

Proactive Release

25 July 2023

The following Cabinet paper and related Cabinet minutes have been proactively released by the Minister of Foreign Affairs

Title	Reference
<i>Cabinet Minute of Decision – Report of the Cabinet External Relations and Security Committee: Period Ended 9 June 2023 (Part 1)</i>	CAB-23-MIN-0226
<i>Cabinet External Relations and Security Committee – Minute of Decision – Solomon Islands: Provincial Airfield Upgrades</i>	ERS-23-MIN-0028
<i>Solomon Islands: Provincial Airfield Upgrades</i>	

Some parts of this information release would not be appropriate to release and, if requested, would be withheld under the Official Information Act 1982 (the OIA). Where this is the case, the relevant sections of the OIA that would apply have been identified. Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.

Key to OIA redaction codes:

- 6(a): to avoid prejudicing the international relations of the New Zealand Government;
- 9(2)(i): to enable Minister and Agencies to carry out commercial activities without prejudice or disadvantage; and
- 9(2)(j): to avoid prejudice to negotiations.



Cabinet

Minute of Decision

This document contains information for the New Zealand Cabinet. It must be treated in confidence and handled in accordance with any security classification, or other endorsement. The information can only be released, including under the Official Information Act 1982, by persons with the appropriate authority.

Report of the Cabinet External Relations and Security Committee: Period Ended 9 June 2023 (Part 1)

On 12 June 2023, Cabinet made the following decisions on the work of the Cabinet External Relations and Security Committee for the period ended 9 June 2023:

ERS-23-MIN-0028

Solomon Islands: Provincial Airfield Upgrades
Portfolio: Foreign Affairs

CONFIRMED

Rachel Hayward
Secretary of the Cabinet



Cabinet External Relations and Security Committee

Minute of Decision

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Solomon Islands: Provincial Airfield Upgrades

Portfolio Foreign Affairs

On 6 June 2023, the Cabinet External Relations and Security Committee:

- 1 **noted** that on 19 April 2021, the Cabinet Business Committee approved ^{s9(2)(i), s9(2)(j)} as total expenditure from all funding sources for the Solomon Islands Provincial Airfield Upgrades [CBC-21-MIN-0043];
- 2 **noted** that the Solomon Islands Provincial Airfield Upgrades project is led and managed by Aotearoa New Zealand, and that total planned expenditure within the mandate referred to above comprises:
 - 2.1 Aotearoa New Zealand's financial contribution of ^{s9(2)(i), s9(2)(j)} (from within the International Development Cooperation allocation within Vote Foreign Affairs);
 - 2.2 Australia's financial contribution of ^{s9(2)(i), s9(2)(j)}
 - 2.3 Solomon Islands' financial contribution of SB\$21 million;
- 3 **noted** that cost increases to the Solomon Islands Provincial Airfield Upgrades project to date have been managed within the existing funding mandate, but that is no longer possible and the limit of the funding mandate will be reached in the short term;
- 4 **approved** ^{s9(2)(i), s9(2)(j)} as the revised total expenditure from all funding sources for the Solomon Islands Provincial Airfield Upgrades activity, which will continue to be managed by Aotearoa New Zealand;
- 5 **noted** that the new mandate cost increase will be met by increasing Aotearoa New Zealand's contribution from within the International Development Cooperation allocation within Vote Foreign Affairs, seeking further contributions from ^{s6(a)} development partners, or a combination of these.

Janine Harvey
Committee Secretary

Present: (see over)

Present:

Rt Hon Chris Hipkins (Chair)
Hon Carmel Sepuloni
Hon Kelvin Davis
Hon Grant Robertson
Hon Michael Wood
Hon Andrew Little
Hon David Parker
Hon Nanaia Mahuta
Hon Kieran McAnulty
Hon Ginny Andersen

Officials present from:

Office of the Prime Minister
Officials Committee for ERS

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Office of the Minister of Foreign Affairs

Cabinet External Relations and Security Committee

Solomon Islands — Provincial Airfield Upgrades

Proposal

- 1 Cabinet approval is required for all Aotearoa New Zealand-managed International Development Cooperation (IDC) activities in excess of NZ\$25 million, regardless of the sources of funding.
- 2 This paper seeks approval of an increased financial authority for an IDC project, the Solomon Islands Provincial Airfield Upgrades (PAU). In April 2021, Cabinet gave approval for ^{s9(2)(i), s9(2)(j)} to be spent on the PAU from all funding sources [CBC-21-MIN-0043]. This paper seeks approval to increase that financial authority to allow for ^{s9(2)(i), s9(2)(j)} to be spent on the PAU from all funding sources, due to cost escalations.
- 3 The PAU is led and managed by Aotearoa New Zealand (including funding of ^{s9(2)(i), s9(2)(j)}, with additional funding from Australia ^{s9(2)(i), s9(2)(j)} and Solomon Islands (SB\$21 million¹). This paper does not seek additional funding as such. Any additional funding would be sourced from within the existing IDC allocation, from other development partners, or through a combination of these things. There are no windfall gains to the Ministry of Foreign Affairs and Trade in the event this allocation is not disbursed. Any funds not applied to this activity will be applied to other IDC activities.

Relation to government priorities

- 4 Supporting a safer, better regulated, and internationally compliant aviation sector in Solomon Islands contributes to Aotearoa New Zealand's foreign policy and development priorities. The PAU is consistent with the *Pacific Resilience Approach*. The *Pacific Resilience Approach* underscores the centrality of the Pacific to Aotearoa New Zealand and acknowledges the most enduring way our region can address the shared, complex challenges we face is through close partnership.

Executive Summary

- 5 The Solomon Islands bilateral IDC programme is one of Aotearoa New Zealand's largest. Its total core allocation for 2021-2024 is NZ\$87.26 million. The Provincial Airfield Upgrades (PAU) is an activity within that programme. It is led and managed by Aotearoa New Zealand, and co-financed with the Governments of Australia and Solomon Islands. The PAU will see major upgrades to the Seghe and Taro provincial airfields, including sealing and lengthening of the runways. The original costing for the PAU following detailed design and scoping was ^{s9(2)(i), s9(2)(j)}

¹ Approximately NZ\$4 million, depending on exchange rates.

- 6 In April 2021, Cabinet gave approval for s9(2)(i), s9(2)(j) to be spent on the PAU from all funding sources [CBC-21-MIN-0043]. However, local and global events have caused significant cost increases, totalling s9(2)(i), s9(2)(j) This has eroded contingency and headroom in the existing financial authority.
- 7 As of now, the total cost of the PAU is s9(2)(i), s9(2)(j) However, additional cost increases of s9(2)(i), s9(2)(j) are anticipated (see Appendix 1 for details). s9(2)(i), s9(2)(j) s9(2)(i), s9(2)(j) The existing financial authority is insufficient to absorb these cost increases and funding in excess of the existing financial authority will be required.
- 8 The cost increases calculation is based on well-known factors. The impact on the current pricing of the contracts is already in play and will in the short term cause the existing financial authority (including its remaining contingency of s9(2)(i), s9(2)(j) to be exhausted. Seeking approval now to increase the financial authority by s9(2)(i), s9(2)(j) s9(2)(i), s9(2)(j) will enable the efficient management of the cost increases.
- 9 Waiting for the financial authority to be fully exhausted would risk incurring further costs in the activity, including paying for contractors' unproductive downtime. An increase in the financial authority a short time ahead of the increases being incurred will also s9(2)(i), s9(2)(j) s9(2)(i), s9(2)(j)
- 10 It is for these reasons that this paper now seeks approval to increase the financial authority approved by Cabinet for the PAU to s9(2)(i), s9(2)(j) The increase is not a request for new funding. The increased financial authority allows for increasing Aotearoa New Zealand's contribution from within the IDC allocation and enables officials to seek further contributions from development partners.

Background

- 11 In April 2021, Cabinet gave approval for s9(2)(i), s9(2)(j) to be spent on PAU from all funding sources [CBC-21-MIN-0043]. The PAU are led and managed by Aotearoa New Zealand and co-financed with the Governments of Australia s9(2)(i), s9(2)(j) and Solomon Islands (SBS\$21 million²). Aotearoa New Zealand's current contribution to the PAU is s9(2)(i), s9(2)(j) The sum of current contributions from all co-financiers totals s9(2)(i), s9(2)(j) s
- 12 The PAU is in implementation. Completion is expected in late-2024. The PAU comprises three 'Separable Portions':
- 12.1 Separable Portion 1, now complete, involved the mining and transport of aggregate as well as Unexploded Ordnance clearance;
- 12.2 Separable Portion 2, yet to commence, will complete Seghe airfield in mid-2024. s9(2)(i), s9(2)(j)

and

² Approximately NZ\$4 million, depending on exchange rates.

³ Dependent on exchange rates.

12.3 Separable Portion 3, which began in early 2023, will complete Taro airfield in late-2023. ^{s9(2)(i), s9(2)(j)}

- 13 To date, the activity's construction programme has experienced 240 days of delays. At commencement, construction completion was projected for December 2023; it is now projected for August 2024 ^{s9(2)(i), s9(2)(j)} The main causes of delays have been border restrictions, civil unrest, cost increases, COVID-19, and other challenges with construction in remote Pacific locations.

Alignment with Solomon Islands Government's development priorities

- 14 Airfields ^{s6(a)} . Aotearoa New Zealand is investing in improving this infrastructure. In addition to the PAU, we are supporting the renewal of the Niue runway. This project has encountered similar budgetary pressures as the PAU.
- 15 Solomon Islands faces aviation infrastructure challenges. Its provincial airfields are ^{s6(a)} dilapidated. This interrupts scheduling, adds risk, reduces connectivity, limits operations by more modern and fuel-efficient aircraft like the Dash-8, and contributes to frustration and high costs of domestic air travel. This poses major obstacles for connectivity, tourism, and access to services and markets. This has adverse impacts on the economy and livelihoods of Solomon Islanders. More reliable, cost effective, and safe air services are essential for economic and social development.
- 16 The PAU's objectives align with Solomon Islands' National Development Strategy 2016-2035. The Solomon Islands Government is prioritising tourism development as an emerging non-extractive industry. ^{s6(a)} The upgrades were included in its Economic Stimulus Package to address impacts of COVID-19.

Aotearoa New Zealand's support to Solomon Islands' aviation sector

- 17 Aotearoa New Zealand has been the lead partner to Solomon Islands in the aviation sector since in 2012. Together, we have implemented several interventions:
- 17.1 build of Munda Airport and resurfacing Nusa Tupe airport in Western Province;
- 17.2 airport management reform and the establishment of Solomon Islands Airport Corporation Limited (SIACL), the state owned enterprise responsible for managing and operating Solomon Islands' airports; and
- 17.3 supporting safety and security equipment, operational and technical training, and fire rescue capability at Henderson International Airport in Honiara.

Analysis

Cost escalations

- 18 The original pre-COVID costing for the PAU was ^{s9(2)(i), s9(2)(j)} including ^{s9(2)(i), s9(2)(j)} contingency. However, local and global events have caused price increases,

totalling ^{s9(2)(i), s9(2)(j)} to date. These cost increases could not have been foreseen when PAU was initiated. The increases have outstripped contingency and will shortly reach the limit of the existing financial authority. ^{s6(a), s9(2)(i), s9(2)(j)}

- 19 The cost increases experienced by PAU are consistent with similar infrastructure projects across the Pacific region, where construction costs are increasing faster than inflation. Inflation has been driven by the global response to the threat of COVID-19 — a combination of excessive demand and constrained ability to produce goods and services. As most Pacific economies either use foreign currencies or have fixed their currency's exchange rates to the United States, Australian, or New Zealand Dollar, they import inflation trends from outside the region.
- 20 Pacific inflation rates are currently six to nine percent and forecast to remain high and volatile for the foreseeable future. Construction costs have risen significantly more than inflation due to increases in the costs of shipping and materials of up to 400 percent since pre-COVID levels. This is in large part attributable to a significant imbalance between demand and supply of shipping services in the Pacific. There are fewer ships servicing Solomon Islands at present. The services that are operating are reluctant to include 'breakbulk' cargo, which is required for the PAU.
- 21 Other factors causing cost pressures include supply constraints, and disruptions due to border restrictions, civil unrest, and Solomon Islands' COVID-19 outbreak.
- 22 As a result of cost escalations and without factoring in further expected cost increases, the total activity cost is now ^{s9(2)(i), s9(2)(j)} This includes a small contingency of ^{s9(2)(i), s9(2)(j)} and remains just within the existing financial authority. At commencement, the PAU had a ^{s9(2)(i), s9(2)(j)} contingency built in; however, as a result of cost escalations, only a ^{s9(2)(i), s9(2)(j)} contingency is possible to keep within the existing financial authority.

Ongoing risks of cost escalation

- 23 Additional funding above the existing financial authority will be required. Cost increases up to ^{s9(2)(i), s9(2)(j)} are forecast while regional and global economic pressures persist and inflation remains volatile. Specific cost risks include:

^{s9(2)(i), s9(2)(j)}

- 24 Exact cost increases are difficult to predict with certainty. However, expected cost increases are based on the regional and global economic environment, time delays experienced to date, inflation, and market factors. Forecast cost increases for activity completion are detailed in Appendix 1. Based on these forecasts, the proposed new financial authority is ^{s9(2)(i), s9(2)(j)}
- 25 I am seeking this additional authority to enable appropriate risk and financial management. ^{s6(a), s9(2)(i), s9(2)(j)}

^{s6(a)}

- 26 If the financial authority is not increased now, there is a risk that as costs increase again, construction may need to be paused until financial authority can be raised. This would result in further costs.

Approach to cost escalations across the IDC programme

- 27 Cost increases in infrastructure activities are impacting the entire Pacific region. Other development partners have reported similar experiences in their activities as those faced in the PAU. In order to manage and mitigate these impacts and associated risks, a variety of project-specific strategies are being applied. These are tailored to the circumstances of each activity. Those strategies are:
- 27.1 **Reduce scope, without objectives being impacted.** Some projects have this capacity and have undergone redesign to ensure cost savings;
- 27.2 **Reduce scope and objectives.** Some projects provide limited flexibility to reduce scope with some impacts on objectives;
- 27.3 **Rework project timelines.** This includes, for example, delaying implementation so that an activity spans triennia;
- 27.4 **Increasing funding through co-financiers.** Some development partners are seeking to support projects in the region;
- 27.5 **Request additional Aotearoa New Zealand finance.** Some activities may seek additional funding from within the IDC funding baseline; and
- 27.6 **No change required.** Some activities have adequate contingency to cover cost escalations.
- 28 Officials have applied these strategies to the PAU. ^{s9(2)(i), s9(2)(j)}

Increased funding through co-financiers has been obtained from Australia. ^{s6(a), s9(2)(g)(i)}
Further
funding has also been obtained from within the IDC funding baseline. ^{s6(a)}

s6(a)

Sources of additional funding

29 Aotearoa New Zealand has increased its financial contribution to the PAU to cover approximately 50 percent of increased costs to date. Funding was sourced from within the IDC funding baseline. Our original contribution when the project started was NZ\$20 million; it is now ^{s9(2)(i), s9(2)(j)} s6(a) Australia has also raised its financial contribution by ^{s9(2)(i), s9(2)(j)} s6(a) to cover the remaining cost increases. Australia's original contribution was AU\$18 million; its contribution is now ^{s9(2)(i), s9(2)(j)} s6(a)

30 The increase in financial authority being sought in this Cabinet Paper allows officials to manage further cost escalations by either increasing Aotearoa New Zealand's contribution from within the IDC allocation, seeking further contributions from ^{s6(a)} s6(a) development partners, or a combination of all of these options. This is not a request for new IDC funding. There are no windfall gains to the Ministry of Foreign Affairs and Trade in the event this allocation is not disbursed. Any funds not applied to this activity will be applied to other IDC activities.

s6(a)

31 Our interventions in Solomon Islands' aviation sector to date have contributed to strengthening social and economic stability in the country. ^{s6(a)}

32 Aotearoa New Zealand is currently the lead development partner in aviation management and infrastructure in Solomon Islands. ^{s6(a)}

33 ^{s6(a)}

34 ^{s6(a)}

s6(a)

35 s6(a)

Risk and risk management

- 36 Delays in large infrastructure projects in the Pacific are common. Challenges can range from natural disasters, to civil unrest (as in November 2021 in Solomon Islands), to unforeseen challenges on construction sites. The PAU has endured challenges and will continue to be tested. Airfield upgrades are complex, made more so by COVID-19 and its impacts on supply chains. This has the potential to impact on cost. The active involvement of the Solomon Islands Government in the project mitigates the risk of further delay. Strong activity and risk management processes also help to mitigate risks.
- 37 Further cost increases will impact the completion of the PAU. To mitigate the risks, officials are applying prudent financial management, and are closely coordinating with contractors and the Solomon Islands Government to determine and respond to these cost increases.
- 38 s6(a), s9(2)(i), s9(2)(j)

Financial Implications

- 39 Approving this request will have no impact on the Crown's operating balance. This Activity uses existing funding allocated from the International Development Cooperation allocation within Vote Foreign Affairs.
- 40 Table 1 displays a breakdown of the original and updated costs of the PAU following cost escalations incurred to date. It also details contributions from development partners. This table does not detail the expected additional cost increases that are forecast. That information is included in Appendix 1.

Table 1: Cost increases incurred to date ⁴		
	Original (NZ\$)	After cost escalations already incurred (NZ\$)
Activity budget	s9(2)(i), s9(2)(j)	
Contingency		
Total activity budget		
Contributions from development partners		
New Zealand (NZ\$)	20,000,000	s9(2)(i), s9(2)(j)

⁴ Updated on 23 May 2023.

Australia (AU\$)	18,000,000	s9(2)(i), s9(2)(j)
Solomon Islands (SB\$)	21,000,000	21,000,000

Legislative Implications

41 This paper has no legislative implications.

Impact Analysis

Regulatory Impact Statement

42 This paper does not require regulatory impact analysis.

Climate Implications of Policy Assessment

43 A Climate Implications of Policy Assessment is not required. Any emissions changes resulting from this work would likely be accounted for in the country in which the activity takes place.

Population Implications

44 N/A.

Human Rights

45 The proposals in this paper are consistent with the Human Rights Act 1993 and New Zealand Bill of Rights Act 1990.

Consultation

46 The Department of the Prime Minister and Cabinet (Policy Advisory and National Security Groups) and Treasury have been consulted in the preparation of this paper.

Communications

47 No specific media release is intended, but Aotearoa New Zealand's contributions on individual programme aspects will be profiled over the duration of the project.

Proactive Release

48 This paper will be released proactively within 30 days, including any redactions as appropriate under the Official Information Act 1982.

Recommendations

49 The Minister of Foreign Affairs recommends that the Committee:

- 49.1 **note** that in April 2021, Cabinet approved ^{s9(2)(i), s9(2)(j)} as total expenditure from all funding sources for the Solomon Islands Provincial Airfield Upgrades [CBC-21-MIN-0043];

- 49.2 **note** that the Solomon Islands Provincial Airfield Upgrades is led and managed by Aotearoa New Zealand, and that total planned expenditure within the mandate at recommendation [49.1] comprises:
- a) Aotearoa New Zealand's financial contribution of ^{s9(2)(i), s9(2)(j)} (from within the International Development Cooperation allocation within Vote Foreign Affairs);
 - b) Australia's financial contribution of ^{s9(2)(i), s9(2)(j)}
 - c) Solomon Islands' financial contribution of SB\$21 million.
- 49.3 **note** that cost increases to the Solomon Islands Provincial Airfield Upgrades to date have been managed within the existing funding mandate but that is no longer possible and the limit of the funding mandate will be reached in the short term;
- 49.4 **approve** ^{s9(2)(i), s9(2)(j)} as the revised total expenditure from all funding sources for the Solomon Islands Provincial Airfield Upgrades activity, which will continue to be managed by Aotearoa New Zealand,
- 49.5 **note** that the new mandate cost increase would be met by increasing our contribution from within the International Development Cooperation allocation within Vote Foreign Affairs, seeking further contributions from ^{s6(a)} development partners, or a combination of these.

Authorised for lodgement

Hon Nanaia Mahuta

Minister of Foreign Affairs

Appendices

Appendix 1: Forecast total cost increases at activity completion

Contract	Original Contract Price at initiation (NZ\$)	Current Price including approved and pending variations ⁵ (NZ\$)	Forecast Total Contract Price at Completion (NZ\$)	Commentary on cost increases
Civil works (Downer New Zealand)	s9(2)(i), s9(2)(j)	s9(2)(i), s9(2)(j)	s9(2)(i), s9(2)(i)	<p>Elements of the civil works contract that have already incurred price increases include bitumen, fuel, airfares, construction materials, and shipping. Significant foreign exchange rates fluctuations and time delays have also contributed.</p> <p>s9(2)(i), s9(2)(j)</p>
Engineer to Contract (AECOM)	s9(2)(i), s9(2)(j)	s9(2)(i), s9(2)(j)	s9(2)(i), s9(2)(i)	<p>The ‘Engineer to Contract’ portion has already incurred cost increases as a result of time delays and increased labour inputs. AECOM has also been engaged for additional Separable Portions.</p> <p>s9(2)(i), s9(2)(j)</p>
Safeguarding and Implementation	s9(2)(i), s9(2)(i)	s9(2)(i), s9(2)(i)	s9(2)(i), s9(2)(i)	<p>The Safeguarding and Implementation contracts have incurred cost delays due to increased safeguarding requirements during Unexploded</p>

⁵ As at 23 May 2023.

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				Ordnance clearance, as well as increases to travel costs including fuel and airfares. s9(2)(i), s9(2)(j)
Other minor contracts	s9(2)(i), s9(2)(j)	s9(2)(i), s9(2)(j)	s9(2)(i), s9(2)(j)	These are historical contracts. No further increases are forecast.
Contingency				s9(2)(i), s9(2)(j)
Total				

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