

Housing New Zealand Corporation Board Investment Committee

14 March 2016

McLean Flats Redevelopment Project

Acting General Manager Asset Development

Executive Summary

1. This business case seeks Investment Committee support of the recommendation to Board for approval of the proposed McLean Flats Redevelopment project at 314 The Terrace, Wellington, involving the redevelopment and refurbishment of 34 new units inclusive of seven car parks.

Recommendations

2. It is recommended that the Housing New Zealand Investment Committee:

- a) **note** [REDACTED] 9(2)(i)
- b) **note** approval of this business case is subject to negotiation of a suitable build contract with the preferred supplier.
- c) **note** the proposed redevelopment will increase rental income potential from a potential of \$0 to \$703k per annum, which despite it being over the Ministry of Social Developments (MSDs) maximum rental threshold, MSD have confirmed they will match due to location, demand and typology.
- d) **note** [REDACTED] 9(2)(i)
- e) **recommend** the redevelopment and refurbishment of 34 new one bed units inclusive of seven car parks with no community room, replacing 16 existing vacant units at 314 The Terrace, Wellington be presented to the Board for approval.
- f) **recommend** the total investment of \$11,881k for the McLean redevelopment which includes the construction cost of \$10,771k and the value of existing land and assets, being \$1,110k (all figures adjusted for inflation), noting there is no write-down of existing assets be presented to the Board for approval.
- g) **note** the project will be funded by the redevelopment budget which forms part of the existing FY15/16, FY16/17 and FY 17/18 Budget and aligns with the unit development costs contained in this budget.

- h) **note** that the People and Property group support the development proposal.
- i) **note** the McLean Flats redevelopment is consistent with the Asset Management Strategy, Wellington Community Action Plan and Wellington Reconfiguration Strategy.

Background

3. On 17 July 2013, the Asset Investment Committee, now Investment Committee endorsed:
 - the proposed retention and refurbishment of the McLean Flats,
 - consideration of developing new terraced units on the McLean site – so that the property returns up to a circa 40 units.
4. In October 2011, the McLean Flats were vacated following a seismic and strength assessment rating. Durability testing carried out also estimated the life span of the building providing refurbishment is completed at 50 years.
5. On the 29 August 2013, the then Asset Development Manager presented to the Board noting that the McLean Flats were below HNZC's standards and required major upgrade, including seismic and structural repairs.
6. At the same meeting, the Board directed management to advance discussions with Victoria University Wellington to sell the combined McLean and Gordon Wilson site, with appropriate easements and access to allow Housing New Zealand to subdivide off and retain the McLean Flats and the site area required for the proposed terrace-houses – noting the Right of First Refusal (RFR) would apply. Management was also asked to provide an outline of the wider Wellington Demand and supply view which would supports the retention of stock in the Wellington region and investigate the best economic option(s) for the Mclean flats building – refurbish, demolish and rebuild in compliance with current planning rules. For referencing purposes the update as provided to the Housing New Zealand Board, 29 August 2013 is provided in the Diligent Resource Centre.
7. In early 2014, Housing New Zealand went to market for Design Build proposals to deliver predominantly 2 bedroom units on key redevelopment sites in Wellington city. A subsequent review of these proposals identified a need for the business to gain a greater understanding of the Wellington city portfolio and the role, in particular, of the central city redevelopment opportunities in supporting improved housing outcomes and portfolio decisions across the city.
8. As a result, a cross-organizational project team from the Asset Development, Property Services and Tenancy Services (now People and Property) groups was established to provide analysis of the our tenants, portfolio and redevelopment opportunities, which would later inform the development of the Wellington Reconfiguration Strategy. Analysis for the strategy identified that there was strong internal and external demand for one bedroom properties throughout the central Wellington area which had the potential to house tenants, particularly requiring access to key social and support services and amenities located within the central area. This paper was presented and approved by the Board in July 2015.

9. The proposed development brief seeks to implement the Wellington Reconfiguration Strategy by providing additional one bedroom supply within the city. The delivery of one bedroom supply in this location enables better tenant outcomes by facilitating ease of access to services and amenities which may assist tenants to maintain their tenancies. In turn, this redevelopment provides Housing New Zealand with the opportunity to increase capacity to consider reconfiguration options that enable the organization to rebalance the portfolio and allow for tactical divestment and investment to improve the overall age and quality of assets.
10. Furthermore, current Ministry of Social Development (MSD) Purchasing Intentions to 2018 outline a need for additional one bedroom units within Wellington above all other bedroom configurations. This development brief would assist in meeting this future demand.

Appendices

11. There is one appendix to this paper:

Appendix 1: Business Case – McLean Flats, Wellington



Patrick Dougherty
Acting General Manager Asset Development



Glen Sowry
Chief Executive Officer

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Housing New Zealand

Business Case – McLean Flats Development, The Terrace, Wellington


Prepared by:	Andrew Showler
Prepared for:	Housing New Zealand Chief Executive
Date:	2 February 2016
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BC Number	

Compulsory sign-offs

Role	Name	Sign-off Date
Chief Executive	Glen Sowry	8 March 2016
Chief Financial Officer	Rose Anne McLeod	21 January 2016
Acting GM Asset Development	Patrick Dougherty	12 February 2016
Regional Manager Tenancy Services	Jackie Pivac	26 January 2016
Associate General Counsel	John Beech	24 November 2015
	Grace Chan	5 February 2016
Manager Procurement	Andrea Morton	9 February 2016
Manager Development Management	Andrew Showler	21 January 2016

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Executive Summary

1. This paper seeks approval of the Wellington redevelopment project being McLean Flats at 314 The Terrace, Wellington.
2. This project proposal seeks to deliver 34 one bed units to meet the demand requirements of the Business in terms of the Asset Management Strategy (AMS), Wellington Reconfiguration Strategy as well as Ministry for Social Development's purchasing strategy and thereby contributes to the provision in reducing the shortage of one bed unit and accommodation in Wellington.
3. The McLean Flats project entails:
 - redevelopment of an existing building and one new building on 1,492 m² rectangular, sloping Housing New Zealand owned site
 - construction of 34 one bedroom units, of which 20 are located in or additional to the existing refurbished building and 14 in the new two-story new fit for purpose units in blocks of four units 100 percent retention by Housing New Zealand
 - project approval prior to negotiating the construction contract.
4. The McLean Flat project provides Housing New Zealand with an opportunity to:
 - limit redevelopment costs by:
 - completing design, specification and resource consenting in-house, prior to contracting
 - retaining the development site during and after the build – avoiding lengthy, complex and costly negotiations and transactions involving land and/or third party sales
 -  9(2)(i)
 - achieve a redevelopment ratio of 1:2 by building 18 new one bed units and refurbishing 16 existing units and building in earthquake prone building .
 - add value to the portfolio – the redeveloped site CMV will be \$11,665k against the existing site CMV of \$1,110k.
 - increase rental income from the portfolio – potential annual rental income from the redeveloped site is \$703k against potential rental income from the existing site configuration of \$0 due to the building being earthquake prone.
 - contribute to the objectives, goals and targets of the AMS, MSD purchasing strategy and Housing New Zealand Wellington Reconfiguration strategy – by providing:
 - housing typologies that match current and forecast demand
 - continued portfolio distribution balancing across Wellington
5. Tenancy Services and Property Services are supportive of this development (Attachment G).
6. Tax risks are low (Attachment I) and Legal risks are low.
7. Financial analysis is at Attachment F.

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8. The project will be funded by the redevelopment budget which forms part of the existing FY15/16, FY16/17 and FY 17/18 Budget and aligns with the unit development costs contained in this budget.

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Business context

Strategic fit

9. In mid-2014, a cross-organizational working group with members from the Asset Development, Tenancy Services and Property Services groups developed the Wellington Reconfiguration Strategy (note this can be made available on request). Wellington City had one of Housing New Zealand's oldest portfolios, which in recent years had resulted in a number of buildings being identified as having significant issues, due to water tightness issues and earthquake prone buildings in the main, leading to a high number of vacant state housing units in Wellington. Along with this, very little redevelopment or divestment had been undertaken in the city. These factors were the main considerations in developing the Reconfiguration Strategy.
10. Through the strategy, Housing New Zealand sought to maintain or slightly increase its portfolio in Wellington City, whilst reconfiguring its assets to improve land utilization, replace aging assets, and obtain a better match to demand. In particular, it was identified that there was need to increase the number of smaller homes, specially one bedroom properties.
11. Overall, the reconfiguration of the Wellington City portfolio would involve divestment, redevelopment and refurbishment, with a focus on replacing current vacant properties with warm, dry, safe homes that match tenant needs.
12. Within the Reconfiguration Strategy, the McLean site is identified as a key development opportunity. The existing building on site is deemed earthquake prone and is currently vacant. The strategy proposed that this site had the potential to provide one bedroom units for high needs tenants due to the site's proximity to social services.

Demand

13. The Ministry of Social Development (MSD) has released purchasing intentions for Wellington out to 2018 signaling their requirements for an additional 70 one bedroom units over the next three years to meet demand. The MSD state that whilst they may purchase above lower quartile rents in order to achieve a suitable outcome for the applicants, MSD will not purchase over the indicative upper limits for weekly market rents determined based on median market rents across the country. In Wellington, these limits are outlined below.

Table 1 Rental limits

Bedrooms	MSD p/w Rental Limits	McLean Flat Market Rental Appraisal p/w
1	\$350	\$385-410
2	\$450	\$460
3	\$550	\$580
4	\$650	-

14. Over the long-term, the Wellington Community Action Plan (CAP) outlines that there will be a need to reduce the portfolio size by 145 homes by 2024, predominantly in the 3 bedroom typology. Across the Wellington CAP, Housing New Zealand's ability to

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house applicants needing one bedroom properties within our current portfolio configuration sits at 49 percent. This indicates that there is a need to provide additional one bedroom units within the portfolio to meet the needs of future applicants. This will require Housing New Zealand to consider how the portfolio is reconfigured to balance out the forecasted reductions in demand coupled with a need to increase one bedroom supply.

15. Within Wellington there are two main social housing providers, Wellington City Council, which has approximately 2200 units, and Housing New Zealand with 1648 properties. Across Wellington city, Housing New Zealand's share equates to 3 percent of all housing across the city, and 7.6 percent of the residential rental market.
16. The McLean site is located within the Wellington Lambton Precinct. Analysis of this precinct demonstrates that there is a high level of underutilization occurring within the portfolio, particularly with regard to the number of tenants currently housed in two bedroom properties who only require a one bedroom unit. Within the precinct, three-quarters of all tenants live in one-person households. While there may be instances of single occupants requiring two bedroom units due to their circumstances, a one bedroom unit for the most part will provide appropriate accommodation to meet the needs of existing tenants.
17. The Wellington Reconfiguration Strategy outlines the need for increased number of one bedroom properties. Reconfiguring the Wellington City portfolio to provide for greater one bedroom supply will enable Housing New Zealand to meet these future external and internal demand requirements. In this there is clear alignment between the Wellington reconfiguration strategy and MSD purchasing intentions.
18. Wellington City Council is currently undertaking a significant refurbishment programme of their existing properties which has allocated government funding support, with an attached requirement that council commit to their involvement in social housing for 25 years. This programme includes the new Arlington project which is a demolition and rebuild of an existing property. This redevelopment will deliver 35 additional new one bedroom units (for a total of 66 one bedroom units on site) along with additional two, three and four bedroom typologies. The council has not identified any further new builds; however, they are currently undertaking a strategic review of their social housing activity.

The case for change

19. Within Wellington, future demand is not the only significant driver for redevelopment within the portfolio. The Wellington portfolio is one of Housing New Zealand's oldest. Redevelopment opportunities such as McLean provide Housing New Zealand with a mechanism through which to actively create additional capacity and enable churn within the portfolio to address issues associated with an ageing portfolio across other key assets within the city. This will enable tactical divestment and investment across the portfolio, supporting the outcomes sought through the Reconfiguration Strategy. In turn this strategy aligns to the Asset Management Strategy and the Wellington CAP by seeking to ensure that homes within the Wellington portfolio are warm, dry, safe and meet the needs of tenants by providing appropriate housing typologies in the right locations.
20. Through the development of the Wellington Reconfiguration Strategy, analysis was completed to understand the types of tenants Housing New Zealand housed and their requirements to access particular social and support services, community and health facilities, and retail or employment environments. The analysis highlighted the interconnectedness of tenant characteristics, housing needs (typologies), service and amenity requirements and the accessibility of these. Many of the support and social services within Wellington are located in the central business district and surrounds, these services range from mental health, drug and alcohol, medical and

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homelessness. Within the area, a proportion of tenants experience a mental health, drug or other incapacity, that may or may not require some level of support or intervention from an external agency. Enabling ease of access for tenants to these services is key to assisting tenants to achieve positive outcomes and remain within their tenancies. Understanding tenant characteristics and associated requirements can influence housing typologies and their locations.

21. Input from Tenancy Services (People and Property Group) in developing the Wellington Reconfiguration Strategy to understand who Housing New Zealand's tenants in Wellington City are, and their requirements was a key component in identifying appropriate housing typologies and locations in Wellington as part of this strategy.

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Business case proposal

Description of existing site and assets

22. McLean Flats is located at 314 The Terrace. The existing building is circa 1940's apartment block of up to 6 stories in height. The building is currently vacant but is configured as 16x one-bedroom units. The total site area is 1492m².
23. The site is accessed by pedestrians and vehicles from The Terrace. There is a shared ROW between Housing New Zealand and VUW (Gordon Wilson Flats), which with the new site layout and parking option does not need reconfiguring.

Figure 1 McLean Flats – Context



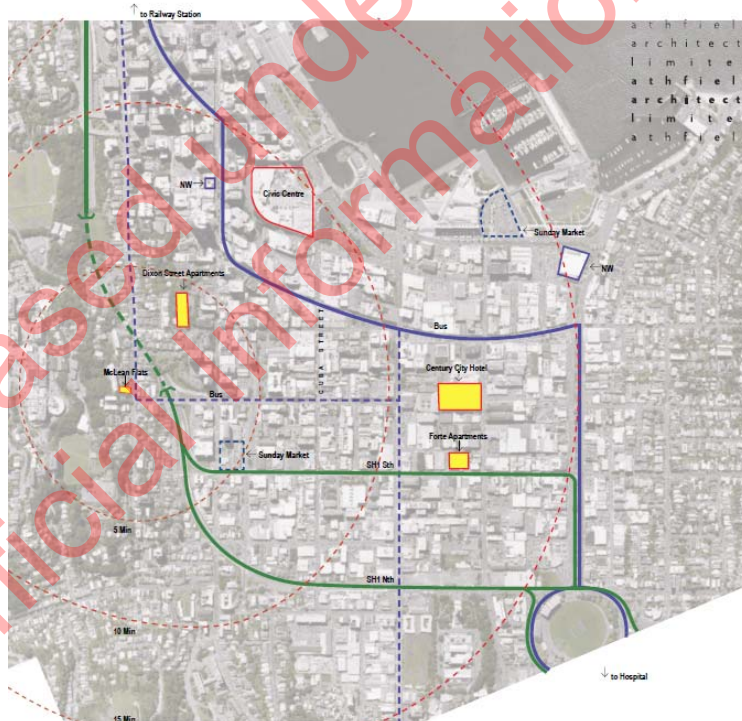
24. The site is within the 'Inner Residential Area'. The maximum building height is 10m, the current building is over 10m in height with the additions being very close to the existing silhouette. The new units comply with the 10m height limit and will be set back so that they will comply with existing daylight angle. If the existing McLean Flats building was demolished then we would have to comply with the 10m height limit.
25. The design must meet the objectives of the Inner Residential Design Guide, the criteria for achieving of this Guide has been considered by the Architects during the design phase.
26. The site currently has SHA status which allows not only fast tracking of the consenting process but places 'enhanced housing affordability' ahead of strict compliance with the RMA. The proposed redevelopment of McLean flats provides enhanced housing affordability and would there meet the criteria for processing under the SHA act.
27. The District Plan requires a ratio of 1:1 car parks. After an independent assessment of car parking requirements for one-bedroom housing, an external traffic engineer has recommended the seven visitor car parking as appropriate for this development. The location of McLean Flats is close to central city facilities and public transportation services. The provision of accommodation primarily for single people with higher needs, means that a low amount of the tenants will not operate a vehicle.

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Location and Amenity

28. The proposed development site is located at 314 The Terrace, in the Wellington inner suburb of Te Aro.
29. The location of McLean Flats is an optimal location for social housing due to its proximity to central city facilities, public transport other community amenities. The site is surrounded by a residential neighborhood with a diverse mix of activities and people living in the area.
30. The site is adjacent to the Gordon Wilson Flats, which was purchased by Victoria University of Wellington (VUW) in 2014. The site is a gateway to the VUW campus and they currently have a District Plan Change being processed to change the zoning of this land from Inner Residential to an Institutional Precinct.
31. VUW have applied to demolish the Gordon Wilson Flats, which is currently listed on the Wellington City Council (WCC) heritage building. When the flats are demolished, this will result in improved light, sunlight access and outlook from the McLean site. It is unknown at this time if VUW will develop the site as student accommodation or educational spaces.
32. The site has a number of positive attributes that make it well suited for a residential development. The size and proportions allow for the design and construction of a complex which with a scale that is ideally suited to one-bedroom units as preferred by Housing New Zealand to meet current demand requirements.

Figure 2 Site Location



Local Property Market

33. The current state of the residential housing market in Wellington Central does not allow Housing New Zealand the opportunity to purchase suitable properties for its investment portfolio in this location.

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34. Based on recent sales data for one-bedroom units in Wellington Central, Colliers have applied net rates between \$6,432 and \$7,136 psm or alternatively value ranges from \$294,000 to \$366,000. A copy of recent sales comparable is below:

Apartments	Unit number	Date	Size (m ²)	Sale Price	Net rate psm
City Fringe/Te Aro					
Nuovo Apartments, 21 Rugby Street	3G	Jul-15	51	\$320,000	\$6,275
	2E	Jul-15	51	\$324,000	\$6,353
	4G	Jul-15	51	\$330,000	\$6,471
	4E	May-15	51	\$335,000	\$6,569
	2G	May-15	51	\$360,000	\$7,059
	3H	May-15	51	\$360,000	\$7,059
	5F	Mar-15	51	\$330,000	\$6,471
	4A	Mar-15	51	\$339,000	\$6,647
	2I	Feb-15	51	\$308,000	\$6,039
	4C	Feb-15	51	\$338,000	\$6,627
	5E	Jan-15	51	\$335,000	\$6,569
	4I	Dec-14	51	\$345,000	\$6,765
5H	Dec-14	51	\$328,000	\$6,431	
Tattoo Apartments, 42 Abel Smith Street	32	Aug-15	52	\$350,000	\$6,731
	35	Jul-15	50	\$345,000	\$6,900
	2	Jan-15	50	\$350,000	\$7,000
Elevate, 30 Taranaki Street	6F	Jul-15	53	\$320,000	\$6,038
	5G	Jul-15	59	\$337,000	\$5,712
	6D	Apr-15	51	\$353,000	\$6,922
	8F	Apr-15	53	\$340,000	\$6,415
Older Developments					
Detroit Apartments, 181 Tasman Street, Mt Cook	6G	Apr-15	59	\$320,000	\$5,424
	12D	Mar-15	51	\$375,000	\$7,353
	11D	Jan-15	51	\$361,500	\$7,088
	8D	Dec-14	51	\$356,000	\$6,980
	9F	Nov-14	53	\$350,500	\$6,613
	11F	Nov-14	53	\$355,000	\$6,698
	5F	Sep-14	53	\$320,000	\$6,038
	9D	Aug-14	51	\$353,000	\$6,922
	10D	Aug-14	51	\$355,000	\$6,961
7 Hanson Street	106	Dec-14	54	\$400,000	\$7,407
	209	Jan-15	71	\$470,000	\$6,056
	310	Dec-14	64	\$500,000	\$7,188
QBA Apartments, 51 Webb Street	1	May-15	50	\$295,000	\$5,300
	11	Nov-14	41	\$246,500	\$6,012
	2D	Dec-14	40	\$265,000	\$6,000
233 Cuba Street	2I	Jul-14	40	\$240,000	\$6,000
	2Q	Mar-15	40	\$240,000	\$6,000
Republic, 10 Lome Street	582	Jun-15	45	\$315,000	\$7,000
Bellagio, 39 Taranaki Street	6F	May-15	53	\$333,000	\$6,283
8 Finlay Terrace	6F	Dec-14	53	\$325,000	\$6,132
	B	Jul-15	53	\$340,000	\$5,849

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35. Sales volumes for Wellington Central apartments are the highest they have been in the past three years, with a progressive increase in sales volumes noted over the past 12 months.
36. There are very few development sales of Inner Residential land in the wider Wellington Area, with the majority of this land being situated significantly further from the CBD than the subject site.
37. Up until recently, inner city developments have tended to provide a sparse number of one-bedroom units with the majority to the complexes made up of two to three-bedroom configurations.
38. The current median house price in the Wellington Region as at August 2015 is \$410,000, compared to a national median sale price of \$450,000 for August 2015.

Options Considered

39. The objectives for the feasibility study were to:
 - Define building configurations that best responded to site characteristics and neighborhood while creating a good quality housing environment that was safe, socially inclusive and fully integrated into the community.
 - Provide one bedroom units options only, which are identified by Housing New Zealand is in greatest demand in Wellington Central.
 - Provide accommodation that meets Housing New Zealand asset standards and design guidelines, with enhanced finishes to the same quality that is currently being provided in Auckland.
 - Identify options that comply with Wellington City Council District Plan requirements, therefore minimizing the potential for a notified resource consent process.
40. The existing McLean flats building is in a state of disrepair and is understood to be at 20% of NBS. Engineering advice recommends replacing the brick infills on the north and south facades, once these areas are addressed the likely rating would be 68% of NBS, above the HNZ standard of 67%. The existing building could likely be rated higher after further intrusive testing.
41. One-bedroom configurations are preferred, with units ranging in size from 45-49m², increasing to 51m² for the units in the existing building if the decks are removed.
42. Each one-bedroom unit aims to achieve the minimum standards set out by the Housing New Zealand guidelines but the existing building provides some compromise due to the existing structural grid and floor to ceiling heights. This is however not deemed to be significant.
43. Various unit configurations were investigated to assess different unit typologies that could be accommodated on site. The options analyzed include:
 - Option 4A: Retain existing building (16 one-bed units) plus 4 new roof tops units, and 11 new units to the balance of the site. 31x one-bedroom units.
 - Option 4B: Demolish the existing building and building 31 new units, 28 one-bedroom and 3x two-bedroom units.
 - Option 4A+3: Retain existing building (16 one-bed units) plus 4 new roof tops units, and 13 new units to the balance of the site. 34x one-bedroom units. Including decks.

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- Option 4A+3: No decks to existing: Retain existing building (16 one-bed units) plus 4 new roof tops units and 14 new units to the balance of the site. 34x one-bedroom units. Decks to new apartments, non to units in the existing building.
44. Note the community room has now been utilized as a residential unit.

Recommended Option

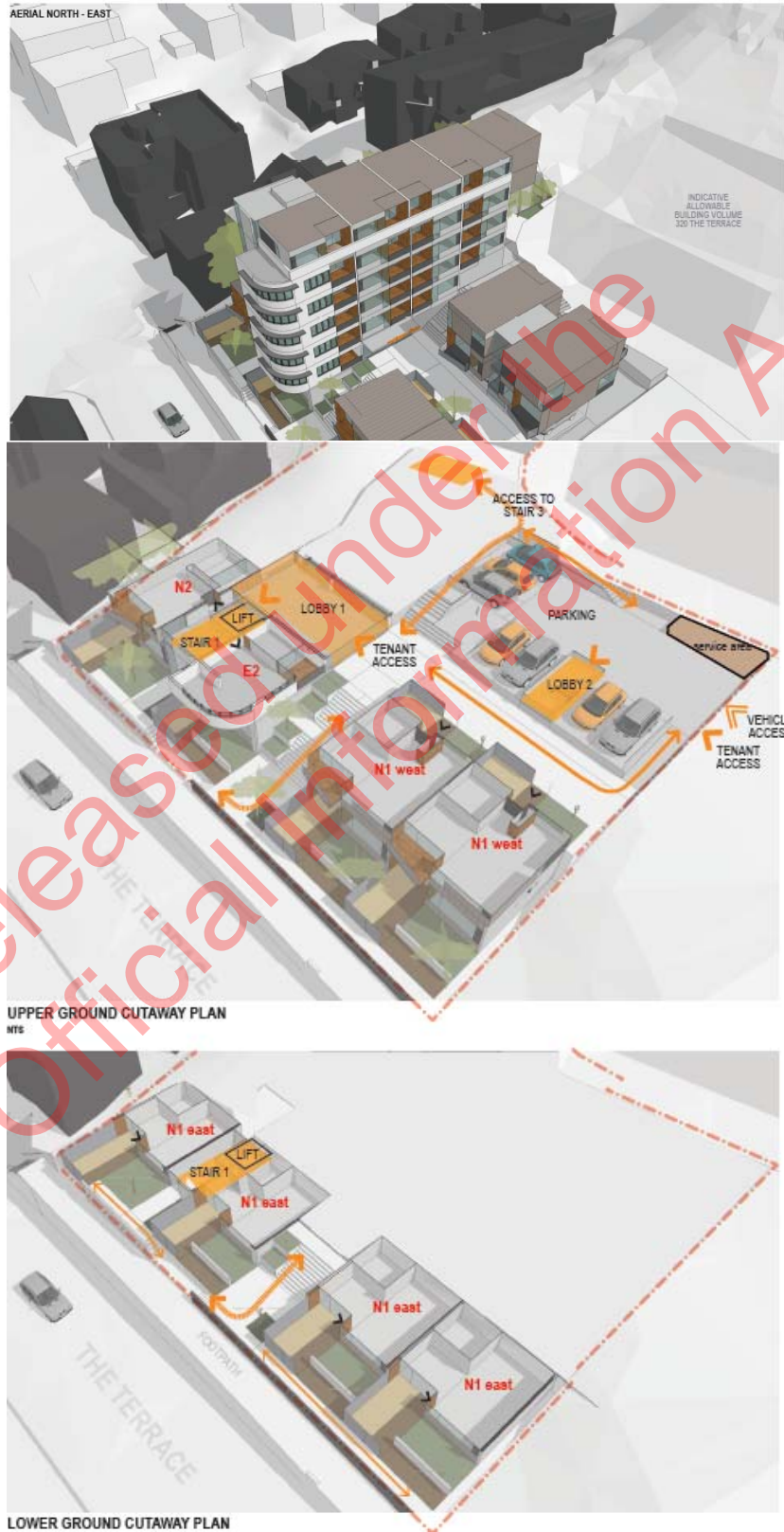
45. Option 4A+3 (34x one-bedroom units with decks to the new building only) was preferred as it offered the best financial return and also meets Housing New Zealand demand for one-bedroom units. A comparison of the feasibility, is assessed under the section *Financial Feasibility*. The option to demolish and rebuild was by far the most uneconomic solution.
46. The existing McLean Flats building is not a listed heritage building with Wellington City Council, but it does have townscape and architectural qualities in terms of what it represents as a social housing project of its time and its architectural character and art deco qualities.
47. McLean Flats is located on an elevated sloping site on the western edge of Te Aro Basin. The elevated nature of the site means the existing building can be seen from a number of locations within the city basin and the surrounding streetscape. This provides opportunities for an increased profile and identity for the development.
48. All units are dual aspect offering views in two directions and provide strong visual connections within the site and beyond which can assist with minimizing social isolation and provides good quality living environment with good daylight, ventilation and a sense of space.
49. The community garden is a terraced area that links the upper ground courtyard with the Stair 3 Lobby entry to the west, where there are areas for a community garden and fruit trees for tenants to be able to grow food.

Figure 3 Plan of Proposed Development



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Figure 4 McLean Flats – Proposed Design



Impact on Tenants

50. The TLO team have successfully relocated all tenants that were previously in residence on the site.

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Financial Feasibility

Valuations

51. Colliers International, registered property valuers, have considered the existing assets and the potential development to determine an estimated value. Their full valuation report is appended to the business case (Attachment E).
52. Colliers International have recently assessed the current market valuation of McLean Flats at 314 The Terrace, at \$1,276,500 including GST. This includes the underlying market value and improvements.
53. Colliers International have been provided the typical typologies designed for one-bedroom apartments McLean Flats and have determined the average value for these properties.

Table 2 As-if Complete finished valuations - Average

TYPICAL HOUSE TYPE	ESTIMATED MARKET VALUE	MARKET RENTAL ASSESSMENT
1 Bedroom Unit (4A+3 no deck)	\$320,824	\$385-\$400
1 Bedroom Unit (4A+3 incl. deck)	\$334,853	\$390-\$410
Car parks	\$40,000	-

Construction Costs

54. The construction costs currently allow to strengthen the existing building to 100% NBS. It is not likely that the proposed upgrade of the building would in itself trigger a legal requirement to strengthen the building beyond the 68% achieved by removal of the brick infills because there is no change of use and the building is not being added to significantly. However for the purposes of the current feasibility study it has been assumed that HNZ would wish to take a long term view of the property asset and, noting that the building is being 'renewed' in all other respects, that strengthening of the building to 100% NBS is a more appropriate long term approach. Should Housing New Zealand wish to consider strengthening to something less than 100% then the strengthening options and cost savings can be assessed further during the concept design stage.
55. Construction costs have been estimated by Rider Levett Bucknall (RLB) based on an outline specification, design assumptions from Athfield Architects and Dunning Thornton engineers. It is important to note that the estimates are based on considerable assumptions given the limited design information available at this early stage in the design lifecycle. Accurate construction drawings and detailed specifications are needed to precisely determine construction costs.
56. The total construction estimate for the 4A+3, exclusive of decks to existing building scheme is \$7,212,140 excluding land, fees and contingency. This estimate is based on a gross floor area of 2540m² and a construction rate of approximately \$2,800/m².
57. Build costs on similar projects in Wellington have ranged from \$2,400m² – 3,200m².
58. Estimates of professional's fees and Local Government Fees and charges have been included sourced from similar scale projects.

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59. The entire development for 4A+3, exclusive of decks is expected to cost \$11,503,180 million including GST, and including the land value. [REDACTED] 9(2)(i)

60. [REDACTED] 9(2)(i) [REDACTED] sis is

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Procurement Options

61. The procurement models described below have been considered for the development of McLean Flats.

ID	Name	Description
1	Design & Construct	<p>Housing New Zealand undertakes the development and owns all the units on completion.</p> <p>Housing New Zealand retains a design team to partially develop the scheme design. This developed design is tendered out with a Requirements Specification, and the contractor designs and builds to those requirements.</p>
2	Design & Construct – Novated	<p>A variant of the above option, the client's design team is novated to the contractor at the completion of the 30% design. The contractor bids to complete the design and construction using the client's design team</p>
3	Design-bid-build	<p>Housing New Zealand undertakes the development and owns all the units on completion.</p> <p>Housing New Zealand retains a design team to prepare full design documentation and tenders the finished design to a contractor.</p>
4	Developer-led buyback	<p>Housing New Zealand define their requirements for the site including type and numbers of stock, specification and quality expectations. Housing New Zealand then sells the parcel of land to a developer and buys back a pre-agreed number of units (in this case, all units) at completion of construction at a pre-agreed market rate. A variant on this model is for Housing New Zealand to provide the land free of charge.</p> <p>This option could also be delivered by a well-funded builder.</p> <p>This option was rejected as being more expensive due to the finance charge and developer overheads associated with the developer holding the project.</p>

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5	Develop or investor-led leaseback	<p>Housing New Zealand define their requirements for the site including type and numbers of stock, specification and quality expectations. Housing New Zealand then sells the parcel of land to a developer and leases back a pre-agreed number of units (in this case all units) at completion of construction at a pre-agreed market rate. A variant on this model is for Housing New Zealand to provide the land free of charge.</p> <p>In this scenario the developer would be unable to convert from social housing to other uses in the future, limiting the potential upside for the developer on expiry of the leaseback period.</p> <p>This option was rejected as being more expensive due to the finance charge and developer overheads associated with the developer holding the project.</p>
6	PPP	<p>Housing New Zealand enters into a hybrid model with a developer or social housing provider, or a combination, on a shared risk and return basis.</p> <p>McLean Flats is too small to consider the involvement of a third party housing provider.</p> <p>This option was rejected as being more expensive compared with a tendered approach due to the overheads associated with establishing and managing the PPP structure. There may also be finance charges and associated with the developer or provider, depending on the PPP model used.</p>

Evaluation of Delivery options.

62. The following requirements were adopted based on our understanding of the project characteristics and HNZ requirements:

ID	Criteria	Description
1	Value for Money, considering	<p>Overall financial performance. The forecast cost of delivery for the procurement method taking into account such things as the extent of market competitive pricing, the degree to which Housing New Zealand requirements can be defined for tendering.</p> <p>The extent to which the procurement method can provide cost savings through innovation in design outcomes</p>
2	Overall price risks	<p>Includes consideration of how well the procurement model deals with cost risks such as in-ground risk, unforeseen issues, existing buildings/structure, interface risks and the associated risk of time-related Contract Variations.</p>

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3	Quality outcomes – design and construction	How well does the procurement method allow Housing New Zealand to control the design outcomes such as amenities, shared services, space and light? How well does the procurement method allow Housing New Zealand to control the quality of construction for the specified design?
4	Time to completion and programme risk	The extent to which the procurement method can shorten design and construction durations. Includes the extent to which procurement options may increase (or decrease) timeframes due to Housing New Zealand procurement and other internal processes.
5	Contractor capacity, availability and interest	Contractor capacity, availability and interest to bid the project under the procurement model proposed.

Evaluation

Criteria	1 – D&C	2 – D&C novated	3 – Design-bid-build
1. Value for Money	L Unable to provide cost certainty regarding refurbishment due to unknowns..	L Unable to provide cost certainty regarding refurbishment due to unknowns	H Detailed design and thorough investigations should provide a well-coordinated set of drawings. Contractor unable to provide innovation through design phase
2. Price risk	M Unable to provide cost certainty for refurbished apartments (Approx 50%)	M Unable to provide cost certainty for refurbished apartments (Approx 50%)	H Any drawing errors resulting in variations will be at the Client's cost. Balance of risk between Contractor and Client.

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3. Quality	M No Contractor input into the design or planning of the project as they are not appointed during the design stage.	M No Contractor input into the design or planning of the project as they are not appointed during the design stage.	H Client can have direct control over the design and quality
3. Time	H Shorter duration due to overlap of design/construct.	H Shorter duration due to overlap of design/construct.	M Typically the traditional method is slower than design-build
4. Market interest	L Low interest due to risks associated with this approach.	L Low interest due to risks associated with this approach.	H Minimal risk to Contractor.
TOTAL SCORE H=3, M=2, L=1	9	9	14

63. Due to the combination of refurbishment and new build units, the preferred procurement methodology for delivery is through traditional design-bid-build process. This enables the Contractor to price based on a fully coordinated set of detailed design drawings. With the total project cost exceeding \$10m, Housing New Zealand will be required to openly advertise the procurement via the Government Tendering service (GETS). The design-bid-build procurement option provides the most competitive price and least risk option for the redevelopment of McLean Flats. There are some advantages in retaining the current design team as the knowledge of the site and project be retained. A two stage procurement process to test the markets interest and shorten the final negotiation period would be the least time consuming process.
64. Interviews were conducted with five Wellington construction companies of varying sizes but all with a history and capability to deliver a building of this scale and nature. All contractors are very interested in the project regardless of delivery and procurement model (i.e. traditional or design and build).
65. There is a forecast shortage of construction projects for the Wellington Market in 2016. The timing of this project is likely to experience favorable construction market in 2016. Specific themes from the contractor interviews were as follows:
66. A number of them have been involved in tender process with Housing New Zealand before that have not proceeded, therefore they would require assurances that the projects were going to proceed before investing in a tender process.
67. There are both advantages and disadvantages in combining this project with others development projects being considered. There is advantages to being to offer greater

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continuity of work to the contractor and subcontractors which might attract marginally better pricing and priority service. The disadvantage is that the scale of the combined projects may preclude smaller contractors from being able to deliver sites concurrently introducing risk. There would be no P & G savings as the sites are geographically separated.

Financial Feasibility

68. The preliminary financial development feasibility is shown in the table below. A more detailed assessment of the financial Impact to Housing New Zealand in attached in Attachment F.
69. It is proposed that Housing New Zealand retains 100% of the completed units to meet current Housing New Zealand demands for one-bedroom units in this location.

Table 3 Development Feasibility - based on Traditional Procurement Approach (No decks)

McLean Block, The Terrace, Wellington		Scheme 4A + Retain Existing building NO DECKS +4 ROOF + 10 New Units PLUS 3 new units to rear with decks		Rev 1 20.01.16	
Site Redevelopment					
HNZ 100% Owned with HNZ as Developer					
Valuation		HNZ			
HNZC	No	Value	Total		
Refurbish existing McLean Block - 1 Bed units	16	\$	5,584,000		
Community room (could also be fitted out as apartment)	1	\$	303,000		
New 1 Bed units above existing building	4	\$	1,316,000		
New 1 Bed units	10	\$	3,258,000		
New rear units	3	\$	924,000		
Carparking	7	\$	40,000	\$	280,000
Total (Average)	34	\$	334,853	\$	11,665,000
Total Value on Completion				\$	11,665,000
Construction	No.	Area	Rate p.s.m.	Cost	Total
A1 - Existing Building Structural strengthening	1	1629	\$ 728	\$ 1,185,912	\$ 1,185,912
A3 - Existing building roofing and recladding	1	1629	\$ 262	\$ 426,798	\$ 426,798
A2 - New units - Structure	1	911	\$ 1,067	\$ 972,037	\$ 972,037
A4 - New units - roof and cladding	1	911	\$ 357	\$ 325,227	\$ 325,227
A5 - Lift (In 1 No. Existing)	1	1629	\$ 106	\$ 172,674	\$ 172,674
A6 - Existing apartment fitout (No.16)	1	801	\$ 1,720	\$ 1,377,720	\$ 1,377,720
New apartment fitout (no.18)	1	820	\$ 1,630	\$ 1,336,600	\$ 1,336,600
Circulation area fitout	1	522	\$ 1,236	\$ 645,192	\$ 645,192
Additional parking cost				\$ 100,000	\$ 100,000
Community room	1	52	\$ 1,865	\$ 96,980	\$ 96,980
Net saving from deletion of decks on existing building levels 1 to 5 (excluding community room)	16	no		\$ (3,000)	\$ (48,000)
Site works and Services	1	L/S		\$	\$ 471,000
On Site Stormwater Retention				\$	\$ -
Site Works & landscaping	1			\$ 150,000	\$ 150,000
Consent and Consultants					
Professional Fees			12.5%	\$ 7,212,140	\$ 901,518
Council Consent fees (building and resource)	1		3.0%	\$ 7,212,140	\$ 216,364
Dev Contributions Nett					\$ 60,000
Place making- Comms					
Telecom connection charge	17			\$ 1,000	\$ 17,000
Water connection charges	17	incl		\$ -	\$ -
					\$ 1,194,882
GST					
GST on Costs of Houses Retained		100%	\$ 8,407,022	\$	1,261,053
				\$	1,261,053
Overheads & Risk					
9(2)(i)					
Holding Costs					excluded
Funding Costs					excluded
Decanting Costs	1			\$ -	\$ 725,106
TOTAL DEVELOPMENT COST Excluding Land				\$	10,393,181
LAND at CMV (GST Excl)				\$	1,110,000
TOTAL DEVELOPMENT COST Including Land				\$	11,503,181
TOTAL PROJECT MARGIN				\$	161,819
1.4%					

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70. Please note that the above feasibilities do not account for inflation or cost escalation of which the Finance memo (Attachment F) does allow for, in accordance with the Investment Manual. Finance suggest funding is therefore sought for the inflated amount of \$10,771k. Similarly the completion value in the above feasibility is uninflated whereas the value in the Finance memo is inflated.

Financial Analysis

71. The financial feasibility calculations based on RLB estimates and Colliers valuations are summarized below.



73. Decks could be added to the no deck option by forming them outside of the existing building envelope. This would align with Housing New Zealand requirements to provide decks and almost be cost neutral (i.e. cost offset by deck added value), however the provision of external decks to the existing building will be a challenge architecturally, given the Art Deco style of the existing building. Athfield Architects, the company contracted via the procurement process in 2014, have stated that the architectural integrity would be severely compromised and they are opposed to external decks on the existing building. Based on this advice, this option was not pursued further.
74. After further consultation, the preferred option is confirmed as 4A+3, consisting of a total of 34 units, with no decks to the existing units.

Risk analysis

75. The main business and service risks that might create, enhance, prevent, degrade, accelerate or delay the achievement of the investment objectives are identified in Attachment H.
76. It is deemed that all risks which have been identified are at acceptable levels and can be managed.

Tax implications

77. This project does not raise any development activity tax implications (Attachment I).

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Legal and regulatory implications

78. Legal have advised that the proposed redevelopment does not raise any unusual legal implications (Attachment K) given:
- this is a site which Housing New Zealand has owned;
 - it is to be retained throughout the build process;
 - Housing New Zealand intends to retain the end product for rental housing purposes;
 - the build will be on one of Housing New Zealand's approved build templates; and
 - the project is a "strategic fit".

Procurement

79. The sourcing of the team to deliver the McLean project commenced with the appointment of Athfield Architects in January 2015, following an RFP process undertaken in late 2014. Further procurement processes will be required to appoint the balance of the design team (such as traffic planners, if required for the unusual site), a development /project management partner to act as Housing New Zealand's agent (Housing New Zealand does not intend to manage this in house for this project) and a procurement process to select and contract the contractor to deliver the project.
80. There are no Housing New Zealand panels in place for the Wellington market and Housing New Zealand has undertaken no pre-qualification processes. Housing New Zealand has connected with Government sector agencies with active construction programmes underway, to leverage the available market analytics and consider pre-qualification processes in order to expedite the sourcing processes, where possible. The proposed processes are outlined in Attachment J.

Communications

81. Housing New Zealand has ongoing, well established relationships with the stakeholders and community surrounding this site with whom there has been an ongoing commitment that we will be open and transparent about our plans.
82. A communications and engagement plan will be drafted to support the outcome from this paper.

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Project implementation

83. The project will be run over one continuous stage – all the new supply housing on the site will be constructed and delivered at the same time. Project delivery is expected in mid 2017. Key project milestones indicators are set out below.

Table 5 Key Milestones and Estimated Delivery Programme

KEY MILESTONES	ESTIMATED DATES
Stakeholder Engagement including VUW	Second quarter 2016
Resource Consent Lodgment	Third Quarter 2016
Resource Consent Approved	Fourth Quarter 2016
Contractor Engaged	Fourth Quarter 2016
Units Completed	Second Quarter 2018

84. Upon approval of this business case the following activities will occur:
- Asset Development Group will begin discussions with Wellington City Council in order to prepare a revised resource consent application for lodgment mid next year.
 - A communications and stakeholder engagement plan will be prepared. Housing New Zealand will engage with affected stakeholders and inform them of our intentions.
 - Once consents are obtained, construction contracts will be tendered. Contract execution will be entered into based on the approvals sought in this business case.
 - Updates will be provided to the Board as key milestones are achieved.
85. Andrew Showler, Manager Development Management team, will lead the McLean Flats project.

Attachments:

Attachment A	Architects Design Report
Attachment B	Final Design Option + new parking layout option.
Attachment C	Planning Memo
Attachment D	Draft Programme
Attachment E	Valuation Report
Attachment F	Financial Analysis
Attachment G	Property and Tenancy Services memo
Attachment H	Risk Analysis
Attachment I	Tax Implications
Attachment J	Procurement Memo
Attachment K	Legal Implications
Attachment L	Demand and Portfolio Review