

The Treasury

Budget 2011 Information Release

Release Document

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Treasury Report: CERA: Cost of Setting up a New Department

Date:	30 March 2011	Report No:	T2011/640
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Action Sought

	Action Sought	Deadline
Prime Minister (Rt Hon John Key)	Agree to the recommendations, subject to the Order in Council being made to establish the Canterbury Earthquake Recovery Authority (CERA)	Monday 4 April 2011
Minister of Finance (Hon Bill English)	Agree to the recommendations	Monday 4 April 2011
Minister for Canterbury Earthquake Recovery (Hon Gerry Brownlee)	Agree to the recommendations	Monday 4 April 2011
Associate Minister of Finance (Hon Simon Power)	Agree to the recommendations	Monday 4 April 2011
Associate Minister of Finance (Hon Steven Joyce)	Agree to the recommendations	Monday 4 April 2011

Contact for Telephone Discussion (if required)

Name	Position	Telephone	1st Contact
Andrew Blazey	Manager, Sector Monitoring	[1]	✓
[1]			

Ministers' Office Actions (if required)

None.

Enclosure: No

Treasury Report: CERA: Cost of Setting up a New Department

Purpose of Report

1. This report provides you with advice on the expected costs of running the Canterbury Earthquake Recovery Agency (CERA) for the 15-month period from 1 April 2011 to 30 June 2012 and seeks Budget Ministers' approval to fund CERA for that period.

Analysis

2. On 28 March 2011, Cabinet agreed that:

Budget Ministers, in consultation with the Minister for Canterbury Earthquake Recovery, should determine the amount of funding to be appropriated for CERA and any additional amount to be held in a tagged contingency for this purpose.
3. This report provides Budget Ministers with the estimated operating costs of CERA. A tagged contingency to fund earthquake related costs will be the subject of a separate paper.
4. Treasury and SSC have estimated the operational expenditure for CERA, in order to meet the deadline for including Vote CER in the 2011 Budget documents for Cabinet.
5. A draft organisational structure has been prepared on the assumption of employing 45 to 55 full time employees in Christchurch and Wellington. The salaries for these staff were derived using estimates of Wellington departmental average salaries. Staff numbers and the organisational structure are based on discussions with the State Services Commission. Although the structure may change, it provides a basis for developing a departmental budget.
6. The salary and expenses of the chief executive are to be recovered from CERA by the SSC. The recommendations in this paper include an appropriation for SSC to pay the chief executive's salary and expenses based on that recovery from CERA.
7. A large proportion (approximately 45%) of the estimated operating cost is for external expertise in communications, legal, engineering, economic and planning services. This reflects CERA's requirement for independent, expert advice as an input into key decisions. Although some of this capability is likely to be held in-house, we expect that the magnitude of some of the required decisions is likely to benefit from independent advice. We also expect that this may require international expertise and have made some allowance for such costs.
8. We have assumed that CERA's asset base will not be significant in relation to administrative functions and that major asset expenditure would be drawn upon using a tagged contingency. As such, costs relating to insurance, depreciation and capital charge are calculated based on departments of a similar size.
9. In that regard, the labour cost is also comparable to similar sized organisations, for example operating budgets for MCH and MORST was approximately \$12 million, and CERA's equivalent cost is also approximately \$12 million. We have then adjusted that cost base for CERA to build in the significant use of external advisors. Table 1 details the allocation of estimated costs:

Table 1: CERA Departmental Expenditure Summary

CERA Operating Cost Summary (\$'000) ex GST	2010/11	2011/12
	3 months	12 months
Personnel costs	960.0	7,933.7
Research, consultancy	2,100.0	9,750.0
Accommodation, IT, Vehicles	174.0	972.0
Capital charge	21.3	85.0
Depreciation	109.3	437.0
Other & contingency	600.0	2,400.0
Total 15 month spend	3,964.6	21,577.7

10. The budget in the first three months of CERA's operation is not one quarter of the 12 month budget because it assumes assistance from other agencies (local and central government) to second staff and other resources. Treasury and SSC will provide its costing assumptions to CERA; the general assumptions are as shown in the table below:

Table 2: Departmental Budget Assumptions

Assumption	Comment
Labour	Salaries are calculated at the average salary rate for the public sector in Wellington. That average is 10 - 15% higher than that of Christchurch which is intended to provide some flexibility in the labour mix. A further allowance has been added for recruitment, health & safety, ACC and other associated labour costs.
Shared Services	The use of shared service arrangements from other providers is the assumed model for developing corporate service functions so as to reduce the investment in standalone services that might otherwise be required. CERA is to pay for the shared services.
Time period	At this stage, a budget is required for expenditure in 2010/11 and 2011/12 only. A budget for the remaining outyear period is to be developed by CERA once it is staffed. Expenditure incurred in 2010/11 is to be appropriated in the Supplementary Estimates and funded through Imprest Supply.
Consultancy	The budget includes approximately \$9.7 million per annum in consultancy expenses, including communications, legal, engineering, economic and planning services. These costs are broad estimates based on the likely requirement that CERA will need to access specialist expertise in a prompt manner.
Contingency	A 10 percent contingency sum has been added to the budget given the uncertainty of the cost structure that will be required.

11. We have concluded that CERA's expenses will be incurred under the following departmental outputs:
- Planning for the Recovery; and
 - Implementation of the Canterbury Recovery Programme.
12. Cabinet has established in Vote Canterbury Earthquake Recovery 'Planning for the Recovery' as a departmental output class and appropriated \$0.5 million. We recommend the following output class, 'Implementation for the Recovery', also be established and that the scope of this appropriation be limited to expenses incurred in implementing the recovery of the Canterbury earthquakes.

13. The budget in Table 1 refers to the 15 month period from 1 April 2011 through to 30 June 2012. In Table 3, the total budget is allocated between the two output classes.

Table 3: Output Cost Summary

CERA Output Cost (\$'000) GST exclusive	2010/11	2011/12
Output Class 1: Planning for the Canterbury Recovery	2,973.4	16,183.3
Output Class 2: Implementation of the Canterbury Recovery Programme	991.2	5,394.4
Total 15 month spend	3,964.6	21,577.7

14. Joint Ministers will be able to adjust the allocation of funding across output classes in the October Baseline Update for 2011/12.

Risks and Assumptions

15. The budget assumptions and draft structure for the new department have been prepared without detailed planning information or a full understanding of the roles the new department is to perform; as such estimating the cost of the new department is based on broad estimates and market relativities. In the initial budget periods we have built in additional allowances for establishing capability and a prompt pace of activity. The department may not spend all of these estimated costs and any under spend may be returned to the Crown at the end of each financial year.

Consultation

16. SSC has been consulted and jointly prepared the assumptions in this report. DPMC has been informed of his report.
17. The Office of the Minister for Canterbury Earthquake Recovery was consulted on this report.

Recommended Action

18. We recommend that you:

a **note** that Treasury and SSC have estimated CERA's operating costs for the first 15 months from 1 April 2011 to 30 June 2012, based on a draft organisational structure;

b **agree** to establish in Vote Canterbury Earthquake Recovery a departmental output expense appropriation 'Implementation for the Recovery Programme' and that the scope of this appropriation be limited to expenses incurred in implementing the recovery of the Canterbury earthquakes;

Agree/disagree.
Prime Minister

Agree/disagree.
Minister of Finance

Agree/disagree.
Minister for Canterbury
Earthquake Recovery

Agree/disagree.
Associate Minister of Finance

Agree/disagree.
Associate Minister of Finance

c **note** that Cabinet has already established in Vote Canterbury Earthquake Recovery a departmental output expense appropriation 'Planning for the Recovery' and an initial amount of \$0.500 million in 2010/11;

d **agree** to increase Vote State Services (Remuneration and Related Employment Costs of Chief Executives appropriation) by \$0.558 million to cover the Canterbury Earthquake Recovery Chief Executive's remuneration and expenses in 2011/12;

Agree/disagree.
Prime Minister

Agree/disagree.
Minister of Finance

Agree/disagree.
Minister for Canterbury
Earthquake Recovery

Agree/disagree.
Associate Minister of Finance

Agree/disagree.
Associate Minister of Finance

e **agree** to the following increases in appropriation to cover the first 15 months of CERA's operations with a corresponding impact on the operating balance;

Agree/disagree.
Prime Minister

Agree/disagree.
Minister of Finance

Agree/disagree.
Minister for Canterbury
Earthquake Recovery

Agree/disagree.
Associate Minister of Finance

Agree/disagree.
Associate Minister of Finance

	\$ million – increase/(decrease)				
	2010/11	2011/12	2012/13	2013/14	2014/15 & Outyears
Vote Canterbury Earthquake Recovery Minister for Canterbury Earthquake Recovery Departmental Output Expense: Planning for the Recovery (funded by revenue Crown)	2.473	16.183	-	-	-
Departmental Output Expense: Implementation for the Canterbury Recovery Programme (funded by revenue Crown)	0.991	5.394	-	-	-
Vote State Services Minister of State Services Non-Departmental Other Expense: Remuneration and Related Employment Costs of Chief Executives	-	0.558	-	-	-
Total Operating Expenses	3.965	21.577	-	-	-

- f **agree** that the proposed changes to appropriations in recommendation (e) above for 2010/11 be included in the Supplementary Estimates and that, in the interim, the increase be met from Imprest Supply;

Agree/disagree.
Prime Minister

Agree/disagree.
Minister of Finance

Agree/disagree.
Minister for Canterbury
Earthquake Recovery

Agree/disagree.
Associate Minister of Finance

Agree/disagree.
Associate Minister of Finance

Andrew Blazey
**Manager, Sectoring Monitoring
for Secretary to the Treasury**

Rt Hon John Key
Prime Minister

Hon Bill English
Minister of Finance

Hon Gerry Brownlee
**Minister for Canterbury
Earthquake Recovery**

Hon Simon Power
Associate Minister of Finance

Hon Steven Joyce
Associate Minister of Finance