

The Treasury

Infrastructure Funding and Finance Information Release

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Treasury Report: Infrastructure Funding and Finance – Infrastructure Levy Model

Date:	8 April 2019	Report No:	T2019/72
		File Number:	SH-3-2-18-16-1-1

Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Grant Robertson)	Agree the contents of this report	29 April 2019
Minister of Housing and Urban Development (Hon Phil Twyford)	Agree the recommendations of this report	15 April 2019
Minister for the Environment (Hon David Parker)	Agree the contents of this report	15 April 2019
Minister for Local Government (Hon Nanaia Mahuta)	Agree the contents of this report	15 April 2019
Minister for Infrastructure (Hon Shane Jones)	Agree the contents of this report	15 April 2019
Associate Minister of Transport (Hon Julie Anne Genter)	Agree the contents of this report	15 April 2019

Contact for Telephone Discussion (if required)

Name	Position	Telephone		1st Contact
Emma White	Senior Analyst	[39]	[39]	✓
Stacey Wymer	Director	[39]	[39]	

Actions for the Minister's Office Staff (if required)

Return the signed report to Treasury. **Forward** a copy of this report to the Minister of Commerce and Consumer Affairs.

Note any feedback on the quality of the report

Enclosure: No

Treasury Report: Infrastructure Funding and Finance: Infrastructure Levy Model

Executive Summary

Introduction

1. In September 2018 the Cabinet Economic Development Committee (DEV) directed Treasury and the Department of Internal Affairs (DIA) to report back on alternative financing models to fund local infrastructure, and any associated legislation that would be required to underpin these models.
2. The use of alternative financing models is being explored because most high growth councils¹ are close to their maximum debt levels (with debt at 250% of revenue), which constrains their ability to borrow to deliver infrastructure. Without appropriate financing and funding tools, infrastructure supply cannot meet demand. Infrastructure is a necessary enabler for development and most bulk infrastructure is provided by local authorities.
3. The goal of alternative financing models is to free infrastructure investment from local authority financial constraints.
4. The treatment of the alternative financing model by credit rating agencies is critical; if the rating agencies' view any debt raised through an alternative financing model as being an obligation of local authorities, the goal will not be achieved. The credit rating agencies' require there is no legal or moral recourse to the local authority should the alternative financing model fail. This means that no liability (actual or contingent) under the alternative financing model can sit with the local authority and an entity independent of the local authority must have the power to levy directly.

Infrastructure Levy Model

5. This report outlines the proposal to establish an alternative financing model referred to as the Infrastructure Levy Model (the "Model"). The Model is designed to enable new infrastructure projects and upgrades to existing infrastructure to be delivered without being limited by local authority financial constraints.
6. The core of the Model involves the setting of a multi-year Levy (the "Levy") which is paid by beneficiaries of infrastructure projects. The Levy is enabled by legislation and levied by a Special Purpose Vehicle (SPV) which is responsible for financing all or part of the infrastructure project, and has the power to collect the Levy. The SPV may also itself (but doesn't always need to) have a direct role in commissioning construction of the infrastructure. The infrastructure will be transferred to the local authority post construction for nil consideration.
7. A fundamental element of the Model is the provision of a Government Support Package (GSP) to cover certain contingent residual risks. These are the contingent residual risks that would normally sit with the local authority ^[38]
[38] The GSP is critical to ensuring that there is no recourse back to the local authority and therefore meeting rating agency requirements.

¹ High growth councils include Auckland, Hamilton, Tauranga and Queenstown.
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8. This Model is intended to complement, rather than replace, local government infrastructure provision. The Model represents an evolution of the alternative financing model developed by Crown Infrastructure Partners (CIP).
9. While the Model is targeted to the provision of local government infrastructure, it also provides a tool that can be used to support the funding of central government infrastructure initiatives.

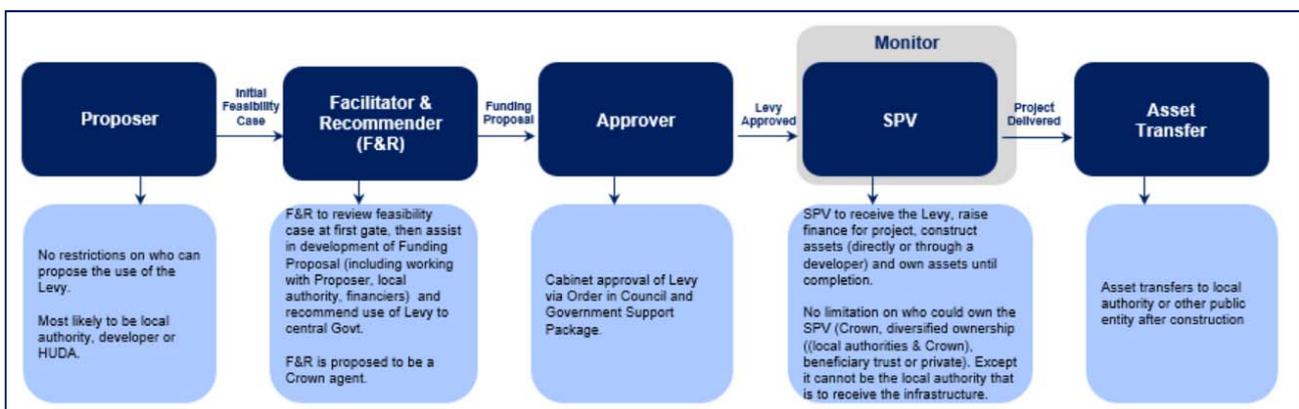
Why is legislation required?

10. Legislation is required to enable the Model. Primarily, the legislation is needed to allow an SPV to collect the Levy (akin to a targeted rate) that can be set for a long period of time (up to 50 years). The ability for an entity independent of local authorities to collect the Levy (that in turn is used to fund the construction of infrastructure) is fundamental to ensure the delivery of infrastructure is not limited by the financing constraints of local authorities.
11. Legislation is also needed to provide the SPV with certain powers during the construction of the infrastructure.
12. The legislation is proposed to be enabling and permissive rather than prescriptive. This reflects that the legislation will need to cover a range of scenarios and infrastructure types and to allow the Model to evolve over time. Given the permissive nature of the legislation, more detailed guidance will need to be developed to cover matters such as how beneficiaries might be identified and how the Levy might be allocated among beneficiaries.

How the process will work

13. The process requires the Levy for each infrastructure project to be approved by the Crown through an Order in Council (OIC). The OIC will set out the details of the Levy including the amount that can be recovered, the term of the Levy (up to 50 years), the beneficiaries of the project who will be subject to the Levy, and the basis of allocating the total Levy between the beneficiaries.
14. The diagram below outlines the process for how an infrastructure project might be identified and a Levy raised.

Process for setting a Levy



Key considerations

15. The Model represents a significant change to the status quo. To accelerate infrastructure delivery, the Model will require greater Crown involvement and the transfer of some risks to the Crown. Whether the development of the Model is “worth it” requires consideration of what will be required to enable the Model, whether the Model will be used and what the counterfactual is. We expand on these considerations below:

Crown involvement is vital

16. Crown involvement and the provision of statutory powers is fundamental to the Model working. Under the status quo, all decision rights and risks for the provision of local infrastructure sit with the local authority (and are ultimately borne by ratepayers). For the Model to work certain decisions rights and risks will transfer to the Crown:
 - a. Final approval of the Levy will sit with the Crown;
 - b. Crown will provide cover for residual risks if they arise (via a GSP), which would ordinarily sit with the local authority ^[38]
[38]

There are protections in the Model to help manage the risk of the GSP being called and the extent of any call (see section five); and
 - c. Due to the level of control that Crown has over the SPV (design of the SPV, approval of the Levy), pursuant to the relevant accounting standard, the assets and liabilities of the SPV will consolidate onto the Crown balance sheet. The overall impact on the Crown balance sheet should be immaterial because the assets and liabilities will offset.
17. Overall, the Model means that the Crown is more involved in the provision of local infrastructure than would ordinarily be the case. This may lead to a general expectation (above the Crown’s agreed obligations) that the Crown will step in if the SPV fails. However, Ministers should be aware that the Crown’s involvement does not constitute an underwrite or full guarantee and is designed to only cover certain contingent residual risks that cannot be borne by the local authority.

The Model involves the creation of a new Levy – with safeguards

18. It is a fundamental part of New Zealand’s constitution that powers to tax are authorised by Parliament. The levy proposed has characteristics similar to a tax – payment is compulsory and is necessarily backed by potentially punitive consequences for non-payment. Accordingly, strict oversight provisions are proposed to avoid potential abuse of the levy power. These include:
 - a. the design and maximum income generated by the Levy must be approved by OIC;
 - b. the Auditor-General has a statutory role to audit the financial statements of the SPV applying the Levy, whether publicly or privately owned; and
 - c. there is a statutory monitor with step in powers to take over aspects of the management of the SPV necessary to ensure the levy is lawfully collected and applied.

19. Some SPV's may have monopoly like features in specific local markets. We have considered whether SPV's should be subject to regulation by an independent regulator such as the Commerce Commission. However, the Model legislation and Levy setting process (in particular the OIC) include a number of safeguards to replicate the regulatory regime for utilities and therefore provide appropriate consumer protections. At this time, extending the Commerce Act to regulate the SPVs is not recommended. Further commentary on this matter is set out in paragraph 124 to 127.

The Model will make a difference – where there are financing constraints

20. We have worked with local authorities and CIP to investigate possible projects to be funded using the Levy (see Appendix A). This has identified that there are some significant projects where using the Model will bring forward infrastructure and therefore accelerate the provision of housing. It has also identified projects where dealing with planning and consent issues will also be required. This highlights the importance of moving forward with other elements of the Urban Growth Agenda and in particular the spatial planning pillar and Resource Management Act (RMA) reform. Removing the financing barrier may encourage local authorities to deal with other constraints more quickly.

The alternatives for the Crown are not costless

21. Without some form of Crown intervention to ease financial constraints for local authorities, the delivery of infrastructure and therefore housing will remain slow. Lack of housing costs the Crown in many ways and is a significant driver of demand for Crown provision of affordable, social and emergency housing. Put simply, the status quo option will continue to cost the Crown.
22. In addition, the alternative options involve more fundamental intervention by the Crown and begin to distort the costs and benefits of infrastructure. These include:
 - a. Increasing local authority borrowing capacity. This would require agreement of local authorities ^[33]
[33]
 - b. Government directly funding the costs of local infrastructure. This would impact on Budget Responsibility Rules.
23. [33]
24. On balance, and taking into account what the alternatives are, we think the Model is an important additional tool for financing infrastructure. It is not without risks and will require the establishment of two new functions (the recommender/facilitator and the monitor). The recommender/facilitator and the monitor have a critical role in supporting Cabinet to make informed decisions on the use of the Levy, managing the risks to the Crown and ensuring the interests of beneficiaries are safeguarded.

Strategy for rolling out the Model

25. How the Model is rolled out will be important. We recommend that the Model is initially used on greenfield sites before being rolled out to brownfield sites. This approach will enable the Model to be tested in less complex projects where beneficiaries opt in, which will reduce risk to the Crown and assist with the acceptance and understanding of the Model by local authorities, beneficiaries and the broader community.

26. At least initially, the Crown will need to own the SPV and account for its activities. A key focus over time will be minimising the risk that sits with the Crown through reducing the scope of the GSP and exploring different SPV ownership structures. Different SPV ownership structures could include joint Crown/Council or private ownership either at the time the SPV is set up, or upon construction of the asset.
27. We will also continue our engagement with the rating agencies to seek further flexibility in the Model that will reduce complexity but still meet their requirements. In particular we are keen to continue testing with rating agencies whether projects that have already been constructed by local authorities and sit on the local authority balance sheet can be refinanced using the Model.

Next Steps

28. We will shortly provide the Minister of Housing and Urban Development with a draft Cabinet paper covering the recommendations in this paper. We will follow up with the Minister of Housing and Urban Development's office regarding the circulation of the Cabinet paper to UGA Ministers and coalition partners.
29. A subsequent Cabinet paper will be required before the end of April to confirm;
 - a. the extent of SPV powers during construction (specifically Resource Management Act and Public Works Act powers to acquire land and interests in land, and local authority powers to access land to manage infrastructure); and
 - b. how the Model relates to the insolvency regime in New Zealand.

Consultation

30. Treasury and the DIA have consulted with the Ministry of Housing and Urban Development, Ministry for the Environment, Ministry of Transport, Ministry of Business Innovation & Employment and the New Zealand Transport Agency (NZTA). Department of Prime Minister and Cabinet, Te Puni Kokiri, Land Information New Zealand and Ministry of Justice have been informed.

Recommended Action

We recommend that Ministers:

- a) **note** that in June 2018, officials reported to Ministers on options to address local authority financial constraints including: central government funding infrastructure directly; alternative financing models; local authorities selling assets to fund infrastructure; and expanding local authority borrowing through the Local Government Funding Agency.
- b) **note** that in considering the June 2018 report, Ministers asked officials to focus on alternative financing models and this decision was endorsed by the Cabinet Economic Development Committee in September 2018.

The Infrastructure Levy Model

- c) **agree** to the establishment of an Infrastructure Levy Model.

Agree/disagree

- d) **note** that the involvement of the Crown is fundamental to the Infrastructure Levy Model working.
- e) **agree** to present a Cabinet paper to the Cabinet Economic Development Committee recommending the establishment of an Infrastructure Levy Model.

Agree/disagree

- f) **provide** any feedback on this report to officials.
- g) **forward** a copy of this report to the Minister of Commerce and Consumer Affairs.

Levy

- h) **note** that the legislation will need to include a mechanism for setting the Levy and definitions for the type of infrastructure and costs that can be covered by the Levy.
- i) **agree** that the mechanism to access a Levy involves the use of an Order In Council approved by Cabinet for each project.

Agree/disagree

- j) **agree** that the Levy be used to fund infrastructure projects that meet the definition in this report of 'eligible infrastructure'.

Agree/disagree

- k) **note** that the legislation has a permissive scope of costs that can be funded by the Levy on the basis that the actual costs to be funded by the Levy will be agreed on a project-by-project basis.
- l) **agree** the Levy regime set out in Appendix B of this report.

Agree/disagree

- m) **note** that Treasury officials will report back with guidance on beneficiary identification and Levy setting principles prior to the legislation being enacted.

Proposer

- n) **agree** that any 'person' be able to propose a project be funded by the Levy.

Agree/disagree

Facilitator and Recommender

- o) **note** that the Infrastructure Levy Model includes a Facilitator to assist with the preparation of proposals to access the Levy.

- p) **note** that the Infrastructure Levy Model includes a Recommender function to ensure Cabinet decisions on whether to use the Levy are well informed and independent of the proposer.

- q) **agree** that the Recommender and Facilitator be the same entity and be Crown-appointed.

Agree/disagree

- r) **note** that Treasury officials will report back on the appropriate entity to be the Recommender and Facilitator and associated funding arrangements by July 2019.

Approvals

- s) **agree** that the matters to be considered by Cabinet when setting a Levy (outlined in paragraph 60 of this report) be incorporated in legislation.

- t) **note** that local authorities have legitimate interests in the use of the Levy.

- u) **note** that officials have developed two local authority approval options to ensure these interests are provided for in approving the Levy.

- v) **select** from either of the following options;

Option 1 – Endorsement

agree that local authority endorsement is required before Cabinet can approve the use of the Model. Local authority endorsement is in relation to ensuring the assets are of an acceptable quality and are compatible with broader networks and that the financial consequences of vesting can be managed. In addition local authorities are required to endorse the Levy unless it would impact on their ability to collect revenue in the future.

Agree/disagree

OR

Option 2 – Consultation

agree that the relevant Local authority be consulted whether the assets are of an acceptable quality and are compatible with broader networks, the financial consequences of vesting can be managed, and the extent to which the Levy impacts on their ability to collect revenue in the future. Cabinet will take this consultation into account when approving the Levy, but is the ultimate decision maker. When seeking the approval of Cabinet the Recommender will put forward the local authorities' view and it will be given due consideration but is not binding.

Agree/disagree

- w) **discuss** with officials if you would like further advice on requiring local authorities to accept infrastructure assets financed using the Model without their consent.

Discuss/no discussion required

Special Purpose Vehicle

- x) **agree** that local authorities be required by legislation to collect the Levy on behalf of the SPV if the SPV requires it; and the parties agree terms.

Agree/disagree

- y) **agree** that legislation specify that any monetary development contributions already collected for a project that is funded by a Levy be transferred to the SPV.

Agree/disagree

- z) **note** that there are a range of SPV ownership options and structures.

- aa) **agree** the legislation not exclude any SPV ownership options or structures.

Agree/disagree

- bb) **agree** the proposed monitoring, reporting, intervention and disclosure regime for SPV's outlined in this paper.

Agree/disagree

- cc) **note** that Treasury officials will report back on the recommended monitoring entity for SPV's by July 2019.

Asset transfer

- dd) **note** the legislation will enable SPV's to own assets during construction and not be prevented from ownership during the term of the Levy.

Agree/disagree

- ee) **note** that officials will shortly prepare a Cabinet paper regarding the proposed approach to the powers of the SPV during the construction period.

Government Support Package

- ff) **note** the Government Support Package is an integral part of the rating agency requirements of the Infrastructure Levy Model.

- gg) **agree** that a Government Support Package will be provided as part of projects funded by the Infrastructure Levy Model.

Agree/disagree

- hh) **note** the terms of each GSP will be agreed on a case by case basis, ^[38]
[38]

Consequential changes

- ii) **agree** to consequential changes to local government legislation to ensure consistency between the Model and local government legislation.

Agree/disagree

Insolvent Transactions

- jj) **note** that officials will provide further advice on whether the Levy legislation be used to avoid a situation where parties are unfairly treated in an insolvency of the SPV.
- kk) **agree** that officials from the Ministry of Business, Innovation and Employment, Department of Internal Affairs and Treasury provide further advice to Cabinet about how insolvent transactions relate to the Infrastructure Levy Model.

Agree/disagree

Stacey Wymer
Director

Hon Grant Robertson
Minister of Finance

Hon Phil Twyford
Minister of Housing and Urban Development and Transport

Hon David Parker
Minister for the Environment

Hon Nanaia Mahuta
Minister of Local Government

Hon Shane Jones
Minister of Infrastructure

Hon Julie Anne Genter
Associate Minister of Transport

Treasury Report: Infrastructure Funding and Finance: Infrastructure Levy Model

Purpose of Report

1. In September 2018 the Cabinet Economic Development Committee (DEV) directed Treasury and the Department of Internal Affairs (DIA) to report back on alternative financing models to fund local infrastructure, and any associated legislation that would be required to underpin these models.
2. The goal of alternative financing models is to free infrastructure investment from local authority financial constraints. The timely delivery of infrastructure is critical to enable and accelerate housing development and to improve housing affordability.
3. This report outlines a new alternative financing model to fund and finance local infrastructure – referred to as the Infrastructure Levy Model (the “Model”). This involves the creation of a Levy (the “Levy”) paid by the beneficiaries of infrastructure projects. Legislation is required to enable the Model.
4. The purpose of this report is to:
 - a. set out how the Model and Levy will work;
 - b. seek agreement on the proposed policy positions to implement the Model and draft the required legislation; and
 - c. identify the key risks and outstanding issues to implementing the Model.
5. The report is divided into nine sections:

Section 1: Background

Section 2: Objectives

Section 3: Overview of how the Model and Levy will work

Section 4: Infrastructure Levy Model and process

Section 5: Government Support Package

Section 6: Consequential amendments to legislation

Section 7: Accounting treatment, income tax and GST

Section 8: Risks

Section 9: Next steps

Section 1: Background

6. This report is part of the cross-government work on the Infrastructure Funding and Financing (IFF) pillar of the Urban Growth Agenda (the UGA). The main objective of the UGA is to improve housing affordability, underpinned by affordable urban land.

7. The supply of infrastructure is currently constrained by financial restrictions on local authorities, which provide most local infrastructure. The financial restrictions are a mix of technical factors and behavioural issues that constrain borrowing by local authorities (referred to in this report as the financial constraints).
8. The technical factors include:
 - a. the Local Government Funding Agency (LGFA) borrowing covenants – which require debt as a percentage of revenue to remain below 250%;
 - b. the financial prudence regulations of the Local Government Act – which discourage borrowing costs rising above 15% of revenue; and
 - c. the financial strategies set by each local authority as part of its Long Term Plans.
9. The LGFA covenants establish hard upper limits on the ability of local authorities to increase debt levels, while the financial prudence regulations reinforce a cautious approach to debt on the part of local authorities.
10. The behavioural issues include the desire of local authorities to retain strong credit ratings (which assists in minimising the cost of borrowing) and the self-imposed limits set up by local authorities within their financial strategies. These behaviours are a consequence of ratepayer preferences for low debt and low rates.
11. We provided you with a report in June 2018 outlining in greater detail these constraints and setting out the options available to reform the funding and financing of local infrastructure (TR 2018/1087 refers).
12. Of the options outlined in our June 2018 report, investigating alternative financing models was recommended to provide an enduring solution to the financial constraints faced in the provision of local infrastructure. In September 2018, DEV directed Treasury and DIA to report back to DEV on alternative financing models to fund local infrastructure, and any associated legislation that would be required to underpin these models.
13. Subsequently, officials have developed an alternative financing model ^[33]
[33]
14. ^[33] officials have been working with local authorities, other government agencies and legal and commercial advisors to refine and work through policy issues to implement the Model.

Section 2: Objectives

What are we trying to achieve?

15. We have sought to develop a model which enables infrastructure projects to be funded and financed without being limited by the financial constraints faced by local authorities (especially high growth local authorities). Most high growth councils are close to their maximum debt levels (debt below 250% of revenue), which constrains their ability to borrow to deliver infrastructure. A consequence of this is that there is a long list of unfunded but economically viable infrastructure projects that cannot proceed unless self-funded by developers.

16. We consider that alternative financing models should be explored because:
- a. it allows viable projects to proceed outside of the local government financial constraints and allows the system to be responsive to demand;
 - b. it allows costs to fall on the communities and homeowners who benefit from the new infrastructure;
 - c. it makes the viability of the project the decision, removing the trade-offs which local authorities often have to make when allocating capital;
 - d. it allows for greater rigour and transparency in the allocation of risk and costs to the appropriate parties;
 - e. it provides price signals to ensure investment occurs where it is most needed;
 - f. it will allow for a much greater quantity of debt to be leveraged from revenue streams than would be possible through a local authority; and
 - g. it provides a pipeline designed to allow new capital to flow into the system.
17. These alternative financing models would complement – rather than replace – local government infrastructure provision. The Model represents an evolution of the Crown Infrastructure Partners (CIP) model.

Key considerations in designing the model

18. The development of an alternative financing model has raised a range of policy issues. In providing advice on these policy issues and assessing different options, the following considerations have guided us:
- a. **Rating agency requirements:** The key matter that a rating agency will consider is whether the alternative financing model creates any legal or moral recourse back to the local authority. If there is recourse then the debt raised through the alternative financing model will be subject to the local authority financial constraints. Ultimately, this means that the goal of alternative financing models will not be achieved.
 - b. **Public policy considerations:** This is about ensuring that the Model is consistent with general policy principles such as fairness, efficiency, sustainability and that entities undertaking investment on behalf of beneficiaries/Levy-payers are subject to appropriate accountability arrangements.
 - c. **Implementation considerations:** This is primarily about the willingness of parties to use the Model including local authorities, developers and financiers.
 - d. **Replicability and scalability:** This is about ensuring that the Model is fit for purpose (both for now and how it might evolve over time) and ensuring that it can be replicated across a variety of different infrastructure projects and locations.
19. These considerations are not independent of each other and in some cases trade-offs need to be made.

Why is legislation required?

20. Legislation is required to enable the Model. Primarily, the legislation is needed to allow new entities the ability to collect the Levy (akin to a targeted rate) over a long period of time (up to 50 years). This legislation will mark a significant change to the status quo in three key respects:
 - a. First, it will enable new entities (Special Purpose Vehicles (SPVs)) to have statutory levying powers akin to a targeted rate. Anything less than the new entity having the power to levy directly (such as a local authority transferring or assigning their powers) will not alleviate the financial constraints faced by local authorities (i.e. the debt will still be included in the local authorities' debt to revenue ratio).
 - b. Secondly, it will enable the Levies to be set for a long period of time (up to 50 years). Currently, a local authority can only set a rate for one financial year but can borrow for extended periods. This is because they have no cap on their liability and no ability to declare bankruptcy. They also have the ability to offer rates, including the ability to levy rates, as a security for borrowing. The absence of these rights for an SPV is a barrier to the financing of infrastructure projects and the SPV requires the certainty provided by multi-year Levies to secure finance.
 - c. Thirdly, the SPV will be responsible for providing the infrastructure and needs powers that local authorities would usually use to achieve this.

Evolution of the Crown Infrastructure Partners (CIP) model

21. In November 2018, the Government (via CIP) and Auckland Council announced the Milldale development (Milldale) north of Auckland. Milldale involved the use of an alternative financing and funding mechanism, including the use of infrastructure payments to be paid by beneficiaries of the development.
22. While the Milldale model was able to access long term financing without being limited by the financial constraints of the local authority, it has limitations as to its replicability. This is because the Milldale model relies on a contract where beneficiaries agree to pay the infrastructure payments. This approach is difficult to replicate in a situation where there are many beneficiaries, existing beneficiaries, and/or beneficiaries who are unwilling to contribute.
23. By contrast the Model is enabled through legislation which means that identified beneficiaries are required to pay the Levy (much as homeowners are required to pay local authority rates).

Section 3: Overview of how the Model and Levy will work

24. The core of the Model involves the setting of a multi-year Levy (up to 50 years) which is paid by beneficiaries of infrastructure projects. The Levy is enabled by legislation and levied by the SPV who is responsible for financing all or part of the project, and has the power to collect the Levy.² The SPV may also itself (but doesn't always need to) have a direct role in commissioning construction of the project.

² In practice we expect the SPV will want the relevant local authority to collect the Levy on its behalf.
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25. A fundamental element of the Model is the provision of a Government Support Package (GSP) to cover certain contingent residual risks. These are the contingent residual risks that would normally sit with the local authority ^[38]
[38] The GSP is critical to ensuring that there is no financial recourse back to the local authority and therefore ensuring that the debt of the SPV is not included in the rating agency assessment of the local authorities' borrowings. More information on the GSP can be found in section five of this report.
26. This section provides an overview of the design of the Levy. The details of the Levy regime can be found in Appendix B. Where appropriate the design of the Levy mimics many of the rating provisions within the Local Government (Rating) Act 2002 (LGRA).

Setting of the Levy

27. A Levy for each infrastructure project will be set by Order in Council (OIC). The OIC will set out the details of the Levy including:
- a. the amount that can be recovered, and any relevant milestones;
 - b. the term of the Levy (expected to be 25 – 50 years);
 - c. the beneficiaries of the project who will be subject to the Levy; and
 - d. the basis of allocating the Levy between beneficiaries.
28. The OIC may also set out further conditions or limitations on the use of a Levy for a project (for instance, a limit on the amount of Levy revenue that can be applied to costs such as the equity return).
29. We considered whether Cabinet (by OIC), a delegated Minister, a delegated Crown body or a delegated local authority should approve the use of a Levy. Our legal advice was that Cabinet approval of a Levy via an OIC was the most constitutionally robust approach and therefore, reduces the risk of judicial review of the Levy.
30. We propose that the legislation enable a permissive approach to beneficiary identification and allocation of the Levy between beneficiaries³. Under the proposed approach it will be possible for the Levy to be phased to incentivise development (e.g. larger amounts upfront and smaller amounts in later years) or to be allocated according to those that benefit the greatest from the infrastructure (e.g. by proximity to infrastructure).
31. Feedback from local and central government is that the process of identifying beneficiaries and allocation choices can be complex and we intend to issue policy guidance to assist in those decisions.

Use of the Levy

32. The Levy is to be used to fund new infrastructure projects and upgrades to existing infrastructure by agreement with the Crown and relevant local authority/s (more information on the approval process for the Levy can be found in section four).

³ The allocation of the Levy among beneficiaries could depend on various factors, such as; geographical land area; use of land; activities permitted on land; and value of the land.

33. We have developed a scope of 'eligible infrastructure' to define the type of projects that a Levy can be used for. In setting the scope of eligible infrastructure we considered:
 - a. The range of infrastructure required to enable housing and urban development including ancillary infrastructure (such as community facilities).
 - b. Broader infrastructure requirements to unlock housing or to enable housing between urban centres (including projects which may span several local authorities).
 - c. Definitions of infrastructure used in potentially relevant statutory definitions, by CIP and the eligibility criteria applied by the Housing Infrastructure Fund.
 - d. Whether infrastructure is typically funded by local authorities or through central government funding.
 - e. Whether there are existing and well-functioning funding and financing mechanisms in place for certain types of infrastructure.
34. Taking into account these considerations, the proposed scope of eligible infrastructure means new or upgraded infrastructure within the following categories:
 - a. water, wastewater, stormwater
 - b. transport and associated infrastructure (including bridges and tunnels), and cycleways and footpaths [to include local roads and State Highways]
 - c. public transport infrastructure, including rail, busways, park and ride, exchanges, stations, shelters
 - d. community amenities to the extent they form a part of a wider project
 - e. environmental resilience infrastructure, such as flood protection, pump stations and environmental restoration
35. The scope will expressly exclude:
 - a. housing
 - b. any gas, telecommunications, electricity, or other services networks
 - c. solid waste disposal or recycling; and
 - d. schools, hospitals, prisons, social housing.
36. The proposed legislation to establish the Housing and Urban Development Authority (HUDA) may contain some relevant definitions and we will take these into account during the legislative process.

Costs funded by the Levy

37. The legislation will need to articulate what costs can be funded by the Levy. We recommend the legislation make it possible for a wide range of costs to be covered by the Levy. The exact make-up and extent of the costs to be covered by the Levy will be considered on a project-by-project basis taking into account affordability for the beneficiaries. The proposed list of eligible costs to be included in legislation are listed below:
- a. Construction costs – including direct construction costs, insurance and project contingency costs.
 - b. Project establishment costs of the Proposer, Facilitator (where these are directly attributable to a specific project funded by the Levy), bidders⁴ and SPV owner, with limitations governing eligibility set out in guidance material.
 - c. SPV operating costs including management and administration costs.
 - d. Asset operating and maintenance costs prior to vesting.
 - e. Financing costs including debt interest costs, equity costs (where relevant), arrangement, commitment and agency fees and reserve accounts.
 - f. Enforcement and intervention costs.
 - g. Levy collection costs most of which will be paid to a local authority to collect the Levy.
 - h. SPV monitoring costs.
 - i. [38]
 - j. Any of the costs referred to in (a) to (c) above that have been incurred by another party and which the SPV is liable to fund or reimburse (this would be the case in a situation where the SPV did not construct the assets or took over the construction of assets from a local authority and used Levy revenue to repay local authority debt).

Recommended actions:

note that the legislation will need to include a mechanism for setting the Levy and definitions for the type of infrastructure and costs that can be covered by the Levy.

agree that the mechanism to access a Levy involves the use of an Order In Council approved by Cabinet for each project.

agree that the Levy be used to fund infrastructure projects that meet the definition in this report of 'eligible infrastructure'.

note that the legislation has a permissive scope of costs that can be funded by the Levy on the basis that the actual costs to be funded by the Levy will be agreed on a project-by-project basis.

agree the Levy regime set out in Appendix B of this report.

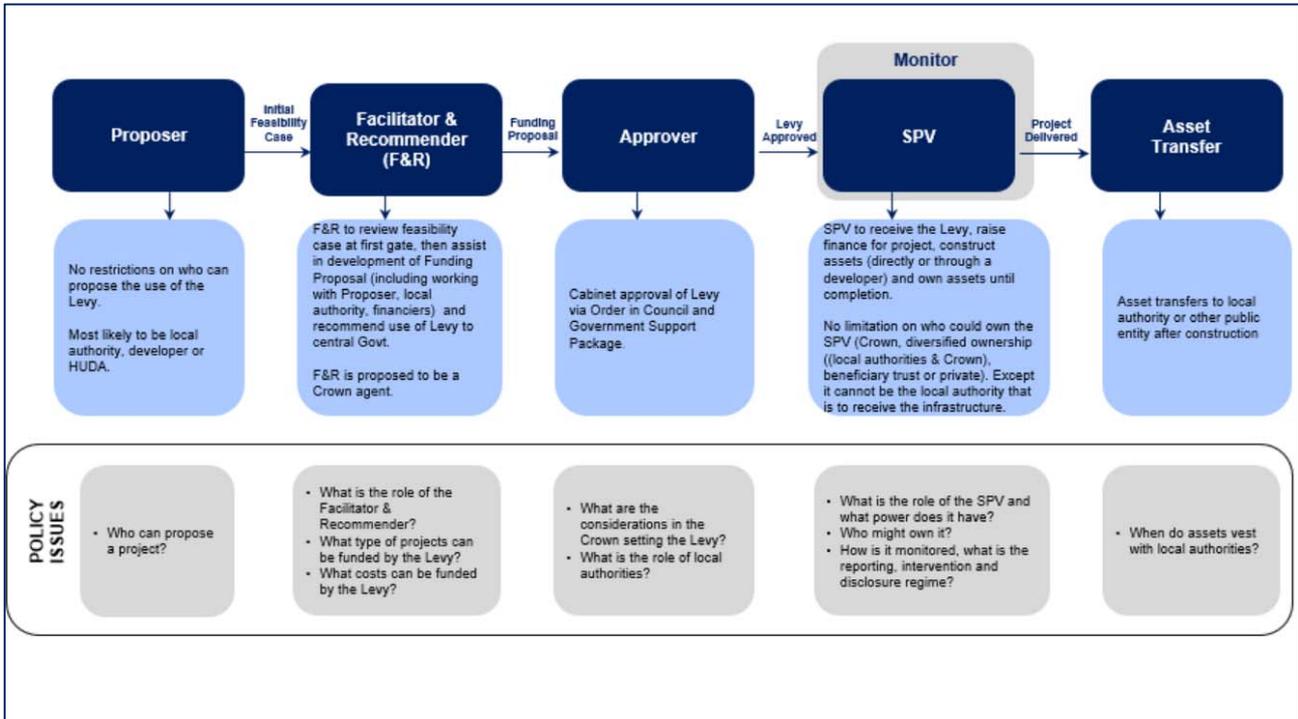
note that Treasury officials will report back with guidance on beneficiary identification and Levy setting principles prior to the legislation being enacted.

⁴ Including potentially unsuccessful bidders whose costs are considered reasonable by the Facilitator and Recommender.
T2019/72: Infrastructure Funding and Finance – Infrastructure Levy Model

Section 4: Infrastructure Levy Model and process

38. This section describes in more detail the process to take a project from conception through to being funded by a Levy and then (if not already in public ownership) transferred back to a public entity. In doing so, we identify the key policy issues (bottom row of the following diagram) and address these.

Process for setting a Levy



39. This section is ordered by following the progress of a project starting with the role of the 'Proposer' below.

Proposer



40. The role of the Proposer is to identify and put forward a project to be considered to be funded by the Levy. To encourage uptake of the Model (and given the range of other safeguards in place to ensure the Levy is used appropriately), we have not limited who can propose that a project be funded by the Levy. In practice, we expect the most likely Proposers will be local authorities, developers and the HUDA.

41. In addition, there will be guidance available to the Proposer to inform them about the type and likely size of projects that could be funded by the Levy, process for getting a Levy approved and beneficiary identification and allocation methods. This guidance will help to ensure that projects which have a realistic prospect of getting approved for a Levy are put forward.

Recommended actions:

agree that any 'person' be able to propose a project be funded by the Levy.

Facilitator and Recommender



42. As the approver of the Levy (and any GSP), the Crown will need to be advised by a party independent of the Proposer on whether to approve a Levy. We propose that the Crown appoint a party to act as both the recommender of the Levy (the Recommender) and also to facilitate and filter proposals from Proposers seeking to access the Levy (the Facilitator).
43. We considered separating the role of the Facilitator and Recommender as there is a potential conflict of interest between facilitating proposals and then objectively recommending which proposals are approved by Cabinet. However, we consider that this issue can be managed by either the Ministry of Housing and Urban Development or the Treasury providing second opinion advice to Ministers on the recommendations made by the Recommender. In addition we expect the Facilitator and Recommender will need to work closely with other agencies across Central Government to ensure that projects are sequenced in a coherent manner, especially where a project places pressure on other sectors (e.g. the provision of connecting transport by NZTA).
44. We also considered whether there should be one or multiple Facilitators. We concluded that having one Facilitator would be efficient, lead to consistent advice about the use of the Levy and enable a body of expertise to be developed to ensure that the Model is replicable.
45. A decision on who acts as the Facilitator and Recommender is not required for legislation. We recommend the Recommender and Facilitator role be undertaken by a Crown-appointed body. However, further work is required to identify who the Crown-appointed body will be and how they will be funded. Consistent with their current role, one option is for CIP to be the Facilitator and Recommender. Treasury will provide a separate report back on these matters.
46. The Facilitator will receive an Initial Feasibility Case from the Proposer, covering:
- a. project background and objectives;
 - b. current state of the project;
 - c. proposed asset and SPV ownership model;
 - d. who the Proposer is; and
 - e. an estimate of the amount of the Levy to be paid by beneficiaries.

47. The purpose of the Initial Feasibility Case is to provide a high level assessment of whether the Model is suitable for the project, without incurring significant cost for either the Proposer or the Facilitator.
48. Once through this initial assessment⁵, the Proposer (with assistance from the Facilitator) will develop the Funding Proposal, which will be used for final approvals and negotiation of any GSP. As part of the approval the Recommender will review the final Funding Proposal, which will need to include:
 - a. a detailed project overview including information on the consents that have, or will need to have, been obtained to proceed with construction of the asset(s);
 - b. detail on the structure and application of the Levy;
 - c. the commercial and financial business case for the project;
 - d. how the infrastructure will be procured; and
 - e. an assessment of the Levy against the Central Government approval criteria (see “Approver” section below).

Recommended actions:

note that the Infrastructure Levy Model includes a Facilitator to assist with the preparation of proposals to access the Levy.

note that the Infrastructure Levy Model includes a Recommender function to ensure Cabinet decisions on whether to use the Levy are well informed and independent of the Proposer.

agree that that the Recommender and Facilitator be the same entity and be Crown-appointed.

note that Treasury officials will report back on the appropriate entity to be the Recommender and Facilitator and associated funding arrangements by July 2019.

Approver



49. The legislation needs to explain who approves the Levy for a project. The ultimate approval right will reside with the Crown (Cabinet), which will have the right to approve (or reject) a Levy by OIC. There are choices for how involved local authorities are in the approval process.
50. Local authorities will be required to provide all other project approvals (including the approval of consents) as they normally would. This approval section relates only to the approval of the use of the Model and Levy for a project.

⁵ Any projects that do not pass the high level assessment will be referred back to the Proposer to consider whether they are re-scoped or whether the proposal to use the Model is abandoned.

Local Authority Role

51. This section sets out the following:
- a. the key points of interest for local authorities in using the Model;
 - b. how the approval process in the Model could provide for local authority interests; and
 - c. whether the local authority approval process should be included in legislation.
52. When considering the role of local authorities in the approval process for the Model, the following key factors are relevant:
- a. Local authorities have genuine interests (outlined in the table below) in the use of the Model; in particular they will have ongoing responsibility for the assets.
 - b. The Government is increasingly seeking to work in partnership with local authorities to address urban growth challenges.
 - c. The Government is seeking to decouple local authority decisions on planning from local authority financial constraints.
 - d. The potential reluctance of local authorities to use the Model and Levy due to political considerations.
53. The approach taken will depend in part on the weightings of these factors. We note that the Model is only intended to overcome the financing constraint for local infrastructure and does not deal with planning and consenting issues.
54. Analysis of these matters can be found in the table below.

Summary of local authority interests and approval options	
<p>What are the key points of interest for local authorities in using the Model?</p>	<p>We do not consider that local authorities should have broad approval rights in relation to the use of the Model. Rather any rights should be focussed on the key points of interest for the local authority; being:</p> <ol style="list-style-type: none"> 1. Practical and financial interests relating to the asset vesting back to the local authority: <ul style="list-style-type: none"> a. asset quality/compatibility with wider networks – whether the assets are built to required standards and compatible with existing networks (and whether any wider network effects can be managed); and b. ability for the local authority to plan for and meet the operational and maintenance (O&M) costs once the asset has vested. These costs could be significant and in the range of 2% to 5% of the capital cost annually (\$100M project would equate to annual O&M costs of \$2M to \$5M and on a \$1Bn project would equate to annual O&M costs of \$20M to \$50M). 2. Affordability – whether the payment of the Levy will compromise their ability to collect rate revenue from beneficiaries.

Summary of local authority interests and approval options

<p>How will the approval process in the Model provide for local authority interests?</p>	<p>We have developed two broad options for local authority approvals for Ministers to consider. The main difference between the options below is whether local authority has a binding (endorsement) or non-binding (consultation) role in approving the use of a Levy.</p> <p>Option 1: Endorsement – Local authorities are required to endorse that the assets are of an acceptable quality and are compatible with broader networks and the financial consequences of vesting can be managed. In addition local authorities are required to endorse the Levy unless it would impact on their ability to collect revenue in the future.</p> <p>Option 2: Consultation – Local authorities are consulted on; whether the assets are of an acceptable quality and are compatible with broader networks, the financial consequences of vesting can be managed, and the extent to which the Levy impacts on their ability to collect revenue in the future. When seeking the approval of Cabinet, the Recommender will put forward the local authorities' view and it will be given due consideration but is not binding.</p> <p>Practically, however, because of the requirement to vest the asset back to the local authority, the local authority does have a potential veto right under either option.</p> <p>To remove this veto would require either:</p> <ol style="list-style-type: none"> 1. The SPV to continue to own and maintain the asset. Whilst the legislation does not preclude this from occurring, there are a number of challenges involved in the SPV owning and operating assets in the long term, such as restrictions on who can own land that has a legal 'road' status and statutory conditions attached to the terms under which a local authority can enter into arrangements for the provision of water services. 2. The legislation to include provisions to force the local authority to accept the assets. This approach would: <ol style="list-style-type: none"> a. be inconsistent with the broader partnership approach that the government is promoting with local authorities; b. restrict a local authorities' ability to effectively conduct their duties and meet their obligations under the Local Government Act 2002; and c. potentially lead to a request for financial support from the Crown as the financial consequences of taking the assets could be significant. 3. Utilising the HUDA. This is because the HUDA has a framework for managing: <ol style="list-style-type: none"> a. physical operation and management of assets while vesting occurs (the HUDA itself will manage assets, whereas the SPV's under the Model will not be able to do this easily); b. how assets will be vested to the local authority; and c. consenting issues which would be required in the event a local authority is not supportive of the project.
<p>Is the local authority approval process included in the Model legislation?</p>	<p>Official's preferred approach is that local authority approval rights (whether it be option 1 or option 2) should be prescribed in legislation and relate only to the three matters above (i.e. the local authority should not have broad approval rights in relation to the use of the Model). Legislation provides clarity of what is expected of both local authorities and Ministers.</p>

Approval of any other roles or support

55. For any given project there may also be other support requested from a local authority. This might include a direct financial contribution to a project from a local authority and/or any operation and maintenance contracts with the SPV that may be required.
56. Local authorities will negotiate these matters on their own terms. However, there is no approval mechanism required in the Model (and legislation) to enable this to occur as a project is progressed.

Timing of local authority approval rights

57. The timing of approvals is likely to vary from project-to-project. Subject to the agreed approach on the role of local authorities, the legislation should require that all necessary approvals are held before a project and Levy are approved by an OIC. In practice, the timing of approvals will be important and where possible these should occur:
 - a. as early in the process as is possible (to provide the parties with assurance to proceed with developing a funding proposal); yet
 - b. still late enough to ensure that approvals are based upon developed proposals that can be costed with reasonable accuracy.
58. Subject to the agreed approach on the role of local authorities, we propose that local authority confirmation (to the extent required) is provided at two stages of the process:
 - a. An **in-principle Letter of Commitment** at the feasibility stage. This is intended to ensure that time and resources are only committed to advancing proposals for viable projects.
 - b. A **formal endorsement or consultation statement** at the approver stage⁶.

Crown approval process

59. Cabinet will have discretion to approve a Levy by OIC on the advice of the Recommender and Facilitator. The OIC will include the specifics of the Levy (as outlined in paragraph 27 above). If a GSP is required for the project it will be approved by Cabinet, on the advice of Treasury, at the same time as the OIC is considered.
60. We recommend the following matters be considered by Cabinet when setting a Levy and be incorporated in legislation. These are loosely based on the Local Government Act 2002 (LGA)⁷ and include:
 - a. the distribution of benefits between the project community (as a whole), identifiable parts of the project community, and individuals;
 - b. the period in or over which those benefits are expected to occur;
 - c. the extent to which the actions or inaction of particular individuals or a group contribute to the need to undertake the project;
 - d. the extent of any other contribution towards the costs of the project;

⁶ Before an OIC is approved, the affected local authority will be required to formally endorse or provide a consultation statement covering the matters described in the table under paragraph 54.

⁷ Specifically, section 101(3).

- e. the affordability and sustainability of the Levy over the intended period;
 - f. any other matters of practicality, efficiency or equity relevant to the Levy; and
 - g. the extent of benefits (if any) outside the project community.
61. The benefit of including these matters in legislation is that it provides some clarity to Proposers and the Recommender and Facilitator whilst preserving options for Cabinet to place weightings on different matters that are the most important to them, and to accommodate a wide range of potential projects.
62. We expect that the Funding Proposal prepared by the Facilitator and Recommender will provide an assessment of the proposal against each of the considerations to help inform Cabinet's decision.

Recommended actions:

note that local authorities have legitimate interests in the use of the Levy.

note that officials have developed two local authority approval options to ensure these interests are provided for in approving the Levy.

select from either of the following options;

- **Option 1 - Endorsement**

agree that local authority endorsement is required before Cabinet can approve the use of the Model. Local authority endorsement is in relation to ensuring the assets are of an acceptable quality and are compatible with broader networks and that the financial consequences of vesting can be managed.

In addition local authorities are required to endorse the Levy unless it would impact on their ability to collect revenue in the future.

OR

- **Option 2 - Consultation**

agree that the relevant Local authority be consulted whether the assets are of an acceptable quality and are compatible with broader networks, the financial consequences of vesting can be managed, and the extent to which the Levy impacts on their ability to collect revenue in the future. Cabinet will take this consultation into account when approving the Levy, but is the ultimate decision maker. When seeking the approval of Cabinet the Recommender will put forward the local authorities' view and it will be given due consideration but is not binding.

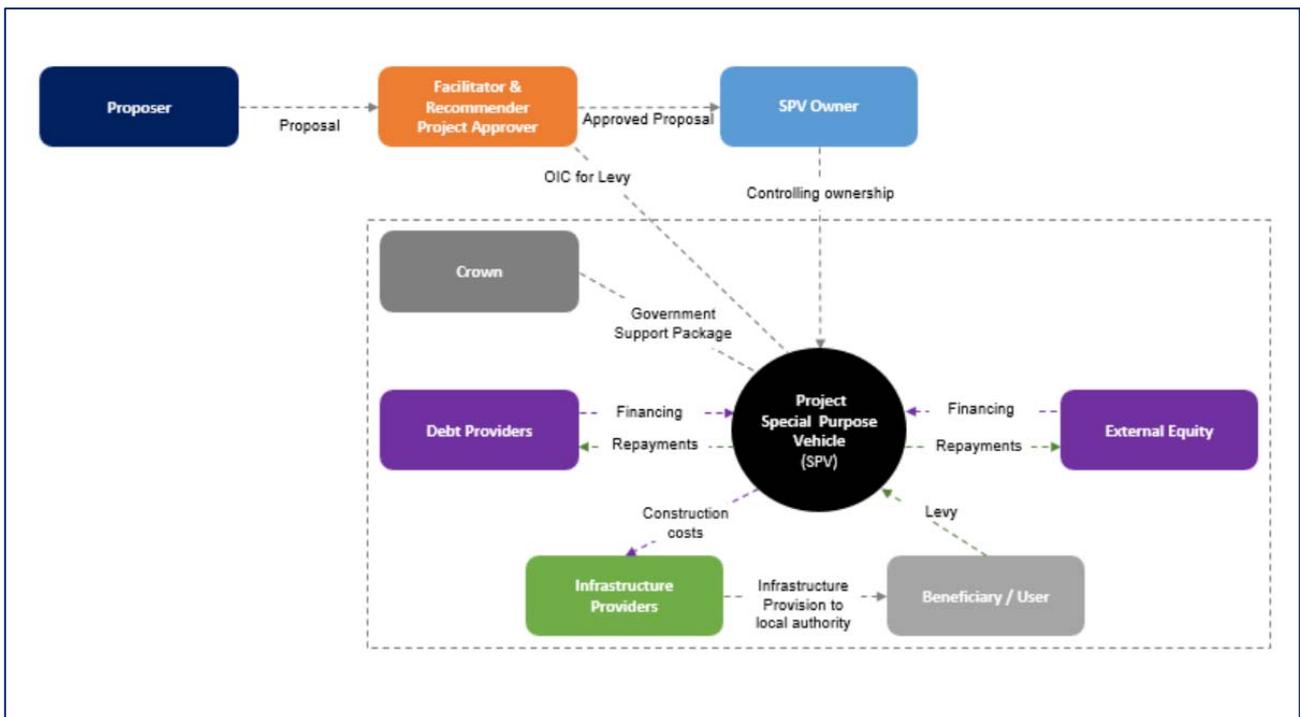
discuss with officials if you would like further advice on requiring local authorities to accept infrastructure assets financed using the Model without their consent.

agree that the matters to be considered by Cabinet when setting a Levy (outlined in paragraph 60 of this report) be incorporated in legislation.

Special Purpose Vehicle (SPV)



63. The use of an SPV that is not owned by the local authority is required to ensure infrastructure projects can be delivered without being limited by local authority financial constraints. The diagram below sets out how the SPV is ring-fenced from local authorities and its relationship with debt and equity providers.



64. The Levy provides the SPV with access to a long-term funding stream that enables capital to be raised to finance infrastructure. The SPV will:
- collect the Levy;
 - raise capital (utilising the Levy revenue stream);
 - finance infrastructure;
 - commission construction and transfer the infrastructure to the relevant local authority (or other relevant public entities) – if the SPV has a direct role in construction for any project; and
 - repay any finance raised for infrastructure.

Collection of the Levy

65. The SPV will be empowered through legislation to collect the Levy. The legislation will enable the SPV to collect the Levy directly (invoicing beneficiaries directly) or by entering into an arrangement with the relevant local authority for it to collect the Levy on behalf of the SPV (where the Levy would be included as a separate line item on the rates bill).
66. We believe the optimal arrangement is for the SPV to enter into a collection arrangement with the local authority. This is from an efficiency perspective (local authorities have existing systems in place to allocate and collect the Levy from beneficiaries) and to enhance the bankability of the Model (default risk on items charged through the local authority rates bill is low). On the Milldale project undertaken by CIP, the financiers noted that the collection agency arrangement with the relevant local authority was critical to securing a lower financing rate.
67. There is a choice about whether the local authority be required by legislation to enter into a collection agreement with the SPV or whether the SPV is required to negotiate this on a project-by-project basis. Allowing local authorities to decide if they want to enter into an agreement with the SPV is consistent with central government wanting to work in partnership with local authorities. However, the efficiency and bankability considerations are fundamental to the Model working in practice.
68. Therefore, we recommend that the legislation require that the relevant local authority collect the Levy, if requested to do so by the SPV. This requirement will be subject to the SPV covering the local authorities' reasonable costs and expenses in providing the collection service. A disputes resolution process may be required if agreement cannot be achieved.
69. This legislative requirement would cover the standard collections role only (e.g. including the Levy on the rates bill, reminder notices and collecting and accounting for payments). The legislative requirement would not extend to enforcement action – as we expect there would be considerable resistance from local authorities to taking enforcement action on behalf of another party (however a local authority could still agree to perform such a role by agreement).

Security, Priority and Enforcement of the Levy

70. The Model's security, priority and enforcement regime has been modelled on the LGRA, which applies to local authority rates. This means that the Levy will effectively be secured against the land in the same manner as local authority rates and have priority behind local authority rates but ahead of any other claims against that land (e.g. mortgages) on enforcement. In practice if a Levy is unpaid and enforcement action is required, the amounts recovered would be applied first towards any unpaid rates and then towards the Levy.
71. If there is more than one Levy being levied on the same unit of land, the Levies will have priority in the order in which they came into existence (i.e. the earlier Levy will have priority over the later Levies). This provides certainty because the SPV with the subsequent Levy will be aware of earlier ones, so can factor this into their models. This ensures that the security of earlier Levies are not undermined by subsequent Levies (similar to the ranking of mortgages and secured charges).

Raising finance

72. The SPV will raise finance and enter into financial arrangements (such as hedging) in relation to the infrastructure project.

73. We expect the SPV will need to manage two finance risks in the course of its operations; base rate risk and margin risk. Encouragingly in the Milldale transaction the Accident Compensation Corporation provided a 35 year fixed interest rate. This reflects a positive evolution in the development of New Zealand capital markets. It will enable better matching of debt with the length of the proposed Levy (25 to 50 years) and should reduce the risk that the Crown is required to take financing risks.

Construction of the infrastructure

74. There are a range of ways in which the SPV could provide infrastructure. The possible structures include the SPV constructing infrastructure assets by subcontract or the SPV providing finance to a third party (e.g. a developer) to construct the infrastructure.
75. In order to retain flexibility, we recommend that the legislation should not prescribe or restrict the SPV to utilise particular structures for the construction of the infrastructure.

Contribution of development contributions

76. It is possible that a local authority may have already begun collecting (or have the right to collect) development contributions under the LGA for a particular project. It is proposed that the legislation will require the transfer of relevant existing development contributions to the project being funded by the Levy.
77. To prevent double charging, previously paid development contributions may be a factor in the design of the Levy. In addition, once the Levy has commenced, development contributions will not be permitted for the project infrastructure to be financed by the SPV. This will not preclude developers making voluntary capital contributions to expedite their ability to proceed.

SPV ownership

78. SPV ownership structures could range from Crown owned through to privately owned. The only SPV ownership structure that would not work is ownership by the local authority that is to receive the infrastructure (which would not meet rating agency requirements).
79. We propose that the legislation retain sufficient flexibility to enable any ownership option.
80. Officials at the high growth councils have expressed a strong preference that the SPV be at least initially owned by the Crown on the basis that the Model represents a significant change for their elected members and that non-Crown ownership of the SPV may negatively impact on uptake of the Model. We consider that local authority buy-in for the Model is important and this means that it may be necessary for the Crown to own the SPV's initially.
81. However, this approach has implications for the Crown balance sheet and may set a precedent for future projects funded by the Levy. We will provide further advice on SPV ownership so that Ministers can make a decision on SPV ownership preferences in advance of the legislation being introduced into Parliament.

Monitoring, reporting and intervention regime

82. Given the levying powers being provided to the SPV a robust monitoring, reporting and intervention regime is essential to ensure transparency, oversight and, that, ultimately the Levy is resistant to challenge. The proposed regime is set out in the table below:

Monitoring	Reporting	Intervention
<p>Crown-appointed Monitor for each SPV.</p> <p>Monitor to approve application of OIC by SPV (e.g. approval of annual Levy calculations).</p> <p>Monitor to receive periodic reporting from the SPV in respect of the Levy and the project.</p> <p>Monitor to receive reporting from the SPV on material events and to be able to require information from the SPV.</p> <p>Monitor to receive and action any complaints.</p>	<p>SPV required to release its audited Annual report.</p> <p>No Official Information Act requirements (unless they already exist (i.e. if SPV is Crown/local authority)) as the Monitor will most likely be subject to the OIA.</p>	<p>Power for the Monitor to direct the SPV to address significant problems with the Levy.</p> <p>Power for the Crown to exercise SPV's rights if the SPV has not complied with the Monitor's previous direction to address significant problems with the calculation of the Levy.</p>

83. A decision has not yet been made on who the appropriate Monitor is for the Levy. A report back will be provided on this matter at the same time as a recommendation on the entity to be the Facilitator and Recommender.

Disclosure regime

84. To ensure that beneficiaries and other interested parties (such as prospective purchasers of land that is subject to a Levy) are aware of and understand the implications of the Levy. We recommend that the legislation include a disclosure regime that addresses mandatory disclosure to beneficiaries, mandatory disclosure to interested parties on request and mandatory public disclosure.

Mandatory disclosure to beneficiaries

85. We recommend that the regime for mandatory disclosure to beneficiaries be modelled on existing LGRA provisions – in particular including requirements that:

- a. levies be disclosed to beneficiaries on an annual “assessment” (either an SPV assessment or a rates assessment where a local authority is acting as collections agent) which provides a full description of the Levies – as with rates, the issuance of the assessment would establish the liability to pay the Levy; and
- b. an invoice must be sent to beneficiaries when a payment is due (either by the SPV or by a local authority where it is acting as a collections agent).

Mandatory disclosure to interested parties on request

86. The proposed regime for mandatory disclosure on request consist of:
- a. an obligation on local authorities to disclose Levies in Land Information Memoranda (LIMs), which can be obtained for a fee by any person, at any time, for any property and from one known and central place – this would involve an amendment to the Local Government Official Information and Meetings Act 1987, and would also be supported by an obligation on the SPV to provide the local authority with the requisite information about the Levies for this purpose if the local authority is not collecting the Levy; and
 - b. an obligation on local authorities to include information about Levies on the rates record for any property – we recommend this option as inspection of the rates records is often an alternative/supplement to obtaining a LIM. It is free, unlike a LIM, and is part of the standard conveyancing procedure to inform what rates apportionments are required on settlement.

Mandatory public disclosure

87. Finally, we recommend that the proposed regime for mandatory public disclosure consist of:
- a. an obligation for there to be a publicly accessible website maintained with all information in relation to Levies – people would be made aware of the website through their interactions with a relevant local authority when obtaining a LIM, or undertaking a search of rates records. This is similar to the Milldale project, where a website has been established with information on the amounts payable by landowners; and
 - b. a statutory role for the Monitor (or other suitable Crown body) to inform the public on how the Model works and its impact on properties – we have recommended such a role as it will be important that beneficiaries and communities are informed about the effect of Levies, and their impact on properties. In particular, beneficiaries will need to understand the Levies so that they can be taken into account when agreeing to purchase a property. This may involve, for instance, the operation of the website referred to above, and other measures to ensure the public have access to information on how the Model works.
88. We also considered whether to require the Levies be registered on certificates of title to land. However, we do not consider that such an approach is required as a registration obligation would go well beyond the existing disclosure regime for rates, would add on some additional cost to the SPV, could be an inconvenience to the land owner, and in our view is not likely to provide for significantly more effective disclosure (over and above the measures we have recommended).

Recommended actions:

agree that local authorities be required by legislation to collect the Levy on behalf of the SPV if the SPV requires it; and the parties agree terms.

agree that legislation specify that any monetary development contributions already collected for a project that is funded by a Levy be transferred to the SPV.

note that there are a range of SPV ownership options and structures.

agree the legislation not exclude any SPV ownership options or structures.

agree the proposed monitoring, reporting, intervention and disclosure regime for SPV's outlined in this paper.

note that Treasury officials will report back on the recommended monitoring entity for SPV's by July 2019.

Asset Transfer



89. Assets constructed under the Model will vest in the entity that typically owns these assets (e.g. local authority, council-controlled organisation). We have investigated options for when vesting could occur and whether there are any restrictions or other legal implications of an SPV owning and/or operating assets at various points of the asset life-cycle. These options included:

Ownership of the infrastructure asset	Commentary
SPV never owns the asset (asset is always owned by the local authority)	Not recommended – This is unlikely to meet the requirements of the rating agency – although the legislation will not expressly preclude this option to preserve future flexibility.
SPV owns the asset during construction but the asset vests with the relevant local authority at the end of construction	Recommended – This will meet rating agency requirements. Will require SPV to have some legislative powers during the construction period. Will mean the assets is vested back to the local authority after construction and will form part of the asset network.
SPV owns the asset for the duration of the Levy and operates the asset	Not recommended – This would require the SPV to have a number of legislative powers to operate and maintain the asset over the term of the Levy (25 to 50 years) that are not generally provided to non-government bodies. It also means that the asset does not form part of the network. For these reasons this option is unlikely – although the legislation will not expressly preclude this option to preserve future flexibility.

90. The recommended option balances meeting rating agency requirements and limiting the legislative powers required by the SPV.

Powers required by the SPV during construction

91. The current legislative settings assume that the type of infrastructure possible under the Model will be constructed, owned and operated by either local authorities or central government agencies. As a consequence provisions within the Resource Management Act 1991(RMA), the Public Works Act 1981 (PWA), and some sections in the Local Government Acts 1974 and 2002 present impediments to the preferred option of the SPV constructing the assets.
92. For the Model to succeed, there needs to be an appropriate mechanism to enable land to be designated for the works to be constructed by the SPV, and enabling compulsory acquisition of land for those works if necessary. The SPV may need, in some circumstances, the ability to exercise (or have someone exercise on their behalf) powers that are currently reserved for local authorities.

93. There are a range of options for dealing with these issues. Officials from interested agencies have had an initial discussion but have not agreed a preferred option at this stage. Officials will report back to Cabinet with further advice shortly.
94. The Ministers for Māori Development and Land Information are undertaking broader work on the issues and options for the treatment of Māori land under the PWA. This includes both the acquisition of Māori land and the offer back of former Māori land under the PWA. No firm policy decisions have been made yet as options are still being developed. Officials advise against making any specific decisions in relation to the treatment of Māori land under the Model legislation until the broader work has been completed. This will ensure that SPVs are treated consistently with other network utility operators.

Recommended actions:

note the legislation will enable SPV's to own assets during construction and not be prevented from ownership during the term of the Levy.

note that officials will shortly prepare a Cabinet paper regarding the proposed approach to the powers of the SPV during the construction period.

Section 5: Government Support Package (GSP)

95. Currently, in the delivery of infrastructure projects funded by local authorities, the relevant local authority takes on the contingent residual risks that are not transferred to another party (either because these risks cannot be transferred or will not be priced efficiently).^[38]
[38]
96. For projects progressed under the Model, these risks will exist. However, these risks can't be borne by local authorities without impacting on the rating agency assessment of local authority finances. In addition, rating agencies' indicated any risks that are not explicitly allocated will be assumed to rest with the local authorities. If these risks remain with the local authorities, then there is financial recourse to the local authorities and the Model won't work.
97. Therefore, contingent residual risks will need to be explicitly allocated. Aside from the local authorities, the other options for who could bear these risks include:
- a. Financiers –^[38]
[38]
 - b. Beneficiaries –^[38]
[38]
 - c. Contractor - To the extent possible we expect the SPV will enter into fixed price contracts or a certain level of contingency will be included in the contract.^[38]
[38]
 - d. Crown – while this approach is not costless for the Crown, and would require risks to be monitored, it is consistent with the risk position that the Crown takes on large Crown funded infrastructure projects (e.g. transport projects).

98. To ensure the cost of managing these risks are minimised and to make the Model work we propose that residual risks associated with infrastructure projects funded by the Levy sit with the Crown via a GSP. The GSP will be in place for the life of the Levy, but will be scaled back at the end of the construction phase, which is when the risks are the greatest.
99. In addition, we have considered how calls on the GSP could be mitigated – this includes:
- a. building a contingency into the Levy to cover potential risks (likely to be most applicable to deal with construction cost overruns and financing related risks);
 - b. independent due diligence in relation to construction cost, contractors and developers;
 - c. use of insurance; and
 - d. ensuring appropriate governance structures including robust monitoring, reporting and intervention regimes.

[38]

101. The GSP will be provided on a case by case basis by contract between the Crown and the SPV. Treasury will be responsible for making independent recommendations to Cabinet on the use of the GSP. This provides a level of independence from the project and will help ensure that there are the appropriate incentives to ensure that the GSP is minimised.
102. Cabinet ultimately retains the right to decide on the scope and scale of the GSP on a case by case basis.

Recommended actions:

note the Government Support Package is an integral part of the rating agency requirements of the Infrastructure Levy Model.

agree that a Government Support Package will be provided as part of projects funded by the Infrastructure Levy Model.

note the terms of each GSP will be agreed on a case by case basis, [38]

[38]

Section 6: Consequential amendments to legislation

103. Officials have also considered the need for consequential amendments to legislation to ensure the Model will work.

Local Government Legislation

104. We propose amendments to the Local Government Official Information and Meetings Act, LGRA and Land Transport Management Act. Specific changes are required to clarify that:
- the Model is not inconsistent with the Local Government Act⁸; and
 - the Model can be used by Auckland Water Organisations (i.e. Watercare) without placing them in breach of their obligation to keep the overall costs of water supply and waste-water services to its customers at the minimum levels.

Insolvent transaction provisions in the Companies Act 1993

105. The Model will involve an SPV constructing assets and vesting those assets in a public body, such as a local authority. The local authority will not be required to pay for those assets, rather payment for the assets is funded by the beneficiaries through the Levy.
106. This is a fundamental feature of the Model, but may have unintended consequences in the event of an insolvency of a SPV. The insolvent transaction provisions enable a liquidator to reverse a transaction where the recipient has not *directly* paid full value for the asset. In the Model, the local authority will not *directly* pay full value of the asset to the SPV, the value is paid for by the beneficiaries. In a liquidation, this could result in a scenario where beneficiaries are paying for the asset and the local authority has to pay the liquidator again for the asset.
107. Officials will provide further advice to Cabinet on whether the Levy legislation needs to address this issue.

Recommended actions:

agree to consequential changes to local government legislation to ensure consistency between the Model and local government legislation.

note that officials will provide further advice on whether the Levy legislation be used to avoid a situation where parties are unfairly treated in an insolvency of the SPV.

agree that officials from the Ministry of Business, Innovation and Employment, Department of Internal Affairs and Treasury provide further advice to Cabinet about how insolvent transactions relate to the Infrastructure Levy Model.

Section 7: Accounting treatment, income tax and GST

108. Due to the bespoke legislative and commercial structure of the Model there are a number of GST, income tax and accounting treatment impacts to be aware of. The positions below set out the indicative position but this may change if there are material amendments to the Model.

⁸ Sections 136 and 137 of the LGA do not apply to a funding arrangement approved by the Crown under the Model - without such a provision, aspects of the Model could be argued to be inconsistent with provisions (in particular, the provisions in s137 requiring local government organisations to retain control over the pricing of water services and the development of policy related to water services).

Accounting Treatment

109. A key driver in determining the accounting treatment is who controls the SPV. Accounting standards mean that the party that controls the SPV will need to consolidate the SPV's assets and liabilities onto its balance sheet. Control may result from ownership interest and commercial and other binding arrangements.
110. Regardless of who owns the SPV, the Crown will most likely control the SPV. This is because of:
- the Crown's involvement in the SPV's purpose and design;
 - the Crown's ultimate right to approve the details of the OIC;
 - the fact that the local authorities and ultimately the Crown will receive the benefit of the infrastructure assets constructed and financed by the SPV; and
 - that significant risks related to the SPV's activities are expected to be borne by the Crown through the GSP.
111. The table below provides analysis of the circumstances under which the SPV would or wouldn't consolidate onto the Crown's balance sheet⁹. This will need to be worked through on a project-by-project basis. Scenario one and two seem the most plausible at this time, but if the Model evolves, non-consolidation may be possible.

Scenario	Crown owns the SPV	Crown controls the SPV	Does the SPV consolidate onto Crown balance sheet?
1	Yes	Yes	Yes - the Crown fully consolidates the assets and liabilities of the SPV. The impact of this on the Crown balance sheet will be limited to a grossing up of the assets and liabilities of the SPV (i.e. it is not expected to result in the recognition of material additional net liabilities). Any net difference will likely reflect a timing difference only.
2	No (SPV privately owned or diversified ownership)	Yes	Yes
3	Yes	No	No – would only reflect Crown's investment in SPV as owner.
4	No (SPV privately owned)	No	No

Income Tax

112. The advice is that the activities of the SPV will be considered under the financial arrangement rules – which means that the revenue and expenses should both be spread over the term of the project, minimising the risk of a significant timing mismatch and therefore upfront tax liability with refunds occurring over the period of the Levy. Liaison with the Inland Revenue Department (IRD) will be required to confirm this.

⁹ Note that the SPV's balance sheet will reflect its assets and liabilities in all of these scenarios as whether the Crown consolidates the SPV or not has no impact on the SPV's balance sheet.

GST

113. There are two considerations in relation to Goods and Services Tax (GST). The first is whether GST should apply to the Levy and the second is whether the SPV is carrying out a taxable activity (and can therefore claim GST on costs incurred).

Whether GST applies to the Levy

114. The initial advice is that GST would not apply to the Levy. This is because statutory levies are generally not subject to GST as they are not consideration for a supply (i.e. they are not sufficiently linked to a supply of goods or services).

115. In addition, there is precedent for similar levies not being subject to GST, the infrastructure payment made by beneficiaries in the Milldale transaction (undertaken by CIP) was confirmed by IRD as not being subject to GST.

116. In comparison rates are subject to GST, most ratepayers are not registered for GST and therefore cannot claim the GST back. Accordingly, if the Levy does not attract GST and the SPV is able to claim GST on costs incurred, there will be a benefit to the beneficiaries compared to general rates. However, this will have a negative impact on Crown revenue assuming the projects would have otherwise been delivered by local authorities and funded by rates.

117. The other potential risk created by the Levy not being subject to GST is that it could ignite debate as to whether GST continue to be collected on general local authority rates.

118. We will be seeking a binding ruling from IRD to confirm the position.

Whether the SPV is carrying out a taxable activity

119. In order to claim GST on costs incurred, a SPV will need to have a taxable activity for GST purposes. This will depend on the specific structure of the SPV and we will be testing possible structures with the IRD.

Section 8: Risks

120. In this section we outline the risks associated with implementing the Model. We have ordered these risks according to:

- a. first order risks – these are risks which are fundamental to the Model working; and
- b. second order risks – these are risks that go to how successful the Model will be and how widely it will be used (Appendix C).

121. All risks will be monitored and, where necessary, mitigations will be put in place to help manage these.

First order risks

Level of Support required by Central Government

122. To enable the Model, the Crown will be taking on certain decisions rights and risks that currently sit with the local authority. This creates the following risks:
- a. The Crown will provide cover for residual risks if they are arise (via a GSP). The risks associated with the GSP and management of these risks are summarised in Section 7 above and in Appendix D (SPV failure scenarios).
 - b. Due to the level of control that Crown has over the SPV (design of the SPV, approval of the Levy), pursuant to the relevant accounting standard, the assets and liabilities of the SPV will consolidate onto the Crown balance sheet. This should not result in additional net liabilities as the assets and liabilities will offset.
 - c. Ownership of the SPV remains with the Crown and doesn't evolve over time.
 - d. Lobbying of the Crown by beneficiaries because final decision rights regarding the granting of the Levy sit with the Crown.
 - e. Because of the greater decision rights of the Crown and Crown ownership of the SPV, it may give rise to a general expectation (above the Crown's agreed obligations) that the Crown will provide direct financial assistance if the infrastructure project fails before completion (over and above any GSP risks that the Crown might bear) or after completion (which is when the local authority assumes responsibility for the assets).
123. To manage these risks we propose that in any communication about the Model, the Crown be clear that;
- a. its role in providing the Model is to support local authorities by removing a road-block but that otherwise local authorities remain responsible for the delivery of local infrastructure;
 - b. ownership of the SPV may change over time and the Crown is interested in exploring different ownership structures with local authorities; and
 - c. local authorities are still involved in the process to agree the Levy (by supporting the use of the Levy and accepting the assets at the end of construction) and that this Model is a partnership between the Crown and local authorities.

Consumer/beneficiary protections

124. Some SPV's may have monopoly like features in specific local markets. This raises a question about whether they should be subject to regulation by an independent regulator such as the Commerce Commission. Where there is private ownership of some other natural monopoly assets such as electricity lines or airports, the Commerce Act 1986 has been amended to allow specific regulation of the charges of those companies with oversight by the Commerce Commission.
125. However, extending the Commerce Act to regulate the SPVs is not recommended due to the fact that Levies under the Model will already be directly regulated under legislation, and due to the time and costs involved.

126. Instead officials propose that the Levy setting process (in particular the OIC) include a number of safeguards to replicate the regulatory regime for utilities and therefore provide consumer protections. These include:
- a. local authority involvement in the Levy setting process to ensure that the Levy is affordable in the context of rates;
 - b. Cabinet Approval (including the Minister of Commerce and Consumer Affairs) – who will want to satisfy themselves before approving a Levy that there is no monopoly pricing and that the costs that beneficiaries face are affordable;
 - c. the OIC regulating both how much the SPV spends on projects but also the types of expenditure which are levied on beneficiaries;
 - d. the Facilitator and Recommender being a Crown appointed body – part of their role will be to ensure that there are contestable processes for key cost elements of infrastructure projects;
 - e. the Treasury will consult with the Commerce Commission and Ministry of Business Innovation and Employment on the development of guidance for the Facilitator and Recommender to guard against monopoly pricing and ensure beneficiaries interests are protected;
 - f. the SPV will be monitored by a Crown appointed body to ensure that it complies with the OIC with respect to the setting of the Levies (therefore Commerce Commission oversight is not required); and
 - g. in cases where the maximum possible Levy is not specified at the time that the OIC is approved, Cabinet will have the opportunity to specify any additional monitoring or oversight arrangements to ensure beneficiaries/consumer protections are appropriate.
127. Notwithstanding the above, there is a risk that a Levy payer could complain to the Commerce Commission, and given the possible natural monopoly nature of IFF projects, the Commission could decide to launch a Part 4 inquiry that recommends that the Minister of Commerce and Consumer Affairs impose economic regulation via OIC. Whilst both MBIE and our legal advisors consider the risk of this occurring is small, it is a non-trivial risk that Ministers should be aware of, particularly given the range of projects that are proposed to use the Model.

Local authorities' willingness to use the Levy

128. The future behaviour of local authorities towards using the Model will govern its ultimate success. We have taken steps to involve local authorities in the development of the Model, including:
- a. regular dialogue with high growth councils in relation to the Model;
 - b. a series of workshops with officials from high growth councils to walk through our policy development proposals and solicit their feedback;
 - c. engagement with officers of high growth councils to assess how the Model will work in practice with reference to actual projects; and
 - d. Ministerial engagement with elected local authority members.

129. However, local authorities may be slow or reluctant to adopt the Model (although we note funding pressures in Auckland in particular are now more acute). Issues that have been identified which may impact the willingness of local authorities to adopt the new model include:
- a. Perceived loss of control of local authority responsibilities;
 - b. Concern over the affordability/uncertainty of the Levy for beneficiaries;
 - c. Concern over the ultimate owner of the SPV – high growth councils have indicated that they want the SPV to be owned by the Crown;
 - d. Difficulty adapting to using the Model; and
 - e. Objection to the project itself (i.e. a local authority may prefer urban growth to occur first in areas other than where a Levy is proposed).
130. We propose to mitigate these risks by seeking input from local authorities at two stages in the process of developing a funding proposal. This involvement will provide local authorities with the opportunity to indicate any concerns, and provide Ministers with visibility over the nature of any concerns to inform their decision making process.

Rating agency decisions

131. The assessment of the Model by credit rating agencies' is critical to the success of the Model. ^[34]
[34]

132. [34]

133. [34]

134. If there is a fundamental change in the approach taken by the credit rating agencies' in relation to related obligations for government related entities then this could undermine the Model. We note that any proposed changes will be well signposted and consulted on ^[34]
[37]

135. If there are any potential changes to the methodology used by rating agencies' that would impact on the Model, officials will advise Ministers.

Second order risks

136. Summarised below are the risks that impact how successful the model will be and how widely it will be used. The risks are listed below and discussed further in Appendix C:
- a. Unwilling beneficiaries
 - b. Development may be incentivised away from brownfields
 - c. Beneficiary allocation choices
 - d. Affordability and acceptability of the Levy
 - e. Equity issues with the use of the Model
 - f. Ability for the Levy to cover the full cost of the infrastructure
 - g. Use of the Model may place pressure on funders of complementary infrastructure
 - h. Powers given to a third party
 - i. Communication with local authorities and beneficiaries
 - j. New Legislation

Section 9: Next steps

Timing

137. We have developed a draft timeline for the consideration of policy and legislative issues, Cabinet paper and potential introduction of legislation, see below.

Date	Activity
April	Ministers to consider Draft Cabinet paper and RIS
April	Cabinet paper and RIS lodged with Cabinet Office
May	Cabinet paper and RIS considered at the Cabinet Economic Development Committee
May	Cabinet to ratify or consider the Cabinet paper and RIS
May	PCO to receive drafting instructions for the legislation
Second half of 2019	Bill introduced into the house

Appendix A: Possible projects for the Model

[37]

Appendix B: Proposed Levy Regime

Proposed Levy Regime	
Feature	Proposed approach
Levy commencement and length	Legislation enables the start of the Levy period and length of the Levy, to be determined on a project-by-project basis, but that the maximum length of the term be 50 years.
Prepayment of Levies	Legislation will not provide for prepayment of Levies as this would add complexity and undermine predictability of cashflows, impacting finance.
Costs funded by the Levy	<p>Legislation enables the Levy to fund the following categories of costs:</p> <ul style="list-style-type: none"> • Construction costs including direct construction costs, insurance and project contingency costs. • Project establishment costs of the proposer, facilitator (where these are directly attributable to a specific project funded by the Levy), bidders and SPV owner, with limitations governing eligibility set out in facilitator guidance material. • SPV operating costs including management and administration costs. • Construction, project establishment and SPV operating costs that have been incurred by another party and which the SPV is liable to fund or reimburse (e.g. if the SPV did not construct the assets or took over the construction of assets from a local authority and used Levy revenue to repay local authority debt). • Asset operating and maintenance costs prior to vesting. • Financing costs including debt interest costs, equity costs (where relevant), arrangement, commitment and agency fees, reserve accounts and enforcement / intervention costs. • Enforcement and intervention costs. • Levy collection costs most of which will be paid to a local authority to collect the Levy. • SPV monitoring costs. [38]
Ability to vary the Levy	<p>The Levy may under some circumstances vary over the term of the Levy period. There are three options for the variability of the Levy:</p> <ul style="list-style-type: none"> • Levy does not vary – the Levy is set at a maximum levy amount. In this circumstance the beneficiary knows the maximum possible levy, however, the SPV does not have flexibility to access additional Levy revenue if it is required. • Levy can be varied – up to a maximum specified amount. The SPV would have the power to increase the Levy from the initial amount if certain risks eventuated (e.g. construction costs increased) up to a maximum amount. In this circumstance beneficiaries would know the maximum possible Levy and this would give the SPV flexibility to access additional Levy revenue under certain circumstances if it is required. • Levy can be varied and there is no maximum specified Levy. The SPV would have the power to vary the Levy under certain circumstances – but the Levy has no upper or maximum limit. This option results in the least certainty for beneficiaries but provides the maximum flexibility for the SPV in the event costs vary. <p>In all circumstances the Levy could reduce (e.g. in the event of over-collection and the Levy is rebated). Choices about whether the Levy can be varied do not need to be made now but will be made at the time the OIC is approved, and in conjunction with decisions about the scale and scope of the GSP.</p>
Excess charging regime (in the event the Levies are more than required to complete the project)	Legislation will include a framework for how excess Levies be used. In summary, in most cases there will be a reduction in future Levies, but potentially there could be refunds or a shortened Levy term. Specific requirements for any project will be included in the OIC.

Proposed Levy Regime	
Feature	Proposed approach
Identification of beneficiaries	<p>The legislation enable a permissive approach for land-based Levies to identify beneficiaries of project depending on various factors, such as:</p> <ul style="list-style-type: none"> • Geographical land area • Use of land • Activities permitted on land • Value of the land <p>Beneficiaries in future urban zone land are anticipated to be included in the Levy. However, second wave beneficiaries (located outside the anticipated future urban zone) are anticipated to be excluded from the Levy on the basis that they will not substantially benefit from the infrastructure.</p>
Exemptions, postponement or remission of Levy	The legislation include provision for exemptions, postponements and remissions in the same way as currently applies for rates.
Invoicing and collection of Levy	Legislation to include provision for the SPV to directly invoice and collect the Levy or to contract with the relevant local authority. Legislation will include 1) the ability for the SPV to access the rating information database and overrides of the Privacy Act (for purposes of collection) and 2) a requirement for the relevant local authority to act as collection agent where required by the SPV.
Priority of Levy	Legislation to enable Levies to be second-ranking (after local authority rates, and before all mortgages, encumbrances etc).
Enforcement	Legislation to enable the SPV to hold all legislative rights to enforce revenue in the same way a local authority can. This includes the right to sue payor's mortgagee for debt and right to require a forced land sale (after statutory timeframes have elapsed).
Security over Levy	Legislation to enable the SPV to grant security over its Levy rights, and for a receiver to be appointed to, and administer, those rights. This will be necessary in order for the SPV to raise finance on the strength of the Levy, as anticipated under the Model. These provisions would be based on similar provisions in respect of rates in the LGA, but (unlike under the LGA) they would not permit a receiver to set a new rate.
Objections	Legislation to outline an objection regime for objections from beneficiaries on how the Levy has been calculated, but not the Levy itself.

Appendix C: Second Order risks

Unwilling beneficiaries

1. The Model will enable the power to levy residents who have not opted-in to a project area. In some cases this will include unwilling beneficiaries. Mitigation of this risk is challenging, as there are many variables that lead to a beneficiary being unwilling.
2. In a greenfield development scenario the risk of unwilling beneficiaries is more remote as purchasers and developers will likely be fully aware of, and are able to 'opt-in', to the Levy. This risk is higher in instances where brownfield development is funded and financed via the Model due to the impost of the Levy on existing residents. Wilful non-payment may occur with consequential costly recovery actions needed.
3. Under certain circumstances (e.g. land banking) the Model may assist in breaking the impasse due to the cash impact of the Levy. However, it may also impact on those who are unable to afford the Levy (such as people on fixed incomes). Beneficiary identification, equity and affordability will be important considerations in the Levy design process which will help mitigate this risk. For example for existing residents, the Levy could be phased in or only become payable after a certain period of time or event (such as the sale of the house).

Development may be incentivised away from brownfields

4. As the Model will be more easily applied to greenfield projects (due to the greater simplicity of identifying beneficiaries and those who opt-in) it may encourage development away from brownfield areas. This may have environmental impacts and also work against the governments wider urban development objectives. This risk will be mitigated through implementation of the wider UGA work programme which focuses on improving spatial practices and addressing constraints to intensification.

Beneficiary identification and allocation choices

5. The accurate and fair allocation of costs in brownfield and greenfield areas may be challenging, particularly where a project funded by the Levy has network impacts or where there are existing residents and second wave beneficiaries. This is not a new issue with current methods of recovering costs, such as development contributions, consistently under recovering actual cost. The Model will provide greater transparency of infrastructure cost but beneficiary identification and allocation is still likely to be contentious. We will work with other government agencies and local authorities to develop guidance.

Affordability and acceptability of the Levy

6. There is a risk that the Levy is unaffordable either in the context of total rates payable, or on an individual basis. If the Levy is not affordable it may lead to non-payment by beneficiaries and pose a risk to the project more generally. This risk is being addressed through the disclosure regime and by affordability being one of the considerations for Cabinet when approving the use of the Levy.

Equity issues with the use of the Model

7. There is a risk that local authorities primarily use the Model in areas where the resident community are less likely to seek to challenge the Levy and/or apply pressure on local politicians. If this occurs, it could mean that areas with a greater proportion of renters and affordable housing are most significantly impacted by the Levy.
8. These equity risks are matters that the Facilitator and Recommender will need to closely monitor and further advice will be provided to Ministers if required.

Ability for the Levy to cover the full cost of the infrastructure

9. In some cases, it may be unaffordable for beneficiaries to cover the full cost of the infrastructure. Or it may be inappropriate for the beneficiaries to cover the full costs because there are wider community benefits. In these cases a contribution from the local authority¹⁰ or other related party (e.g. NZTA) might be required deliver the projects.

Use of the Model may place pressure on funders of complementary infrastructure

10. If successful, the use of the Model will accelerate the delivery of infrastructure projects and may require complementary projects to be funded sooner than envisaged (e.g. transport projects). There is a risk that if these complementary projects are not funded, it will hold back the delivery of viable infrastructure projects.
11. Addressing this risk will rely on the ability of government agencies responsible for infrastructure, such as transport, to be adaptive and to be involved in the feasibility stage of proposals to identify and mitigate these risks. The work under the spatial and urban planning pillars of the UGA should help to deal with these issues as a more integrated approach is taken to planning, to identify and agree all infrastructure that is needed to develop a certain area.

Powers to be given to a third party

12. The power to Levy will be given to an SPV which may be owned privately or have a level of private capital. Whilst there are safeguards around the Levy and what the Levy can be used for, this could still be controversial. In most cases the SPV will only own the asset during construction, the asset will vest back to the local authority immediately after construction.

Communication with local authorities and beneficiaries

13. The Levy and use of an SPV could be misinterpreted by the public, beneficiaries, local authorities or the media. Unfavourable public commentary on the Levy could lead to non-payment. To manage this risk Treasury will prepare a communications plan for any announcements about the introduction of legislation and will work with your offices to arrange briefings of key stakeholders in advance of any announcements.
14. Additionally, the complexity of the Model may undermine uptake from developers and local government, and requires sophisticated understanding from political decision makers, officials, developers and consumers. Transparent and clear supporting material will be developed to avoid misconceptions and assumptions and increase the likelihood of uptake.

New Legislation

15. There are inherent risks with implementing new legislation and ensuring that it works as envisaged, particularly when working to compressed timeframes. We have sought to mitigate this risk through engagement and consultation with local authorities and other key stakeholders who will use the Model (financiers, developers and contractors). Officials have also been supported by Crown Infrastructure Partners, legal, commercial and capital market advisors.

¹⁰ Which be funded by general rates or future development contributions.

Appendix D: Failure Scenarios

We have, in this section, set out various “problem” scenarios and how those scenarios would play out in practice.

For this purpose, we have assumed the following facts:

- a single SPV (owned by the Crown) is established to fund, construct and deliver network infrastructure for a new greenfields development;
- the SPV is empowered under an OIC to levy rating units within the boundaries of the development;
- the Levy is a 35 year uniform Levy which commences on day 1 of the project (with developer landowners paying the Levy initially), and provides for fixed increases over a set 4 year ramp period;
- the SPV has raised debt finance from a bank syndicate, including a contingency facility;
- a fixed price contract (with some exclusions) has been entered into with a contractor;
- the Crown has provided a GSP that provides support ^[38]
- the SPV has entered into a vesting agreement under which the network infrastructure will vest in a local authority;
- the Levy has been modelled to provide sufficient headroom to enable the SPV to call on, and repay, the contingency facility if needed but (in order to have a finite cap on the Levies payable by beneficiaries) ^[38]
- ^[38] and
- in exchange for the GSP, the Crown is given a suite of step-in and other control rights in respect of the SPV and the project that are exercisable in agreed events (including if it becomes likely that the Crown will need to make a payment under the GSP).

Against that factual background, the problem scenarios we have considered are:

1. there are significant cost overruns during the construction phase;
2. the project ceases to be viable during the construction phase (such that the infrastructure cannot be delivered);
3. the SPV incurs significant financial difficulty during the post-construction (financing) phase; and
4. the infrastructure assets fail during the post-construction (financing) phase.

We have also considered, in each case, what would happen in these scenarios in the status quo (i.e. for a project that is funded and delivered by a local authority itself).

Problem Scenario 1 – cost overrun during construction phase

Under this scenario, a major issue arises during the construction phase that leads to increased construction costs.

The SPV will be able to draw on the contingency facility to finance those costs, and can repay the additional drawings from the Levy revenue (without having to increase the Levy).

However, further issues during the construction phase then occur and it appears likely that these will lead to a further increase in the construction costs. ^[38]

^[38]

[38]

By comparison, under the status quo, any cost overrun would be borne by the local authority itself (without any Crown support) and in some way passed on to the community (e.g. through general rates).

Problem Scenario 2 – project ceases to be viable during construction phase

Under this scenario, a major issue arises during the construction phase that means that the commencement (or continuation) of construction is no longer viable. This may for instance be due to a change in law, a challenged consent or a major economic downturn.

As the project is no longer viable, the Levy should not be continued for the full term. The “excess Levies” regime proposed for the Act should operate to limit the amount of revenue that can be collected (or at least require the SPV to rebate any amount that is not applied towards eligible costs). However, this may still involve the Levy continuing for some time. In order to bring about the cancellation of the Levy, either:

1. the SPV could make a request to the Crown (with the consent of all requisite parties, e.g. financiers) that the Levy is cancelled – in this event the Crown could then cancel the Levy [38]
2. (if no such request is forthcoming) the Crown could elect to cancel the Levy – [38]
[38]

[38]

[38] It is conceivable that the Crown could defer cancelling the Levy until such time as sufficient Levy revenue has accrued to cover the applicable costs [38]
[38] however this would involve the beneficiaries paying an amount towards a project that is not delivered.

By comparison, under the status quo, if a project ceased to be viable any project costs already incurred (and any break costs), would be borne by a local authority and in some way passed on to the community (e.g. through general rates).

Problem Scenario 3 – SPV in financial difficulty post-construction phase

Under this scenario, the construction phase is complete, the infrastructure has vested in the local authority and is operational and working, however a significant group of beneficiaries simply refuse to pay the Levies.

This risk primarily falls on the SPV and its financiers. The SPV would be entitled to exercise the proposed enforcement rights under the Act (which include suing the beneficiaries for payment, claim payment against the beneficiaries’ mortgagees, and commencing forced sale processes). Those rights should ultimately see the SPV collect the relevant payments. However, the timing issue (delayed payments) may result in the SPV being unable to service its debt in the meantime, and the appointment of a receiver to the SPV. The receiver will then be able to exercise the SPV’s rights to compel payment.

There is however a risk that the group of beneficiaries put pressure on the Crown to intervene (particularly if forced sales become necessary) - possibly on the basis that the Crown enabled the structure and was the owner of the SPV.

By comparison, under the status quo, ratepayers might refuse to pay rates to a local authority where they oppose the project or the costs being imposed on them (as in the Kaipara example), and a local authority might need to take enforcement action itself to recover them. However rates non-payment might be considered to be less likely as rates are not specific to a project.

Problem Scenario 4 – infrastructure failure during post-construction phase

Under this scenario, after the construction phase is complete and the infrastructure has vested in the local authority, the infrastructure fails.

As the assets have already vested in the local authority, this will be borne by the local authority. Upon vesting, it will be expected that any contractor warranties will have been assigned to the local authority and accordingly the local authority will be able to exercise any relevant warranty rights. The local authority may also hold insurance for the relevant event.

Neither the SPV, nor the Crown (under the GSP), will have any continuing liability for the assets post-vesting. The Levies will continue to be payable to the SPV notwithstanding the infrastructure failure.

The same result would apply under the status quo (that is, infrastructure failure is the local authority's risk).