MINISTRY OF EDUCATION
TE TĀHUHU O TE MĀTAURANGA

Education Report: Update on the close out of the Christchurch Schools Rebuild Programme

To:	Hon Chris Hipkins, Minister of Education		
Date:	10 June 2022	**Priority:**	High
Security Level:	In Confidence	**METIS No:**	1271731
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Purpose of Report

The purpose of this paper is to update you on progress to close out the Christchurch Schools Rebuild programme [METIS 1273723 refers]. Market pressures have resulted in significant price escalations since the close out review was completed in March 2021. As the completion of the programme will be phased over the next 3-4 years, further price escalation is expected. This paper seeks agreement to:

1. An adjustment to the close out funding to reflect current market costs. The close out review now seeks $271 million (an increase of $66 million from what was approved in METIS 1273723). This difference accounts for real standard price escalation, to ensure that the scope of your chosen approach to complete the programme can be achieved.

2. Manage future escalation by including an additional programme risk contingency of 9(2)(j)

The education report also includes the draft Cabinet Paper for your approval, seeking agreement to close out the Christchurch Schools Rebuild programme, and transition schools back to business-as-usual asset management processes. It also seeks approval for ten project level delegations that have been updated following the close out review adjustment.

Summary

1 The Christchurch Schools Rebuild (CSR) programme was established in 2013 to build new, rebuild or repair 115 schools damaged by the 2010 and 2011 earthquakes.

2 The programme is now in its ninth year, and it is appropriate to consider how to complete the programme, and to transition Christchurch schools back to business-as-usual asset management.

3 In early 2021, the Ministry commissioned an independent Close Out Review (COR), to establish the options and expected cost to complete the programme and identify the

implications of transitioning CSR schools back into the business-as-usual asset management process.

4 In October 2021, the Ministry presented you with the recommendations from the COR. Following this, you directed the Ministry to prepare a Cabinet paper seeking agreement to close out the CSR programme following your chosen approach [METIS 1273723 refers].

Table 1: Approved approach to complete the programme

Description	**Additional Funding Required (CapEx)**	**Risks**	**Implications**
Delivers essential remediation works, with partial modernisation and upgrade works where these can be efficiently co-delivered by the existing programme	$205 million	Upgrade works deferred School expectations not fully met	Deferred liabilties will be prioritised against wider portfolio requirements, and may take up to 20 years to be delivered

Reflecting Updated Costs

5 The COR was conducted in March 2021. Since then, there has been 12 months of programme progress, as well as ongoing unprecedented levels of inflation and price escalation due to COVID-19 related pressures on the construction market.

6 To reflect the unprecedented inflation between the completion of the review and now, the Ministry has re-baselined the COR costs to complete the programme under the option you approved.

7 The Ministry estimates that the funding to complete the programme will need to be revised from $205 million to 9(2)(f)(iv) [redacted] This difference accounts for real standard price escalation, to ensure that the scope of your chosen approach to complete the programme can be achieved.

Managing Future Escalation

8 There is likely to be further cost escalation while the programme is phased out over the next 3-4 years. It is difficult to predict future cost escalations and the impact on actual tender prices. However, it is important that a process is in place to manage future escalation so that project delivery is not delayed unnecessarily.

9 Therefore, the Ministry recommends that escalation be managed through a programme risk contingency of 9(2)(j) [redacted]

10 This approach would ensure that the Ministry is able to be responsive and reactive to future escalation, ensuring the financial climate is reflected and the programme budget reflects actual tender prices at the time projects go to market.

11 Without additional funding the Ministry will be unable to deliver the scope of your chosen approach to complete the programme, and some projects would need to be deferred until funding becomes available, which could take several years.

12 It is important to note that the scope of your chosen approach to conclude the programme remains the same. The additional funding required will only address

essential projects and limited upgrade and modernisation works where delivery now is prudent.

Programme progress

13 The CSR programme is a proven infrastructure programme that has consistently delivered at a large scale. As at June 2022, the programme has completed works at 75 of the 115 schools, benefiting 30,000 students.

14 The programme has met spend targets every year, continuing to deliver throughout the impacts of COVID-19 and unprecedented levels of inflation. To date $998 million has been spent through the programme. As an existing programme, the Ministry is well positioned to spend additional funding by utilising the existing governance and delivery frameworks.

15 The adjustment to the COR funding has not caused any delays to projects. The adjustment is in response to cost escalations that have had impacts across the whole sector so that future construction can progress.

16 The Ministry has prepared the draft Cabinet paper for your approval, seeking agreement to your chosen approach to complete the programme. This is attached as Annex 1.

17 If you agree to introduce a buffer to manage future cost escalation, total close out funding adjustment sought from Cabinet will be $301 million. 9(2)(j) [redacted] risk contingency funding, subject to prioritisation through future Budgets.

18 The Ministry recommends the paper is lodged in June-July 2022, after Budget 22 decisions. This is because decisions in this paper would relate to Budget 23 and future budgets. The draft Cabinet paper has no impact on Budget 22.

Recommended Actions

The Ministry of Education recommends you:

a. **note** that that in 2021 the Ministry commissioned an independent Close Out Review (COR) of the CSR programme to establish the options and expected costs to close out the programme.

Noted

b. **note** that on 19 October 2021 you approved $205 million of additional funding to complete the CSR programme [METIS 1273723].

Noted

c. **note** that due to unprecedented cost escalations the Ministry seeks approval to adjust the close out funding to reflect the current financial climate.

Noted

d. **agree** that the funding required to deliver your preferred close out option is revised from $205 to 9(2)(j) [redacted].

Agree/Disagree

e. **note** that there is likely to be further price escalation as the programme is phased out over the next 3-4 years.

Noted

f. **agree** that future escalation is managed through a programme risk contingency of 9(2)(j) [redacted]

Agree/Disagree

g. **agree** that the Ministry prepare a draft Cabinet paper seeking agreement to your preferred approach to complete the programme and increasing the programme envelope by $301 million.

Agree/Disagree

h. **note** that the total close out funding of $301 million will be sought through future Budget processes.

Noted

i. **note** that if the close out funding does not reflect the updated costs, the Ministry will be unable to deliver the scope of your chosen approach to complete the programme.

Noted

j. **not release** this education report at this time because it contains commercially sensitive budget information that may prejudice the Ministry's ability to negotiate commercially.

Release/Not release

Scott Evans	Hon Chris Hipkins
Hautū Te Puna Hanganga, Matihiko	**Minister of Education**
10 / 06 / 2022	__/__/____

Background

1 The COR was conducted in March 2021 to establish the expected costs to complete the CSR programme and identify the implications of transitioning CSR schools back into our business-as-usual asset management process.

2 The review identified multiple options to complete the programme. On 19 October 2021 you selected the option to complete the programme by increasing the programme budget by $205 million [METIS 1273723 refers].

3 This approach will deliver the intended scope of the original programme and meet stakeholder expectations, while also considering the need to invest in other areas of New Zealand.

Reflecting Updated Costs

4 The COR identified $205 million to complete the programme, however this was based on estimates at the time of the review. Since then, 12 months of significant, unprecedented cost escalation has occurred.

5 According to Statistics New Zealand data, between 2015-2021 construction costs increased by around 2.5%-4.5% per year. In 2021 construction costs increased by 7.5%. To reflect the unprecedented inflation between the completion of the review and now, the Ministry has re-baselined the COR costs to complete the programme to ensure the essential scope can be delivered.

6 The Ministry estimates that the funding required to complete the programme based on current costs has risen from $205 million to 9(2)(j) [redacted]. This difference includes real price increase due to Standard General Escalation from 1 June 2021 to May 2022, set at 8.8%.

7 KPMG has conducted an independent review of this price analysis and supports the adjustment to 9(2)(j) [redacted] to reflect updated costs.

8 The Ministry has employed a series of actions to manage cost escalations within the current programme budget where possible. This has included ensuring all funding is essential, as well as creating efficiencies by co-delivering.

9 Increasing the close out review funding to 9(2)(j) [redacted] reflects the up-to-date costs to ensure the essential scope can be delivered.

Proposed approach to manage future escalation

10 There is likely to be further cost escalation while the programme is phased out over the next 3-4 years. To ensure the close out funding accounts for future risk of cost escalation, the Ministry proposes managing additional cost increases through project risk contingency of an additional 9(2) [redacted]

11 An adjustment of 9(2) [redacted] is equivalent to an increase to the total programme envelope of 9(2)(j) [redacted]

12 It is difficult to predict future cost escalations and what the actual tender price will be when projects go to market. An additional 9(2) [redacted] of project risk contingency would introduce a buffer to allow the Ministry to manage and respond to future escalation, to ensure the scope can be delivered as the programme is phased out.

13 An [redacted] adjustment is reasonable as it is based on observed price escalation across the sector due to Covid-19 related cost impacts, set at 9% as well as annual inflation of 2%. Project risk contingency of [redacted] is also in line with risk provision for medium risk projects in other property programmes across the portfolio.

14 There are a range of benefits of the proposed approach to manage future escalation:

Table two: Benefits of proposed approach to future escalation

Benefit	Explanation
1. Reflects financial market	Ensures future escalation is accounted for so that project budget is a result of actual tender over budget when projects go to market.
2. A buffer is in place to manage updated costs	The future years of this programme have been considered, avoiding the Ministry having to seek additional close out funding from Cabinet in the future.
3. Projects are not at risk of being deferred	Ensures there is enough funding to avoid deferring or delaying projects.
4. Investment decisions are balanced against a need to invest in other areas of New Zealand	Additional funding will be sought through the annual budget process, ensuring decisions are considered within the context of other financial decisions and allow for trade-offs to be made in the context of wider priorities.
5. No significant capital commitment from the Crown is required immediately	Funding would be phased out over the next 3-4 years.

15 The proposed approach will not change the scope of your preferred option to close out the CSR programme. The increased programme risk contingency will ensure the programme is able to respond to price increases.

16 If the close out review funding is allocated, but the increased programme risk contingency is not approved, the Ministry will continue to deliver the projects. However, should cost pressures mean there is insufficient funding available to deliver the full scope of works, some projects will be deferred. The deferred liabilities would be shifted to other property programmes, such as the NSRP.

17 This would mean delivering the work over a longer timeframe, as projects would be prioritised against others in the national programme. We would also miss the opportunity to leverage off the existing suppliers and capacity currently available to us through the CSR programme.

18 CSR is a proven infrastructure programme with a strong track record of spend and delivery. As at June 2022:

Table Three: Christchurch School Rebuild Programme Status (May 2022)

Number of Projects	Project Stage
75 schools	Complete
24 schools	Construction
14 schools	Planning and Design
2 schools	Yet to enter programme
	**A further 3 schools expected to be completed by end of 2022*
	Total Spend: $985 million

19 As an existing programme the Ministry is well positioned to convert any additional funding from drawdown to spend quickly by utilising the existing governance and delivery frameworks.

Next Steps

20 We have attached the draft Cabinet paper which seeks Cabinet agreement to increase the programme budget by $301 million 9(2)(j) [redacted] The paper will also seek the Delegated Financial Authority for CSR projects over $35 million.

21 The Cabinet paper does not seek the CSR funding as a Budget 23 pre-commitment and funding would still be subject to future budget priorities.

22 Once you have provided direction on completing the CSR programme, we will update the draft Cabinet paper. We recommend that this paper is lodged in June-July 2022, after Budget 22 decisions. This is because decisions in this paper would relate to Budget 23 and future budgets. The draft Cabinet paper has no impact on Budget 22 decisions.

Financial Implications

23 The following table outlines the breakdown of the additional funding to be sought for the CSR programme.

Table four: Christchurch School Rebuild Close Out Review Funding Summary

	Current envelope	October COR funding	Revised COR funding
Funding	$1.353 b	$205 m	$301 m 9(2)(j) [redacted]
Total programme envelope	$1.353 b	$1.558 b	$1.654b

24 The funding is not required immediately and would be sought through the annual budget process as with the current CSR programme. However, for the Ministry to undertake the necessary planning and to be able to enter contracts, a Cabinet commitment to the overall funding top up is required to close out the programme.

25 As an existing programme, the Ministry is well positioned to convert any additional funding from draw down to spend quickly by utilising the existing governance and delivery frameworks.

26 The graph below summarises the funding profile of the programme and forecasts how the additional close-out review funding will be spent to close out the programme.

9(2)(f)(iv)

[redacted]

27 [redacted]

28 The Ministry will only seek to draw down funding as it is required to deliver the projects. This would be achieved through a slight increase in annual CSR bids from 2023/24, minimising the impact on Crown funding.

Project level delegations

29 The Cabinet paper also seeks approval for updated project delegations for ten CSR projects over $30 million.

30 Following the close out review, these project budgets have been updated to reflect the scope agreed in METIS 1273723, and costs that reflect the latest market prices.

31 The funding for these projects will be met from the COR adjusted CSR programme envelope of $1.654b.

Proactive Release

32 The Ministry recommends this education report is not released at this time because it contains commercially sensitive budget information that may prejudice the Ministry's ability to negotiate commercially. The report also contains advice that is yet to be considered by Cabinet.

Annex 1 - Draft Cabinet paper: Completing the Christchurch Schools Rebuild Programme