

# The Treasury

## Budget 2017 Information Release

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Chair  
Cabinet Committee on Economic Growth and Infrastructure

## **NOVEMBER 2016 EARTHQUAKE: FUNDING THE REINSTATEMENT OF THE SOUTH ISLAND TRANSPORT CORRIDORS**

### **Proposal**

1. We propose the Committee:
  - 1.1. note that the total cost of reinstating SH1 and MNL has been refined down to a range of \$1.1 billion – \$1.33 billion
  - 1.2. note progress and expenditure to date on the initial recovery works on the severely damaged South Island transport corridors - State Highway 1 (SH1) and the Main North Line (MNL)
  - 1.3. <sup>[37]</sup>
  - 1.4.
  - 1.5.
  - 1.6.
  - 1.7.
  - 1.8. note that the difference between the lower and upper bound of the roading cost range will be recorded as a fiscal risk

- 1.9. note that New Zealand Transport Agency (NZTA) has also identified between \$195 million – \$240 million of roading improvements that will be funded from the National Land Transport Fund (NLTF) if they go ahead
- 1.10. note that the NZTA and KiwiRail will report back to Joint Ministers in June 2017 on progress and at that point the NZTA will confirm its final plans for the improvements work
- 1.11. note that communications about the reinstatement will be handled by the Minister of Transport and the Minister of Finance jointly and it is our intention that we announce an update on the situation through the Minister of Finance’s pre-Budget speech.

**Executive summary**

- 2. The cost estimate range for reinstating SH1 and MNL has been narrowed from the original cost estimate of between \$1.4 billion to \$2.0 billion to a range of \$1.1 billion – \$1.33 billion. This covers road reinstatement costs of \$812 million – \$912 million <sup>[25]</sup>
- 3. Good progress has been made on initial recovery works and NZTA and KiwiRail still expect to have the corridor open by December 2017. The works to date have involved debris clearance, opening the inland road into Kaikōura and strengthening the alternative State Highway route via Lewis Pass. NZTA and KiwiRail have also developed a Concept Design for reinstating SH1 and MNL. The main feature of this Concept Design is that approximately 2.5 km of the route north of Kaikōura will be realigned around the largest slips and into the coastal marine area.

4. <sup>[37]</sup>

4.1. <sup>[37]</sup>

4.2.

5. <sup>[25]</sup>

, as a charge against the Budget 2017 Capital Allowance, as Table 1 shows below:

**Table 1: Proposed SH1 reinstatement funding**

	2016/17 \$m	2017/18 \$m	2018/19 \$m	Total \$m
Reinstatement of SH1	69	325	418	812

6. This funding will be provided through an appropriation in 2016/17 and 2017/18. The 2018/19 costs will be set aside as a tagged capital contingency. The difference between the lower and upper bound of the range will be recorded as a fiscal risk.
7. The reinstatement has considerable risks. Slip clearance, design and construction are occurring concurrently, within a tight deadline to reopen the corridors. The risks will be mitigated through:
  - 7.1. strong project governance – NZTA and KiwiRail have set up North Canterbury Transport Infrastructure Recovery (NCTIR) to manage the work and optimise costs. NCTIR includes NZTA, KiwiRail and contractors. An oversight group of senior officials from NZTA, KiwiRail, the Ministry of Transport, the Treasury and an independent observer will also be established.
  - 7.2. regular reporting to Joint Ministers.
8. In addition to the reinstatement costs, NZTA has identified possible roading improvements of between \$195 million – \$240 million that will be funded from the National Land Transport Fund (NLTF) if they go ahead.
9. NZTA and KiwiRail expect to complete detailed design for the reinstatement in June 2017, and will report back to Joint Ministers then to confirm their final plans for the improvements work.
10. We propose that communications about the reinstatement will be by the Minister of Transport and the Minister of Finance jointly. It is our intention that we announce an update on the situation through the Minister of Finance’s pre-Budget speech.

## **Background**

11. The earthquakes in November 2016 severely damaged SH1 and KiwiRail’s MNL north and south of Kaikōura. Immediately, the Government took several decisions to advance the repair of the severed road and rail links.
12. On 5 December 2016, Cabinet, inter alia [CAB-16-MIN-0675 refers]:
  - 12.1. agreed to rebuild and improve SH1 and MNL along their current coastal route, with improvements to the safety and resilience of the route, at an estimated cost in the range of \$1.4 billion to \$2.0 billion
  - 12.2. agreed to fund, in principle, the uninsured cost of reinstating MNL
  - 12.3. agreed to fund the roading component of the costs of the reinstatement works along the coastal alignment

- 12.4. agreed that any Crown contribution to the reinstatement and the funding approach will be confirmed as part of Budget 2017
- 12.5. invited the Minister of Transport and the Minister of Finance to report back to the Economic Growth and Infrastructure Committee with updated cost estimates and a proposed Crown-led funding approach in early 2017.
13. On 20 December 2016, the Governor-General signed an Order in Council to expedite the reinstatement of the coastal route, the Hurunui/Kaikōura Earthquakes Recovery (Coastal Route and Other Matters) Order 2016.
14. [37]

### Estimated cost range of reinstatement

15. Since the earthquake and Cabinet’s agreement to reinstating SH1 and MNL along their current alignment, NZTA and KiwiRail have been undertaking initial recovery works and developing designs for the reinstatement. NZTA and KiwiRail have narrowed the estimated cost range of the reinstatement to \$1.1 billion – \$1.33 billion (including rail and road). This reduction has occurred because of fast progress with design, more knowledge about the work ahead as the result of experience to date, and greater understanding about quantities and risks.

### Initial recovery works

16. NZTA formed NCTIR to undertake the reinstatement work. NCTIR includes NZTA, KiwiRail, Downer New Zealand Ltd, Fulton Hogan Ltd, HEB Construction Ltd and Higgins Contractors Ltd. Initial recovery works involved debris clearance, opening access into Kaikōura via the Inland Road (Route 70) and strengthening the alternative State Highway route via Lewis Pass to cope with the additional traffic.
17. The NLTF has absorbed the cost of the remedial work on the roading network. KiwiRail has met approximately [25] of costs to the end of February 2017. Table 2 below sets out expenditure to date and describes the work undertaken.

**Table 2: Reinstatement work to the end of February 2017 and cost**

Activity	Cost \$m	Description of work	Comment
SH1 and MNL reinstatement	[25]	Helicopter sluicing and initial design work	[25]
Lewis Pass alternate route		Repairs, geotechnical assessments and design of remedial works	Funded from the NLTF.
Route 70 Inland Route		Slip clearance and repairs	Funded from the NLTF.

Emergency works	[25]	Clearing obstructions and making the road and rail system safe	Funded from the NLTF and by KiwiRail.
Rail track works		Reinstating minor to moderate track damage	[25]
<b>Total</b>	<b>\$44.1</b>		

### **NZTA and KiwiRail Concept Design for the reinstatement**

18. NZTA and KiwiRail have developed a Concept Design for the proposed reinstatement. This assisted in narrowing the range of the cost estimate. The main feature of the Concept Design is that SH1 and MNL will be reinstated along their existing footprint, with the exception of approximately 2.5 km of predominantly road corridor. This corridor will be realigned around the toes of the largest slips into the coastal marine area. SH1 and MNL will be realigned in some other areas but the realignment will not encroach on the coastal marine area.
19. The rail connection between Picton and Christchurch will be reinstated largely on the pre-earthquake alignment. At several of the worst affected slip areas, rail is located inside tunnels, so the extent of damage from major slips is less than to the road corridor. A much shorter length of rail corridor will require realignment, including in one of the major slip areas. SH1 and MNL will be realigned in some other places to go around smaller slips but the realignment will be within the existing corridors and will not encroach on the coastal marine area. Diagrams showing the slips and the proposed realignments are attached at Appendix A.

### **Breakdown of the estimated costs of the reinstatement by corridor section**

20. Table 3 below breaks down the estimated reinstatement costs by corridor section based on the lower bound of the cost range, and describes the work needed.
21. The cost estimates have more certainty at the northern and southern ends of the corridors. For example, KiwiRail has good knowledge and extensive experience of repairing and replacing rail bridges. Most uncertainty attaches to the Clarence to Oaro section because of the nature of the damage, and most of the cost will lie in these middle sections. There are many unknowns where slip clearance and slope stabilisation is concerned, and some of the issues and their implications will only become known as the work is carried out.
22. NZTA and KiwiRail plan to have MNL and SH1 open by the end of December 2017, with limited access as soon as safely achievable. Finishing work will continue into 2018/19. Further design work will be required to develop a detailed timeline.

**Table 3: State Highway 1 and Main North Line cost estimates by corridor section**

Section of Corridor (North to South)	State Highway 1		Main North Line	
	Comment	Estimated cost of repairs (lower bound) \$m	Comment	Estimated cost of repairs (lower bound) \$m
Picton to Seddon	[25]			
Seddon to Clarence				
Clarence to Kaikōura				
Kaikōura to Oaro				
Oaro to Cheviot				
Cheviot to Christchurch				
Total: (lower bound)				
Total: (upper bound)				

## Financial implications

### ***Current estimated cost of the reinstatement***

23. NZTA's and KiwiRail's estimate of the cost of the reinstatement, exclusive of any insurance recoveries for KiwiRail, are shown in Table 4 below by financial year. These figures represent the current best estimate of costs.

**Table 4: SH1 and MNL cost estimates by financial year**

	<b>Estimated total range</b>	<b>Estimated costs in 2016/17</b>	<b>Estimated costs in 2017/18</b>	<b>Estimated costs in 2018/19</b>	<b>Estimated balance of cost (upper bound)</b>
	<b>\$m</b>	<b>\$m</b>	<b>\$m</b>	<b>\$m</b>	<b>\$m</b>
SH1 reinstatement	[25]				
Rail reinstatement					
<b>Total of road and rail excl. insurance recoveries</b>					

24. Cost estimates for the reinstatement will be updated once the detailed design is complete.

### ***Funding the rail reinstatement***

25. [37]

26. [25]

27. [33]

28. As part of Budget 2017 decisions, we are also proposing a capital appropriation for KiwiRail totalling \$450 million over two years. [37]



29. [37]

30.

31.

### **Funding the roading reinstatement**

32. In November 2016, Cabinet agreed that the Crown would fund the roading component of the reinstatement. Another option would have been to fund the cost, or part of it, from the NLTF, for example, future NLTF-funded projects could be reprioritised.

33. Given the pressures on the NLTF, a Crown grant is the preferred option to fund the roading reinstatement. To enable this, we propose the establishment of a non-departmental capital appropriation in Vote Transport entitled “Reinstatement of South Island State Highway 1” with a scope “*This appropriation is limited to the reinstatement of State Highway 1 north and south of Kaikōura*”.

34. We also propose setting aside a tagged capital contingency for the estimated \$418 million of roading reinstatement costs in 2018/19. We propose that this contingency can be drawn upon following approval by Joint Ministers of detailed design and refined cost estimates for the reinstatement.

35. Table 5 below shows how the Crown funding will be phased:

**Table 5: Phasing of Crown funding for SH1 reinstatement**

	2016/17 \$m	2017/18 \$m	2018/19 \$m	Total \$m
Non-departmental Capital Expenditure: Reinstatement of South Island State Highway 1.	69	325	418	812

36. The difference between the lower and the upper bounds of the cost range of the roading reinstatement costs will be recorded as a fiscal risk.

37. We also seek authorisation for the Minister of Finance and the Minister of Transport acting jointly to make changes to the appropriation, if required by progress on the reinstatement.

## Fiscal implications

38. Under the preferred option for funding the reinstatement, <sup>[37]</sup> will be recorded as a pre-commitment against the Budget 2017 Capital Allowance. <sup>[37]</sup> reinstatement is already
39. The difference of <sup>[25]</sup> between the proposed Crown funding for the roading reinstatement of <sup>[25]</sup> at Budget 17 and the upper bound of the cost range for the roading reinstatement will be recognised as a fiscal risk in the Budget Economic and Fiscal Update 2017.
40. <sup>[37]</sup>

## Risks of the reinstatement

41. The reinstatement is challenging. Clearance, design and construction are occurring together, within a tight deadline to reopen the corridors. The key risks to the Crown are cost and timing risks.
42. The key cost risks are associated with the uncertainties presented by the large slips in the Kaikōura to Oaro section of the corridors. As the design process progresses, more will become known about the nature of the challenges faced by the reinstatement and the cost range can be narrowed.
43. The precise nature of the severe slips is unknown. This means that the proposed timeline for re-opening the corridors is subject to considerable uncertainty. This uncertainty has flow-on effects on the local and national economy, especially the tourism and freight transport sectors. There is also a potential reputational risk for the Crown if the project is not delivered to the publicly committed timeline.
44. To mitigate these risks, we consider that strong governance is essential for this reinstatement work. As noted previously, NZTA and KiwiRail have set up NCTIR. NZTA and KiwiRail, along with the non-owner participants, are responsible for optimising the costs of undertaking the agreed work.
45. An oversight group of senior officials from NZTA, KiwiRail, the Ministry of Transport, the Treasury and an independent observer is also being established. The group will also monitor the project to make sure it is managed well and is delivered in line with Cabinet decisions.
46. We will receive monthly updates and progress reports from NZTA on the reinstatement and on the performance of the alternate Lewis Pass route.
47. We will also receive a report back from the NZTA and KiwiRail by 30 June 2017 on progress, including an updated funding and risk assessment. This will follow completion of the detailed design phase of the reinstatement. The report back will confirm NZTA's final plans for any proposed improvements.

48. [25]

49. The Treasury will monitor progress of the rail component of the reinstatement through its position on the oversight group, and its existing relationship with the KiwiRail Board and management.

50. [25]

[37]

51. The Kaikōura coast and its inland routes contain an abundance of sensitive environments. The coast contains several significant archaeological and cultural sites, nationally important wildlife and associated habitats, and is known for its amenity and visual values. The scale of the works and multiple work sites pose risks to this environment. These risks include disturbing wildlife, reducing habitat availability, disturbing and affecting archaeological sites, and reducing amenity values. These culminate in a reputational risk for the Crown because environmental risks and their management often have visible outcomes in the public eye.

52. Critical to managing the environmental risks is building a robust relationship with the project's key stakeholders in the Restoration Liaison Group, a Group required under the Order in Council. This Group includes iwi and regulatory authorities responsible for authorising and managing environmental approvals. NCTIR will implement construction environmental management procedures and protocols to manage site-specific effects, with monitoring and auditing processes to benchmark the environmental compliance.

### **Roading improvements**

53. NZTA has identified possible roading improvements in addition to the reinstatement works. It estimates the cost of this improvement work to range from \$195 million – \$240 million. The work would include widening curves, edge protection, slow vehicle bays, pull over areas, parking areas, a cycle-walk path (Okiwi to Half Moon) and toilets. This would take place in the Clarence to Oaro section of the corridor.

54. These will be funded from the NLTF if they go ahead. We expect that the proposed improvements will be further considered by the NZTA Board and a decision will be made by the Board in June 2017.

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[25]

## Consultation

55. NZTA and KiwiRail have been consulted on this paper. The Department of the Prime Minister and Cabinet has been informed.

## Human rights, gender, disability, legislative implications and Regulatory Impact Analysis

56. There are no human rights, gender, disability, or legislative implications arising from this paper. A Regulatory Impact Analysis is not required.

## Publicity

57. The Minister of Transport announced the Government's commitment to the reinstatement of the Kaikōura coastal route on 15 December 2016. If the Committee agrees to the proposals in this paper, we plan to announce that the Government has confirmed funding for the reinstatement through the Minister of Finance's pre-Budget speech.
58. <sup>[37]</sup>

## Recommendations

59. The Ministers of Transport and Finance recommend that the Committee:

### *Progress to date*

1. **note** that the total cost of reinstating SH1 and MNL has been refined down to between \$1.1 billion to \$1.33 billion
2. **note** progress and expenditure to date on the initial recovery works on the severely damaged South Island transport corridors - State Highway 1 (SH1) and the Main North Line (MNL)

### *Rail reinstatement funding*

3. **note** Cabinet previously agreed to fund, in principle, the uninsured cost of reinstating MNL [CAB-16-MIN-0675 refers]
4. <sup>[37]</sup>
5. <sup>[37]</sup>

6. [37]

7. [37]

8. [37]

*Roading reinstatement funding*

9. **note** Cabinet previously agreed to fund the roading component of the South Island transport corridors reinstatement [CAB-16-MIN-0675 refers]
10. **note** that the cost of reinstating SH1 will be in the range of \$812 million – \$912 million
11. **agree** to Crown funding of [25] to fund the cost of reinstating SH1 in 2016/17 and 2017/18
12. **agree** to establish the following appropriation to give effect to recommendation 11 above:

Vote	Appropriation Minister	Title	Type	Scope
Transport	Minister of Transport	Reinstatement of South Island State Highway 1	Non-departmental Capital Expenditure	This appropriation is limited to the reinstatement of State Highway 1 north and south of Kaikōura.

13. **approve** the following changes to appropriations to give effect to the policy decision in recommendation 11 above, with a corresponding impact on net debt:

Vote Transport Minister of Transport	\$m – increase/(decrease)				
	2016/17	2017/18	2018/19	2019/20	2020/21 & outyears
Non-departmental Capital Expenditure: Reinstatement of South Island State Highway 1	69.000	325.000	-	-	-

14. **agree** that the proposed changes to appropriations for 2016/17 in recommendation 11 above be included in the 2016/17 Supplementary Estimates and that, in the interim, the increase be met from Imprest Supply
15. **agree** that the proposed changes to appropriations in recommendation 13 above are managed as a charge against the Budget 2017 Capital Allowance
16. **authorise** the Minister of Finance and the Minister of Transport acting jointly, to make changes to the appropriation established under recommendation 12 above, if required by construction progress on the reinstatement
17. **agree** to set aside a tagged capital contingency of \$418 million for the estimated 2018/19 estimated roading reinstatement
18. **agree** that any drawings on the tagged capital contingency in recommendation 17 above will be managed as a charge against the Budget 2017 Capital Allowance
19. **delegate** authority to the Minister of Transport and the Minister of Finance acting jointly, to approve drawings on the tagged capital contingency in recommendation 17 above, subject to completion of detailed design and refinement of cost estimates
20. **agree** that the expiry date of the roading tagged capital contingency in recommendation 17 above will be 30 June 2018
21. **note** that the difference between the lower and upper bounds of the roading reinstatement cost range will be recognised as a fiscal risk in the Budget and Economic Fiscal Update 2017

#### *Risks*

22. **note** the risks to the reinstatement, particularly the risks around costs and timing, and that these risks will be managed through strong project governance and regular reporting to Joint Ministers

#### *Improvements*

23. **note** that the New Zealand Transport Agency (NZTA) has also identified between \$195 million – \$240 million of improvements that will be funded from the National Land Transport Fund if they go ahead

#### *Next steps*

24. **note** that the NZTA and KiwiRail will report back to Joint Ministers on progress by 30 June 2017 and NZTA will confirm its final plans for the improvements work
25. **note** that communications about the reinstatement will be handled by the Minister of Transport and the Minister of Finance jointly and it is our intention that we announce an update on the situation through the Minister of Finance's pre-Budget speech.

Hon Simon Bridges  
**Minister of Transport**

Dated: \_\_\_\_\_

Hon Steven Joyce  
**Minister of Finance**

Dated: \_\_\_\_\_