements (incorporating the deeds of lease) have been signed, the PMCoE will transfer the lead role to the participating agencies for implementation, and will continue to provide support and oversight.
27. Appropriate external specialised providers will be utilised in areas such as architectural, construction project management, tenant advocacy and quantity surveying, to ensure that risks to the Crown for delivery are mitigated.

⁶ Cabinet Office Circular CO (10)2

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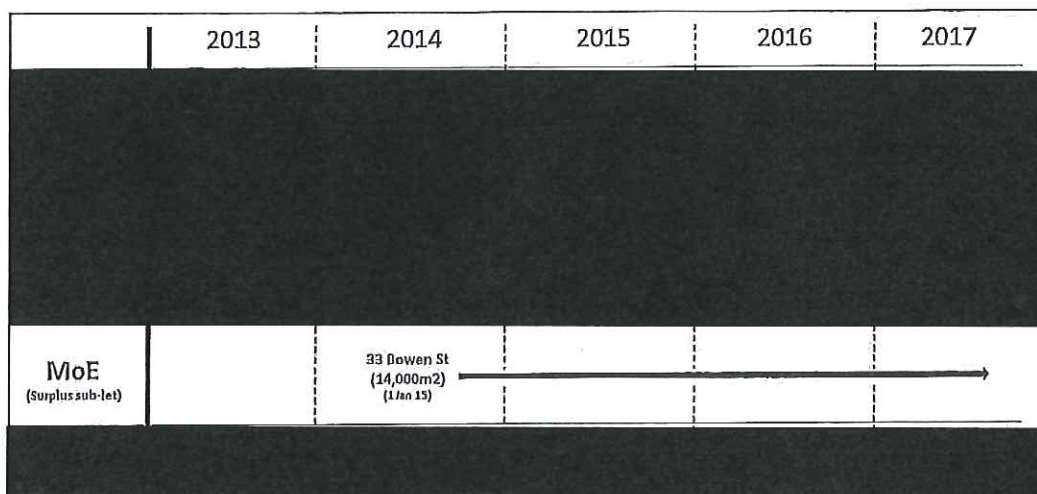
Preferred solution and rationale (from attached business case)

28. A summary of the preferred accommodation solution is as follows:

- [Redacted]
- [Redacted]
- [Redacted]
- MoE: Will relocate to 33 Bowen St when MBIE agencies vacate in 2014. Some refurbishment will be required before MoE takes occupation, likely to bring it up to 82% NBS.
- [Redacted]

29. The staging and timing of this preferred solution can be shown diagrammatically as follows:

Diagram 1: Preferred Option



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30. The preferred solution will not lock the Crown into a long-term solution that is inflexible to the changing requirements agencies will likely face, particularly if FTE numbers change. Initiatives such as shared services or the relocation of non-centre facing staff to sites outside of the Wellington CBD will reduce the space requirement of some agencies. This risk will be mitigated by PMCoE, under its Functional Leadership Property mandate, undertaking a strategic portfolio approach to management that is able to identify other appropriate agencies with leases that can backfill surplus space in the procured buildings as it becomes available.



32. The key outcomes from the business case and procurement process are as follows:

- **No additional funding** – The preferred solution requires no additional funding from the Crown over the 20 year appraisal period and any projected shortfalls will be absorbed by the participating agencies within their existing baselines.
- **Enhanced agency effectiveness** - The preferred solution optimises effectiveness through co-location of agencies into a single site each, as opposed to the multiple sites that they currently occupy.⁷
- **Projected savings** – [REDACTED] are projected to achieve baseline savings over the 20 year appraisal period, despite ongoing increases to property-related goods and services.
- **Establishment of initial sector clusters** – [REDACTED] this creates enhanced collaboration, business effectiveness, cost efficiencies, and opportunities to explore further initiatives such as shared back office services.

⁷ Collectively the participating agencies currently occupy 19 buildings, which will reduce to 5 with the preferred solution implemented.

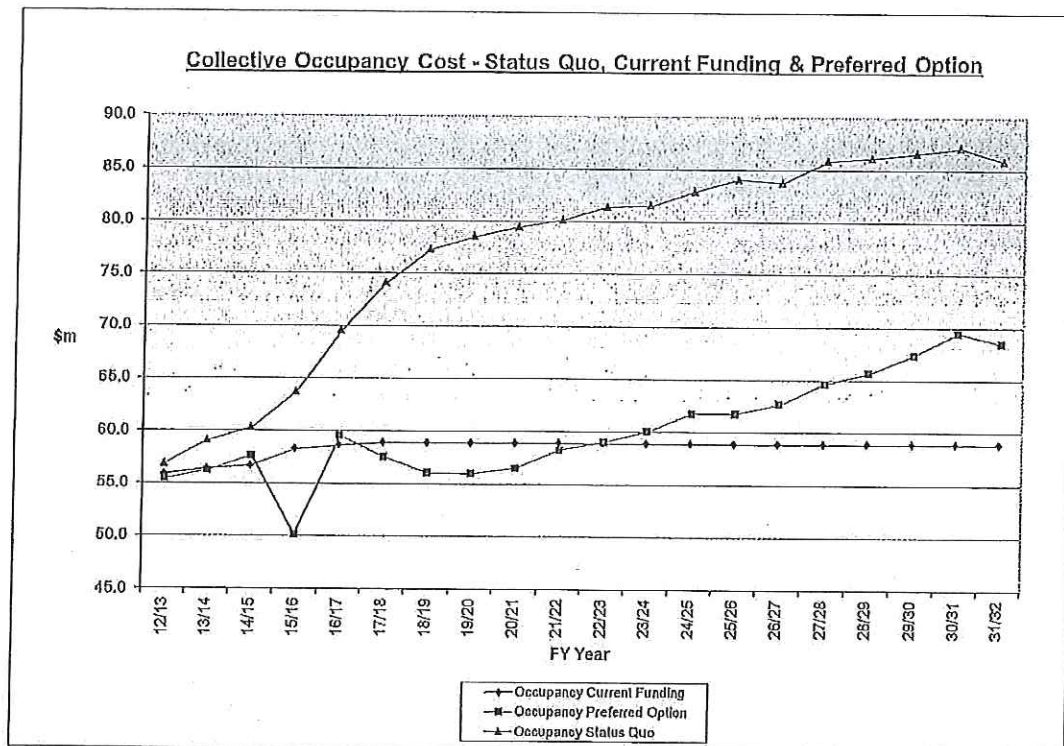
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- **Improved building safety and business continuity capability** – All new sites will be significantly better in terms of efficiency and safety standards than the status quo. This will provide greater employee safety and satisfaction, and improved business continuity capability. The preferred buildings offer a modest but appropriate level of accommodation for public sector employees.
- **Non-centre facing ongoing development** – No non-centre facing sites met the criteria for short-listing during the business case process. A separate detailed project will be undertaken by PMCoE during 2013 in order to progress this initiative. This analysis does not impact upon the decisions to secure the preferred solution. Any subsequent decision to re-locate non-centre facing staff will allow for the a corresponding backfill of surplus footprint.
- **Minimal disruption** - With the exception of part of [REDACTED] this solution minimises the disruptions associated with the re-location of agencies, while also minimising any lease tails prior to occupation.
- **Reduction in short-medium term fiscal pressures** – Based on the projected costs and associated funding arrangements, the preferred solution will not require the collective participating agencies to absorb shortfalls until the 2028/29 year.
- **Improved flexibility** – The Crown is able to respond more effectively to changing head office requirements with the greater centralisation of the government's property portfolio management and increased commonality of workplace design and standards.
- **Better procurement process for agencies and building owners** – Savings of up to \$1m on this single process for government agencies and also means building owners submit one proposal rather than responding to multiple RFP requests. Further savings are likely through collaboration in the negotiation process.
- **Changing market dynamic** – The Crown is able to leverage its economies of scale in the procurement of property-related goods and services while also creating an over-supply of office accommodation in the market through a significant reduction in its footprint, thus mitigating future rental increases on a like-for-like basis.

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Diagram 2: Occupancy Cost - Status Quo, Current Funding & Preferred Option



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Financial Implications

34. The preferred solution results in a significant reduction in potential cost escalation compared to the status quo, and the residual cost pressures can be absorbed within the existing baselines of all participating agencies. No additional funding is sought in respect of this proposal.

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⁸ Occupancy cost = Gross Rent + Utilities + Other + Fit-out depreciation

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36. These figures represent the results of the tender process and are subject to negotiation. It is expected an overall deal will be achieved that is more favourable than this for the participating agencies. In addition, there may be further savings achieved through greater commonality of property standards and joint procurement of office fit-out.

37. The 20-year whole-of-life funding arrangements by agency, as compared to the status quo, are as follows:

Table 2: Funding Arrangements by Agency

Expense Type	MOE	
	SQ	PO
Operating (\$m)		
• Total Occupancy Cost	210.90	166.26
• Other	0.82	2.86
• Depreciation	34.48	21.36
Sub-total	246.20	189.47
Existing operating provision (inc depn)	177.83	177.83
Shortfall (-) to be funded from baseline	(68.36)	(11.63)
Capital (\$m)		
• Main contract & subdivis	27.64	14.81
• Soft fitout	5.25	4.76
Total to be funded from cash reserves	32.79	19.67

Key: SQ = Status Quo, PO = Preferred Solution

38.

Consultation

39.

Ministry of Education,

40. A Risk Profile Assessment was done on the project and SSC advised on 7th August 2012 that it posed a Medium risk and that no Gateway Review was required. An Independent Quality Assurance (IQA) was conducted by KPMG on both the procurement and business case processes. No significant issues were identified and amendments were incorporated from their feedback.

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[REDACTED] were consulted on the procurement approach and process undertaken to ensure there were no risks to the Crown. None were identified.

Legislative Implications

41. There are no legislative implications.

Regulatory Impact Analysis

42. There are no regulatory impact implications.

Gender Implications

43. There are no gender implications.

Disability Implications

44. The final property solution delivered will fully comply with all disability requirements by law. There are no adverse disability implications, and the proposed solution results in a higher level of code compliance of office accommodation for these agencies, which will include requirements for disabled facilities.

Publicity

45. We anticipate interest from the property industry in this co-ordinated approach, which is a change from previous government procurement processes. This will be managed by the media team of MSD on behalf of the PMCoE.

46. This co-ordinated approach is an early application of the functional leadership mandate, and therefore the Minister of State Services may release communications as required, in consultation with State Sector Reform Ministers.






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Recommendations

47. It is recommended that the Committee:

1. **note** that the Property Management Centre of Expertise (PMCoE) and the participating agencies have identified a preferred head office accommodation solution, following a joint procurement and business case process;
2. **approve** the attached business case and the preferred accommodation solutions for the Ministries of [REDACTED] Education; [REDACTED]
[REDACTED]
3. **delegate** to Joint Ministers (Minister of Finance and responsible agency Minister) the authority to agree to the final investment decision for each agency's accommodation [REDACTED] within a 5% variance of the collective anticipated NPV whole of life costs of \$592.48 million (Cabinet authority is required for investment decisions with a whole-of-life cost over \$25 million, as per Cabinet Office Circular CO (10)2);
4. **direct** the Chief Executive of the [REDACTED] in consultation with the Ministries of Education, [REDACTED] to negotiate development agreements for the preferred buildings and report to those Ministers delegated in recommendation 3 above for approval;
5. **direct** the Chief Executive of the Ministry of Social Development to negotiate a development agreement with alternate short-listed suppliers from the PMCoE-led request for proposal process, in the event that an agreement cannot be reached with a preferred supplier;
6. **invite** the Minister of State Services to release media statements in relation to this co-ordinated procurement and business case process within the context of functional leadership;
7. **note** that despite projected increases for property-related costs across the 20 year appraisal period, the preferred solution:
 - i. does not require additional Crown funding;
 - ii. [REDACTED]
 - iii. achieves cost avoidance of \$339.86m compared to the projected status quo;
 - iv. [REDACTED]
8. **note** that in addition to the benefits above, it is also estimated that agencies have collectively saved the equivalent of approximately \$1 million in reduced procurement and business case processes. Building owners have also benefited from the streamlined process to respond to multiple government agencies;
9. [REDACTED]

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10. **note** that the PMCoE will undertake a project in 2013 to evaluate the costs and benefits of occupying sites in lower cost locations outside the Wellington Central Business District for non-centre facing functions;
11. **note** that if there are any reductions to the area requirements for CBD-based head office accommodation for the participating agencies, the PMCoE will be able to identify other government agencies to occupy this space, thereby mitigating the cost to the Crown;
12. **note** that the preferred accommodation solution offers buildings with greater levels of safety and standards than those already occupied by the participating agencies, improving staff safety and reducing the risk to business continuity; and
13. **note** that collectively the participating agencies have had a reduction of 30% in their property footprint (124,447m² to 87,522m²), and will occupy the following space as part of the preferred solution:
 - i. 
 - ii. 
 - iii. 
 - iv. 
 - v. MoE: Current footprint: 21,179m²; Preferred option footprint: 13,179m²; and
 - vi. 



Hon Dr Jonathan Coleman
Minister of State Services

7.11.12

Appendix 1: Agency Preferred Solution Funding Summary

14



REDACTED

