



Cabinet

CAB Min (11) 32/16

Copy No:

Minute of Decision

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Canterbury Earthquake: Voluntarily Acquired Insured Residential Red Zone Properties: Procurement Processes and Costs

Portfolio: Canterbury Earthquake Recovery

On 5 September 2011, Cabinet:

Background

- 1 **noted** that:
 - 1.1 in June 2011, Cabinet approved the Canterbury Earthquake Recovery Authority making an offer to buy the insured residential properties in the Christchurch initial red zone [CAB Min (11) 24/15];
 - 1.2 in August 2011, Cabinet approved an offer to buy Kaiapoi insured residential homeowners whose properties which have been re-zoned from orange to red [CAB Min (11) 30/18];
 - 1.3 in light of the strong interest in the red zone offers, take-up is expected to begin immediately;
- 2 **noted** that transaction costs need to be appropriated to progress the acquisition and management of Christchurch and Kaiapoi insured residential red zone properties;

Financial implications

- 3 **agreed** to establish a new Non-Departmental Other Expense appropriation "Management of Voluntarily Acquired Insured Residential Red Zone Properties";
- 4 **agreed** that the scope of this appropriation be "this appropriation is limited to expenses related to third party providers involved in transactions associated with the Crown's acquisition of voluntarily acquired insured residential red zone properties in Canterbury";
- 5 **approved** the following changes to appropriations to provide for transaction costs incurred by the Canterbury Earthquake Recovery Authority with third parties on behalf of the Crown, relating to the acquisition and management of insured residential properties in Canterbury, with respect to the initial red zones announced on 23 June 2011 and the Kaiapoi red zones announced on 18 August 2011, with a corresponding impact on the operating balance:

	\$m-increase/(decrease)				
	2011/12	2012/13	2013/14	2014/15	2015/16 & Outyears
Vote Canterbury Earthquake Recovery Minister for Canterbury Earthquake Recovery					
Non-Departmental Other Expense: Management of Voluntarily Acquired Insured Residential Red Zone Properties	\$80.910	-	-	-	-

- 6 **agreed** to establish a new Departmental Output Expense appropriation “Management of Voluntarily Acquired Insured Residential Red Zone Properties”;
- 7 **agreed** that the scope of this appropriation be “This appropriation is limited to expenses associated with the acquisition, valuation and management of voluntarily acquired insured residential red zone properties in Canterbury”;
- 8 **approved** the following changes to appropriations to provide for transaction costs incurred by the Crown relating to the acquisition and management of insured residential properties in Canterbury, with respect to the initial red zones announced on 23 June 2011 and the Kaiapoi red zones announced on 18 August 2011, with a corresponding impact on the operating balance:

	\$m-increase/(decrease)				
	2011/12	2012/13	2013/14	2014/15	2015/16 & Outyears
Vote Canterbury Earthquake Recovery Minister for Canterbury Earthquake Recovery					
Departmental Output Expense: Management of Voluntarily Acquired Insured Residential Red Zone Properties	\$2.491	-	-	-	-

- 9 **approved** the following changes to appropriations to provide for demolitions and related costs incurred by the Canterbury Earthquake Recovery Authority with third parties on behalf of the Crown, relating to the acquisition and management of insured residential properties in Canterbury, and with respect to the initial red zones announced on 23 June 2011 and the Kaiapoi red zones announced on 18 August 2011, with a corresponding impact on the operating balance:

	\$m-increase/(decrease)				
	2011/12	2012/13	2013/14	2014/15	2015/16 & Outyears
Vote Canterbury Earthquake Recovery Minister for Canterbury Earthquake Recovery					
Non-Departmental Output Expense: Canterbury Earthquake Property Demolitions and Related Costs and Compensation	\$44.061	-	-	-	-

- 10 **authorised** the Minister for Canterbury Earthquake Recovery and the Minister of Finance to jointly approve any variance to the appropriations by up to 10 per cent where the variation is due to differences compared with estimates of the proportion of houses requiring Crown-funded demolition, and/or the costs of third party providers of demolition and land remediation;
- 11 **noted** that if any variance in demolition or land remediation costs is higher than 10 per cent, further funds will need to be appropriated for the transactions associated with the acquisition and management of voluntarily acquired insured residential red zone properties;
- 12 **agreed** that the changes to appropriations be met from the Canterbury Earthquake Recovery Fund established as part of Budget 2011;
- 13 **agreed** that the proposed changes to appropriations for 2011/12 above be met in the 2011/12 Supplementary Estimates and that, in the interim, the increase be met from Imprest Supply;
- 14 **noted** that:
- 14.1 **Withheld under sections 9(2)(f)(iv) and 9(2)(g)(i) of the Official Information Act;**
 - 14.2 **Withheld under sections 9(2)(f)(iv) and 9(2)(g)(i) of the Official Information Act;**
 - 14.3 **Withheld under sections 9(2)(f)(iv) and 9(2)(g)(i) of the Official Information Act;**
- 15 **noted** that approval to increase these transaction-cost related appropriations will be sought as part of any future decision-making about re-zoning other white and orange zone areas to red, should this occur.

Secretary of the Cabinet

Reference: CAB (11) 516

Canterbury Earthquake: Voluntarily Acquired Insured Residential Red Zone Properties - Procurement Processes and Costs

Proposal

1. Funding of \$127.461 million is sought from Vote Canterbury Earthquake Recovery to progress the transactions around the acquisition and management of voluntarily acquired insured residential properties in the Canterbury red zone (initial red zone and recently re-zoned Kaiapoi properties only).

Executive Summary

2. A process is underway for the acquisition and management of voluntarily acquired insured residential red zone properties. It is estimated that approximately 5,500 insured homeowners from the initial red zones and the recently announced Kaiapoi red zones will take-up government's offer to purchase their properties. An acceptance of the offer to purchase will initiate complex processes with respect to settlement, insurance recovery, demolition, and de-commissioning of land. These are demonstrated in Appendix 1.
3. These processes are estimated to cost \$127.461 million in 2011/12, and this paper seeks approval to appropriate that amount. Table 2 provides a breakdown of these costs per property.
4. Future re-zoning decisions will take into account associated transaction costs at the time that re-zoning is considered, with approval for additional funding (including for transaction costs) sought at that those times.

Background

5. On 23 June, Cabinet approved the Canterbury Earthquake Recovery Authority (CERA) making an offer to buy the insured residential properties in the initial red zone: estimated at about 90 per cent of the 5,200 properties identified in the red zone at that time [CAB Min (11) 24/15 refers]. A further 940 Kaiapoi homeowners have now been re-zoned from orange to red (announced 18 August 2011), and will also receive offers of purchase [Cab Min (11) 30/18 refers]. Initial red zone homeowners received their letters of offer from government on 18 August 2011. The recently Red Zoned Kaiapoi homeowners will receive letters of offer from government from mid-September 2011.
6. In light of the strong interest in the red zone offers, take-up is expected to begin immediately.

Procurement Design

7. CERA has established a procurement process to give effect to Cabinet decisions to make a direct offer to red zone homeowners.¹ This includes making the offers; acquiring, managing, and demolishing the properties; and recovering insurance.

8.

Withheld under section 9(2)(f)(iv)

Withheld under section 9(2)(g)(i)

9. For these reasons, CERA devised a procurement plan for red zone properties to fit the tight timeframes and to respond to the objectives agreed by Cabinet of:

- a. **certainty** of outcome for home-owners as soon as practicable
- b. **confidence** for people to be able to move forward with their lives
- c. **confidence** in decision-making processes (for home-owners, business-owners, insurers, and investors)
- d. **utilising the best information** available to inform decisions
- e. **providing a simple process** in order to provide clarity and support for land-owners, residents, and businesses in those areas [CAB Min (11) 24/15 refers].

The Procurement Project

10. To effect the procurement of insured residential red zone properties, CERA has established a project with six workstreams as described below.

Table 1: Red Zone Procurement Project and Workstreams

Programme Management: programme definition; programme governance; schedule management; risk and issue management; progress reporting					
Residential Land & Property Acquisition	Insurance Recoveries	Acquired Land & Property Management	Communications	Community Engagement & Support	Infrastructure
Offer development. Dispute resolution. Offer conclusion. Conveyancing. Settlements. Data integrity.	Insurer negotiations – recovery and re-insurance processes. EQC negotiations.	Maintenance. Security. Salvage operations. Demolition.	Response management. Communication material. Media support.	Community engagement. Information hubs. Integrated communities. Community development	Council. Commercial. Public buildings. Roads. Utilities.

¹

Withheld under section 9(2)(f)(iv)

Withheld under section 9(2)(i)

Scope of this paper

11. This paper is concerned with the processes, and associated costs, relating to the acquisition and management of the insured residential red zone properties and to associated insurance recovery, encompassed in the first three procurement workstreams (Table 1 above refers). These are:

- a. residential land & property acquisition
- b. insurance recoveries
- c. acquired land and property management.

12. Approval is sought in this paper to appropriate the costs associated with these procurement processes for the initial red zone and recently announced Kaiapoi properties (only). Subsequent Cabinet papers that seek approval to acquire properties (that are re-zoned from Orange or White to Red) will also seek approval for the transaction costs associated with procurement for those properties.

Out of Scope for This Paper

13. This paper is not concerned with the monies paid to vendors for their properties or with the monies recovered from EQC/private insurers.

- An output has already been established for the monies associated with the cost of properties that are purchased by the Crown [Cab Min (11) 30/18 refers].
- Future papers to Cabinet will identify the costs of acquiring properties that are newly zoned red, and those costs will be appropriated to this output (this has occurred for the recently re-zoned Kaiapoi homeowners).
- There is also a process underway to appropriate the costs of acquiring the initial red zone properties; this could not be done at the time as it was too close to the end of the financial year.

14. Neither is this paper concerned with properties in the red zones other than the voluntary offers with respect to insured residential properties. This paper does not cover, for example, any subsequent purchases of commercial property, vacant private land, publicly owned land or utilities.

Withheld under section 9(2)(f)(iv)

Withheld under section 9(2)(g)(i)

15. This paper is also not concerned with the Crown's contributions towards vendor legal fees.

- An output has already been established for this purpose [Cab Min (11) 27/13 refers].
- Future Cabinet papers that seek approval to acquire properties that are newly zoned red will also seek approval to meet a proportion of vendor legal fees, and those costs will be appropriated to this output (this has occurred for the initial red zone homeowners and for the recently re-zoned Kaiapoi homeowners).

16

Withheld under section 9(2)(f)(iv)

Withheld under section 9(2)(g)(i)

17

Performance Measures for Procurement Processes

18

Withheld under section 9(2)(f)(iv)

Withheld under section 9(2)(g)(i)

19. A range of micro-performance indicators are already operational with respect to detailed processes (such as the proportion of help line calls answered and the proportion of issues resolved within defined timeframes).

Details of the Procurement Processes and their Costs

20. The key steps of the procurement process for individual properties across the three areas of (i) residential land and property acquisition; (ii) insurance recoveries; and (iii) acquired land and property management can be simplified and stylised as shown in Appendix 1.

21. Other than Crown's contribution to vendor legal fees, the cost of the other transactions shown in the flow chart in Appendix 1 have yet to be appropriated. As work is poised to begin on these processes, and third parties need to be contracted in some cases, there is some urgency around appropriating these funds. Key transactions and estimated per property costs associated with these are tabled below.

Table 2

Withheld under section 9(2)(f)(iv)

Withheld under section 9(2)(g)(i)

Withheld under section 9(2)(i)

22. There are 5,200 or so initial red zone properties of which, it is estimated, 4,680 are insured residential properties. With the 940 re-zoned insured residential Katapoi properties, there are approximately 5,620 properties currently or imminently receiving an offer from government. It is estimated that 98 per cent of these will take-up the Crown's offer to purchase: just over 5,500 properties in all.

23. Transaction costs in 2011/12 are estimated at a total of \$127.461 million

Withheld under section 9(2)(f)(iv)

Withheld under section 9(2)(g)(i)

Withheld under section 9(2)(i)

² Assuming 25% of property owners will seek a review and pay a fee of \$500; of which 50 per cent might be successful and be reimbursed. This amount is averaged, here, across all transactions.

24. The \$127.461 million comprises: \$2.491 million departmental; \$44.061 million non-departmental demolition; and \$80.910 million other non-departmental.
25. The proportion of houses that might require demolition, and some of the big ticket costs of third party providers (such as demolition and land remediation costs) are only estimates and are subject to variation: up to a 10 per cent variation in costs (plus or minus) may be a prudent estimate. If actual average per property costs associated with demolition and decommissioning of land are higher than a 10 per cent variation, further funds will need to be appropriated.
- **Average per property demolition quotes** relate to a 150 m² property including the removal of the main building, 30 m² of outbuildings, pathways, driveways, patios, fences, boundary walls, and letterboxes. Potential revenue from salvage is not included. The costs of salvaging materials may be higher than the benefits and so may not be progressed, but this is currently unknown. The per property costs of demolition will differ depending on whether a number of adjoining properties can be demolished at the same time (economies of scale) or if the demolition needs to be 'pepper-potted'. Pepper-potting may need to occur if insurance issues delay the finalisation of settlement on specific properties. If mass demolition is utilised in areas (reducing per property demolition costs) the option of salvage will reduce.
 - **Average costs associated with per property decommissioning of land** post-demolition include: capping of services and laterals, land flattening, vegetation clearance, and grassing. More details of post-demolition work are included in Appendix 1.

Consultation

26. The Treasury and Land Information New Zealand (LINZ) have been consulted in the drafting of this paper. The Department of Internal Affairs has seen this paper. The Department of the Prime Minister and Cabinet was informed.

Financial Implications

27. A non-departmental output expense for Canterbury earthquake property demolition already exists.
28. Appropriations currently do not exist and need to be established for the departmental and non-departmental transaction costs associated with government procurement of voluntarily acquired insured residential red zone properties.
29. All costs are appropriated in 2011/12 year under accrual accounting, as is standard practice. While some of the funds will be paid in the next financial year, the costs themselves will be incurred in 2011/12.
- 30.

Withheld under section 9(2)(f)(iv)

Withheld under section 9(2)(g)(i)

31

Withheld under section 9(2)(f)(iv)

32.

Withheld under section 9(2)(g)(i)

Human Rights

33. The proposals in this paper are not inconsistent with the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993.

Legislative Implications

34. There are no legislative implications arising from this paper.

Regulatory Impact Analysis

35. A regulatory impact statement is not required as there are no regulatory changes.

Gender Implications

36. There are no gender implications associated with the proposals in this paper.

Disability Perspective

37. There are no disability implications associated with the proposals in this paper.

Publicity

38. There are no implications for publicity associated from the proposals in this paper.

Recommendations

I recommend that the Committee:

1. note that transaction costs need to be appropriated in order to progress the acquisition and management of insured residential Red Zone properties;
2. agree to establish a new Non-Departmental Other Expense appropriation "Management of Voluntarily Acquired Insured Residential Red Zone Properties";
3. agree that the scope of this appropriation be "this appropriation is limited to expenses related to third party providers involved in transactions associated with the Crown's acquisition of voluntarily acquired insured residential red zone properties in Canterbury";
4. approve the following changes to appropriations to provide for transaction costs incurred by the Canterbury Earthquake Recovery Authority with third parties on behalf of the Crown, relating to the acquisition and management of insured residential properties in Canterbury, with respect to the initial Red Zones announced on 23 June 2011 and the Kalapoi Red Zones announced on 18 August 2011, with a corresponding impact on the operating balance;

Vote Canterbury Earthquake Recovery Minister for Canterbury Earthquake Recovery	\$m – increase/(decrease)				
	2011/12	2012/13	2013/14	2014/15	2015/16 & Outyears
Non-Departmental Other Expense; Management of Voluntarily Acquired Insured Residential Red Zone Properties	\$80.910	-	-	-	-

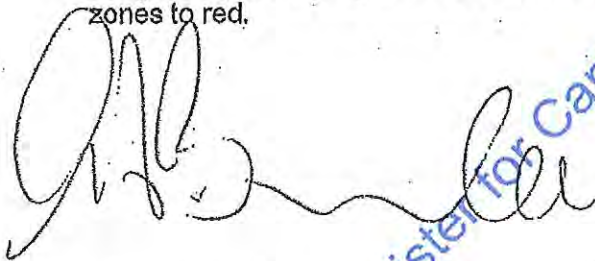
5. agree to establish a new Departmental Other Expense appropriation "Management of Voluntarily Acquired Insured Residential Red Zone Properties";
6. agree that the scope of this appropriation be "this appropriation is limited to Crown expenses incurred through the transactions associated with the Crown's acquisition and management of voluntarily acquired insured residential Red Zone properties in Canterbury";
7. approve the following changes to appropriations to provide for transaction costs incurred by the Crown relating to the acquisition and management of insured residential properties in Canterbury, with respect to the initial Red Zones announced on 23 June 2011 and the Kaiapoi Red Zones announced on 18 August 2011, with a corresponding impact on the operating balance;

Vote Canterbury Earthquake Recovery Minister for Canterbury Earthquake Recovery	\$m – increase/(decrease)				
	2011/12	2012/13	2013/14	2014/15	2015/16 & Outyears
Departmental Other Expense; Management of Voluntarily Acquired Insured Residential Red Zone Properties	\$2.491	-	-	-	-

8. approve the following changes to appropriations to provide for demolitions and related costs incurred by the Canterbury Earthquake Recovery Authority with third parties on behalf of the Crown, relating to the acquisition and management of insured residential properties in Canterbury, and with respect to the initial Red Zones announced on 23 June 2011 and the Kaiapoi Red Zones announced on 18 August 2011, with a corresponding impact on the operating balance;

Vote Canterbury Earthquake Recovery Minister for Canterbury Earthquake Recovery	\$m – increase/(decrease)				
	2011/12	2012/13	2013/14	2014/15	2015/16 & Outyears
Non-Departmental Other Expense; Canterbury Earthquake Property Demolitions and Related Costs and Expenses	\$44.061	-	-	-	-

9. agree that the Minister for Canterbury Earthquake Recovery and the Minister of Finance can jointly approve any variance to the appropriations by up to 10 per cent where the variation is due to differences compared with estimates of the proportion of houses requiring Crown-funded demolition, and/or the costs of third party providers of demolition and land remediation
10. note that if any variance in demolition or land remediation costs is higher than 10 per cent, further funds will need to be appropriated for the transactions associated with the acquisition and management of voluntarily acquired insured residential red zone properties
11. agree that the changes to appropriations be met from the Canterbury Earthquake Recovery Fund established as part of Budget 2011
12. agree that the proposed changes to appropriations for 2011/12 above be met in the 2011/12 Supplementary Estimates and that, in the interim, the increase be met from Imprest Supply
13. note that when the Canterbury Earthquake Recovery Fund was established, an allocation for decisions relating to land damage was developed; there is around \$280 million still remaining within this allocation; and these decisions will reduce this allocation by \$128 million, leaving approximately \$152 million for other land damage decisions
14. note that approval to increase these transaction-cost related appropriations will be sought as part of any future decision-making about re-zoning other white and orange zones to red.



Hon Gerry Brownlee
Minister for Canterbury Earthquake Recovery

02/09/2011

Flow chart of procurement process for individual properties

Property and policy holder consent and data verification		Development and maintenance of settlements database. Web-based tool with secure log on. Preloaded with data from LINZ, Property IQ, rating database etc	
Letter of offer to insured residential red zone property owner (the vendor)			
Vendor engages solicitor and solicitor registers into database for the vendor's property			
Information validated; any concerns investigated and addressed			
Offer option selected			
Option 1	Option 2		
Through database, vendors interested in salvage can register			
Offer challenges/discrepancies reviewed and addressed; may involve a revised valuation			
Insurance validation fed in from database			
Any insurance concerns investigated and addressed			
Vendor's solicitor completes schedule of payments			
Insurer and EQC accept payment schedule			
If property underinsured by more than 20%, adjust purchase price and advise solicitor			
Solicitor completes offer; vendor signs agreement; preferred settlement date booked through database; completed paper work returned. Vendor's solicitor obtains mortgagee's consent to sake (if applicable)			
Any paper work needing correction returned to vendor's solicitor; finalised documentation			
Crown accepts offer and executes sale and purchase agreement			
To Crown solicitor and vendor's solicitor for settlement			Reports
Insurance/EQC recoveries	Demolition		
Reconcile Insurance data with settlement data; any adjustments made	CERA demo team pre-settlement inspection/ scoping of works/ property inspection report; itemised risks, issues, tasks for each property etc		
Settlement			

(Continued: flowchart of procurement process for individual properties)

Insurance recoveries	Demolition	
Development and management of a documents management system	Tendering process/engage demolition provider(s)	Updating of settlements database
Initial information-gathering on losses, claims and policies	Pre-demolition tasks: security; signage; health and safety/risk mitigation; rubbish and dangerous goods removal; termination of services; rates payments; property maintenance; enquiries (0800 number); facilitating access for authorised people; dealing with easement issues; etc	
Retaining and appointing assessment, professional valuation, and advisory services	Property demolition	
Engagement with insurers and EQC, and agreement on demolition and other time-critical issues. Due diligence of insurer and EQC assessment and claim valuation methodologies and processes	Infrastructure removal	
Long-term engagement with insurers and EQC on recoveries with definite resolution and settlements, as required	Post-demolition tasks; inspection; rates payments; land/section maintenance; vegetation clearance; pest and weed control; property information management; street stopping; grassing; liaison with Councils etc	
	Clearance of infrastructure	

Released by the Minister of Natural Resources and Environmental Conservation
 Ministry of Natural Resources and Environmental Conservation
 Earthquake Recovery