

Aide-Memoire: Lincoln University Programme Business Case: Moving Forward

To:	Hon Chris Hipkins, Minister of Education
From:	Gillian Dudgeon, Deputy Chief Executive
Date:	1 July 2019
Reference:	AM-19-00827

Purpose

1. This note updates you on Lincoln University's (Lincoln's) Programme Business Case for its campus redevelopment programme. Lincoln is intending to submit a draft of the business case to you in the next month. This will help inform Ministerial decisions on the \$85 million which has been set aside to contribute to the rebuild of Lincoln's science facilities.
2. We recommend that you proactively release this aide-memoire following any decisions on Lincoln's Programme Business Case, with financial and costing information withheld given it may impact on any future procurement processes undertaken by Lincoln.

Background

3. Following the 2010 and 2011 Canterbury earthquakes, the previous government decided to provide financial support to the three Canterbury-based tertiary education institutes (TEIs) to help them re-build and upgrade their campuses. It was expected that each institution would use its own cash reserves and any insurance settlements towards the rebuilding, and that Crown funding would supplement this. The following support was provided:
 - University of Canterbury (UC) received \$260 million to build new science facilities and upgrade its engineering facilities. This series of major projects is almost complete, with the final stage of the new science facilities expected to be completed later this year.
 - Ara Institute of Technology (then Christchurch Polytechnic Institute of Technology) received \$19 million to upgrade and expand its trades training facilities.
 - Funding was set aside to help Lincoln rebuild its science facilities with \$7.5 million paid in 2014. A further \$85 million remains set aside for this purpose, linked to a joint development with AgResearch which also had to replace its earthquake damaged facilities at Lincoln.
4. The development at Lincoln has been a long, slow process, with many delays during the design and business case development process. In late 2018, an incomplete Implementation Business Case (IBC) was submitted to you and the Minister of Finance for approval and seeking the release of the \$85 million of Crown funding. However, the costs of the building project had increased substantially from what was originally planned and as a result, there was considerable concern about the affordability of the build programme for Lincoln and the associated risks to the Crown.

5. On 6 December 2018, you wrote to Lincoln and AgResearch informing them you were deferring making a final decision on the IBC and gave them until March 2019 to resolve the outstanding issues. Following your decision, AgResearch decided to construct its own facilities at Lincoln. This would allow AgResearch to progress with the initial precinct developments and Lincoln to follow once it had resolved its funding issues and re-scoped the project to ensure that it was affordable.
6. We recently briefed you on Lincoln's 2018 financial results (AM-19-00611 refers). This included updating you on Lincoln's \$45 million insurance settlement and its approach on campus redevelopment following the Joint Facility project no longer going ahead.
7. As part of the Budget 2019 technical initiatives package, the \$85 million in Crown funding to rebuild Lincoln's science facilities was transferred into 2019/20 and outyears (CAB-19-MIN-0088.13 refers). As part of this decision, you are required to report back to Cabinet later in 2019 on Lincoln's revised development plans for the rebuild of science facilities and new arrangements for Crown funding.
8. The Programme Business Case you are about to receive will enable you to reconsider the terms and conditions of the Crown's \$85 million contribution towards the rebuild of Lincoln's science facilities as set out in the 2017 Cabinet decision (CAB-17-MIN-0312.01 refers) and the Crown funding agreement with Lincoln. Many of the decisions and terms of Crown funding are no longer applicable or relevant given the change in project timings and construction plans.

AgResearch build plans

AgResearch is close to making a decision on building on the Lincoln University site

9. Over the past six months, AgResearch has been designing facilities and developing a business case for its development. The AgResearch Board will soon consider a business case on its build options. We understand that it will propose new, modern science facilities and corporate offices. It will also include facilities that will be leased to other tenants – in particular, Dairy NZ, as per the original Joint Facility proposal – but also the possibility for other partners to lease space in the building.
10. While AgResearch is considering a number of possible sites in the Lincoln Township, we understand that its preferred option is on the Lincoln University site **S 9(2)(j)**
[REDACTED]

Lincoln has agreed in-principle to sell the land to AgResearch **S 9(2)(j)**

11. Lincoln has been negotiating a sale and purchase agreement with AgResearch over the past few months, which proposes that Lincoln sub-divides the land and sells it to AgResearch **S 9(2)(j)** (Appendix Two shows the proposed piece of land to be sold). While a sale **S 9(2)(j)** would obviously be below market value, there are considerable advantages for Lincoln in having AgResearch on its site. In particular:
 - it allows specialist facilities and equipment to be shared (e.g. dangerous goods stores);
 - it will promote collaboration between staff of both organisations;
 - being closely associated with a research institution will boost Lincoln's reputation and attractiveness for staff, students and industry partners;
 - AgResearch is likely to start building before Lincoln so it will demonstrate progress on the wider redevelopment of the site, following the earthquakes and the drawn-out process so far; and
 - it provides a good basis for the proposed establishment of a joint post-graduate school with UC as post-graduate students and potential supervisors from AgResearch will be in close proximity.

12. S 9(2)(i)

13. AgResearch is designing its facilities so that they can be built alongside Lincoln's main new science facilities to encourage greater collaboration. Both the AgResearch development and Lincoln's own developments are being planned in line with an overall campus masterplan.

There does not appear to be any regulatory barriers to this proposal

14. The sale of the land does not meet the threshold which requires the Secretary for Education's consent. Even if the land was sold at full market price, its sale would not meet this threshold. Under s195 (4) of the Education Act 1989, the threshold for Lincoln would be \$15 million as it has a group equity value of over \$250 million. There is no impact on the Crown's balance sheet as the land will be owned by AgResearch and be on its balance sheet.

15. Both Lincoln and AgResearch have discussed this proposal with Ngāi Tahu as part of the ongoing working relationship both parties have with them. Lincoln has also discussed the proposal with the Selwyn District Council as a subdivision of the land is needed. We understand that the Council is supportive, but have raised the need for more car parking to cope with the additional number of people on the site. Lincoln and AgResearch have plans to address this matter. We expect these matters will be formally covered in Lincoln's Programme Business Case.

AgResearch has briefed the Minister for Research, Science and Innovation

16. The Ministry of Business, Innovation and Employment (MBIE) has informed us that Minister Woods has been briefed on this proposal and will be considering AgResearch's business case once it has been signed off by its Board. We understand that the final business case will be sent to Minister Woods in July.

AgResearch may still want some surety as to the future of Lincoln

17. AgResearch appears to have some remaining concerns about the future of Lincoln given its past relationship, the financial difficulties that Lincoln has faced, and the discussions with UC. In particular, before committing around \$100 million of capital expenditure it wants to be certain that research and teaching will continue at the Lincoln site. However, given Lincoln's much improved financial position and progress on developing its own campus redevelopment programme, this may now be less of an issue. AgResearch may seek a letter of comfort from you if, following discussions, this remains an issue for them.

Lincoln University: Moving Forward

Greater financial certainty enables Lincoln to plan with more confidence

18. The final insurance settlement gives Lincoln much more certainty about the resources it has to spend on its capital development programme. As at May 2019, Lincoln had \$79 million of cash on hand. Financial forecasts show an ongoing operating surplus over the next ten years.

19. Lincoln has also advanced its asset sales programme focussing on surplus housing close to the campus and on the two farms previously identified. While this is likely to result in a smaller amount than the original S 9(2)(ba)(i) proposed, there is greater certainty about the ability to realise these asset sales. Around S 9(2)(ba)(i) is expected to be realised by the end of 2019.

20. Together with certainty about AgResearch's proposals, this gives Lincoln a good basis to refine its own development plans.

Lincoln is planning a phased approach to its campus re-development

21. Rather than one large building, Lincoln is now looking at a smaller staged set of developments. This will allow Lincoln to fit in with AgResearch's development, to manage decanting and demolition of the Burns building, and to address seismic issues across a number of buildings on the campus. With the programme being broken down into stages, the projects are also more manageable and the phasing can be modified if financial, timing or other pressures arise. However, it is still a large programme of work totalling around \$206 million in capital works.

22. Appendix Two provides an overview of the proposed development plans. However, the overall programme is comprised of the following:

- **Building new science facilities** which are fit for modern research, teaching and learning at an estimated cost of **§ 9(2)(j)**. This includes a small new facility using the same approach as the RfH building constructed immediately after the 2010/11 earthquakes (a simple warehouse type space with a sophisticated internal fit out) called Science South; the upgrade of the Johnson Memorial Laboratories (for large animal research); new glasshouses for research purposes; and a series of new science buildings adjacent to the new AgResearch development. It should be noted that while there is a level of certainty about the costs of the smaller projects, the cost of the new main science buildings may still change. Planning work is already well underway on the Science South project with the aim of having this facility completed by the end of 2020.
- **Replacing or upgrading student support facilities** including the library, gym, and student union facilities at an estimated cost of **§ 9(2)(j)**. Planning is well underway for the upgraded sport and recreation centre, which will provide facilities for the sport and recreation courses and the High-Performance Sport Centres. It will also provide much needed facilities for students on campus. New student accommodation and upgrading existing facilities is in addition to this cost, but is expected to be financed through commercial partnerships – starting with a post-graduate housing development.
- **Repairing earthquake damage** of essential facilities at an estimated cost of **§ 9(2)(j)**.
- **Demolition of the Burns Building** which was substantially damaged in the earthquakes at an estimated cost of **§ 9(2)(j)**. Analysis undertaken in 2014/15 showed that it would cost more to repair and upgrade the building than it would to build a new one. Even if it was upgraded, it would still not meet the requirements for modern teaching and learning given the way it is built. Furthermore, there would be major business continuity problems with upgrading it as there are no decanting facilities available to use.

23. The current proposed programme is in addition to a range of projects that have been completed since the earthquakes:

- Temporary science facilities and redevelopment – RfH, Riddols, demolition of the Hilgendorf building and site preparation (at a cost of **§ 9(2)(j)**);
- Student support – new dining hall/conference facilities and a student hub in the Forbes building which opened in 2019 (at a cost of **§ 9(2)(j)**).

Lincoln's proposed programme also involves new ways of working

24. The programme is wider than just a build programme, and involves modernising research, teaching and learning as envisaged by the 2017 Transformation Board report. Around \$25 million in operational funding has been earmarked to implement these "new ways of operating". These aspects of the programme involve:

- **Expanding the multi-disciplinary Centres of Excellence** – this work is underway with three centres already established (Designing Future Productive Landscapes; Foods for Future Consumers; and Sustainable Tourism for Regions, Landscapes and Communities). Lincoln has invested in expanding the capacity and research programmes as part of the Centres of Excellence.

- **Blended and online learning** – this will not only modernise current programmes, but allow new programmes to be developed and delivered on a modular basis to attract other students unable to study full-time.
- **New land-based post-graduate school** – this will involve AgResearch, UC and other Crown Research Institutes (CRIs).
- **Expanding partnerships** – this includes with AgResearch, continued support for Blinc Innovation (formerly the Lincoln Hub), Ngāi Tahu, the Children’s University with UC, and further partnerships with other universities and CRIs.

The programme benefits both Lincoln and the land-based sector

25. Lincoln has designed the programme to capture as many of the benefits associated with the Joint Facility as possible. The programme is expected to deliver the following benefits for New Zealand as a whole, particularly the land-based sector:

- greater return on research and development through collaboration and improving connections with industry;
- an increase in the number of land-based sector graduates; and
- improving the global competitiveness of the land-based sector.

26. The direct benefits sought for Lincoln and its partners are:

- increased consumer confidence in Lincoln;
- improved ability for Lincoln to attract and grow talent – both staff and students;
- greater collaboration to produce better outcomes than Lincoln could as a standalone university; and
- improved financial outcomes.

The capital programme delivery function at Lincoln has been strengthened

27. Lincoln has previously had little in the way of expertise and capability in capital projects. Even during the Joint Facility project, most of the expertise was held in the joint venture itself, rather than at Lincoln. A new Programme Manager has been appointed who brings considerable development experience, and the capability needs and processes have been reviewed. This is essential in managing a large capital redevelopment programme.

28. Programme and project governance structures have also been set up. These involve a Council sub-committee and senior management programme sponsorship, while appropriate Project Control Groups are to be established. There is an opportunity to increase Council skills and expertise in this area through upcoming appointments.

The programme is affordable but still requires a government contribution

29. The financial modelling undertaken by Lincoln includes a government contribution of \$85 million, as part of the \$307 million capital programme – which is comprised of around \$206 million in capital developments and a further \$100 million on business as usual capital expenditure (e.g. library, IT, equipment, maintenance).

30. Early indications are that the programme would still be affordable with a lower Crown contribution. However, further analysis and more detailed financial modelling will need to be completed before we can draw any definitive conclusions. We will be able to undertake this work when the Programme Business Case is received. However, a careful balance is needed between not providing too much Crown support to Lincoln if it can afford to fund more of the development itself, versus putting too much pressure on Lincoln’s financial position given that there are risks associated with any development of this scale.

31. The 2017 Cabinet decision contained a clause that any insurance proceeds related to building damage over \$20 million were to be offset against the Crown contribution. As previously noted, Lincoln has signalled that it wishes to re-consider those arrangements. The recently received final insurance settlement of \$45 million was comprised of settlements related to building damage, business continuity insurance, and claim preparation costs. However, because it is a global settlement, it is technically not possible to separate out the amounts relating to building damage for the purpose of determining what may be owed to the Crown. However, we estimate that the amount due to the Crown would be in the region of **§ 9(2)(ba)(i)** [REDACTED]
32. The financing of the programme is no longer highly reliant on major EFTS growth as it was with the Joint Facility. Growth is still expected, but there are greater margins in the financial model to manage the risk of lower than expected growth. Overall, EFTS are expected to increase from **§ 9(2)(b)(ii)** [REDACTED] – which equates to growth of around **§ 9(2)(b)(ii)** [REDACTED].
33. International EFTS are expected to grow by **§ 9(2)(b)(ii)** [REDACTED] over the forecast period, which seems realistic given current trends. Domestic EFTS are expected to **§ 9(2)(b)(ii)** [REDACTED] when a substantial amount of the new campus development has been completed. In line with recent trends, and due to the post-graduate school and the collaborations with AgResearch and UC, post-graduate EFTS are expected to increase faster than undergraduate EFTS.
34. While the enrolment forecasts are more sensible than those submitted as part of the Joint Facility IBC, it is still a substantial rate of increase, particularly for domestic EFTS. We will provide more detailed analysis on the enrolment forecasts once Lincoln has fully developed its sensitivity analysis and finalised its full financial models.

The risks of this programme are substantially less than under the Joint Facility project

35. There were significant risks associated with the Joint Facility project, particularly financial risks as the cost of the project grew and funding sources were uncertain. The scope and design of this programme has reduced those risks. The table below highlights the main risks associated with the Joint Facility project and how these have been mitigated in this programme.

Risk	Comment	Change in risk profile
Funding certainty	<ul style="list-style-type: none"> Insurance settlement now secured; borrowings no longer required. Still requires a programme of asset sales, but this is now more tangible and achievable. 	↓
Affordability	<ul style="list-style-type: none"> No longer reliant on significant increases in EFTS. Sensitivity analysis suggests that there is significantly less funding pressure and an ability to manage financial shocks. 	↓
Cost escalation	<ul style="list-style-type: none"> Risk of cost escalation remains, but because projects are staged there are more opportunities to re-plan or scale the project if required. However, only limited work has been done on the design of the main new science building – how it is designed and procured will impact on risk. 	↓
Capability	<ul style="list-style-type: none"> Internal capability has been strengthened through new processes and staff capability. This could be further supplemented by appointment of independent experts e.g. a chair of the Project Control Group. However, as an organisation experience in these sorts of major projects is still lacking. The latest (May 2019) independent review of Lincoln’s capital asset management processes indicated an improvement. 	↓
Timeliness	<ul style="list-style-type: none"> While Lincoln still wants to “get on with it” there is reduced time pressure and more sensible timeframes. Small early projects have been identified – so there will be progress more rapidly, while time is taken on the major build projects. 	↓

Fit with UC partnership proposal

36. The programme builds on some of the practical suggestions for collaboration which featured in the UC and Lincoln partnership proposal submitted to you in December 2018. This includes increasing collaborative research work, joint programmes, and the land-based post graduate-school. There are new joint initiatives which have already commenced e.g. the Children's University and the development of a new joint taught Masters Programme.

Next steps

37. We have been working closely with Lincoln on the development of its Programme Business Case. Lincoln's Council is expecting to endorse a final draft of the business case at its meeting this week and submit it to you. Following its submission, we will prepare formal advice for you, in conjunction with other officials, for your decision.

38. As noted earlier, when the \$85 million in Crown support was carried over as part of the Budget 2019 technical initiatives package, it required you to go back to Cabinet for decisions on the amount, the funding profile, and the terms and conditions of funding. Furthermore, the 2017 Cabinet decisions (taken by the previous Government) tagged the funding to the Joint Facility and thus will need to be rescinded. We will prepare a Cabinet paper for you on this matter should you wish to proceed.

39. Given the changes in the scope and nature of the project, we will need to make changes to the Crown funding agreement with Lincoln. Our assessment is that these are significant drafting changes, so it would be simpler if a new funding agreement was developed. However, similar principles would underpin the agreement.

40. A proposed timeline is outlined below:

- Lincoln's Programme Business Case is submitted – early July
- Analysis of the case by officials, including financial modelling – completed by late July
- Formal advice to you on the Programme Business Case – early to mid-August
- Cabinet decisions – late August/early September
- Crown funding agreement updated and agreed – end of September

41. As noted earlier, Lincoln is already making good progress on some aspects of the development including Science South which is expected to be completed at the end of 2020, the new Sport and Recreation Centre, and its "new ways of operating" projects.

42. The next major milestone for the science redevelopment element of the programme would be a Single Stage Business Case for the main new science buildings in early 2020. Following that, Lincoln would go to market for construction of these buildings. This would mean construction could commence in early 2021 with a view to completion of the first phases for the 2023 academic year.

Consultation

43. We have consulted with the Treasury and the Ministry of Education on this paper.

44. Officials from the Treasury, the Ministry for Primary Industries and MBIE attended a briefing from Lincoln on its revised programme. The slides from this briefing were made available to the Department of Prime Minister and Cabinet and the Ministry of Education who were unable to attend.

45. You may wish to forward this note on to the Minister of Finance and the Minister for Research, Science and Innovation for their information.



Gillian Dudgeon

Deputy Chief Executive
Tertiary Education Commission

1 July 2019

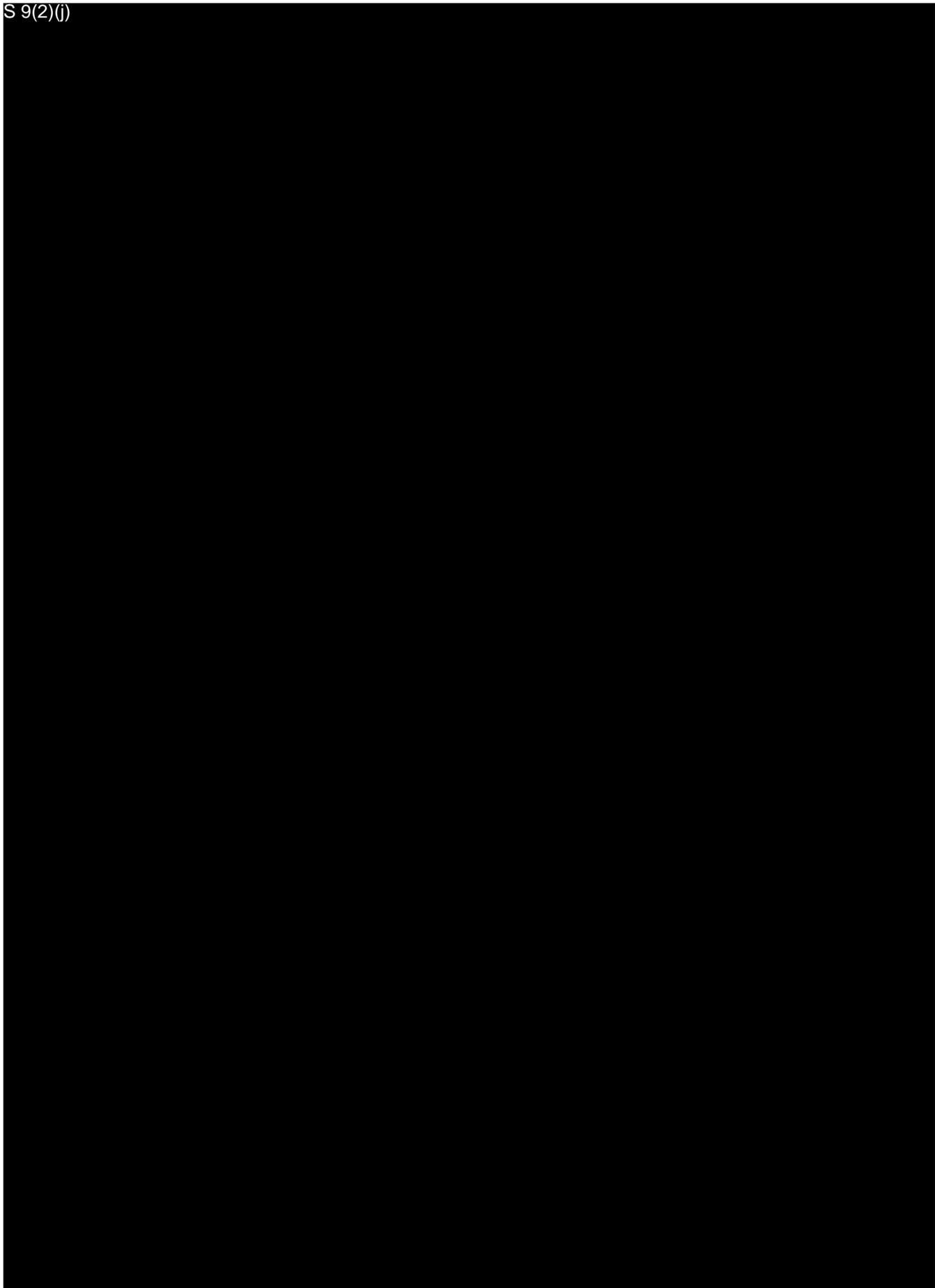
Hon Chris Hipkins

Minister of Education

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Appendix One: Proposed piece of land to be sold to AgResearch

S 9(2)(f)



Appendix Two: Draft Programme Plan – Capital projects

S 9(2)(ba)(i)

