

In Confidence

Office of the Minister of Finance

Office of the Minister of Housing

Cabinet Business Committee

Market headwinds to residential development and construction: supporting affordable housing in build-ready developments

Proposal

- 1 This paper reports back on detailed design and implementation matters for the new streamlined investment processes for the government to acquire or de-risk dwelling sales in housing developments agreed by Cabinet in June [CPC: 22-MIN-0017 refers]. It seeks agreement to:
 - 1.1 the eligibility and assessment criteria for pre-purchase commitments and underwrites;
 - 1.2 delegation of individual investment decisions to joint Ministers.
- 2 It also provides advice on communicating the agreed eligibility and investment criteria to manage sector and public expectations.

Relation to government priorities

- 3 The clearinghouse processes agreed by Cabinet supports a range of Government priorities outlined in the Speech from the Throne, including: reducing homelessness, increasing housing supply, affordability and choice. The proposals also support a broad range of strategic objectives and priorities set out in the Government Policy Statement on Housing and Urban Development.

Executive Summary

- 4 The construction sector is currently facing a number of supply-side and demand-side headwinds that increase the likelihood of some land and houses not being developed in a timely manner, if at all. There is a particular risk that the market will deliver less affordable housing in the places where it is needed most.
- 5 To address these risks Cabinet has agreed to establish new processes to acquire and develop, or de-risk the sale of dwellings in stalled or at-risk developments. This paper proposes a number of detailed design and implementation matters relating to the new processes including:
 - 5.1 eligibility criteria to qualify for support for a prepurchase or underwrite commitment;

- 5.2 the assessment and prioritisation criteria for applications;
- 5.3 decision making relating to:
 - 5.3.1 priority focus areas if the funding allocated is oversubscribed or there is a large volume of applications;
 - 5.3.2 which proposals to support through a prepurchase or underwrite commitment;
 - 5.3.3 the contract terms;
 - 5.3.4 decisions on the end-use of the homes.
- 6 This is a small and targeted intervention that primarily focuses on securing some affordable housing in areas of greatest need which will need to be clearly communicated to manage expectations.
- 7 The proposed eligibility and assessment criteria set out in this paper are key to ensuring that decisions about providing support are transparent and consistent, and that the support itself aligns with the intended purpose and objectives of the new processes. They are also important to manage expectations of potential applicants, and to ensure the quality of applications and the ability to prioritise them, given the likelihood that the funding allocated for underwrites or pre-purchase agreements will be oversubscribed.
- 8 The assessment process will consider due diligence to determine whether the Crown will support a project, and potential end use. Once assessed, applications will be prioritised by the criteria proposed in this paper. Recommendations to support a project will make clear the trade-offs for decision makers in terms of housing outcomes (particularly number of dwellings delivered) and cost and risk to the Crown.
- 9 Te Tūāpapa Kura Kāinga – Ministry for Housing and Urban Development (HUD) will administer the new processes. The clearinghouse and fast-track investment process will be operational in August following approval by Cabinet of the proposals outlined in this paper.

Background - establishing a new central clearinghouse with expediated decision-making processes

- 10 In June 2022 Cabinet agreed to establish new processes to streamline and expediate decisions by establishing a new:
 - 10.1 clearinghouse process to receive and assess approaches from developers wishing to sell land or seek government support to progress developments that are unlikely to be built without government assistance and refer proposals that meet relevant criteria to either an existing government land programme or consideration for a prepurchase or underwrite decision.
 - 10.2 fast-track investment process under which the Crown may commit to purchasing (or underwriting the sale of) suitable homes “off the plans” so that developers wanting to develop their own land can meet their financiers

presale requirements, and commence construction while the detailed arrangements to finalise the dwellings' end-use (e.g. as public housing, affordable rentals or first homes) are being worked through with other government funds and programmes.

- 11 The use of underwrites would enable the construction of more houses on the expectation that in most cases the Crown or the developer would be able to secure an end purchaser prior to the underwrite being triggered. A prepurchase agreement is more likely to be used when the property is likely to be retained in Crown ownership or where the developer does not wish to negotiate with end purchasers directly.
- 12 Land acquisitions will be funded from existing land programme allocations. Prepurchase agreements and underwrites will be funded by up to \$75 million of the Affordable Housing Fund:
 - 12.1 \$65 million to underwrite developments; to cover the acquisition of developments if required with the intention to on-sell them.
 - 12.2 \$10 million for costs such as holding costs, write-downs and loss on sale.
- 13 Those projects progressed through a pre-purchase or underwrite commitment will be supported from existing funds and programmes subject to the final end-use (public, transitional or affordable housing).

Objectives and investment principles

- 14 The primary objective of the new processes is to increase the supply of public, transitional, and affordable housing (for both ownership and rental) where it is needed most.
- 15 The supporting objectives of the new processes are to support the government's broader objectives and priorities for housing and urban development; and maintain construction sector capacity and capability.
- 16 The following investment principles have been agreed:
 - 16.1 Strategic: investment decisions should reflect the government's strategic direction and priorities for housing and urban development as set out in the Government Policy Statement on Housing and Urban Development, MAIHI Ka Ora – the National Māori Housing Strategy, and relevant accountability documents;
 - 16.2 Targeted: investment decisions should reflect local housing needs and aspirations as identified through the Public Housing Plan, place-based partnerships and housing heatmaps; and focus on the locations, typologies and cohorts that are unlikely to be commercially attractive absent government intervention;
 - 16.3 Transparent: the process for identifying and prioritising projects, and the type and quantum of Government investment in projects, should be fair and transparent.

- 16.4 Value for money: the Government's cost and risk exposure should be proportionate to the public benefits, from a whole of government viewpoint, and the risk of moral hazard.

Eligibility and assessment criteria for support through a prepurchase or underwrite agreement

- 17 The proposal is a targeted response focused on developments or stages of developments where construction of houses is yet to commence. Support will not be provided for the completion of partially built houses. This will ensure developers, house builders, and their financiers are still incentivised to see projects through to completion and reduce the potential remediation risks associated with taking on partially built houses.
- 18 To be eligible to apply for support we propose the following eligibility criteria guided by the above investment principles:
- 18.1 Applicant must own or have secured ownership or use of the land (or have an unconditional agreement to own or use the land);
 - 18.2 Applicant is an established developer or house builder with a proven track record of successfully delivering new housing within New Zealand;
 - 18.3 Land has resource consent;
 - 18.4 Construction of the dwellings has not yet commenced, or the stage of development has not yet commenced;
 - 18.5 The development contributes to increasing supply and addressing an unmet housing need in an area and there is a high risk that the development will stall or not complete without Crown support.
- 19 Consistent with the objectives and investment principles, we propose assessing and prioritising development opportunities that meet the above eligibility criteria against the following criteria:

Criteria	Key factors to be assessed
Contribution to increasing supply and addressing unmet housing need	<p>The development must be able to deliver an increased number of houses (this can vary between places)</p> <p>The development meets a need (typology, suitability, affordability etc.) for priority cohorts and locations, including contribution to Māori housing outcomes (assessed against alternatives to Crown support).</p> <p>The development can contribute to maintaining construction sector activity, capacity and capability e.g. understanding workforce impacts as well as potential risks of crowding out local construction activity.</p>
Project	Evidence construction can commence within 6 – 12 months.

readiness	Confidence that the applicant will be able to complete the project, on-time and in-cost, after receiving Crown support.
Cost and risk to the Crown	<p>Evidence that a developer has finance to undertake the development subject to securing pre-sales or underwrites on acceptable terms</p> <p>Forecast costs, revenue and margins are shared with the Crown on an open book basis.</p> <p>Overall value for money assessment.</p> <p>Net public benefit associated with this project including value for money.</p>
Wider government objectives for housing and urban development	How the project supports the Government's wider objectives for example: good access to services and amenities, climate adaptation and mitigation.

Prioritising applications to areas of highest need

- 20 It is difficult to quantify the likely interest in the new fast track investment process, and the resulting delivery. What we support will be dependent on what the market chooses to bring to us (in terms of both location and typology). The eligibility and assessment criteria has been designed to ensure that we can effectively prioritise applications and investment decisions are well targeted (i.e. right house, right place, right price), developments can be progressed at pace and represent value for money, and meet the objectives for public, transitional and affordable housing in areas where it is most needed.
- 21 The size of the market for medium density housing in regional centres is smaller than urban centres, with fewer developers building affordable products in regional areas as the market is still untested in some places. It is likely these areas will require higher levels of support based on the development economics – high land prices and development costs relative to affordability and market rents are challenges for regional centres.
- 22 We recognise there have been some challenges to establishing a sustainable build programme in regional New Zealand, exacerbated by the headwinds. This programme provides an opportunity to secure affordable housing outcomes in communities where there has been delivery challenges utilising the funding for write-downs and losses (up to \$10 million) providing the ability to on-sell properties at loss and drawing other funding support from other funding allocations e.g. the Operating Supplement for Public Housing.

- 23 Prioritising projects in areas of highest need for public and transitional housing and affordable rental housing will contribute to broader government objectives and deliver homes in areas where they are most needed. It will also help to satisfy the supporting objective of this work of maintaining construction sector capacity, particularly in regions that may be more susceptible to negative workforce effects caused by headwinds in the sector. It may also help manage demand should approaches from eligible projects exceed available funding. We recommend that approaches from developers with projects in Public Housing Plan 2021-2024 focus areas¹ and the locations identified through the Affordable Housing Fund as the greatest need for an increased supply of affordable rental housing for those on lower incomes² are prioritised in the first instance.
- 24 This is a targeted initiative to secure affordable housing in planned developments that may not proceed without government intervention, and where we know there is unmet housing need. The relevant trade-off is that areas with well-established delivery pipelines for public and transitional housing (e.g. Auckland and Christchurch) may present projects that are more promising in terms of project readiness and housing delivery, but which do not respond to regional need.
- 25 Should there be a large volume of approaches, we recommend applications are prioritised to areas where delivery of public, transitional and affordable rental housing to date has been slow. This would allow the focus to be on areas where severe housing affordability issues exist, high levels of deprivation are present, and the development economics are challenging. Additionally, this may provide some counter-cyclical support for construction sector workforce in those areas.
- 26 This could be reassessed should we need to scale up the initiative in response to the impacts of market headwinds.

Implementation

Application and assessment process

- 27 Applications will be invited via HUDs website through an open-ended process that would:
- 27.1 outline the Government's overarching objectives and priorities
 - 27.2 set out eligibility criteria for government support
 - 27.3 outline the assessment criteria against which specific proposals are considered and prioritised for support
 - 27.4 set clear expectations that the primary tool on offer is underwriting dwelling sales to assist developers in meeting their presale requirements, or providing a presales commitment for the Crown to purchase the dwellings on completion.

¹ Te Tai Tokerau, Hamilton, Tauranga, Rotorua, Gisborne, Napier, Hastings, Rotorua, Whanganui, Palmerston North.

² Auckland, Tauranga-Western Bay, Rotorua, Napier-Hastings, Wellington Metro, Nelson-Tasman.

- 28 Applications will be quickly assessed, and an initial triage process will provide developers with a rapid indication of whether the government is likely to have an interest in investigating their development opportunity further. The eligibility and assessment criteria will be published so that developers whose proposals are unlikely to proceed can choose not to apply early on.
- 29 The assessment process will utilise existing HUD expertise and includes the following considerations:
- 29.1 Delivery ability – this will assess the capability and capacity of the developer to deliver the project on time and budget. HUD will assess the developer’s experience of delivering similar projects, evaluate the degree of project readiness, the pace of completion and key milestones and ensure that any delivery risks are well understood and mitigations are in place.
 - 29.2 Site review – this will assess the Site and Building Design to ensure that the developments are of high-quality and incorporate good design principles and practices that meet community needs. HUD will assess the functionality and design, durability of materials, and the typology of the development in line with the needs and requirements of the communities they are located in.
 - 29.3 Financial viability – detailed review of the cashflow requirements, project plan, development costings and financing (considering the net public benefit and potential end-use). HUD will assess the market value against comparable transactions, average regional development costs, understand the financing structure for the development including the terms of financing sources and reviewing pre-sales and commitments.
 - 29.4 A place-based assessment to consider the level of unmet housing need in that location and identify indicative options for the end-use tenure. For example:
 - 29.4.1 Planned affordable, public or transitional housing supply in the region (Kāinga Ora and Community Housing Provider delivery intentions);
 - 29.4.2 Capacity and capability of housing providers including Māori and iwi in the area;
 - 29.4.3 Broader plans for housing developments (including local government).
- 30 Once assessed applications will be prioritised by the criteria proposed in this paper. Recommendations to support a project will make clear the trade-offs for decision makers in terms of housing outcomes (particularly number of dwellings delivered) and cost and risk to Crown.
- 31 Crown risk is managed by robust due diligence, following the rules of procurement, relevant statutes, sound commercial principles and by providing competent oversight. Developers and applicants will be required to provide transparent and full disclosure

of details relating to the proposed project to ensure robust due diligence by the Crown.

- 32 The Ministers of Finance and Housing will be updated regularly on proposals received through the clearinghouse. We anticipate this reporting will include regional breakdown, expected dwelling numbers and updates on how these proposals are progressing.

Decision making

- 33 We recommend that the Ministers of Finance and Housing ultimately decide which proposals to support based on the eligibility and assessment criteria above. We also recommend joint Ministers approve the contract terms and direction on the end-use of the homes through the approval and negotiation process.

Communications

- 34 This is a small and targeted intervention that primarily focuses on securing some affordable housing in areas of greatest need. It will be important to manage expectations and ensure rapid decision making.
- 35 We will need to manage any expectations about the extent to which this initiative will help to smooth out the bust cycle or support the construction sector more widely. There may also be a perception that there is scope for the Government to step in and support half-completed developments, where the developer or construction firm has gone into liquidation. Such cases are already attracting media attention. We will need to clearly communicate to the sector the scope of the new fast track investment processes and be clear that ‘rescuing’ half-completed developments is not within scope.
- 36 Alongside information on HUD’s website, communications will be proactively targeted through existing networks and delivery channels. This includes a place-based approach leveraging HUD and Kāinga Ora regional networks. For example, working proactively with local councils, developers and financiers to raise awareness of the new processes.

Financial Implications

- 37 There are no additional financial recommendations arising from this paper because funding of up to \$75 million of the Affordable Housing Fund for the fast-track investment process has already been agreed as follows:
- 37.1 \$65 million to underwrite developments; to cover the acquisition of developments if required, with the intention to on-sell them.
- 37.2 The residual \$10 million for costs such as holding costs, write downs and loss on sale.
- 38 Operational costs including staffing, overheads, due diligence costs, expert advice etc. will be funded via departmental appropriations. This will be partially or wholly drawn down from the departmental Affordable Housing Fund funding of \$2 million per annum.

Legislative Implications

- 39 There are no legislative implications arising from this paper.
- 40 Some of the proposals discussed in this paper could result in the Crown acquiring housing and on-selling it to a registered community housing provider (CHP) to be used as public housing.
- 41 s 9(2)(h)

Population Implications

- 42 The proposals outlined in this paper aim to increase the supply of transitional housing, public housing and affordable housing (for both ownership and rental) where it is most needed. As such they are expected to benefit those members of the population who are most likely to rate their housing as unaffordable including Māori and Pacific peoples, sole parents, recent migrants, low-income earners, non-owner occupiers, the unemployed and people with disabilities.

Human Rights

- 43 There is no inconsistency with the New Zealand Bill of Rights Act 1990 or Human Rights Act 1993.

Consultation

- 44 The Treasury, Kāinga Ora and the Ministry of Building Innovation and Employment were consulted. The Department of Prime Minister and Cabinet was informed.

Proactive Release

- 45 The Minister of Housing intends to proactively release this paper at, or around the time, that further public announcements on the new processes are made.

Recommendations

The Ministers of Finance of Housing recommend that the Committee:

- 1 **note** that on 21 June 2022, the Cabinet Priorities Committee agreed to establish:
- 1.1 a new clearinghouse process to receive and assess approaches from developers wishing to sell land or seek government support to progress developments that are unlikely to be built without government assistance and refer proposals that

³ The appropriate class of registration could be established by the making of regulations under the Act. CHPs would then need to apply for such registration and meet any necessary registration criteria.

meet relevant criteria to either an existing land programme or consideration for a prepurchase or underwrite decision.

- 1.2 a new fast-track investment process under which the Crown may commit to purchasing (or underwriting the sale of) suitable houses “off the plans” so that developers wanting to develop their own land can meet their financiers’ presale requirements and commence construction while the detailed arrangements to finalise the dwellings end use (e.g. as public housing, affordable rentals or first homes) are being worked through with other government funds and programmes.
- 2 **agree** that to qualify for support for a prepurchase or underwrite commitment the:
 - 2.1 Applicant must have secured ownership or use of the land;
 - 2.2 Applicant is an established developer or house builder with a proven track record;
 - 2.3 Land has resource consent;
 - 2.4 Construction of the dwellings has not yet commenced, or the stage of development has not yet commenced;
 - 2.5 Development contributes to increasing supply and addressing an unmet housing need in an area there is a high risk that the development will stall or not complete without Crown support.
- 3 **agree** that applications for support for a prepurchase or underwrite commitment are assessed on the following criteria:
 - 3.1 Contribution to increasing supply and addressing unmet housing need
 - 3.2 Project readiness
 - 3.3 Cost and risk to the Crown; and
 - 3.4 Wider contribution to government objectives for housing and urban development.
- 4 **agree** that, should there be a large volume of approaches, applications are prioritised to areas where delivery of public, transitional and affordable rental housing to date has been slow
- 5 **note** that these priority areas are defined as focus areas under the Public Housing Plan 2021-2024, and those areas identified as locations for the Affordable Housing Fund where there is a shortage of affordable rental housing for those on low incomes.
- 6 **authorise** the Ministers of Finance and Housing to determine:
 - 6.1 priority focus areas if the funding allocated is oversubscribed or there is a large volume of applications;

- 6.2 which proposals to support through a prepurchase or underwrite commitment;
 - 6.3 the contract terms;
 - 6.4 decisions on the end-use of the homes.
- 7 **note** this is a small and targeted intervention that primarily focuses on securing some affordable housing in areas of greatest need which will need to be clearly communicated to manage expectations
- 8 **note** it will be important to be clear and transparent to ensure only development opportunities that meet the eligibility and assessment criteria apply
- 9 **note** a targeted approach through existing networks and channels following agreement to the detailed design and implementation matters.

Authorised for lodgement

Hon Grant Robertson

Minister of Finance

Hon Dr Megan Woods

Minister of Housing