MINISTRY OF HOUSING AND URBAN DEVELOPMENT

Briefing

Developing the Government's progressive home ownership scheme			
Date:	30 October 2019	**Security level:**	In Confidence
Priority:	Medium	**Report number:**	BRF19/20100449

Action sought

	Action sought	Deadline
Hon Dr Megan Woods **Minister of Housing**	**Agree** to the recommendations	4 November 2019
Hon Kris Fa'afoi **Associate Minister of Housing (Public Housing)**	For your information	N/A
Hon Nanaia Manuta **Associate Minister of Housing (Māori Housing)**	For your information	N/A

Contact for discussion

Name	Position	Telephone		1st contact
Caleb Johnstone	Manager, Market & Supply Responses	N/A	s 9(2)(a) [redacted]	
Joanna Gordon	Policy Director, Housing and Urban Settings	N/A	[redacted]	✓
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Other agencies consulted

The Treasury

Minister's office to complete

- ☐ Noted
- ☐ Seen
- ☐ Approved
- ☐ Needs change
- ☐ Not seen by Minister
- ☐ Overtaken by events
- ☐ Declined
- ☐ Referred to (specify)

Comments

Date returned to MHUD:

Briefing

Developing the Government's progressive home ownership scheme

For: Hon Dr Megan Woods, Minister of Housing

Date:	30 October 2019	**Security level:**	In Confidence
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Purpose

1. This briefing seeks your direction on the target cohort/s for the Progressive Home Ownership Fund, the delivery channel that will be used to assist each target cohort, and on the fiscal implications of the Fund for Budget 2020.

Executive summary

2. Cabinet invited you to report back by the end of the year on the high level approach and design features of the Government's Progressive Home Ownership scheme.

3. The design of the Progressive Home Ownership Fund depends on your choice of cohort/s and delivery channel/s. This briefing seeks your decisions on:

   a. potential cohorts that the Progressive Home Ownership Fund could target

   b. the types of Progressive Home Ownership scheme that we continue to investigate

   c. extending the timeframe allowed for households to graduate to full home ownership from 10 years or 15 years, and how to address the subsequent fiscal and budgetary implications of these decisions through Budget 2020.

4. We consider that the Progressive Home Ownership Fund could be most effectively used to support two cohorts, using different channels:

   - households that are unlikely to buy a home without significant support from the Government, including non-financial support. We consider these households would be best supported through expanding schemes offered by providers who are competent in this area.

   - households that cannot get a large enough deposit together to buy a home, due to high rents and fast-growing house prices, and/or have insufficient income to service a low deposit mortgage at current house prices. We consider these households would be best supported through a Government scheme direct to households.

5. To ensure most effective targeting of the Fund, we intend to take a place-based approach, as markets (and therefore affordability) vary in different locations. This means that the settings for the Government scheme, and the mix of cohorts and channels, is likely to vary according to location.

6. Under a place-based approach, we will assess the relevant need against cohorts A and B for each place. For Cohort B, we will adjust the settings for the Crown scheme to reflect the need for Government support in that location.

7. For Cohort A, we will engage providers that already operate in a location[1], starting with providers that are ready to deliver and have an existing customer base. Over time, we will expand the number of providers to ensure that providers who can work with particular customer groups, or in particular locations, are included.

8. Our analysis shows that the 10 year timeframe for recycling funding, required for the Fund to be fiscally neutral, would significantly limit the number of households in the cohorts above that can be helped through the Fund. The concession costs associated with a 10 year timeframe would be around $316 million (undiscounted) and will need to be funded through Budget 2020.

9. However, extending this timeframe to 15 years, as suggested in this paper, would enable the Fund to support more households into home ownership. This will have implications for the fiscal neutrality of the Fund.

10. At this point there are two options:

    1) The Minister of Finance has the ability to change the 10 year timeframe for fiscal neutrality, and we propose you seek agreement from the Minister of Finance and Cabinet, through the December report back, to extend fiscal neutrality to 15 years in this specific case.

       Under this option the principal $400 million will be considered fiscally neutral, but concession costs will still need to be funded through a Budget 2020 bid. Further work is needed to identify this cost over 15 years, but early estimates are that this could be around $558 million (undiscounted).

    2) The principal $400 million is not considered fiscally neutral. A Budget 2020 bid would then be needed to account for the $400 million as a capital allowance. In this case concession costs do not need to be funded.

11. Regardless of which option is chosen, the scheme will have establishment, administration and other operating costs (such as any wrap around support to households) that will need to be funded through a Budget 2020 bid. Early estimates are in the range of $33 million to $80 million.

12. As a result of scheme design, further operating costs are likely to be identified depending on the specifics of the design. For example, costs would vary dependent on whether the Crown takes a fixed dollar amount or a percentage of equity share as households graduate from the scheme. We are unable to estimate these costs until the design is finalised in early 2020.

13. We will continue to work with the Treasury to identify the final costs, and on the budget and fiscal impacts of the Fund, to inform the Cabinet report back.

Recommended actions

14. The Ministry of Housing and Urban Development (HUD) recommends that you:

    1. **Note** that Cabinet has agreed that the funding be set aside for a Progressive Home Ownership Fund and that we will continue to investigate parameters for a Fund that will support schemes through two channels: *Noted*

       1.1. the expansion of progressive home ownership schemes currently offered by community housing providers, iwi and Māori organisations and financial institutions; and

[1] Our procurement approach will include establishing a list of providers at a national level, noting for example where they operate and whether they target particular groups such as Māori or Pasifika.

1.2. direct provision of progressive home ownership schemes by the Crown.

Cohorts to be supported by progressive home ownership

2. **Note** that the Progressive Home Ownership Fund could be targeted to one or more of the following cohorts: *Noted*

   2.1. **Cohort A:** Households that are unlikely to buy a home without significant support from the Government, including non-financial support;

   2.2. **Cohort B:** Households that cannot get a large enough deposit together to buy a home, due to high rents and fast-growing house prices, and/or have insufficient income to service a low deposit mortgage at current house prices; and

   2.3. **Cohort C:** Households that are not home owners yet but who would be able to achieve home ownership without government assistance.

3. **Direct** officials to continue to investigate how the Progressive Home Ownership Fund can assist:

   3.1. Cohort A through the expansion of progressive home ownership schemes currently offered by community housing providers, iwi and Māori organisations, and financial institutions; and *Agree / Disagree*

   3.2. Cohort B through the direct provision of progressive home ownership schemes by the Crown. *Agree / Disagree*

4. **Agree** that we do not further investigate how the Progressive Home Ownership Fund could be targeted towards Cohort C. *Agree / Disagree*

Type of progressive home ownership

5. **Agree** that for the direct provision of progressive home ownership schemes by the Crown, that we only investigate shared equity schemes (that is shared ownership and second mortgage arrangements). *Agree / Disagree*

6. **Note** that rent-to-buy, leasehold, and deferred settlement schemes would be neither cost effective or administratively simple if delivered through the direct provision of progressive home ownership schemes by the Crown. *Noted*

Factors to consider in designing and operating a scheme

7. **Note** that we are developing factors to consider in the design and operation of the PHO Fund, for high level design and prioritisation. *Noted*

Funding and Budget 2020 considerations

8. **Note** that a Budget 2020 bid is required to fund non-fiscally neutral establishment and administration costs, and to make *Noted*

provision for debt/equity risks, and to pay for any other services that may be considered as part of the detailed design.

9. **Note** that there are two elements of fiscal neutrality: *Noted*

   9.1. Whether the principal $400 million is considered fiscally neutral and over what period (that is, over 10 years or extending the fiscally neutral rule in this case to 15 years)

   9.2. Whether any costs associated with the lending are considered fiscally neutral.

Extending the timeframe for households to graduate into full home ownership, and extending fiscal neutrality *Noted*

10. **Note** that requiring funding to be recycled back to the Crown within 10 years will significantly hinder the effectiveness of the Progressive Home Ownership Fund.

11. **Note** that the Minister of Finance would need to agree to consider that funding recycled back to the Crown within 15 years be fiscally neutral. *Noted*

12. **Agree** to forward this paper to the Minister of Finance and seek a decision from the Minister of Finance and Cabinet to extend fiscal neutrality in the specific case of the Progressive Home Ownership Fund to 15 years. *Agree / Disagree*

Fiscal and budgetary impacts

13. **Note** that if the principal $400 million ***is*** considered fiscally neutral, then concession costs of around $316 million will need to be funded through a Budget 2020 bid (or $558 million if extended to 15 years). *Noted*

14. **Note** that (regardless of the recycling timeframe) if the principal $400 million ***is not*** considered fiscally neutral, then a Budget 2020 bid would be needed to account for the $400 million as a capital allowance. In this case, concession costs would not need to be funded. *Noted*

15. **Note** that there are likely to be additional operating costs that are dependent on the final scheme design, and that we are unable to estimate these costs until the design is finalised in early 2020. *Noted*

16. **Note** that once you have directed officials on the approach and high-level design, we will work to identify the size of any concessionary costs, in collaboration with the Treasury. *Noted*

Joanna Gordon	Hon Dr Megan Woods
Policy Director, Housing and Urban Settings	**Minister of Housing**
30/10/19	..... / ..... / .....

Cabinet agreed to make $400 million available for a Progressive Home Ownership Fund

15. Cabinet has agreed to make available $400 million in operating funding to support the delivery of progressive home ownership schemes [CAB – 19 – MIN – 0444 refers]. The aim of progressive home ownership schemes is to provide more people with opportunities to own their own home by reducing the deposit requirements and/or the costs of servicing a mortgage.

16. Cabinet also invited you to report back to Cabinet by the end of the year on the high level approach and design features. One of the key aspects of this Cabinet report back includes the cohort that the Progressive Home Ownership Fund (the Fund) will target.

17. Everything else about the design of the Fund depends on your choice of cohort/s and delivery channel/s. In this context, this briefing sets out the:
    a. potential cohorts that the Fund could target
    b. our recommended delivery channels that are best placed to deliver schemes to each cohort
    c. factors to consider in designing and operating a scheme
    d. decisions needed to deliver the Fund, for example on the timeframe allowed for households to graduate to full home ownership (10 years or 15 years), and decisions to address the subsequent fiscal and budgetary implications of these decisions.

Potential cohorts for the Progressive Home Ownership Fund

We have assessed the options for target cohort based on four key criteria

18. In assessing the options for the different target cohorts, we have considered the following key criteria:
    a. Additionality – that Government support will increase the number of households that would not otherwise become home owners and be complementary to existing schemes
    b. Graduation – that households assisted will be able to successfully graduate from the scheme to move in to full home ownership.
    c. Administrative simplicity – that the mechanism to support households is designed in a way that keeps the administration of the scheme as simple as possible for all parties.
    d. Cost effectiveness – that Government provides the greatest benefit to households at minimum cost.

There are three different cohorts that a Progressive Home Ownership Fund could target

19. We consider that there are three different cohorts that the Fund could target:
    a. **Cohort A:** Households that are unlikely to buy a home without significant support from the Government, including non-financial support.
    b. **Cohort B:** Households that cannot get a large enough deposit together to buy a home, due to high rents and fast-growing house prices, and/or have insufficient income to service a low deposit mortgage at current house prices.
    c. **Cohort C:** Households that are not home owners yet but would be able to achieve home ownership without Government assistance.

20. We are also ensuring that Māori specific needs within each cohort are understood. The Ministry's Māori and Iwi Housing Innovation (MAIHI) framework will assist in reflecting Māori need and aspiration within each cohort. This framework is in development with Māori housing partners (BRF 1920100468 refers).

Description of Cohort A

21. If you intend to help households that are unlikely to buy a home without significant support from the Government, including non-financial support, then you could target Cohort A.

22. This group would have the highest cost per household to get into home ownership, meaning fewer households will be assisted. This group would also need the most support out of any cohort, including non-financial support, such as wraparound financial capability services. Services for building Māori financial capability are in place through Te Puni Kōkiri and some iwi schemes. These could provide a platform for expansion.

23. Households in Cohort A are generally eligible to receive the Government's existing support products (First Home Grant and Loan), and as at the end of October 2019 around 1060 are already being assisted into home ownership by existing progressive home ownership schemes. If you ask that this cohort be a target group for the Fund, then this would need to be done in a way that is either complementary to, or through, existing providers such as Community Housing Providers.

Description of Cohort B

24. Targeting Cohort B would also help households that would not otherwise become home owners. Cohort B is made up of households that cannot get a large enough deposit together to buy a home, due to high rents and fast-growing house prices, and/or have insufficient income to service a low deposit mortgage at current house prices. These households are consistently locked out of the market as their incomes and savings are growing slower than the rate of house prices.

25. While targeting Cohort B would assist more households than Cohort A, the impact on each household will be smaller, as Cohort B are relatively closer to being able to achieve home ownership.

26. Cohort B are generally eligible for the Government's First Home products but in many cases, this is not enough to help them into home ownership. They also earn typically too much to be eligible for existing progressive home ownership schemes offered by providers, that target households in Cohort A.

Description of Cohort C

27. If your objective is to support as many households into homes as possible in a cost-effective manner, then the scheme would target those on the cusp of home ownership. This would have the lowest cost per household, spread across the largest number of households.

28. However, this may not have a significant impact on home ownership in the long term. Cohort C are closer to home ownership. While they would be able to get there faster with assistance from a progressive home ownership scheme, they are likely to buy a home without assistance from the Government. The benefit that a progressive home ownership scheme would provide this cohort is bringing forward their purchase of a home.

29. Targeting this cohort does not impact significantly on those population groups who are currently the furthest from home ownership, Māori and Pacifica.

We do not recommend targeting Cohort C

30. If you were to target Cohort C, then we consider that this would be best done through a Government scheme direct to households, similar to Cohort B.

31. However, this cohort is already likely to purchase a home without government assistance, albeit at a later point in time. This means that over the long-term, this scheme would do little to increase the number of home owners. We do not recommend that we further investigate how the Fund can target Cohort C as it will not increase the number of households that can achieve home ownership in the long term.

Delivery channels that will assist Cohorts A and B

Effectively targeting households

32. Key to most effectively targeting a range of households through the Fund is to take a place-based approach, as markets (and therefore affordability) vary in different locations. As discussed below, different delivery channels would deliver more effectively to different cohorts.

Different delivery channels are better suited to assist different Cohorts

33. Cabinet has agreed that the funding set aside for the Progressive Home Ownership Fund should support progressive home ownership schemes through two channels:
    a. direct provision of progressive home ownership schemes by the Crown; and
    b. the expansion of progressive home ownership schemes currently offered by community housing providers, iwi and Māori organisations and financial institutions.
34. It is possible for Government to target more than one cohort through the Fund. The channels we consider to be best placed to assist these cohorts are discussed below. A key decision that will be needed is the amount of funding that will be allocated between the two channels.
35. If you wish to assist Cohort A, then we recommend doing this through expanding schemes offered by providers who are already competent in this area.
36. There are already several providers that offer progressive home ownership schemes to households in Cohort A. Some of these providers have a proven track record of helping households in Cohort A, albeit at a relatively small scale. We understand, from our engagement, that a large part of this success is due to providers' use of:
    a. **wraparound support** – current providers offer a wide range of wraparound support for households, including financial capability services, discounted utilities deals, and other financial and non-financial support where a household is struggling to remain in the scheme. We understand from our engagement with existing providers that this wraparound support is essential for the success for their schemes, given the target cohort.
    b. **extensive pre-selection processes** – providers typically have extensive selection processes to ensure that the households that are offered progressive home ownership schemes will be successful. In addition, where a household is not quite ready, some providers continue to work with the household to get them in to a place to enter a scheme at a later date.
    c. **offering a range of options to reach home ownership** – some of the larger and more established providers offer a range of progressive home ownership products. This provides a better pathway for households not ready for full home ownership. For example, a household exiting a rent-to-buy scheme may not be ready to take out a commercial mortgage and could instead enter into a shared equity scheme.
37. Given that providers are already successfully assisting this particular cohort, we consider that Government support for Cohort A would be best done by expanding schemes offered by competent providers including community housing providers, iwi and Māori organisations, and financial institutions. Providers have told us that they have the ability to expand their schemes with funding from the Government and report large numbers of households who would like to participate in the progressive home ownership products that they offer[2]. Post Treaty Settlement Entities offer a good example of delivering for Cohort A and MAIHI will look at access to finance options with Māori providers and supporting home ownership on Māori land.

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[2] NZ Housing Foundation reported an interest register of over 7,000 households. Other providers have reported waiting lists of between 400 and 700 households.

38. The process for delivering on this channel is through a Request for Proposals process. We will be engaging with providers on the design of the Request for Proposals approach and high-level process in early November. We will include details of this in your Cabinet paper for the report back by the end of this year. Among other things, the request for proposal process would need to consider not only who but also where it might wish to assist with expanded support for Cohort A. Providers have typically set up in the main urban centres where house prices have been relatively higher and therefore affordability issues are magnified. We will also be considering how this approach would work for households that are in areas where affordability is an issue but there are currently no existing providers.

39. MAIHI could support this work through engaging with iwi and Māori providers on the Request for Proposals approach and in particular considering rural and isolated communities where Māori land may offer opportunity for development, particularly through papakāinga. This is in part dependent on the removal of barriers to Māori land development that MAIHI will also examine.

If you wish to assist Cohort B, then we recommend doing this through the provision of a Government scheme direct to households

40. We consider that Cohort B would be best supported through the delivery of a Government scheme direct to households as this is the area where there is currently a gap in progressive home ownership provision.

41. While there are a number of features to work through to design a Government scheme direct to households, a key design consideration at this point relates to the type of progressive home ownership arrangement that the Government would deliver directly. We consider that a Government scheme direct to households would be best designed as a form of shared equity scheme either in the form of shared ownership or in the form of a secondary mortgage.[3]

42. Other options included rent-to-buy, leasehold and deferred settlement schemes. However, these schemes are not cost effective, as they require Government to own entire homes, which will inherently limit the number of households that could be assisted. These types of schemes also involve more administration and oversight compared to shared equity schemes. For example, they are likely to include bespoke relationships with potential home owners

43. While we are not recommending that we further investigate rent-to-buy (otherwise called Rent to Own) for the Government scheme direct to households, this does not preclude the Government from supporting rent-to-buy schemes through expanding schemes offered by community housing providers, iwi and Māori organisations, and financial institutions. The MAIHI framework is exploring this as part of its consideration of access to finance for Māori.

44. Annex B sets out a summary of the advantages and disadvantages of targeting each cohort, in the context of our recommended delivery channel for support each cohort.

Taking a place-based approach

45. Under a place-based approach, we will assess the relevant need against cohorts A and B for each place. For Cohort B, we will adjust the eligibility settings for the Crown scheme to reflect the need for Government support in that location.

46. For Cohort A, we will engage providers that already operate in a location[4], starting with providers that are ready to deliver and have an existing customer base. Over time, we will

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[3] Either in the form of shared ownership, where Government would be a joint owner on the title of the property, or as a second mortgage. Under either option, the scheme could be designed to charge a concessionary rate of interest (if any) or share in a proportion of capital gains. These are features we will consider as part of the detailed design.

[4] Our procurement approach will include establishing a list of providers at a national level, noting for example where they operate and whether they target particular groups such as Māori or Pasifika.

expand the number of providers to ensure that providers who can work with particular customer groups, or in particular locations, are included.

Helping Māori, Pacific Peoples, and families with children into home ownership

47. There are a number of providers who focus on delivering affordable housing to Māori and to Pacific households. Although most rōpū Māori involved in papakāinga housing and housing developments are currently not registered Community Housing Providers (CHPs), there are more seeking registration and many partner with registered CHPs. A number of Māori providers of Progressive Home Ownership schemes, (for example Ngā Pōtiki a Tamapahore Trust, Ngāi Tahu, Ngāti Whātua o Ōrākei, Waikato Tainui and the six Te Ara Mauwhare rōpū) are emerging. MAIHI is looking at how to support an increase in Māori CHPs, building on the existing sector capacity building focus. The Māori housing sector recognises the need for more kaupapa Māori CHPs, and recognises that some adaptation may be required in the regulatory framework to reflect the particular issues and organisational dynamics of Māori organisations.

48. Te Ara Mauwhare is a set of trials to identify and evaluate innovative models to overcome barriers for low to median income whānau in moving toward home ownership. It aims to:
    - build new models and intellectual property, and evidence about what works, so these can be shared and adopted widely across the Māori housing sector
    - identify changes to policy settings required for these models to be more widely applicable; such as targeted grants, closer integration of government support, or removal of barriers.

49. The Government at the time specified that at least one trial include a home ownership pathway for whānau who are currently receiving the Accommodation Supplement or eligible for Income Related Rent Subsidy. Annex C provides information on the individual trials.

50. As requested by the Minister for Māori Development, Te Puni Kōkiri is providing the initial observations and potential policy matters to address, to inform the development of progressive home ownership options for Māori. To date, for example, the Te Ara Mauwhare trials suggest:
    - the need for an underlying financial capability programme (such as Sorted Kāinga Ora)
    - a 'co-design' approach with capacity for flexibility
    - diversity in models – for example generic shared equity may not work in some markets, and approaches may require multiple or staged approaches such as 'rent to buy' evolving into equity sharing
    - recognition of Treaty issues and in particular the expectation sometimes that housing assistance must be targeted when the development involves whenua Maori to whānau who whakapapa or who are part of an intentional kaupapa Māori community.

51. On 12 November 2019 a wānanga was held with many of the involved Māori providers to discuss how a scheme may work and what some of the specific issues to be addressed are.

52. We understand that other existing providers who focus on assisting low income households assist Māori and Pacific households through their schemes. [redacted] s 9(2)(b)(ii)

53. We consider that there are options for being more focused on assisting Māori, Pacific Peoples and households with children through the design and delivery of the progressive home ownership scheme. While our thinking is still at an early stage in this area, as part of our place-based approach we could specifically ask that potential providers come forward with proposals to assist Māori, Pacific Peoples and families with children.

54. Access to finance is a priority area to address in MAIHI and we have already had discussions with Māori housing partners on solutions that could be developed for Māori in 2020.

Evidence to inform cohort targeting

55. Officials have gathered some initial insights into the size and composition of the cohorts based on Census 2013 data and drawing on recent research. These insights are illustrated in Annex C, using Auckland as a case study.

56. Further analysis is needed to refine the target cohorts and to ensure that scheme policy meets the specific needs of the cohorts, for example, for house size or in specific locations. Market surveys or focus group studies are likely needed to understand the potential uptake among eligible households. Officials will undertake further work in this area to inform the December Cabinet paper.

Factors to consider in designing and operating a scheme

57. We have identified factors that are likely to shape the design and delivery of the schemes funded through the Fund. We will continue to develop and refine these factors as we develop the Cabinet paper.

58. Affecting the high level approach, factors that would improve housing outcomes include:

    a. a preference for new supply, as the ability to purchase a new home tends to indicate affordability in a location.[5] A preference for new supply will also provide opportunities to increase housing supply without driving up house prices in that location

    b. a place-based approach. Places will have different relative sizes of cohorts, and different supply and, thus, affordability issues. The demographics of the households within these cohorts may also vary in different places. We would assess the need in that location and adjust the price points accordingly

    c. additionality where the Fund is used where Government support is required (i.e. where it will not duplicate or stifle existing efforts)

    d. complementing the existing suite of support to home owners (e.g. KiwiBuild, First Home Loans)

    e. ensuring consistency in ownership/participation objectives between the household and the Government.

59. In terms of prioritising the Fund to support particular households, we would expect:

    a. a preference for assisting first home owners and "second chancers" in both Cohorts A and B

    b. a preference for assisting people who already reside and are renting in the area

    c. assisting those households with good credit histories as they would be good candidates for securing a mortgage through a bank, and people who are able to provide some level of deposit

    d. using funding of Cohort A to ensure the Fund is assisting Māori and Pacific households, and households with families.

60. We also note that the funding arrangements will affect the extent to which Cohorts A and B are able to be targeted. The 10 year fiscal neutrality requirement is possibly workable for the Government direct scheme but risks pushing the Government direct scheme toward including increasing numbers of households from Cohort C. The 10 year requirement is likely

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5 In locations where the price point for existing homes is lower than for new supply, there are unlikely to be affordability issues and Government support is not needed. Similar price points for existing and new supply indicate that there are affordability issues, and these locations should be prioritised for Government support.

to put pressure on current providers (if they can, in practice, work within the 10 year limit) to extend into Cohort B or even Cohort C.

Fiscal impacts and impact on Budget 2020

61. The Progressive Home Ownership Fund potentially incurs three types of costs:

    a. establishment, administrative and other operating costs, for which a Budget 2020 bid is required; and

    b. Either

        i. a Budget 2020 bid to cover the cost to the Crown of any interest rate concessions to households that differ from the Crown rate of 6 percent;

        Or

        ii. a Budget 2020 bid for capital.

62. Whether a bid to cover the concession or capital is needed is dependent on decisions about the length of time allowed for households to graduate from the scheme to full home ownership (that is, 10 years or 15 years), and fiscal neutrality (whether the timeframe can be extended to 15 years instead of 10 years).

A Budget 2020 bid will be needed to cover establishment administration and other operating costs

63. Cabinet directed you, as part of your report back, to set out the establishment, administrative and other operating costs for the Progressive Home Ownership Fund and how these will be funded.

64. We recommend that you seek to fund these costs through a Budget 2020 bid to fund:

    a. administration costs, which will cover the costs of managing the Progressive Home Ownership Fund

    b. provision for bad debt where this has not been provided for upfront

    c. other support services, such as any financial capability services that may be provided under a Government scheme direct to households.

65. The exact size of these costs is dependent on detailed design choices, such as how much of the Fund is offered each year. Early estimates are in the range of $33 million to $80 million and officials will undertake further work to identify the size of these costs for Budget 2020.

We recommend that the timeframe to graduate households to full home ownership be extended to 15 years

66. In our engagement with providers of existing schemes, we tested the practicality of the ten-year recycling requirement for their schemes. We heard, almost unanimously, that requiring the funding to be returned to the Crown within 10 years would significantly hinder the effectiveness of their schemes. We understand that providers generally design their schemes on a 15 to 25 year basis, meaning that while some may graduate sooner than this, they do not require households to graduate within ten years. Therefore, the 10 year recycling requirement will affect their operating models.

67. In addition, there will be households that are unable to graduate within ten years. For example, while the NZ Housing Foundation has stated that the average time for a household to exit to date has been five years, this has been gradually increasing over time, and as house prices have increased. The NZ Housing Foundation has advised that it expects the time to graduate to reach around 10 years. As this is an average, some households will not graduate within 10 years.

68. Our modelling for a Government scheme direct to households also supports this for both Cohorts A and B, where households would likely need more time than ten years, if they are to

successfully graduate to a full commercial mortgage and pay no more than 30 percent of household income on mortgage servicing costs.

69. We recommend that the length of time allowed for households to graduate from the scheme to full home ownership (and consequently, for funding to be recycled back to the Crown) be set at 15 years. We consider that 15 years would be sufficient as we have been advised by providers that their schemes are typically designed on a 15 year cycle. We consider that setting the timeframe at less than 15 years will significantly limit the number of households in Cohorts A and B that you can assist into home ownership.

70. s 9(2)(f)(iv) [redacted] Setting the timeframe at 15 years has implications for the fiscal neutrality of the Fund. However, the Minister of Finance can change the 10 year timeframe for fiscal neutrality.

71. Treasury advises that, under the Fiscal Management Approach, the fiscal neutrality rule normally requires capital expenditure to be recovered within 10 years. Any capital investment not returned within this timeframe will generally be charged at the full amount against capital allowance.

72. The Minister of Finance has the discretion to decide that funding for the Progressive Home Ownership Fund returned within 15 years be considered as fiscally neutral. If you wish to proceed with extending the timeframe, we recommend to better reflect the nature of this investment that you seek the Minister of Finance's approval that a longer timeframe for fiscal neutrality also applies in this case.

The Minister of Finance's decision on fiscal neutrality at 10 years or 15 years will affect whether capital or further operating costs are needed

73. If you agree to set the timeframe allowed for households to graduate to full homeownership at 15 years and the Minister of Finance agrees to extend the timeframe for fiscal neutrality, a Budget bid will be needed to cover the cost of any concession to households. This allows more transparent treatment of the concession costs (see below).

74. The concession costs will need to be recognised upfront, both for fiscal management and budgetary purposes. Costs may be offset upfront by any expected revenue - for example, a charge on the shared equity or an interest on the second mortgage but risks potentially undermining the objectives of a scheme.

75. The concession costs are potentially significant. The exact size of the concession costs, and the Budget bid, will depend on a number of factors such as the extent of submarket offering and assumptions about borrowing costs and how the scheme is rolled out.

76. The concession costs may also be greater the further away a household is from achieving home ownership (for example, if targeting Cohort A), as these households will need greater support and therefore will be offered funding at a greater level of concession to successfully exit the scheme.

77. Once we have your direction on the approach and high-level design, as sought in this briefing, we will work to identify the size of any concession costs in collaboration with the Treasury. Early estimates are that these costs would be around $316 million undiscounted over 10 years (or around $558 million, undiscounted, over 15 years), assuming a default cost of capital rate of 6 percent. These costs would change if the Minister of Finance and Cabinet agree to a lower cost of capital.

78. Regardless of the recycling timeframe, if the principal $400 million ***is not*** considered fiscally neutral, then a Budget 2020 bid would be needed to account for the $400 million as a capital allowance. In this case, concession costs would not need to be funded.

79. Further operating costs are expected to arise, dependent on the final scheme design. For example, costs would vary dependent on whether the Crown takes a fixed dollar amount or a

percentage of equity share as households graduate from the scheme. We are unable to estimate these costs until design is finalised in early 2020.

Further work is needed to cost the proposals

80. HUD has been working with the Treasury on assessing the financial cost and fiscal impact of the Government scheme. There remain uncertainties, for example, around specific scheme design as well as critical assumptions such as the discounting rate. These will have a significant impact on costs. Officials will work to resolve these issues for the Cabinet paper.

Ministerial decisions to inform the development of your Cabinet paper

81. For us to begin drafting your Cabinet paper for your report back by the end of the year, and to undertake the detailed design features, we need your direction on:
    a. the target cohort or cohorts that the Progressive Home Ownership Fund seeks to assist
    b. whether you wish to pursue extending the timeframe for funding to be recycled back to the Crown from 10 to 15 years
82. Both of these aspects will influence the financial and non-financial design features needed to implement the Progressive Home Ownership Fund.

Risks

83. We are working closely with the sector and others to manage design and implementation risks.

Consultation

84. We have consulted with Treasury on this paper. We continue to work with the Ministry for Pacific Peoples, Te Puni Kōkiri, and Kāinga Ora.

Next steps

85. We will draft the Cabinet paper based on your direction on cohorts, channels and the fiscal approach.
86. We will provide you with more information on Māori service providers in early December, and continue to further refine information about cohorts.
87. Further work will be undertaken on the relative spend on each channel (that is, how much would be allocated to the Government direct channel and how much might be directed through existing providers), and on the procurement approach and process.
88. We will continue to test the approach with stakeholders, including a workshop on 6 November with providers.
89. We would like to meet with you to discuss this paper at your earliest convenience to inform the development of the Cabinet paper for your report back to Cabinet in December. Our timeframe for the report back to Cabinet is early December.

Annexes

90. Annex A: Glossary of PHO scheme types
91. Annex B: summary table of advantages and disadvantages for targeting each Cohort
92. Annex C: initial insights on target cohort: Auckland case study

Annex A: Glossary of scheme types

Shared equity

Broadly speaking, there are two different forms that shared equity can take. Either as shared ownership or as a second mortgage. Both are described below.

Shared ownership

Under a shared ownership scheme a provider effectively purchases a portion of the property, usually in return for a share of any increase in property value on that property over time.

The household then buys back the portion of the property over time. The household may purchase the portion in a single payment. Alternatively, a scheme can be designed to allow the household to progressively purchase the portion through a series of smaller payments. This is known as "staircasing".

As with any standard investment, the provider would typically share in any losses if the property decreases in value. However, this outcome is less likely as property prices generally increase over the long term. If Government were to offer this type of scheme, then spreading the Government's investment over several properties and markets also reduces the risk of a decrease in value across the portfolio although it cannot remove the risk entirely.

The New Zealand Housing Foundation's shared ownership scheme is an example of this type of scheme.

Second mortgage

Under a second mortgage scheme a provider offers a low interest (or interest free) loan to households. The loan may have a time period in which it is repayable, such as in 10 years' time. In some cases, if the loan is not repaid in this time, a market level interest rate may be charged until it is fully repaid.

The provider can still choose to receive capital gain and/or loss on the equity share through a contractual arrangement.

The main difference between the two schemes is the level of risk to the provider

The main differences between second mortgage and shared ownership are:

- the provider takes on less risk with the investment under a second mortgage. Under shared ownership, the provider is a joint owner on the title of the property. This means that the provider will be jointly liable for any unpaid costs attached to the property, such as rates or mortgage repayments. By contrast, under a second mortgage arrangement, the provider does not have an ownership interest in the property and is simply making a loan.
- the household and equity provider both have an interest to secure the value of the property
- shared ownership schemes consider the equity provider's contribution as equity, whereas a second mortgage is considered to be householder debt. The shared mortgage scheme would lead to higher interest rate costs.

Rent-to-buy schemes

Under a rent-to buy scheme the provider purchases a house outright. It then enters into an agreement with a household that allows the household to rent the property and gives it the right to buy the property at any point within a set amount of time (e.g. five years).

The rent that a household pays is often set at below market rent. This provides the household with some financial headroom to save for a deposit, which it can use when it exercises its right to buy the property. Alternatively, a standard market rent could be charged with the provider setting aside a portion of that rent as a deposit on behalf of the homeowner.

Queenstown Lakes Community Housing Trust, New Zealand Housing Foundation, and Habitat for Humanity are all providers of rent-to-buy schemes.

Deferred settlement schemes

Under a deferred settlement scheme, the provider purchases a house outright. At the same time, it enters into an agreement that gives the participating household the right to purchase the property at a fixed price at some point in the future.

The household typically lives in the property during the deferred settlement period. During this time, the household may pay rent (as a tenant) or a contribution to the costs of ownership e.g. rates and insurance. In the latter case, both parties may be covered by an exemption to the Residential Tenancies Act.

Habitat for Humanity is the only provider that we are aware of that is providing deferred settlement schemes.

Leasehold schemes

Under a leasehold scheme, the provider sells a home to a household but retains ownership of the land underneath the home. The exclusion of land from the purchase lowers the deposit and servicing cost for the homeowner.

The homeowner may be required to pay a ground rent to the landowner (e.g. the government or CHP) for ongoing use of the land. This ground rent would typically be fixed for a significant period of time but periodically reviewed.

In some cases, the homeowner may have the right to purchase the land from the provider at a later date, once it has paid down some of its debt and better able to afford it. There is a risk that increases in land prices may reduce the affordability of purchasing land for the household.

Queenstown Lakes Community Housing Trust offers a form of leasehold scheme through its Secure Home product.

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Annex B: Summary of the advantages and disadvantages for targeting each Cohort

	Cohort A	Cohort B	Cohort C
Who	• Households that are unlikely to buy a home without significant support from the Government, including non-financial support.	• Households that cannot get a large enough deposit together to buy a home and/or have insufficient income to service a low deposit mortgage at current house prices.	• Households that are not home owners yet but who may be able to achieve home ownership without government assistance at a later date.
Delivery Channel	• Delivery through the expansion of progressive home ownership schemes currently offered by community housing providers, iwi and Māori organisations and financial institutions.	• Delivery through the direct provision of progressive home ownership schemes by the Crown.	• We do not recommend targeting this group, but if they were to be targeted, it would be through the direct provision of progressive home ownership schemes by the Crown.
Advantages	• Funding will help a cohort that would not otherwise have become home owners. • Will have a high impact on the households helped into home ownership. • Will be complementary in that it would support existing providers to do more • Relatively administratively simple as providers already have established schemes • Providers have stated high success rates for households exiting for their schemes	• Funding will help a cohort that are unlikely to otherwise have become home owners. • Is complementary towards schemes offered by existing providers. • Will help a moderate number of households with a moderate impact on each household. • We expect that they will be able to graduate to full home ownership within 15 years	• Most cost-effective way to help a large number of households to buy homes • Is complementary towards schemes offered by existing providers. • Households will be highly likely to successfully exit
Disadvantages	• Less cost effective in that it helps a smaller number of households.	• Relatively more administratively complex as Government will have to design and administer the scheme	• May not have a high impact on improving home ownership rates in the long term as it would be assisting households that would achieve home ownership at a later date • Relatively more administratively complex as Government will have to design and administer a scheme
Cost	• Higher cost per household, funding spread over small number of households	• Moderate cost per household, funding spread over a moderate number of households	• Lower cost per household, funding spread over large number of households
Size of potential cohorts (Auckland case study)	Assuming total household income of $50,000 - $90,000: Total possible cohort: 63,100 households, of which • 6,100 households (9.7%) are Māori • 7,700 households (12.2%) are Pacific Peoples	Assuming total household income of $90,000 - $130,000: Total possible cohort: 32,700 households, of which • 2,900 households (8.9%) are Māori • 3,500 households (10.7%) are Pacific Peoples	Assuming total household income over $130,000: Total possible cohort: 314,400 households, of which • 2,500 households (0.8%) are Māori • 3,600 households (0.82%) are Pacific Peoples

* We will do further work to refine this following your feedback on preferred target cohorts

Annex C: Te Ara Mauwhare trials

The Te Ara Mauwahare trials are exploring a range of different progressive home ownership models, as follows:

The trials underway or in development are:

- A long term rent to buy model for very low income whānau, with **He Korowai Trust** in Kaitāia. Surplus homes from Kāinga Ora, refurbished by students at the trades training institute. Includes an Accommodation Subsidy. Whānau moved into 8 homes on the papakāinga in October 2019. Recycling of the rent-to-buy grant around 17 years.

- A rent to buy model for current and recent Kāinga Ora tenants with **Te Tihi o Ruahine Whānau Ora Alliance**. Land purchased from Kāinga Ora to establish two small urban papakāinga in Palmerston North. Recycling of grants around 10 years. [redacted] s 9(2)(f)(iv)
s 9(2)(f)(iv) [redacted]

- NZ Housing Foundation shared ownership model for median income whānau, with **Port Nicholson Block Settlement Trust** as part of its Te Puna Wai development in Wainuiomata, with the homes to be ready in early 2020. Recycling of shared ownership grant at 5 to 7 years.

- A very long term (say 24 years) shared ownership model with the **Chatham Islands Housing Partnership Trust**. Sod-turn due November 2019. Addresses lack of both housing and loan funding on the Chathams.

- NZ Housing Foundation shared ownership model for median income whānau, with **Te Rūnanganui o Ngāti Porou** on its Te Tini site in Gisborne; commitment and timing yet to be resolved. Not yet signed up.

- A whānau housing cooperative combined with a shared equity agreement, working with **Te Taiwhenua o Heretaunga** as part of its Waingākau housing development in Flaxmere. Co-operative housing element of the trial not finalised.

- **Sorted Kāinga Ora** programme to build whānau financial capability – delivered by the six rōpū above and now rolled out on a limited scale within the Te Puni Kōkiri Māori Housing Network.

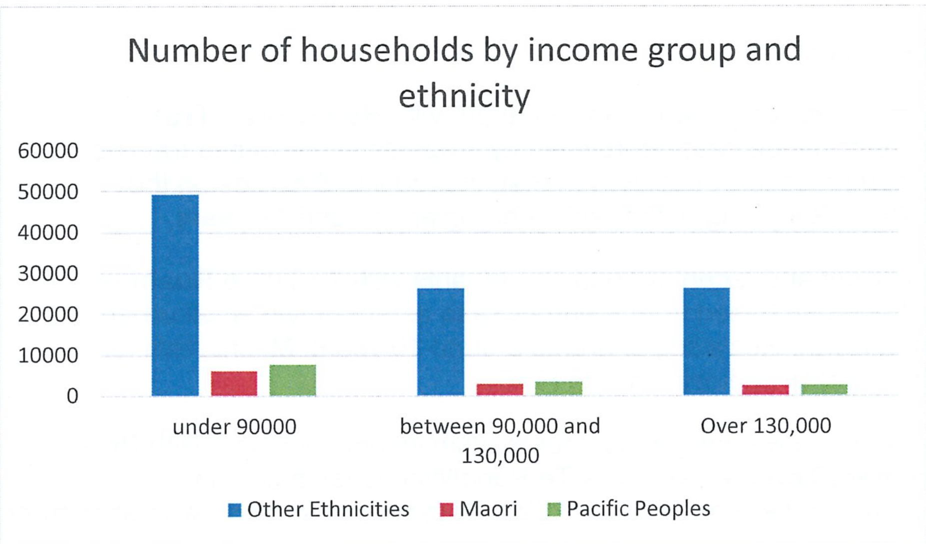
Completion of the design of the trials with Te Rūnanganui o Ngāti Porou and Te Taiwhenua o Heretaunga is likely to be dependent on the viability of the wider housing developments within which the trials are to be nestled. The wider developments are being addressed by the Iwi/Māori Partnerships Programme and the Hastings Place-based Deep Dive demonstration projects.

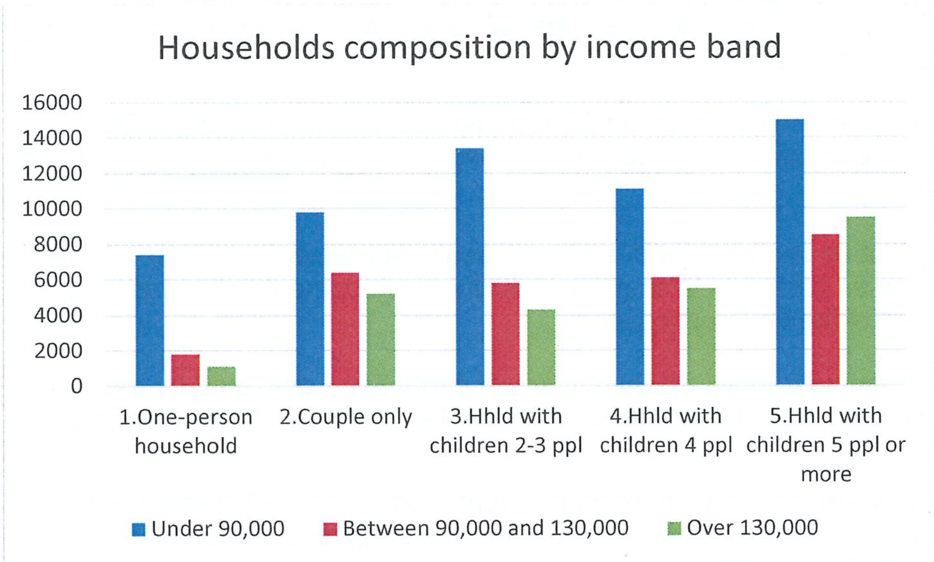
Annex D: Auckland Case Study

Initial analysis by HUD based on census data on Auckland renters shows that there are many renting households who can potentially benefit from a progressive home ownership scheme, depending on the choice of target cohorts and assumptions. Assumptions used here are:

- household reference person under 65
- income over $50,000.

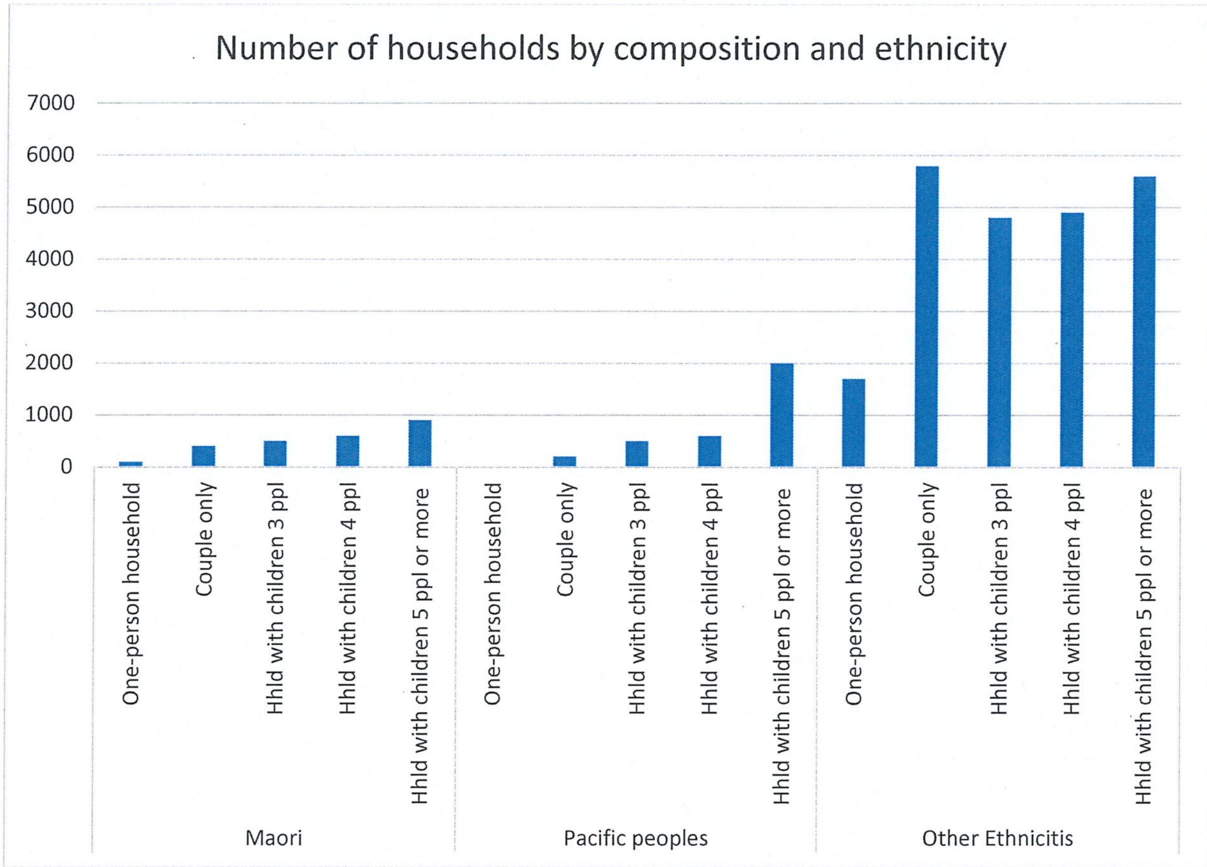
These households differ by ethnicity and composition across income spectrum.





Within these cohorts there are a significant number of households who cannot currently afford a mortgage on a lower quartile house price and do not have access to existing progressive home ownership schemes. This translates to an approximate household income range between $90,000 and $130,000.

We estimate that the size of this cohort is around 32,700 households. Pacific households make up 10.70 percent of the total, while Māori households account for 8.87 percent. Māori and pacific households tend to have a larger proportion made up of larger households.



This cohort is likely to encompass a wide range of households, including modestly paid professional working families in Auckland such as nurses, teachers and police. However, this may exclude some families if there are two incomes in higher end of that income spectrum, for example, in police and teaching (with an estimated combined income of $143,000)[6].

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[6] Based on Mitchell, I (2019) Intermediate housing market and housing affordability trend in Auckland p.88