MINISTRY OF BUSINESS, INNOVATION & EMPLOYMENT
HĪKINA WHAKATUTUKI

COVERSHEET

Minister	Hon Jenny Salesa	**Portfolio**	Building and Construction
Title of Cabinet paper	Residential Earthquake Prone Building Financial Assistance Scheme	**Date to be published**	17 February 2020

List of documents that have been proactively released		
Date	**Title**	**Author**
28 January 2020	Residential Earthquake Prone Building Financial Assistance Scheme	Office of the Minister of Building and Construction and the Minister of Finance.
28 January 2020	Minute CBC- 20-MIN-0002	Cabinet Office
30 November 2018	Potential funding support for earthquake strengthening.	MartinJenkins

Information redacted **YES**

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Some information has been withheld for the reason of Confidential advice to Government and Commercial information.

In Confidence

Office of the Minister of Finance

Office of the Minister of Building and Construction

Cabinet Business Committee

Residential Earthquake-Prone Building Financial Assistance Scheme

Proposal

1. This paper seeks agreement to settings and parameters for a Residential Earthquake-Prone Building Financial Assistance Scheme, including which government agency will administer the loan scheme, and authorisation to access money appropriated in Budget 2019 for Scheme set-up and delivery.

Executive Summary

2. In July 2017, a new Earthquake-Prone Buildings (EPBs) system came into effect that requires EPBs to be remediated within set timeframes to improve life safety.

3. Without substantial financial assistance, some unit owner-occupiers in Residential Earthquake-Prone Buildings (REPBs) (and some household unit owner-occupiers in mixed use EPBs) are likely to face financial hardship meeting their contribution to remediation costs, and may be forced to sell their home/unit. Concerns about this issue are primarily in areas of high seismic risk, such as Wellington city.

4. Budget 2019 therefore appropriated $23.3 million over four years for a REPB Financial Assistance Scheme (the Scheme). The proposed form of assistance for eligible unit owners is a deferred payment loan with a below market rate of interest. This paper outlines a detailed proposal to enable funding to be drawn down to establish and deliver the Scheme.

5. It is anticipated the Scheme will be ready to issue loans in the first half of 2020. A review of the Scheme's settings is proposed 12 months after launch, along with analysis of Scheme take-up (loans issued) and strengthening costs. The findings will be reported to the Minister for Building and Construction and Minister of Finance.

6. Targeted consultation with Wellington City Council, InnerCity Wellington and the Body Corporate Chairs Group has been carried out by officials and the feedback received has been taken into account in developing these proposals.

7. Subsequent to Budget 2019 it was determined that Kāinga Ora has the potential to set up and deliver this Scheme subject to Ministerial decisions. Kāinga Ora inherited a track record of delivering housing-related financial assistance and was established with broadly enabling legislation that provides for making loans for housing purposes on behalf of the Crown.

8. Free and frank opinions

[redacted]

Background

9. Budget 2019 includes $23.3 million over four years to support the remediation of multi-unit, multi-storey REPBs though a loan scheme. Cabinet approval to a detailed proposal to set up and deliver the scheme is required before any expenditure is incurred (CAB-19-MIN-0174.04 refers).

10. Government's decisions in Budget 2019 follow the implementation of a new national system for managing EPBs that came into effect on 1 July 2017. The new EPB system targets buildings and parts of buildings that pose the greatest risk to life-safety or other property in a moderate earthquake event[1]. Multi-unit, multi-storey residential buildings (i.e. buildings that are two or more storeys high and contain three or more household units) are included in the new EPB system (most residential buildings are excluded).

11. The new EPB system divides New Zealand into three seismic risk areas (high, medium, low) for the purpose of setting timeframes for the identification and remediation of EPBs. Territorial authorities are required to identify most potential EPBs within 5, 10 or 15 years (high, medium, low). Once a building has been determined to be earthquake-prone by a territorial authority, timeframes for remediation for most EPBs are 15, 25 and 35 years respectively (high, medium, low).

12. An engineering assessment of less than 34% of the new building standard (NBS) is an important consideration in determining whether a building is earthquake-prone. The level of work required to EPBs under the new EPB system is so the building is no longer earthquake-prone. This means remediation to at least 34% of the NBS.

13. Wellington City Council undertook a significant amount of work to identify and issue notices for EPBs under the previous EPB system under the Building Act 2004. These EPB notices have been carried forward in the new system and so the remediation timeframes in Wellington are a lot sooner than in other parts of New Zealand.

Some unit owners in REPBs face hardship over earthquake strengthening costs – these concerns are primarily in areas of high seismic risk

14. Remediating an REPB when there are multiple unit owners can be complex. Some individual unit owners in REPBs (and some household unit owners in mixed use EPBs) may face financial hardship meeting their contribution to remediation costs agreed by the majority of body corporate unit owners in their building. This is

[1] A moderate earthquake is defined in regulations as '…an earthquake that would generate shaking at the site of the building that is of the same duration as, but that is one-third as strong as, the earthquake shaking (determined by normal measures of acceleration, velocity, and displacement) that would be used to design a new building at that site if it were designed on 1 July 2017'.

because of the decision making requirements under the Unit Titles Act 2010. These costs can include earthquake strengthening costs plus other non-strengthening works to improve the building.

15. Without financial assistance, some unit owners may be forced to sell their home/unit.

16. Changes to the insurance market and insurance costs following the 2010/11 Canterbury Earthquakes and the 2016 Kaikoura Earthquake, as well as bank lending practices, have also contributed to affordability concerns.

The scale of the issue and cost implications for owners

17. The greatest concern about remediation affordability is in high seismic risk areas, where the timeframes for remediation are the shortest and so property owners have less time to raise the capital required for strengthening. High seismic risk areas include Gisborne, Hawkes Bay, Manawatu, Wellington, Kaikoura, Christchurch and the West Coast.

18. Independent advice from MartinJenkins to Ministry of Business, Innovation and Employment (MBIE) in late 2018 estimates that there are currently 216 REPBs housing 1,261 individual units within the 38 territorial authorities in high seismic risk areas. The number of REPBs could increase ahead of 1 July 2022, because councils have until then to identify all EPBs. Most of the known REPBs/units are located in Wellington city where there are estimated to be 128 buildings housing 1,013 individual units.

19. While the exact number of people facing hardship is unknown, MartinJenkins advised officials that it is reasonable to assume that 5% to 20% of REPB owners in high seismic risk areas could face financial hardship in respect of earthquake strengthening costs. Based on current estimates, this translates to between 63 to 252 unit owners who may face financial hardship.

20. MartinJenkins estimates per-unit strengthening costs for remaining REPBs in Wellington City ranging from $14,000 to $788,000. MartinJenkins also estimates that most units in Wellington city could be remediated for seismic strengthening purposes only for less than $200,000. These estimates are based on building consent data provided by Wellington City Council for earthquake strengthening work that has been undertaken in Wellington. These estimates are considered by some stakeholders, in particular InnerCity Wellington, to not be sufficient for many affected owners.

Financial assistance currently available to owners of REPBs is limited

21. Some territorial authorities provide some owners with limited financial support to assist with earthquake strengthening such as limited rates relief. However, this is not sufficient to ensure unit owners facing hardship are not forced to sell. The Government provides financial assistance to owners of earthquake-prone buildings through the HeritageEQUIP fund. However, this assistance is limited to owners of heritage buildings.

Funding for a REPB Financial Assistance Scheme was included in Budget 2019 to assist unit owners facing hardship over earthquake strengthening

22. Budget 2019 appropriated $23.3 million over four years for the Scheme. Funding appropriated includes $10 million in capital for lending assistance, plus funding for set-up and ongoing administration costs for a loan scheme. Cabinet approval to a detailed proposal to set up and deliver the scheme is required before any expenditure is incurred (CAB-19-MIN-0174.04 refers).

Proposed Scheme objectives

23. The overall objective of the Scheme is to contribute to unit owner-occupier wellbeing by supporting unit owner-occupiers in REPBs (and household unit owner-occupiers in mixed use EPBs) in areas of high seismic risk that are facing hardship in meeting the costs of earthquake strengthening. Supporting eligible owner-occupiers with some costs will help reduce the risk of such owners being forced to sell their homes/units.

24. The Scheme will also further incentivise EPB remediation within statutory timeframes under the Building Act 2004, which has life safety benefits.

A loan scheme is proposed; not a grant or shared equity

25. Budget 2019 approved funding for lending assistance for affected unit owners in REPBs (and household unit owners in mixed use EPBs) as a deferred payment loan with a below market rate of interest. Because the Scheme supports the private retention of home ownership over a long period of time, an affordable loan is an appropriate form of assistance. It also avoids contention around the role of government in body corporate decisions and creating additional ongoing Crown obligations.

26. A non-repayable grant would need to be at a much lower financial level and would not adequately address the affordability issues facing affected unit owners. A small grant is also unlikely to create further incentives to strengthen REPBs or improve a borrower's capacity to repay a commercial loan. A grant also involves a transfer of taxpayer funded wealth to private property owners. A grant scheme would also be inequitable for those who have already strengthened their buildings.

27. Shared equity is generally intended to assist buyers into affordable home ownership, not for building improvements. The size of the potential equity share could create issues around existing mortgages, relationship property, the treatment of levies, insurance, council rates, maintenance.

Proposed Scheme settings

28. The proposed settings aim to balance fairness to taxpayers by minimising unnecessary wealth transfers to building and home owners. The proposed loan scheme settings are outlined in four tables, on the following pages.

Scheme Settings on owner eligibility (including hardship)

29. MBIE and the Treasury examined the hardship approaches of Inland Revenue (income tax hardship and KiwiSaver); Kāinga Ora (formerly Housing New Zealand), Ministry of Health, Ministry of Social Development and Wellington City Council Housing. As they use strict asset/income testing they are not suitable for people who own property.

30. We propose that applicants demonstrate that they cannot get finance from a lender as the key hardship indicator. Without financial help it is probable that sale, voluntary or forced, will result. Table 1 outlines the proposed eligibility criteria for determining what unit owners should be eligible for the Scheme.

Table 1: Owner eligibility (including hardship)

No.	Recommended proposal	Rationale
1	The unit owner cannot obtain finance covering the full seismic retrofit cost from one of the Reserve Bank of New Zealand registered bank or non-bank deposit takers; *Or*	• Only banks with appropriate standing and repute are permitted to be registered banks. • Reserve Bank registered lenders will best know the owner's investment position. • Minimises risk of fraud with lenders operating under 'know your customer' policies. • Enables the Scheme to 'top up' partial finance offered by banks and non-banks. • Simple to identify hardship if the owner cannot get a loan. • Filters out those of means from those who genuinely cannot obtain finance.
	If offered a loan from a registered bank or non-bank deposit taker, the owner is required to sell their unit when the building is no longer earthquake prone as part of the loan condition; *Or*	• While some lenders may approve finance for seismic retrofit, some loans could be conditional on the unit's sale when the seismic work is finished. • Forced sale is hardship and this proposal will prevent unit owners from having to sell after seismic retrofit has been completed.
	If offered a loan from a registered bank or non-bank deposit taker, it would cause significant financial hardship.	• There may be a small group of people who can obtain finance for seismic retrofit, however this would cause the unit owner significant financial hardship.
2	A unit owner must be a New Zealand Citizen; ordinarily resident in New Zealand or an overseas person	• A common theme of public assistance is a citizenship or residency requirement. • Overseas persons allowed under the *Overseas Investment Act 2005* are

	allowed under the *Overseas Investment Act 2005*.	Australian and Singaporean citizens, who are authorised to purchase property in New Zealand. • Maintains consistency with recent changes to the *Overseas Investment Act 2005.*
3	The unit owner must be an owner-occupier of that unit for the duration of the loan.	• This is to ensure that the loan is not available to residential property investors. Investment in residential property is essentially a commercial undertaking and if the owner is unable to raise the finance to strengthen the building, they have the option to sell their property (without losing their home).
4	The unit owner is required to have an adequate credit history.	• Prevents the Crown issuing loans to people who are a poor credit risk (i.e. facing a court order or are insolvent). Ensures applicants as a minimum are not: o in default of a mortgage, charge, or another security; o subject to a Court Order or Tenancy Tribunal Order. • A consumer credit report checks basic creditworthiness to minimise the Crown's risk exposure and maintain public confidence in the Scheme.
5	In all cases where owner eligibility criteria are unfulfilled, the applicant would be able to seek discretion from the Chief Executive of Kāinga Ora over the determination of hardship.	• To address unforeseen circumstances, some flexibility on unit owner eligibility is needed to fulfil the Schemes objectives. • The Chief Executive of Kāinga Ora would have discretion over matters such as illness/sickness, job loss etc.

Scheme settings on unit and building eligibility

31. We propose that the Scheme is limited to units purchased before 1 July 2017. This is because the owners purchasing units after this date should be fully aware of the current EPB remediation requirements. Table 2 outlines the proposed unit and building eligibility requirements.

Table 2: Unit and building eligibility

No.	Recommended proposal	Rationale
6	The Scheme is limited to units: • purchased before 1 July 2017; *and*	• Owners purchasing units after this date should be fully aware of EPB remediation requirements.
	• within a building in an area of high seismic risk, which is two or more storeys in height and contains	• References definitions in the *Building Act 2004* and ensures hostels and boarding houses are not covered.

	three or more household units (or is a household unit within a mixed use building); *and*	Also clarifies that household units in mixed use earthquake-prone buildings are covered. • Limits the Scheme to areas of high seismic risk only, reflecting where concerns have primarily arisen.
	• within a building subject to a territorial authority-issued EPB notice.	• An EPB notice must be issued once a territorial authority has determined a building is earthquake-prone. • This prevents building owners 'self-declaring' what is earthquake prone in order to access the Scheme.

Loan settings for the Scheme

32. It is proposed that loans are only to fulfil seismic retrofit requirements to achieve seismic performance up to 100% NBS. Table 3 outlines the proposed loan settings and other important terms and conditions to operationalise the Scheme.

Table 3: Loan settings

No.	Recommended Proposal	Rationale
7	Loans are for only for seismic retrofit to achieve seismic performance *up to* 100% NBS.	• The new EPB system requires works to be carried out so that a building is no longer earthquake prone (i.e. this means remediation to at least 34% NBS). While strengthening is possible to more than 100% NBS, this does not relate to any legislative requirement under the Building Act. • Loans are only for direct retrofit construction costs and reinstatement up to current Building Code requirements, engineering costs related to an agreed repair plan and other costs that may be required by regulation, e.g. fire safety upgrades and upgrades for people with disabilities. • Excluded costs are personal (e.g. accommodation), retrospective (e.g. work already done), and anything that increases a building's capital or amenity value beyond seismic work (e.g. adding extra units, additional balconies, or extra carparks). • Aligns with the objectives of the Scheme to help those in or facing hardship with the actual cost of seismically strengthening their unit.
8	The maximum loan secured against any one unit would not exceed $200,000 (but with discretion for the	• The proposed cap fits within the Budget envelope and means *at least* 50 loans could be issued.

	Chief Executive of Kāinga Ora to approve amounts above this level on a case-by-case basis).	• MartinJenkins estimates a cap of this size should provide for most units (using Wellington City Council provided information). Subsequent discussions with Wellington City Council also suggest this. • A cap prevents a small number of very large loans denying the majority access to finance. • The proposal allows for flexibility to go above the proposed cap on a case-by-case basis (e.g. if unit strengthening costs were $250,000).
9	Loans become repayable: • On the unit's sale or disposal. • 12-months after the last owner's death. • Borrower default. • If the unit owner is no longer an owner-occupier	• The Crown expects loans will be repaid and repayment triggers relate to the unit's disposal, death of the owner (the time proposed ensures that the loan cannot be legally challenged) and where the borrower defaults (e.g. personal insolvency or obtaining a loan by deception). • Aligns with event based triggers found in similar commercially offered loan products. • The Crown also expects the loan to be repaid if the unit owner is no longer an owner-occupier and has effectively become a residential investor.
10	Provides for voluntary loan repayment (with no early repayment fees).	• Allowing borrowers to make periodic or lump sum voluntary repayments is standard for any loan. • Borrowers can voluntarily repay loans to reduce its impact up to when their unit is disposed of.
11	The Scheme will not pursue negative equity.	• Depending on market conditions, there is a risk that loans (scheme and mortgages) may see the unit worth less than what is owed. • The Scheme will remit what is owed (principal and interest) after the sale of the unit to avoid negative equity.[2] • Being more generous will likely only benefit other creditors.
12	The Scheme will comply with the *Credit Contracts and Consumer Finance Act 2003* (*CCCFA*).	• Broadly the *CCCFA* provides general rules of credit contracts and sets out disclosure requirements. • The *CCCFA* puts an obligation on lenders to ensure that borrowers make

[2] Inland Revenue has advised that the remitted loan would be considered as taxable income for the borrower.

		informed borrowing choices before they sign a loan agreement.
13	The obligations under the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (AML Act) and the Financial Services Providers (Registration and Dispute Resolution) Act 2008 (FSP Act) will be met.	• MBIE as a Schedule 1 SSA listed entity is exempt from the AML Act and FSP Act. • Kāinga Ora is not exempt from the AML Act and may be required to apply for an exemption to the AML Act. Kāinga Ora already has an exemption for the First Home grant and Tenant Home Ownership grant, Housing Innovation Fund and Loan Administration Services. See https://www.gazette.govt.nz/notice/id/2018-go5514
14	Loans would be secured by a mortgage, charge, or another security against the unit's record of title (or equivalent).	• Building insurance (a Unit Titles Act requirement for body corporates), is a common condition that is tagged to mortgage-like loans. • Without this loans would be unsecured. • Protects the Crown's interests by having security over the unit, albeit, ranking behind any existing security (e.g. mortgages) and insurance.
15	Applications to the Scheme would close on 30 June 2027.	• This is considered to be a reasonable time for unit owners in high seismic risk areas to respond, taking EPB identification timeframes into account. It also incentivises owners to apply and remediate their buildings within statutory timeframes.
16	Successful applicants to pay half of the actual cost of establishing the loan (establishment fee) to a maximum of $500.00.	• A fee partially meets loan costs including property valuation, assessing the application, legal and security interest registration. • A fee is common with property loans and would be capped at $500.00 (and subtracted from what is borrowed). Indicative costs include: o valuation ($500-$800) o Mortgage Priority Instrument ($80-$176). • Establishment fees are consistent with loans e.g. Energy Efficiency and Conservation Authority (EECA) charges 10% on Crown Loans while registered banks charge between $0 (KiwiBank) to $500 (ANZ).

17	Scheme settings to be reviewed 12-months after becoming operative.	• Scheme settings reviewed and if necessary, changed to ensure it is working as envisaged. • Ensures the proposed settings are working for unit owners and taxpayers.

Interest rate settings for the Scheme

33. We have looked into three options for interest rate settings. These were interest free; a fixed interest rate for the Scheme's entire duration; and a below market rate of interest loan with five-yearly review.

34. An interest free loan could be seen as an implicit subsidy to private property owners and provides no incentive to repay. This approach would be costly for taxpayers and is inconsistent with the interest rate concessions appropriated in Budget 2019. Charging an interest rate also aligns with what was appropriated in Budget 2019.

35. We propose a below market rate of interest. The actual rate of interest would be based on a discount applied to the Reserve Bank's rolling monthly average of five-year fixed interest residential mortgage. We consider that this approach offers the best mix of affordability and certainty for owners while incentivising repayment. Over the life of the scheme it would make allowance for loan defaults and writing off loans if there is insufficient equity.

36. Under these settings and if set in December 2019, the interest rate would be 3.70% per annum. Some major banks are currently offering fixed rates at around 3.50%. However, there is not a like-for-like comparison. The headline rates advertised by banks are not available for low-equity loans (which this scheme proposes), are fixed for a shorter period of time, and are generally only available to new customers.

37. Table 4 outlines the proposed interest rate settings for the scheme and the rationale.

Table 4: Interest rate settings for the Scheme

No.	Recommended Proposal	Rationale
18	A below market rate of interest set at 60% of the sum of: • the Reserve Bank's monthly average of five-year fixed interest rates; and • a low-equity margin of 1.25%.	• The Scheme Interest Rate aligns with the interest rate concession appropriated in Budget 2019 and relies on the Reserve Bank's monthly B20 Statistics (five-year fixed interest rates). • A low equity margin reflects that Scheme borrowers are a higher risk because their regular lender is not prepared to lend to them (fully or partially). • Provides a rate of interest that is below the market. For example, if a loan was taken out in December 2019, the Scheme Interest Rate would be 3.70%, compared to the RBNZ recorded average five-year fixed rate of 4.91%.

		• The proposed interest rate balances affordability for borrowers while ensuring that taxpayers will have the $10m loan capital repaid in the long term taking into account inflation, loan defaults and loan remissions arising from negative equity. • The proposal recognises that some eligible borrowers may be on low, fixed or variable income and that they are unlikely to afford a truly market-based interest rate for low equity loans.
19	Interest rates are fixed for five-years with rate reviews at loan anniversary; *and*	• Keeps the rate of interest aligned with market trends over time with certainty for borrowers and the Crown alike. • At the end of five-years the rate is reviewed and re-fixed for the next five-years • Concessions calculated on Multi-Year Appropriation basis reflecting the long term nature of the Scheme. • Simplifies loan administration. • The Crown can budget for future concessions.
	Interest rates will be calculated daily and compound annually.	• Interest is calculated daily to minimise interest costs when a loan is repaid but is compounded annually, to reduce the overall cost of the loan upon borrowers. • Simple but fair way to calculate loan interest rates, especially when loans are being repaid to a particular day.

Scheme implementation and review

38. Cabinet agreed that expenditure will not be incurred until it has approved a detailed proposal (CAB-19-MIN-0174.04 refers).

39. It is not practical for the 38 territorial authorities in high seismic risk areas to administer individual loan schemes, Commercial Information

40. After considering the matter, we propose that Kāinga Ora deliver this Scheme on behalf of the Crown. This proposal is consistent with the objectives of the Scheme, which are to enable eligible unit owners to sustain home ownership and avoid the loss or forced sale of their homes.

41. Kāinga Ora already administers financial products on behalf of the Crown. It has a financial products team and its portfolio includes the First Home grant, First Home Loan and Kāinga Whenua Loan scheme, as well as Tenant Home Ownership. Kāinga Ora confirms that it has existing expertise, staff and systems that it could build off (though it would have to hire some new staff). Conversely, another agency

would have to recruit a new team and grow the necessary skills, capabilities and expertise and develop the loan documentation and systems for the Scheme.

42. Under Section 13 (1) of the *Kāinga Ora* – Homes and Communities Act 2019*,* Kāinga Ora, on behalf of the Crown, is able to *"to provide people with home-related financial assistance; and to make loans, or provide other financial assistance, to local authorities and other entities for housing purposes"*. In addition, section 13(1) of the Act also states that the entity has a function to *"provide housing or services related to housing as agent for the Crown or Crown entities".*

43. Kāinga Ora has agreed to deliver and manage the scheme. This is supported by Minister of Finance, Minister of Housing and Minister for Building and Construction. Kāinga Ora indicated that they can deliver the Scheme cost effectively while still providing its core services.

44. Free and frank opinions

45. Following confirmation from Cabinet that Kāinga Ora will deliver the Scheme, we will change the existing appropriations to non-departmental so the Scheme can be delivered using the appropriated funding in Vote Building and Construction.

46. It is further proposed that the Scheme settings be reviewed 12-months after launch, along with analysis of Scheme take-up (loans issued) and strengthening costs. This is to be reported back to the Minister for Building and Construction and the Minister of Finance.

47. Confidential advice to Government

Consultation

48. The following agencies were consulted on the proposals in this paper: Department of the Prime Minster and Cabinet, Reserve Bank of New Zealand, Inland Revenue, Ministry of Housing and Urban Development, Kāinga Ora, Ministry of Social Development (Office for Seniors and Office for Disability Issues), and the Department of Internal Affairs, Ministry for Culture and Heritage.

49. The following external stakeholders were consulted: Body Corporate Chairs Group, InnerCity Wellington, and Wellington City Council.

50. Overall, Wellington City Council was broadly supportive of the key elements of the scheme. They considered that the financial cap of $200,000 per unit should be enough to support strengthening of 80%-90% of affected units.

51. InnerCity Wellington and the Body Corporate Chairs Group feedback centred on the flexibility of the Scheme, including on the level of assistance available per unit and what costs could be funded by the assistance.

52. InnerCity Wellington and the Body Corporate Chairs Group considered that there needed to be more flexibility on the financial cap on the loans. A concern was also raised that the cut-off date for applications (10 years from the commencement of the new EPB system) was too short. Officials consider that the proposed 12-month review of Scheme settings is the appropriate time to look at these issues.

53. InnerCity Wellington and the Body Corporate Chairs Group also raised concerns about alternative accommodation costs, and other costs such as legal fees and insurance. As noted earlier in this paper, these costs are not intended to be covered by this assistance package.

Financial Implications

54. In Budget 2019, $23.3 million ($10.0m capital, $13.3 million operating) was appropriated for the scheme's loan capital, administration and concessionary element. Treasury's view is that, similar to other loans funded by the Crown, the concessionary element of this scheme should be appropriated, but not counted against Budget allowances. This is to avoid "double counting" the cost of the loan, as the $10 million of capital funding has already been counted against the Budget allowance.

55. As market rates will fluctuate as individual loans are settled, the concessionary amount that should be appropriated for the scheme will change to reflect the current value of the interest concession. We propose that Cabinet delegate authority to the Minister for Building and Construction and the Minister of Finance to amend the appropriated concessionary amount as necessary to reflect changes in market rates and the quantum of loan capital issued. No funding will be required for variations in the concessionary element; as noted above, changes in the value of the concessionary element of the Scheme are not counted against Budget allowances.

56. Given increased certainty about operational funding requirements, but noting the remaining uncertainty about when loan funding will be drawn down, we propose to establish two multi-year appropriations (MYAs) and one annual appropriation within Vote Building and Construction and transfer the funding from the existing multi-category appropriation. The MYAs will run from 1 February 2020 to 30 June 2024 for loan capital and the concessionary operating appropriation. The annual appropriation will be for Scheme setup and administration.

Legislative Implications

57. There are no legislative implications from this proposal.

Human Rights, Gender Implications and Disability Perspective

58. The proposals in this paper have no implications under the New Zealand Bill of Rights Act 1990 or the Human Rights Act 1993. There are no gender implications arising from this paper. Upgrades for people with disabilities that may be required under the Building Act 2004 when strengthening is carried out are within scope of proposed loan funding, and the funding may help support these being carried out (where these are required).

Publicity and Proactive Release

59. We intend to issue a press release to mark the Scheme entering detailed design after Cabinet decisions are made.

60. We propose that this Cabinet paper, associated minutes and a background report from MartinJenkins (November 2018) are proactively published on MBIE's website subject to any necessary redactions.

Recommendations

1. **Note** that Budget 2019 appropriated $23.3 million in funding ($10.0m capital, $13.3 million operating) to set up and deliver the Residential Earthquake-Prone Building Financial Assistance Scheme (CAB-19-MIN-0174.04 refers);

2. **Note** that the Minister for Building and Construction was required to provide Cabinet with a detailed proposal for Scheme set up and delivery before expenditure is incurred);

Owner eligibility, including hardship

3. **Agree** that there will be eligibility criteria for this Scheme, including for hardship;

4. **Agree** hardship is defined for this Scheme as:

    4.1 the inability of a unit owner(s) to obtain finance for EPB seismic retrofit from a Reserve Bank of New Zealand registered bank or non bank deposit taker; or

    4.2 where finance from one of the above entities can be obtained it is conditional upon the unit being sold when the building is no longer earthquake prone; or

    4.3 where finance from one of the above entities can be obtained, but would cause the owner significant financial hardship;

5. **Agree** a unit owner must be a New Zealand Citizen, those ordinarily resident in New Zealand, or overseas persons allowed under the *Overseas Investment Act 2005*;

6. **Agree** that a unit owner must be an owner-occupier of that household unit for the duration of the loan;

7. **Agree** applicants must have an adequate credit history to reduce Crown risk**;**

8. **Agree** that the Chief Executive of Kāinga Ora, will have discretion to approve loans that would otherwise fall outside of agreed owner eligibility criteria;

Unit and building eligibility

9. **Agree** that the scheme is limited to units purchased before 1 July 2017;

10. **Agree** that the unit must be within a building in an area of high seismic risk and which is two or more storeys and contains three or more household units (or is a household unit within a mixed use building);

11. **Agree** that the unit must be within a building subject to a territorial authority issued earthquake-prone building notice**;**

Loan settings

12. **Agree** that the loans are only for seismic retrofit to achieve seismic performance up to 100% of the new building standard (NBS)**;**

13. **Agree** that the maximum loan secured against any one unit would not exceed $200,000 (but with limited discretion for the Chief Executive of Kāinga Ora to approve amounts above this level on a case-by-case basis);

14. **Agree** that loans become repayable on the unit's sale, 12 months after the last owners death, if the owner is no longer an owner-occupier or if the borrower defaults**;**

15. **Agree** that the loan provides for voluntary loan repayments (with no early repayment fees);

16. **Agree** that the Scheme will not pursue negative equity (the scheme will remit what is owed from the point where negative equity is reached);

17. **Note** that the scheme will comply with the Credit Contracts and Consumer Finances Act 2003;

18. **Note** that the obligations under the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 and the Financial Services Providers (Registration and Dispute Resolution) Act 2008 will be met**;**

19. **Agree** that loans will be secured by a mortgage, charge, or another security against the unit's record of title (or equivalent);

20. **Agree** that applications to the Scheme will close on 30 June 2027;

21. **Agree** that successful applicants to pay half of the actual costs of establishing the loan (establishment fee) to a maximum of $500.00**;**

22. **Agree** that the scheme settings will be reviewed 12 months after becoming operative**;**

Interest rate settings for the Scheme

23. **Agree** that a below market rate of interest is set on the loans;

24. **Note** that the below market interest rate for the Scheme would be set at 60% of the sum of the Reserve Banks monthly average of five year fixed interest rates and a low equity margin of 1.25%;

25. **Agree** that the interest rates are fixed for five years with rate reviews at loan anniversary and interest rates will be calculated daily and compound annually;

Implementation effectiveness and review

26. **Note** that Minister of Finance and Minister for Building and Construction consider that Scheme effectiveness is best met by Kāinga Ora establishing and delivering this Scheme on behalf of the Crown;

27. **Note** that the Kāinga Ora Establishment Board has considered its proposed role and agrees to provide a delivery service under this scheme, if required;

28. **Agree** that Kāinga Ora will establish and deliver this Scheme on behalf of the Crown;

29. **Note** that if Cabinet agrees that Kāinga Ora will deliver the Scheme that the existing appropriations will be changed to non-departmental so the Scheme can be delivered using the appropriated funding in Vote Building and Construction;

30. **Agree** that the Scheme settings, including operating costs, be reviewed 12-months after launch, along with analysis of Scheme take-up (loans issued) and strengthening costs, with this to be reported back to the Minister for Building and Construction and the Minister of Finance;

Financial implications

31. **Agree** to establish new appropriations in Vote Building and Construction as set out below with effect from 1 February 2020 to 30 June 2024:

Vote	Appropriation Minister	Title	Type	Period	Scope
Building and Construction	Minister for Building and Construction	Residential Earthquake-Prone Building Financial Assistance Scheme Loan Capital MYA 2019 - 2024	Non-Departmental Capital Expenditure	Five year multi-year appropriation 2019/20 to 2023/24	This appropriation is limited to providing loans approved within the Residential Earthquake-Prone Building Financial Assistance Scheme.
Building and Construction	Minister for Building and Construction	Residential Earthquake-Prone Building Financial Assistance Scheme Loan Concession MYA 2019 - 2024	Non-Departmental Other Expenses	Five year multi-year appropriation 2019/20 to 2023/24	This appropriation is limited to the expense incurred in unwinding the discount rate used in the present value calculation of the loans within the Residential Earthquake-Prone Building Financial Assistance Scheme.
Building and Construction	Minister for Building and Construction	Residential Earthquake-Prone Building Financial Assistance Scheme - Set Up and Administration Costs	Departmental Output Expenses	Annual appropriation	This appropriation is limited to the set-up costs and ongoing administration costs of the Residential Earthquake-Prone Building Financial Assistance Scheme.

32. **Approve** the following changes to appropriations to give effect to the policy decisions above, with no impact on the operating balance and net core Crown debt over the forecast period:

	$m – increase/(decrease)				
	2019/20	2020/21	2021/22	2022/23	2023/24 & Outyears
Vote Building and Construction Non-Departmental capital Expenditure	10.000				

Residential Earthquake-Prone Building Financial Assistance Scheme Loan Capital MYA 2019 - 2024 (funded by revenue Crown)					
Vote Building and Construction Non-Departmental capital Expenditure Residential Earthquake-Prone Building Financial Assistance Scheme MCA Residential Earthquake-Prone Building Financial Assistance Scheme Loan Capital (funded by revenue Crown)	(5.000)	(5.000)	-	-	-
Vote Building and Construction Non-Departmental other expenses Residential Earthquake-Prone Building Financial Assistance Scheme Loan Concession MYA 2019 - 2024 (funded by revenue Crown)	4.800				
Vote Building and Construction Non-Departmental other expenses Residential Earthquake-Prone Building Financial Assistance Scheme MCA Residential Earthquake-Prone Building Financial Assistance Scheme Loan Concession (funded by revenue Crown)	(2.400)	(2.400)	-	-	-
Vote Building and Construction Departmental output expenses Residential Earthquake-Prone Building Financial	3.000	2.500	1.500	1.500	1.500

Assistance Scheme - Set Up and Administration Costs (funded by revenue Crown)					
Vote Building and Construction Departmental output expenses Residential Earthquake-Prone Building Financial Assistance Scheme MCA Residential Earthquake-Prone Building Financial Assistance Scheme - Set Up and Administration Costs (funded by revenue Crown)	(3.000)	(2.500)	(1.500)	(1.500)	(1.500)

33. **Agree** that the proposed changes to appropriations for 2019/20 set out above be included in the 2019/20 Supplementary Estimates and that, in the interim, the increases be met from Imprest Supply;

34. **Note** if Cabinet agrees that Kāinga Ora will deliver and establish the Scheme on behalf of the Crown then the appropriations for Scheme set up and administration shown in recommendation 32 will be changed to include the cost savings as shown in the table below, and savings achieved will be returned to the Crown:

	2019/20	2020/21	2021/22	2022/23
Cost reduction ($m)	0.750	0.750	0.375	0.375
Percentage saving	25%	30%	25%	25%

35. **Note** that the indicative funding profile for the new two multi-year appropriations described above is as follows:

	$m – increase/(decrease)				
Indicative annual spending profile	2019/20	2020/21	2021/22	2022/23	2023/24 & Outyears
Residential Earthquake-Prone Building Financial Assistance Scheme Loan Capital MYA (funded by revenue Crown)	5.000	5.000	-	-	-
Residential Earthquake-Prone Building Financial Assistance Scheme Loan Concession MYA (funded by revenue Crown)	2.400	2.400	-	-	-

36. **Agree** to delegate responsibility for updating the appropriated concessionary component of the Scheme to reflect changes in market rates and the quantum of loan capital issued to the Minister of Finance and Minister for Building and Construction;

37. **Authorise** the expenditure of money appropriated in Budget 2019 by Kāinga Ora for the purpose of setting up and delivering the scheme;

38. **Authorise** the Deputy Chief Executive Finance of Kāinga Ora to approve changes to the proposed Scheme settings and parameters that are consistent with the proposals in this paper**.**

Authorised for lodgement

Hon Grant Robertson
Minister of Finance

Hon Jenny Salesa
Minister for Building and Construction