REPORT 4

EARTHQUAKE STRENGTHENING – INCENTIVES AND SUPPORT

1. Purpose of report

This report updates the Committee on financial incentives for Earthquake Prone Buildings (EQPB) and recommends that two additional incentives are included in the consultation on the 2014/15 Draft Annual Plan.

It also signals the policy work that may come back to the Council to be considered as part of the next Long Term Plan in 2015/16.

2. Executive summary

The Council has focussed existing earthquake strengthening incentives on supporting our heritage building owners to strengthen their buildings through the Built Heritage Incentive Fund and the Resource Consent Fee Subsidy Fund.

The aim is to extend incentives to also include non-heritage earthquake prone building owners who are taking positive action to strengthen the buildings they own, and to ensure that our charging regime does not unfairly penalise this important work. The outcome sought is to make the city safer by encouraging building owners of our highest risk earthquake prone buildings (with NBS ratings of equal to or less than 33%) to strengthen their buildings. It is proposed that Council adds the following incentives to its package to support earthquake strengthening within the city:

Incentive Type	**Details**
Rates Remissions	• A rates remission **during strengthening works** if the building is unable to be tenanted (an extension of the existing *of Rates Remission Policy*); and • A rates remission **after seismic strengthening** to delay the impact of any post strengthening valuation increases on rates for a period of 3 years
Building Consent Fees Subsidy Fund	A fund to refund 10% of building consent fees (up to $5,000 in total) for earthquake prone building projects to be applied upon completion of strengthening works.

3. Recommendations

Officers recommend that the Governance, Finance and Planning Committee:

1. *Receive the information.*
2. *Note that the Council adopted its Rates Remission and rates Postponement Policies as part of the 2012/22 Long Term Plan.*
3. *Agree the proposed amendments to the Rates Remission Policy as set out in Appendix 1 and summarised as follows:*
   (a) *renaming the section 2.3 "Remission of Downtown Levy Targeted Rates on Property Under Development Policy" to "Remission of Targeted Rates on Property Under Development or Earthquake Strengthening Policy"; and*

   (b) *amending the scope of the policy under section 2.3 to include remission of the commercial, industrial and business sector targeted rate and the base sector targeted rates and extend the application of this remission to beyond the downtown levy area.*

   (c) *including a new section 2.6 on the "Remission of Rates for Buildings Removed from the Earthquake Prone Buildings List".*
4. *Agree that the proposed amendments to the Rates Remission Policy be consulted on as part of the 2014/15 Draft Annual Plan using the special consultative procedure.*
5. *Agree to include a building consent fee subsidy fund as outlined in Appendix 2 at a cost of $100,000 per annum in the 2014/15 Draft Annual Plan for consultation.*
6. *Note that the Built Heritage Incentive Fund is funded in the 2014/15 Draft Annual Plan but is not currently provided for beyond 2014/15 and funding will need to be considered during the next Long Term Plan process.*
7. *Instruct officers to progress the assessment and feasibility of tools that may extend Council's incentive package into supporting the financing of strengthening projects, including but not limited to:*
   (a) *lending arrangements which are repayable through targeted rates attached to a property; and*

   (b) *a loan guarantee scheme.*

4. Background

4.1 Previous Decisions

Overall Approach and Team Established

In September 2011, the Strategy and Policy Committee agreed to take a broad approach to addressing earthquake prone buildings and city resilience. This meant expanding its regulatory role as required in the Building Act 2004 to considering what other activities it would be involved in. An Earthquake Resilience business unit was established in the Council to manage this work and oversee the assessment and strengthening of Council's building portfolio. The outcomes for our role in city resilience were agreed as follows:

- Our buildings and homes must be safe to occupy
- Any emergency response must not be impeded (strategic routes)
- Economic disruption from an event must be minimised (CBD, strategic routes, residential)
- Our economy needs to be protected and allowed to grow now, without perception of significant risk
- Heritage and city character is important and needs to be protected.

A report was presented to the Committee in February 2012 that highlighted the cost implications of a Christchurch type scenario for Wellington. Some priority activities were agreed and $1.45 million allocated in the Long Term Plan for these.

Increased BHIF Funding in 2012

An update was presented to the Committee in September 2012 and again in February 2013 including financial incentives. The following incentives were agreed in the 2013/14 Annual Plan focussed on assisting our heritage building owners:

- Increasing the Built Heritage Incentive Fund (BHIF) to $360,000 (from $329,000) per annum;
- Adding $40,000 funding in the heritage team for a part-time resource to work proactively with owners of earthquake prone heritage buildings so we can target and ensure best use of the BHIF;
- Agreed to prioritise the BHIF towards earthquake strengthening projects and implemented a 3 stage earthquake grant funding programme:
    - Stage 1 – for feasibility and assessment work
    - Stage 2 – for detailed drawing and investigation of a preferred option
    - Stage 3 – a contribution towards resource consent fees and completion of actual works
- Agreed to utilise any of unspent Resource Consent Fee Subsidy Fund ($50,000 per annum in total) as a "top up" to the BHIF during the March grant round.

In addition to these specific financial incentives, work continues on improving our consenting processes, facilitation of outcomes with building owners, our IEP assessment process, the review of our heritage list and planning rules, and responding to the changing legislation in this area.

4.2 What is happening in the market?

Since January 2012, 47 buildings have come off our EQP list. Market comment from CBRE, Colliers and the banking sector is that they are seeing considerable seismic strengthening progress in our prime, A and B grade office buildings. The tenants of these buildings are driving this work with their expectations being a minimum of 75% of NBS, and for government 80% of NBS and owners are responding to retain tenants, and to maintain the value of their buildings.

In the C and D office space market there are greater seismic strength issues. However in the D grade office space, cost is still a priority factor for the tenants, and the levels of NBS required by tenants of those buildings is more variable.

Generally the market is responding, but it must be recognised that this is a long term process requiring building owners to work through the options that best works for their buildings. Developers are identifying purchase and development opportunities arising from the need to strengthen buildings. We are observing more occurring in this space and it is realistic to expect that some buildings are likely to need to change ownership to enable them to be strengthened and developed.

Discussions with banks indicate that they are willing to work with Council on opportunities. There is also an acceptance that their current operating practises may need to change to address the EQP risk in Wellington. Again, they are still responding to this issue.

In summary, the market is still working through the EQPB issues and we are certainly not at a "market failure" point where clear intervention steps to be taken by the Council. It is our recommendation that we add to our package of incentives to assist the process, and any consideration of a more significant intervention role be considered as part of the next Long Term Plan when this decision can be balanced with all other funding decisions.

4.3 Legislation change

The Government proposes to amend the Building Act with the following effects:

- the requirement for local authorities to have an EQPB Policy will be removed and national standards for earthquake strengthening will be set in legislation
- the earthquake status of all commercial buildings and all residential buildings with two or more stories and three or more separate residential units will need to be assessed within five years of the legislation being enacted (currently our policy requires only pre-1976 buildings to be assessed)
- buildings with a seismic strength of 33% or less of the current National Building Standard (NBS) will be considered earthquake prone
- once assessed, EQP buildings will have 15 years to be strengthened
- TLA's will be able to set shorter timeframes for buildings with public safety or strategic importance concerns (to be defined in the regulations).

These changes are likely to come into effect in 2015. Our current policy is similar to these proposed changes and the Council does not perceive any difficulties in implementing these changes.

4.4 The Earthquake Prone Building List as at 30 November 2013

Our Initial Evaluation Process (IEP) has assessed 4,485 pre-1976 buildings that meet the policy criteria (all commercial and residential with 2 or more storeys and 3 or more separate units) and has 648 buildings still to assess. There are 623 remaining on the EQPB List.

The following information details the status of the earthquake prone buildings list as at 30 November 2013:

Detail	**Number of buildings**
Buildings currently assessed as EQP	623
Heritage buildings assessed as EQP	141 (23%)
Buildings Use:	
Commercial use	493 (79%)
Residential use	30 (5%)
Mixed use	100 (16%)
Location:	
Te Aro/Mt Cook	247 (40%)
Newtown	81 (13%)
Wellington Central	80 (13%)
Other	208 (34%)

To ensure that our incentives package is achieving the best value for money to ratepayers it is important that they are focused on the most important buildings. These are the buildings that are important to Wellington and present a significant public good by virtue of either;

- their heritage value to the city
- their location, either on a strategic route or within our CBD and critical to our economic resilience outcomes.

This work will follow the review of the heritage list due to be reported to councillors in February 2014.

5. Discussion

The Council has done a lot of work on earthquake strengthening of heritage buildings over the last 15 years. While awareness of the issue has been heightened since the Canterbury quakes, it is not a new issue for Wellington. Heritage buildings account for 23% of the current earthquake prone buildings list.

5.1 Council's role in funding seismic strengthening of privately owned buildings

The current incentives, the BHIF and Resource Consent Fee Subsidy Fund, focus on assisting heritage building owners to strengthen their buildings.

We are now recommending additional incentives to encourage owners of other earthquake prone buildings to make their buildings safe to live and work in.

Proposed options

Officers are recommending that the Council amend the Rates Remission Policy to enable:

- Rates to be able to be remitted while a building is being strengthened if it is unable to be occupied and there is no revenue stream available to the owner from the rating unit during the construction period. This is an extension of an existing provision within the Rates Remission Policy which covers remission of the Downtown Levy during similar construction periods.
- Adding a new section to the Rates Remission Policy to allow for any increased rates payable on earthquake strengthened building to be remitted. The building owner may apply for this remission for a period of 3 years after the removal of the building from the earthquake prone building list. For strengthened buildings, the remission shall equate to the increased rates (general rate, downtown levy, targeted commercial or residential rates, stormwater and sewerage rates but excluding metered water charges) payable due to the valuation uplift that may reasonably arise from seismic strengthening works.

It is also recommended that a building consent fee subsidy fund is established to alleviate the cost burden on property owners faced with earthquake prone buildings requiring significant strengthening costs. The subsidy would be calculated as 10% of the Wellington City Council charges included in the building consent cost, up to a maximum of $5,000 per consent

These changes are aimed at continuing to encourage building owners to strengthen their buildings as quickly as possible, to ensure that Wellington is safe to live and work, and to ensure that the Council's rating and charges mechanisms are aligned with these aims.

5.2 Other options

Officers are not recommending introducing any tools that extend Council's incentive package to provide loans, loan guarantees or similar products at this time. The reasons for this are:

a) The banking sector is willing to fund strengthening projects where the property owner is able to meet their loan prepayment obligations and LVR ratios are on not breached (ie that stay within acceptable levels of credit risk).

b) The Council also does not know enough about the financial position of our building owners to know how many building owners would be approved under, and therefore benefit from such a scheme. More work understanding this area is required.

c) Careful consideration is required as to why the Council would enter this market and expose ratepayers to credit risk that the banking sector would not take on.

The Long Term Plan is the appropriate time for decisions of this nature and financial significance when balance can be given against other investment decisions that will impact our debt capacity.

Lending and recovery through targeted rates

Officers have previously looked at a scheme where the council could support lending arrangements between banks and individuals by directing loan repayments via targeted rates. The key benefits of this model are our ability to dictate longer repayment terms for the property owner and at more favourable interest rates than can be achieved in the market place. This model required changes to rating legislation to enable rates to be used for this purpose (without the Council being party to the lending), and also has taxation issues that require addressing. This initiative has not been able to be progressed with Central Government.

Council as a direct lender

An alternative model utilises the same targeted rate principles, however places the Council as the direct lender to property owners. In principle it is similar to the GWRC Warm Wellington scheme where targeted rates are used to recover insulation grants to residential property owners (which are funded by GWRC debt in the first instance). This model is however not immediately transferable to earthquake strengthening loan arrangements (funded directly by the Council).

The majority of our EQP buildings are commercial properties and therefore the tax implications need to be considered. A scheme repaid through a targeted rate would be subject to GST so unless you are GST registered this would be an additional cost to normal lending arrangements. The treatment of principal loan repayments incorporated in our rates bill needs to be considered as the intention is not to provide property owners with a means to have tax benefits. These arrangements would need to be discussed and worked through with the IRD and may involve seeking binding rulings or changes to tax legislation to adequately address. We will need to take further advice on this.

Compared the GWRC scheme, any loans for earthquake strengthening are likely to be large and significantly increase an owners rating liability. Credit risk assessment is not a component of the GWRC scheme because the size of grants being provided under this scheme is insignificant.

Banks may also take issue with us entering the market especially if the Council had first preference in the event of a default and particularly where they did not approve extending that funding to a property owners due to credit risk and LVR criteria being breached.

The LGA has been amended since the introduction of the GWRC scheme and there is a greater onus on the Council to be operating in a financially prudent manner.

Loan Guarantee Scheme

Officers are investigating an alternative scheme where the Council could agree to guarantee the seismic strengthening portion of a loan arrangement between a bank and property owner. This would enable marginal lending deals to progress on the strength of our guarantee, with the Council taking on a level of credit risk (that is yet to be determined) and receiving a fee to do so.

In effect this scheme utilises our AA credit rating and strength of our balance sheet to provide additional security to banks in their lending arrangements with property owners. The Council would not take on any increase in debt unless there was a call on our guarantee in the event of loan default. The Council would control which buildings and properties we were willing to support under such an arrangement, but it would be offered to whichever bank the property owner is seeking lending from.

This work is in its infancy, however we seek the Council's guidance on whether such a scheme is something this Council would pursue.

Increasing Grant Funding Levels (eg BHIF)

The appropriate level of grant funding made available through a grant scheme is always a point for consideration. The BHIF fund is well subscribed and during the last funding round with applicants being granted just less than half of the funding amounts requested.

The key point of note regarding the BHIF is that there is no funding at all in our current long term plan from 2015/16 and therefore the fund in its entirety will need to be reconsidered as part of the next long term plan. Given the constraints on the 2014/15 rates increase it is recommended that consideration of the appropriate grant scheme to support heritage and wider earthquake strengthening outcomes occurs as part of the 2015/16 long term plan process.

Earthquake Bonds

It has sometimes been discussed that the Council should issue Earthquake bonds. However they are another form of debt to the Council that would add debt to the Council's books and not an incentive tool. This is a question on how we fund those incentives. It is therefore officer's advice that this is a secondary funding decision and is not something to pursue in the 2014/15 Draft Annual Plan.

6. Financial implications

The proposal will add $100,000 per annum (for the next 15 years) to the opex budgets of the Council for introduction of a building consent fee subsidy.

The rates remission proposals will not add anything to our overall rates requirement, but they will cause a redistribution of rates of between $200,000 and $500,000 per annum depending on when earthquake strengthening occurs and the value uplift this creates on our earthquake prone properties.

7. Conclusion

The earthquake strengthening issue is still being responded to by many sectors of the market from developers, financiers and insurers. Over the next 5 years the Council will undertake assessments on our post-1976 buildings and we will have a clear view on the scale of the problem in our newer buildings after that IEP process is complete.

The Council's response needs to be as equally considered to reflect the significance of the issue, and the role we play in strengthening privately held buildings. Our focus on achieving our city resilience outcomes needs to be balanced with our responsibilities to our ratepayers to act in a financial prudent and considered manner.

The links with our economic development strategy are important as improvements in the economy and business will also increase the demand for office space which in turn will provide property owners and banks the confidence to invest in their buildings.

Improving our current package of support for earthquake strengthening is important and adding rates relief and building consent subsidies is a further step to assist building owners.

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Kiri Rasmussen, Manager Economic Development Projects

SUPPORTING INFORMATION

1) Strategic fit / Strategic outcome

The policy supports Council's overall vision of Wellington Towards 2040: Smart Capital which seeks to have infrastructure that creates a secure and resilient city.

2) LTP/Annual Plan reference and long term financial impact

The earthquake resilience project is contained in the Council Long Term Plan and any changes arising from this paper will be consulted on as part of the 2014/15 Draft Annual Plan

3) Treaty of Waitangi considerations

N/A

4) Decision-making

This paper does not include significant decisions. The report sets out a number of options and reflects the views and preferences of officers and those with an interest in promoting city resilience in an earthquake event.

5) Consultation
a) General consultation

Any recommendations and decision made from this paper will be consulted on as part of the 2014/15 draft annual plan.

b) Consultation with Maori

N/A

6) Legal implications

Potential legal risks for Council have been raised as appropriate.

7) Consistency with existing policy

Amendments and a new rates remission policy are recommended in this paper. Other policy matters are consistent with existing policy.

APPENDIX 1 – Proposed changes to the Rates Remission Policy.

Amendment to Section 2.3

2.3 REMISSION OF DOWNTOWN LEVY TARGETED RATE ON PROPERTY UNDER DEVELOPMENT OR EARTHQUAKE STRENGTHENING

REMISSION STATEMENT

The Council may remit part or all of the Base targeted rate, Commercial, industrial and business targeted rate and the Downtown Levy targeted rate ~~on land classified under the Council's commercial, industrial and business differential and located in the "downtown area" as defined within our Funding Impact Statement Rating Mechanisms,~~ where the property is deemed to be 'not fit for purpose'.

POLICY OBJECTIVE

To provide rates relief for ~~downtown commercial~~ property temporarily not fit for purpose due to the property undergoing development or earthquake strengthening and therefore not receiving the benefits derived by contributing to the Commercial industrial and business sector targeted rate, Base sector targeted rate or the Downtown Levy.

CONDITIONS AND CRITERIA

A remission of the Commercial industrial and business sector targeted rate, Base sector targeted rate or the Downtown Levy may be granted ~~to rating units that are classified under the Council's commercial, business and industrial differential and located in the "downtown area" as defined within our Funding Impact Statement Rating Mechanisms~~ where the property is temporarily not fit for purpose. Under this policy "not fit for purpose" is defined as where:

a) the property (rating unit) will not hold sufficient consents to permit occupation and,
b) the property (rating unit) will not be used for any purpose, apart from the construction of buildings, premises or associated works, or earthquake strengthening works and
c) the property (rating unit) will not generate any revenue stream

The above criteria will apply to and must be met by an entire rating unit, as identified in the Council's rating information database.

APPENDIX 1

Additional Section 2.6 to be added to the Rates Remission Policy as follows.

2.6 REMISSION OF RATES FOR BUILIDNGS REMOVED FROM THE EARTHQUAKE PRONE BUILDINGS LIST

REMISSION STATEMENT

The Council may grant a remission on a property's rates where the property was on the earthquake prone building list and the owner has taken action to remove that building from the list either by strengthening that building to beyond 33% of the New Building Standard (NBS) or by removing the building from the site. The building owner may apply for this remission for a period of 3 years after the removal of the building from the earthquake prone building list.

For strengthened buildings, the remission shall equate to the increased rates (general rate, downtown levy, targeted commercial or residential rates, stormwater and sewerage rates but excluding metered water charges) payable due to the valuation uplift that may reasonably arise from seismic strengthening works.

For removed buildings, the remission shall equate to 10% of the rates (general rate, downtown levy, targeted commercial or residential rates, stormwater and sewerage rates but excluding metered water charges) payable on the property.

POLICY OBJECTIVE

The objective of this remission policy is to minimise the rates impact of valuation increases arising for property owners who have taken positive action to address the structural safety of their earthquake prone buildings.

CONDITIONS AND CRITERIA

A remission of rates may apply under the following conditions and criteria:

i. the building must have been on the Earthquake Prone Buildings list[1]

ii. the building owner must have taken action to remove their building from this list either through seismic strengthening or building removal

iii. the remission must be applied for within 12 months of the building being removed from the Earthquake Prone Buildings list and will apply for 3 rating years only (the property owner does not need to reapply in years 2 and 3)

iv. the remission will apply to the general rate, downtown levy, targeted commercial or residential rates, stormwater and sewerage rates (hereinafter referred to as "the rates")

v. the remission will not be available retrospectively for buildings already removed from the list prior to this policy being implemented

vi. the remission is only available to the property owner who has taken action to remedy their building. It will not be available to a third party purchaser of the building even if a sale took place within 3 years of the building being removed from the Earthquake Prone Buildings list

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[1] as maintained by Wellington City Council

vii. for earthquake prone buildings that have been seismically strengthened to > 33% NBS the following conditions and calculations will apply:

a. the remission application will be accepted after the building has been removed from the Earthquake Prone Buildings List

b. the remission will be calculated as the additional rates payable due to the valuation uplift that may reasonably arise from the seismic strengthening project[2]

c. If there has been no property valuation uplift as a result of seismic strengthening work then no remission will be calculated

d. The Council's average annual rates increase will still apply

viii. for earthquake prone buildings that have been removed from the site the following conditions and calculations will apply:

a. the remission application will be accepted after evidence of the building removal has been provided to Council and the building has been removed from the earthquake prone building list.

b. the remission will be calculated as 10% of the rates payable on the property for the 3 years following the acceptance of the remission application.

VALUATION CHANGES

Wellington City Council is on a 3-yearly valuation cycle for all properties in the city. City-wide valuations are performed by Quotable Value New Zealand Limited as at September and are used to calculate rates from the next rating year commencing 1 July. The next city-wide valuation will occur as at September 2015 and will be used to calculate rates for the rating year commencing 1 July 2016.

Properties are also subject to "maintenance valuation adjustments" at any time between the valuation cycles when there has been a measurable value change, usually triggered by improvement works.

Building owners will be notified when the capital value of their property has changed. Rates will be calculated using the new capital value from the next rating year commencing 1 July.

APPLICATION

This remission may be applied for at anytime during the year. If approved, the remission will take effect either from the next rating year (1 July), or will be backdated to take effect from the start of the current rating year at the nomination of the property owner and agreement with the Council. The remission will cease after 3 years from the agreed effective start date.

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[2] Property valuation adjustments will occur either as part of the Council's 3-yearly city wide revaluation cycle, or through "maintenance" valuation adjustments that occur in between cycles where improvement works have taken place resulting in a measurable value change. Building owners will be notified of any valuation change in both circumstances. Under both circumstances rates are not impacted until the next rating year commencing 1 July. Council reserves the right to use its discretion in determining valuation changes that may reasonably arise from seismic strengthening under this policy.

APPENDIX 2 – BUILDING CONSENT FEE SUBSIDY FUND

A building consent fee subsidy fund is proposed to alleviate the cost burden on property owners faced with earthquake prone buildings requiring significant strengthening costs.

It is anticipated the following criteria would apply:

i. The subsidy would apply only to those buildings on our Earthquake Prone Buildings (EPB) List.

ii. The subsidy would be calculated as 10% of the Wellington City Council charges included in the building consent cost, up to a maximum of $5,000 per consent.[3]

iii. The subsidy would be made available after completion of the strengthening works evidenced by issuance of a CCC and removal of the building from the Council's EPB List.

[3] This would exclude charges such as the BRANZ fees