

Treasury Report: Budget 2008: Capital Initiatives in Vote Housing

Date:	29 February 2008	Report No:	T2008/296
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Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Dr Michael Cullen)	Read before the Bilateral with the Minister of Housing	Before 4pm on Wednesday 5 March
Associate Minister of Finance (Hon Trevor Mallard)	Read before the Bilateral with the Minister of Housing	Before 4pm on Wednesday 5 March

Contact for Telephone Discussion (if required)

Name	Position	Telephone		1st Contact
<i>[information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]</i>				✓
Rowena Phair	Manager, Children and their Families	<i>[deleted – privacy]</i>	<i>[deleted – privacy]</i>	

Minister of Finance's Office Actions (if required)

None.

Enclosure: Yes

Treasury Report: Budget 2008: Capital Initiatives in Vote Housing

Attached is a briefing for the bilateral between the Minister of Finance and Minister of Housing at 4 p.m. on 5 March 2008 to discuss the budget initiatives for Vote Housing.

The bilateral briefing is structured as follows:

Recommendations	p. 3
Analysis by Vote	p. 8
One-page initiative summaries	p. 15

We expect the key issues for discussion will be:

1. **Hobsonville Urban Development** – Treasury recommends only funding the costs of Precinct One (the first phase), as well as any other costs that need to occur concurrently with Precinct One. This would be consistent with the approval process for the development and help ease the pressure on the capital allocation.
2. **Shared Equity Home Ownership Pilot** – Treasury recommends equity shares should range between 10% and 30%, in line with Cabinet's original decision, rather than only having 30% shares as proposed by HNZA. This will reduce the cost of the scheme by \$22.3 million, and still reach the same number of households.
3. *[information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]*
4. *[information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]*

Recommended Action

We recommend that you **read** the attached briefing and use it as the basis for making decisions in your bilateral with the Minister of Housing at 4 p.m. on 5 March 2008.

Rowena Phair
for Secretary to the Treasury

Hon Dr Michael Cullen
Minister of Finance

Recommendations

INITIATIVES FULLY SUPPORTED BY TREASURY

[information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]

INITIATIVES PARTIALLY SUPPORTED BY TREASURY

a Hobsonville Urban Development

analysis p. 8

- CBC has previously agreed to the creation of an integrated community at Hobsonville (refer CBC Min (06) 22/16). HNZC seeks \$74.813 million in capital funding for the Hobsonville development between 2008/09 and 2012/13. *[information deleted in order to enable the Crown to carry out commercial activities without disadvantage or prejudice]*
- The development costs of Hobsonville were previously to be funded via a loan from HNZC to the Crown. HNZC's loan was to be financed from its working capital borrowing facility. HNZC and Treasury support the proposal to fund these by direct appropriation, as the cost to the Crown is lower than private borrowing by HNZC.
- Treasury recommends only funding the costs of Precinct One (the first phase), as well as any other costs that need to occur concurrently with Precinct One. This would be consistent with the approval process for the development (precinct by precinct) and help ease the pressure on the capital allocation.

	<i>\$million - increase/(decrease)</i>					
	<i>2007/08</i>	<i>2008/09</i>	<i>2009/10</i>	<i>2010/11</i>	<i>2011/12</i>	<i>2012/13</i>
<i>Capital (GST excl)</i>						
Department	-	6.875	17.517	20.600	3.490	26,331
Treasury	-	6.875	17.517	13.448	(4.731)	(11.235)

b Shared Equity Home Ownership Pilot**analysis p. 9**

- Cabinet has previously agreed to a two year shared equity pilot (refer CAB Min (06) 47/2B). HNZA seeks \$55.173 million over two years for a pilot of shared equity loans to 500 households. HNZA's bid is calculated on the basis of all households receiving a 30% equity loan.
- Treasury recommends that the equity shares should range between 10% and 30%, consistent with Cabinet's decision (refer CBC Min (07) 3/6). This will reduce the cost of the scheme to \$32.925 million over two years, and still reach the same number of households.
- A paper is going to POL on 12 March seeking to expand the scheme.
- Treasury notes that work is yet to be completed on the means for rationing the loans, although Cabinet's decision to target the scheme at new supply could potentially partially address this issue.

	<i>\$million - increase/(decrease)</i>				
	<i>2007/08</i>	<i>2008/09</i>	<i>2009/10</i>	<i>2010/11</i>	<i>2011/12</i>
<i>Capital (GST excl)</i>					
Department	-	28.023	27.150	(5.316)	(7.091)
Treasury	-	17.853	15.072	(3.911)	(4.929)

INITIATIVES NOT SUPPORTED BY TREASURY

- c** *[information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]*

- d** *[information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]*

e Rural Housing Programme and Papakianga Loan Scheme analysis p. 11

- HNZC seeks \$3 million in capital in 2008/09 to continue the Papakianga loan scheme. These loans are available for building or buying housing on Maori land held in multiple ownership where commercial finance is not available.
- Treasury does not support the continuation of the Papakianga loan scheme because the small number of loans (five in 2006 and potentially ten in 2007) means that it only reaches a very small number of households.
- Treasury notes that in October 2007 the Minister of Housing agreed to a substantial work programme to promote building on Maori land, with priority given to establishing demonstration housing partnerships with iwi and land

owning trusts.

- If Ministers wish to continue the Papakianga loan scheme, Treasury recommends providing \$1.5 million which would be sufficient to fund six loans, with funding for a further two loans the subject of an in-principle transfer of \$0.5 million in the March Baseline Update.

	<i>\$million - increase/(decrease)</i>				
	<i>2007/08</i>	<i>2008/09</i>	<i>2009/10</i>	<i>2010/11</i>	<i>2011/12</i>
<i>Capital (GST excl)</i>					
Department	-	3.000	-	-	-
Treasury preferred option	-	-	-	-	-
Treasury scaled option	-	1.500	-	-	-

f *[information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]*

g Energy Efficient Warm Homes

analysis p. 12

- HNZC seeks \$77.7 million of capital over five years to increase the rate of the energy efficiency programme in state houses. This funding would mean that upgrades were completed within 4 to 6 years, rather than 10 to 14 years.
- Treasury recommends that HNZC reprioritise other elements of its modernisation programme to fund this initiative. Reprioritisation of funding sought in this bid would equate to 5.2% of HNZC's modernisation budget in 2008/09 and 10.4% of its modernisation budget in 2009/10.
- Alternatively, if reprioritisation is not possible, a loan from DMO to HNZC could be provided, reflecting that this proposal would bring forward expenditure that is budgeted to occur in any case. However, this would still count against the capital

allocation.

	<i>\$million - increase/(decrease)</i>				
	<i>2007/08</i>	<i>2008/09</i>	<i>2009/10</i>	<i>2010/11</i>	<i>2011/12</i>
<i>Capital (GST excl)</i>					
Department	-	3.400	13.500	18.100	18.700
Treasury	-	-	-	-	-

- h** *[information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]*

Vote Housing – Analysis

Analysis of Initiatives

- Capital funding is being sought for Vote Housing through this bilateral. Operating funding is being sought through the Families Young and Old theme. This is summarised in the table below:

	<i>\$million - increase/(decrease)</i>				
<i>Funding sought for Vote Housing in Budget 2008</i>	<i>2007/08</i>	<i>2008/09</i>	<i>2009/10</i>	<i>2010/11</i>	<i>2011/12 & Outyears</i>
<i>Operating (GST excl)</i>					
At this bilateral	<i>[information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]</i>				
Through Theme Families Young and Old					
TOTAL OPERATING					
TOTAL CAPITAL					

- Of the operating funding sought through the Families Young and Old theme, *[deleted – confidentiality of advice]* relates to capital initiatives being discussed in this bilateral.

INITIATIVES FULLY SUPPORTED BY TREASURY

[information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]

INITIATIVES PARTIALLY SUPPORTED BY TREASURY

Hobsonville Urban Development (recommendation b)

- CBC has previously agreed to the creation of an integrated community at Hobsonville (refer CBC Min (06) 22/16). The Hobsonville development business case was signed off by joint Ministers in December 2006.
- HNZC seeks \$74.813 million in capital funding for the Hobsonville development between 2008/09 and 2012/13. *[information deleted in order to enable the Crown to carry out*

commercial activities without disadvantage or prejudice]. There are some uncertainties around the amount and timing of the capital expenditure and revenues, particularly given the potential for resource management delays. It is anticipated that earthworks will begin in 2008 and construction of houses will begin in 2009.

5. Cabinet has previously noted that the Hobsonville development would be funded from two sources – long-term debt through the Debt Management Office for the purchase of additional land, and working capital for operating expenses (refer CBC Min (06) 22/16). Because the development is being undertaken on behalf of the Crown under the Housing Act 1955, all funding must be appropriated. Both HNZC and Treasury support the proposal to appropriate the money directly, rather than funding the development via a loan to the Crown funded from HNZC short-term private borrowings, because it comes at a lower cost to the Crown.
6. Treasury recommends only funding the costs of Precinct One (the first phase), as well as any other costs that need to occur concurrently with Precinct One. This would be consistent with the approval process for the development (precinct by precinct) and help ease the pressure on the capital allocation. Funding for future precincts would represent a specific fiscal risk.

Shared Equity Home Ownership Pilot (recommendation c)

7. Cabinet has previously agreed to a two year shared equity pilot (refer CAB Min (06) 47/2B). HNZC seeks \$55.173 million over two years for a pilot of shared equity loans to 500 households. The scheme is aimed at relatively better off renters who cannot afford the cost of servicing the mortgage on a lower quartile property in high priced areas (prices above \$250,000).
8. CBC has recently agreed that all shared equity loans be targeted to new supply (refer CBC Min (08) 4/2). CBC also agreed to consider expanding the proposed shared equity pilot (refer CBC Min (08) 4/2). A paper will go to POL on 12 March seeking to expand the scheme. An expanded scheme would reduce unmet demand. HNZC still needs to report back on the means for managing demand (refer CBC Min (07) 3/6).
9. HNZC's bid is calculated on the basis of all households receiving a 30% equity loan. CBC previously agreed to equity shares of between 10% and 30% of the house price (refer CBC Min (07) 3/6). HNZC has put forward this proposal as a means of helping manage demand.
10. Treasury supports the pilot but recommends that the equity shares range between 10% and 30%, in line with Cabinet's original decision. Any decision to expand the scheme should be on the same basis. This will reduce the cost of the two year pilot of 500 loans to \$32.925 million over two years, and still reach the same number of households. It will also enable an evaluation of the relative demand for a range of equity shares between 10% and 30%.

INITIATIVES NOT SUPPORTED BY TREASURY

[information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]

[information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]

Rural Housing Programme and Papakianga Loan Scheme (recommendation f)

11. Cabinet agreed in principle to a new delivery model for the rural housing programme in October 2007 subject to funding in Budget 2008 (refer CBC Min (07) 23/14). It did not consider the continuation of the Papakianga loan scheme.
12. HNZN seeks \$3 million in capital in 2008/09 to continue the Papakianga loan scheme for one year. These loans are available for building or buying housing on Maori land held in multiple ownership where commercial finance is not available. The loan is secured over the house only.
13. While Treasury considers the objective of promoting building on Maori multiple-owned land addresses a market failure, it does not support the capital bid because it questions the merit of continuing a scheme which only assisted five households in 2006 and potentially ten households in 2007.
14. Treasury notes that in early 2007 the former Minister of Housing called for additional options to address Maori housing need, including promoting housing on multiple-owned Maori land. In October 2007 the Minister agreed to a substantial work programme with priority given to establishing demonstration housing partnerships with iwi and land owning trusts.
15. If Ministers wish to continue the Papakianga loan scheme, Treasury recommends providing \$1.5 million which would be sufficient to fund six loans, with funding for a further two loans the subject of an in-principle transfer of \$0.5 million in the March Baseline Update.

[information deleted in order to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials]

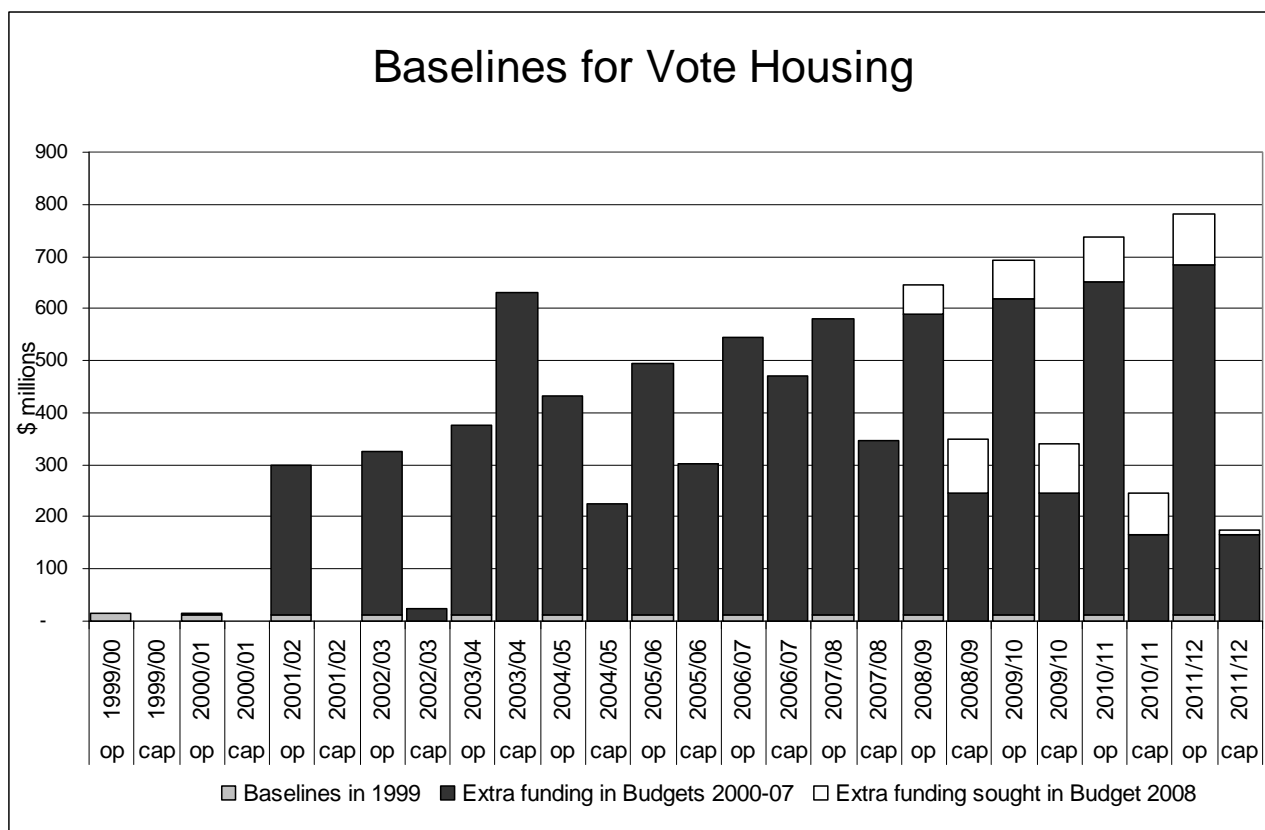
Energy Efficient Warm Homes (recommendation h)

16. HNZC seeks \$77.7 million of capital over five years to increase the rate of its energy efficiency programme in state houses. Between 18,700 and 29,700 out of 64,061 state houses require upgrading. Currently around \$4 million of rental income is applied to the programme annually to upgrade 2,200 homes. At this rate all state houses will be upgraded in 10 to 14 years. The additional funding sought will mean that upgrades are completed within 4 to 6 years. The programme provides insulation, hot water cylinder wraps, pipe lagging and energy efficient heaters.
17. Treasury recommends that HNZC reprioritise other elements of its modernisation programme to fund this initiative. We note the potential health and environmental benefits of these upgrades and consider they should be a priority for HNZC's modernisation programme. We understand that HNZC plans to spend \$65 million on modernisation in 2008/09, increasing to \$130 million in 2009/10. Reprioritisation of the funding sought in this bid would equate to 5.2% of HNZC's modernisation budget in 2008/09 and 10.4% of its modernisation budget in 2009/10.
18. If reprioritisation is not possible, a loan from DMO to HNZC could be provided, reflecting that this proposal would bring forward expenditure that is budgeted to occur in any case. However, a loan would still count against the capital allocation.

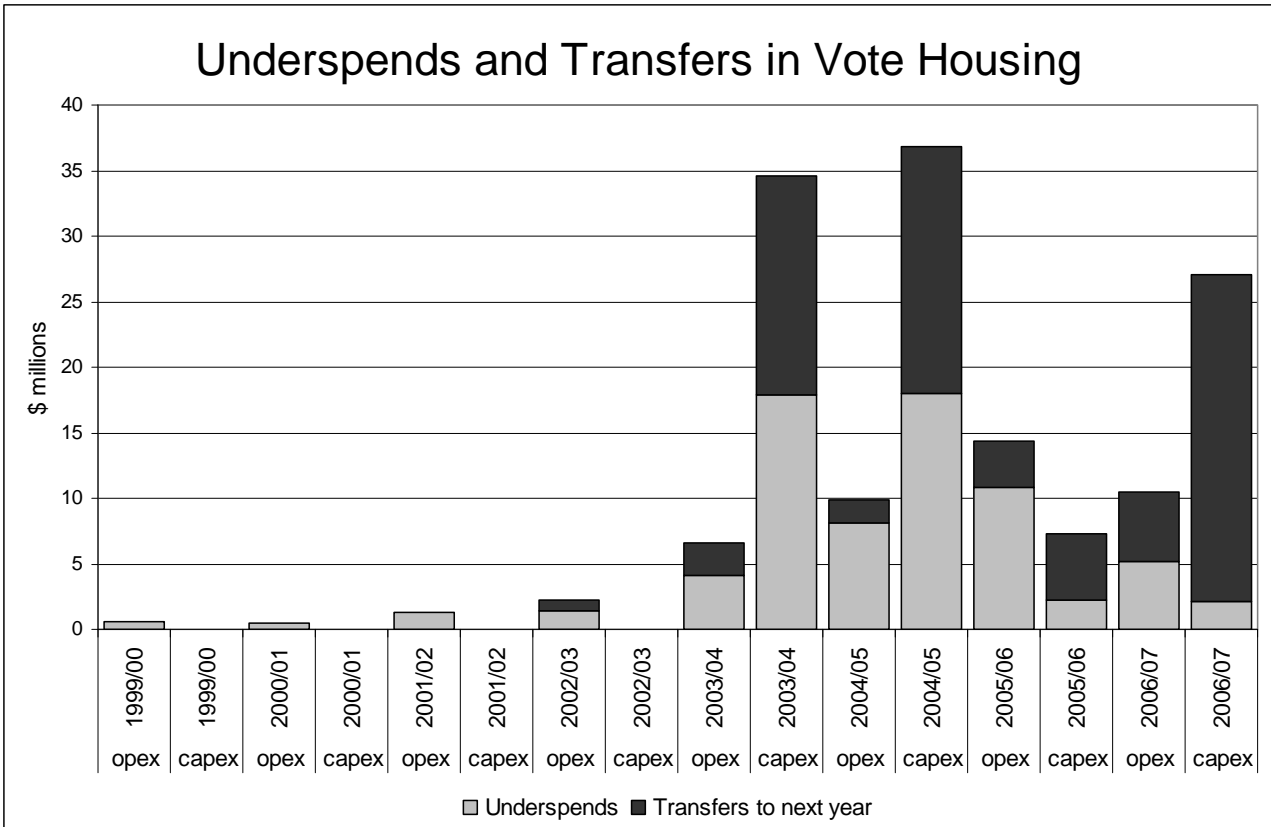
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Analysis of Vote

19. Vote Housing baselines (both HNZC and DBH) are shown in the graph below.



20. The large increase in the operating baseline in 2001 was largely due to the introduction of income related rents. \$192 million of the increase in the operating baseline between 2001/02 and 2007/08 is due to an increase in the income related rental subsidy. The subsidy has increased for two reasons: market rents have been increasing at a faster rate than tenants' incomes, and the number of state houses has increased.
21. Departmental baselines (DBH) have increased by 396% between 2001/02 and 2007/08, from \$13.6 million to \$67.6 million. There was a particularly marked increase in the period 2004/05 to 2006/07 (from \$15.7 million in Budget 2003 to \$73.1 million in Budget 2006), largely arising from the response to the leaky building problem (funding provided to implement tighter regulatory controls and the provision of a resolution service).
22. Non-departmental baselines (HNZC) have increased by 2245% between Budgets 2001 and 2007, from \$1.2 million to \$28.4 million. There was a particularly large increase in Budget 2005 (from \$5.0 million to \$24.5 million), owing to the introduction and expansion of a number of initiatives (rural housing, home ownership education programme, community renewal, healthy housing, mortgage insurance scheme and increasing the policy capability of HNZC).



23. HNZN has a history of capital transfers between years. This is largely due to delays in HNZN's capital acquisition programme.

24. Departmental appropriations (DBH) were underspent by approximately \$5 million per year between 2004/05 and 2006/07. Non-departmental appropriations (HNZN) were underspent by approximately \$3 million in 2005/06 and \$2 million in 2006/07.

One-page Initiative Summaries

One-page summaries of the initiatives for discussion at this bilateral are attached on subsequent pages.

File Note 26 May 2008

The Department of Building and Housing requested the following text be inserted to clarify paragraph 21 on page 13.

“The Department was established in November 2004. A range of functions were transferred into the Department from other entities along with the associated funding. In 2004/05 responsibility for Building Act 2004 Implementation and Building Regulation and Controls outputs transferred from the Building Industry Authority and responsibility for an occupational licensing regime for building practitioners transferred from the Ministry of Economic Development. In 2005/06 the Weathertight Homes Resolution Service was transferred from the Department of Internal Affairs and in 2006/07 the Electrical Workers registration system transferred from the Ministry of Economic Development.

It is therefore inappropriate to try and compare the baselines of the former Ministry of Housing with the current Department of Building and Housing.”