The Treasury

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[40]	Not in scope	

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Reference: T2017/515 SH-4-5-7

THE TREASURY
Kaitohutohu Kaupapa Rawa

Date: 9 March 2017

To: Minister of Finance (Hon Steven Joyce)

Deadline: None

Aide Memoire: School Property Growth Package: Implications of Scaling

Purpose

At a discussion on the draft social sector package on Friday 3 March you asked for more information about the School Property Growth Package capital initiative (the initiative) for Budget 17. You asked specifically about:

- the implications of a range of scaling options, and
- the impact of new capital injections on the pipeline of school property projects.

Scaling Options and Implications

The initiative is supported by the 2017 School Property Programme Business Case (PBC), which provides three options for investment. The full package would require [33] capital injection. The 'minimum' option [33] delivers roll growth only, and an 'intermediate' option [33] provides a scaled package.

Even the 'intermediate' option in the PBC would represent the largest capital injection the Ministry of Education (the Ministry) had ever received. In Budget 16, Ministers agreed $727.281 capital injection for the Ministry, but this included significant funding for the Christchurch Schools Rebuild and the second and third New Zealand Schools Public Private Partnerships, as described in Table 1 below.

Table 1: Budget 2016 Capital Injection - Ministry of Education

Initiative	$m
School Property Growth Package	270.577
Christchurch Schools rebuild	127.790
New Zealand Schools Public Private Partnership – Project Two	151.567
New Zealand Schools Public Private Partnership – Project Three	177.347
Total	**727.281**

While the initiative is phased across out-years, it does not cover total costs for school property over the next four years. The current approach to funding expansionary school property projects, since Budget 14, has been for the Ministry to prepare an annual Programme Business Case for projects commencing in the coming fiscal year. Whatever level of investment Ministers decide on for Budget 17, there will be another School Property Growth Package initiative at Budget 18.

For this years' initiative, roll growth could be phased across fewer years to reduce the size of the commitment, and additional roll growth for out-years deferred to Budget 18. Many of the new schools and expansions in the full package are also deferrable, but the roll growth only 'minimum' package is unviable. We have been working with the Ministry to describe other scaled options that better balance risk.

The attached A3 (Appendix 1) describes the full package from the PBC, and three scaling options. The 'impact statement' section of the A3 outlines risks associated with the 'Treasury minimum option' (in green). In formulating the Treasury recommended options we have considered:

- certainty of funding requirement – including land acquisition and capacity
- certainty of network projections – related to demand and pace of developments in the local network, and
- fiscal envelope – affordability of the project in Budget 2017.

The main risks we see with the minimum option from the Treasury draft capital package are:

- [33]
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Impact on the Pipeline

The Education Infrastructure Service is currently managing expansionary projects for six new schools, seven expansions, and four kura across the country, which were funded in each Budget from 2013 through to 2016. They also manage a capital injection-funded roll growth programme of over $100m per year, and a redevelopment programme of around $200m per year funded from annual depreciation.

There is significant growth in the pipeline, driven by increasing rolls impacted by high net migration and urbanisation (and 'Aucklandisation'). [34] addressing infrastructure pressures over the next ten years in Auckland alone will [34] While high rates of growth means that the risk of oversupply in Auckland in the next five years is low, parental choice and other school-based factors make anticipated demand in specific local areas difficult to forecast. There are also substantial roll growth rates in other regions including Otago and Bay of Plenty, but the scale of rolls in Auckland and the number of schools already experiencing capacity pressures makes it a high priority.

Due to the changeable nature of forecasts, approving funding for specific schools more than a few years before the projected opening date, or before a suitable site has been identified, carries the risk that network projections and priorities change before builds can commence. [33]

. In addition, the Ministry may not be able to deliver on a capital programme of significantly increased scope, due to:

- current construction market constraints, particularly in Auckland, and
- departmental capacity constraints, evidenced by large departmental capacity initiatives for the Education Infrastructure Service in Budget 17 [33]

The initiative includes a [33] per annum departmental capacity component, which would support delivery of a larger capital programme. We have proposed treating all departmental capacity initiatives across the Ministry equally, funding at a scaled rate for two years only, to maintain the system while giving the Ministry sufficient time to develop its thinking about its future operating model. We recommend scaling the operating component of this initiative to [33] per annum, to align with the Ministry's current-year gains from legal settlements that will not be available in future years.

In recent years, the Ministry has also made significant capital transfers at the March Baseline Update (MBU), confirmed at the October Baseline Update (OBU) to re-phase capital spending, reflecting issues such as:

- site acquisition and designation issues for new schools and kura,
- changes in demographic forecasts leading to expansions being postponed, and
- other programme delays outside of the Ministry's control.

Table 2 shows capital transfers for the last three years, including MBU 2017 changes.

Table 2: Capital transfers

Capital Transfers	**MBU & OBU 2015 ($m) (confirmed)**	**MBU & OBU 2016 ($m) (confirmed)**	**MBU 2017 ($m) (proposed)**
New schools and expansions	29.883	64.220	[33]
Christchurch Schools Rebuild	48.030	85.560	
Roll growth programme		60.321	
In-principle transfers			
New schools and expansions			
Christchurch Schools Rebuild			
Roll growth programme			
Totals	**77.913**	**210.101**	

**To be confirmed at OBU 2017*

Under the current arrangements where the Ministry seeks funding for specific projects which require a long lead-in, we can expect large transfers to continue while new injections are required for higher priority projects. In the Auckland Education Growth Plan (due to be completed in late 2017) the Ministry aims to take a more integrated view to strategic planning in the Auckland region, considering the property and policy options to address network efficiency, demand pressures, and educational outcomes over the next ten years (SEC-16-Min-0061 refers).

[33]

It is difficult to judge what share of delays in the capital programme are due to the Ministry's departmental capacity constraints, but EIS have indicated that having received only a one-year increase in departmental funding (of $8m) at Budget 16 has limited their ability to forward-plan. We are confident that by continuing this for the next two years (through the operating initiative Supporting Infrastructure Service Delivery), the Ministry will be able to support delivery of a scaled School Property Growth Package initiative. Other operating funding (depreciation and capital charge) associated with the Schools Property Growth Package initiative scales with the size of the capital injection.

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